WHAT MAKES THEM TICK?

EXPLORING THE ANATOMY OF MAJOR MICROENTERPRISE FINANCE ORGANIZATIONS

Elisabeth Rhyne
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ACCION

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FOREWORD

What is it, indeed, that makes microenterprise finance tick? The authors do an excellent job of describing ***how*** microfinance institutions tick, but we never find out ***why*** they tick. They don't explain the driving force that keeps these institutions vibrant and alive nor do we ever find out why so many microenterprise organizations have been established so fast.

To find out what makes them tick, just ask any loan officer from a microenterprise organization out in the barrio visiting clients. It's the gleam in the eyes and the smile on the face of a customer when she learns that a bank is actually going to trust her. This may be the best news she's had in months, and her future suddenly looks brighter. Clients of microenterprise organizations are often astounded that for the first time a formal institution is going to take them seriously and treat them as people of importance.

For the staff of BancoSol, and I'm sure for staff at many microenterprise institutions, it is extraordinarily motivating to be involved in transactions based on trust. Our staff feel privileged to be part of a movement that is shattering the conventional wisdom of bankers everywhere about the poor. That's why they are willing to put in long hours and walk long miles to do their jobs.

The institutions analyzed in this monograph are bringing banking back to its roots. They are re-discovering character-based lending. These lending techniques, each a little different in the institutions covered here, build bonds of mutual trust between borrowers, their peers, lenders and the local community. These methods work! They produce a virtuous circle of trust and repayment. And, as is always the case with a good idea whose time has come, character-based lending is mushrooming throughout the world.

Of course it takes more than trust to run a large microfinance institution. It takes structures, systems, strategies, training and information. The authors of the monograph explain just how these pieces fit together to make a healthy institution. But as you read, don't forget the secret of what really makes them tick.

Francisco "Pancho" Otero
Managing Director, BancoSol
July 4, 1994
Yungas, Bolivia

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ABBREVIATIONS

ADEMI	*Asociación para el Desarrollo de Microempresas, Inc.*
BancoSol	Banco Solidario, S.A.
BKK	Badan Kredit Kecamatan
BRI	Bank Rakyat Indonesia
BUD	Strategic Business Unit
GCC	Group Credit Company
GNP	Gross National Product
IDB	Inter-American Development Bank
K-REP	Kenya Rural Enterprise Foundation
KUPEDES	General Rural Credit
NGO	non-governmental organization
PRODEM	*Fundación para la Promoción y Desarrollo de la Microempresa*
SIMPEDES	General Rural Savings
SEF	Small Enterprise Foundation
USAID	United States Agency for International Development

CHAPTER I

INTRODUCTION:

INSTITUTIONAL COMPETENCE AND THE ACHIEVEMENTS OF MAJOR MICROENTERPRISE FINANCE ORGANIZATIONS

This monograph examines the building blocks of institutional competence for microenterprise finance by comparing several of the largest and best-known microenterprise finance organizations.

I.A. Microenterprise Finance in Context

For millions of individuals in developing countries, microentrepreneurial activity represents the sole or primary source of income. However, the woman selling fruit in the weekly market, the woodworker fashioning a chair, and other microentrepreneurs have been excluded from formal sector financial institutions because they have been long presumed to be un-creditworthy.

Since the late 1970s, however, techniques have emerged for providing financial services -- credit and savings -- to this previously untapped market, and clients have received these new services with great enthusiasm. The stories of individuals receiving a loan for the first time are testimony to the valuable role such services can play in poor communities. Methodologies have been fine-tuned to fit the needs of local communities often with great success. These techniques have become the basis for a flourishing infant industry throughout developing countries devoted to increasing the access of the poor to financial services.

The current challenge for service providers is to achieve massive scale -- because the potential market is vast -- even while attaining high degrees of financial self-sufficiency. And while the challenge is great, a number of institutions in very diverse settings are meeting it.

The ability of such institutions to achieve scale and self-sufficiency can be attributed both to effective credit and savings methodologies and to the strength and competence of the organizations themselves. These two elements -- effective methodology and institutional competence -- are closely intertwined and equally relevant. Yet writings on microenterprise finance have focused largely on methodologies, while there have been relatively few explorations of the components of institutional strength.[1] In particular, there have been few organizational comparisons focusing on the institutional dimension. This monograph, by focusing on the institutional strengths that successful microenterprise finance organizations exhibit, will attempt to describe what skills or competencies allow institutions to:

- ***Become financially self-sufficient***
- ***Expand outreach to a nationally significant scale***
- ***Survive over time***

This focus reflects the challenges facing institutions in what has been called the new world of microenterprise finance,[2] and this monograph is intended to set the stage for further progress in building competent institutions that serve the poor.

I.B. Analytic Approach

The approach taken here is to compare and contrast successful institutions, focusing on four: Grameen Bank in Bangladesh; Bank Rakyat Indonesia's (BRI) Unit Banking System in Indonesia; Banco Solidario, S.A., (BancoSol) in Bolivia; and Actuar Bogota in Colombia. Other similar institutions, such as the *Asociación para el Desarrollo de Microempresas*, Inc. (ADEMI) in the Dominican Republic, Badan Kredit Kecamatan (BKK) in Indonesia, Kenya Rural Enterprise Programme (K-REP) in Kenya, the Small Enterprise Foundation (SEF) in South Africa, and credit union systems in Africa, are referenced where appropriate to demonstrate that institutional competence in microenterprise finance can be found in many places.

The institutions analyzed here differ in many dimensions. They seek different development aims, use varying methodologies to provide a variety of services, and take several different institutional forms (e.g., non-governmental organization [NGO] or bank). They operate in cultural and economic settings as different as rural Bangladesh and urban Colombia. They operate at different scales: the two Asian programs, Grameen Bank and BRI's unit system, each have nearly two million active borrowing clients, while the two South American programs are now approaching 50,000.

Despite the differences, these institutions have much in common. The source of their commonality is the commitment of each to providing financial

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1 Among them are Elaine Edgcomb and James Cawley, "The Process of Institutional Development: Assisting Small Enterprise Institutions Become More Effective," and Maria Otero, "The Evolution of Nongovernmental Organizations toward Financial Intermediation," in Otero and Rhyne, eds., 1994.

2 See Otero and Rhyne, eds., 1994.

services to clients financial institutions previously ignored, on as large a scale as possible, and on a financially self-sustaining basis. To do this, the institutions have each developed a similar set of institutional competencies, some of them quite extraordinary. This monograph seeks to distill these elements of competence for the emerging field of microenterprise finance, with the aim of identifying the fundamental underlying principles that make for successful microenterprise finance institutions.

An Organic Conceptual Framework. After an introduction to the institutions and a background review of financial structure in Chapters I and II, the remainder of the monograph focuses on program operations. Chapter II, while it does treat important issues of financial structure, is not intended to be a thorough discussion of the subject. Readers who are already familiar with the institutions discussed here may wish to glance quickly through Chapters I and II, which are introductory in nature.

The core of the paper, Chapters III through VI, examines four important systems operating in microenterprise finance institutions, which can be viewed in analogy to the systems of living organisms. Chapter III presents the skeleton, or institutional structure, of each organization, focusing on the location of functions within each institution, and comparing productivity and costs. The performance of the retail outlets, where interaction with clients takes place, is particularly important. Chapter IV examines the use of information (this could be called the circulatory system, but perhaps the analogy shouldn't be pushed too far). Adding flesh to the bone, Chapter V reviews human resource use: staff recruitment, training, motivation, and evaluation. Finally, Chapter VI views the living institutions as wholes, observing them as they meet challenges arising at various stages in their life cycles, such as growing, innovating, and coping with shocks. It begins with a discussion of leadership and decision making. Thus, Chapters III through V compare the anatomy of the institutions, while Chapter VI looks at how these component parts work together to maintain institutional health.

At the end of each chapter, a brief section summarizes the conclusions of that chapter regarding the particular shape of competence in microenterprise finance. These summaries, taken together, form a portrait of the elements that contribute to scale, self-sufficiency, and longevity, and are summarized briefly in Chapter VII.

I.C. History and Background of the Institutions

This section introduces the four principal organizations by summarizing the origins, mission, and services of each.

Grameen Bank. In 1976, Dr. Mohammed Yunus, an economics professor at Chittagong University, began an experimental project to show that the extremely poor people of rural Bangladesh, among the poorest people in the world, could be creditworthy. During the next few years, the Grameen project evolved a lending methodology that still forms the basis of its now nationwide program. (Table 1 highlights major milestones in the evolution of Grameen Bank and other institutions.) Grameen Bank makes loans based on groups of five people who are held jointly liable for loans made to each group member. Several groups are joined to form a "center," through which an additional layer of guarantee is added. Loans are made for one-year terms, with weekly repayments, and at present they carry an interest rate of 20 percent. Borrowers are also required to make small, regular contributions to a group savings fund and an emergency fund. In 1983, Grameen was licensed by the Bangladesh government as a bank. Since that time it has added housing loans and, in 1992, seasonal loans for experienced borrowers.

Grameen Bank serves severely impoverished, mainly illiterate people, and over the years it has focused increasingly on women, such that 94 percent of its clients are now women. Many of its members had not carried out income generating activities of their own before taking a loan, and thus, activities receiving Grameen financing are generally very simple, such as buying and tending a dairy cow or a flock of ducks. In addition to its mission of poverty alleviation through credit, Grameen Bank pursues a social development agenda, embodied in its "Sixteen Decisions" for members to adhere to, which span topics including sanitation, nutrition, family planning, and education. Grameen Bank also carries out a range of projects, such as promotion of informal village schools, distribution of seeds and seedlings, and special projects such as fisheries and textile production.

The BRI Unit Banking System. The Bank Rakyat Indonesia is one of five state-owned commercial banks in Indonesia. Its particular mandate is to serve rural areas. BRI's Unit Banking System is a network of very small retail outlets throughout Indonesia operating at levels below BRI's regular branches (below both in terms of geographic location in smaller towns and in terms of loan size).[3] The units were created in the early 1970s as conduits for subsidized farm credit provided in tandem with technical support by the Ministry of Agriculture for adoption of the "green revolution" rice varieties and farming practices. This credit program, known as BIMAS, featured all the hallmarks of traditional directed credit: it lost money for BRI, repayments were poor, and benefits were appropriated by elites.

In 1984, the units were overhauled and new services were introduced, beginning with KUPEDES (an acronym for General Rural Credit), a largely character-based loan offered to any productive enterprise. KUPEDES involves only individual lending, not group loans. An expanded package of savings

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3 It is important to note the clear distinction between the bank as a whole and its unit banking system. However, as this monograph treats only the unit system as the subject being compared, the names BRI, BRI unit system, and BRI units will, at times, be used interchangeably.

instruments was introduced in 1986, offering savings clients a variety of mixes of liquidity and returns. Of these, SIMPEDES (General Rural Savings), a passbook savings program offering unlimited withdrawals, was designed to be the most attractive to local savers and has remained the most popular. The KUPEDES loans generally carry terms of three to 24 months, typically with monthly repayments. The effective KUPEDES interest rate is 33 percent per year. SIMPEDES rates vary with market conditions and have ranged from zero to 1.125 percent per month.

A central aspect of the Unit Banking System is its insistence that each retail unit be profitable. In fact, the units provide a major share of BRI's total profits each year. A banking ethos prevails throughout the system, with staff seeing themselves as making a contribution to rural development by being profit-making bankers.[4] The Unit Banking System serves a variety of clients, most of whom were not previously served by financial institutions. However, it does not generally serve the poorest stratum or the smallest rural centers, and less than half of its borrowers are women.

BancoSol. *Banco Solidario, S.A.* began operations in February 1992 as a fully licensed commercial bank in La Paz, Bolivia, with an explicit focus on microenterprises. It offers financial services — at present, mainly solidarity group loans—with the objective of promoting the socio-economic development of small-scale enterprises and the self-employed. Under the solidarity group methodology, prospective borrowers form groups of four to seven people to jointly guarantee loans in lieu of collateral. Loans start small, with a short term, generally three months. Renewal loans of progressively larger size are available if borrowers repay promptly and fully. Loans are available either in local *bolivianos* or in U.S. dollars (as is standard in Bolivia's heavily dollarized financial sector). BancoSol currently has 18 branches operating in four cities throughout Bolivia.

BancoSol emerged from PRODEM, the *Fundación para la Promoción y Desarrollo de la Micro Empresa*, a non-profit microlending institution founded in 1986. Created as a partnership between ACCION International and prominent members of the Bolivian business community, PRODEM initiated the urban solidarity group lending program and built its operations to a level of strong financial self-sufficiency. PRODEM and its supporters decided to create a bank largely for the purpose of relieving PRODEM's funding constraints (see Chapter II), and as BancoSol opened, PRODEM's portfolio and much of its staff were transferred to BancoSol (in return for ownership shares). In addition to owning a controlling interest in BancoSol, PRODEM remains active, with a mission to pursue more experimental activities. It is presently developing a lending program in the Bolivian rural areas.

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[4] Richard Patten, Harvard Institute of International Development. Interview, November 1993.

TABLE 1

TIMELINE OF EVENTS AT MAJOR MICROENTERPRISE FINANCE ORGANIZATIONS

(Parentheses indicate the number of borrowers at year end.)

	GRAMEEN BANK	BRI UNIT BANKING SYSTEM	PRODEM/BANCOSOL	ACTUAR BOGOTA
1970		BIMAS rice intensification project begins. Unit *desas* created.		
1974		Kredit Mini program (subsidized precursor of KUPEDES) begins.		
1976	Lending begins in Chittagong district as a University experiment.			
1979	Official "Grameen Bank Project" launched. Lending begins in Tangail district. (2,200)			
1980		Kredit Midi program launched.		
1983	Established as a bank by government ordinance.	Financial sector reforms, including interest rate deregulation, and dismantling of credit ceilings.		
1984	"Sixteen Decisions" developed. Housing loans introduced. (121,000)	Introduction of KUPEDES (general rural credit) and pilot savings program. (640,000)	ACCION conducts feasibility study in Bolivia.	
1986	Government ordinance amended to increase ownership by borrower-shareholders to 60 percent. (209,500)	Unit banking system reached break-even point. SIMPEDES extended nationwide. (1.2 million)	Establishment of PRODEM as NGO.	

TABLE 1

TIMELINE OF EVENTS AT MAJOR MICROENTERPRISE FINANCE ORGANIZATIONS (cont'd)

(Parentheses indicate the number of borrowers at year end.)

	GRAMEEN BANK	BRI UNIT BANKING SYSTEM	PRODEM/BANCOSOL	ACTUAR BOGOTA
1987			PRODEM begins lending. (1,200)	
1988				Actuar Bogota founded as non-profit. Solidarity group lending begins. (400)
1989		Unit banking system extends to urban areas. Volume of savings exceeds volume of loans. (1.6 million)	COBANCO committee established to transform PRODEM into a bank. (7,400)	
1991	Salary cost increased by 50 percent; major changes introduced; increase in interest rates and staff productivity. (1.04 million)	Government institutes tight monetary policy. Major drought. KUPEDES growth slows. (1.8 million)		Large loan received from commercial banks. (15,000)
1992	Seasonal loans introduced. (1.39 million)		BancoSol opens as private commercial bank. (approx 40,000)	Individual lending begins. (24,000)
1993	(1.59 million)	(1.86 million)	Savings program pilot projects conducted in two regions. (46,400)	Opening of first *Centro de Servicios*. Opening of Finansol. (37,500)

In 1993, BancoSol began a pilot project to offer savings services, which, in the spirit of BRI's savings program, offers a package of instruments from which the saver can choose the most appropriate mix of liquidity and returns. The services are expected to be offered throughout the bank during 1994. BancoSol has a dual mission, involving strong social values originating from PRODEM as well as newer shareholders' concerns for making commercial returns on investment. BancoSol is consciously attempting to demonstrate that financial services for microenterprises can be provided profitably on a fully commercial basis by the private sector.

Actuar Bogota. The *Corporación ACTUAR por Bogota* is a private, non-profit corporation founded in 1988 in Bogota, Colombia, and affiliated with ACCION International.[5] Its 13 branches offer credit, training, and technical assistance to two types of clientele. *Famiempresas*, who constitute the vast majority of Actuar clients, are family-run businesses involved primarily in commercial activities that receive short-term, working capital loans through a solidarity group mechanism. *Microempresas* borrow as individuals (with guarantees) and usually represent small industrial, commercial, or service-oriented production units. Most individual borrowers began as members of solidarity groups. Although Actuar Bogota began operations solely in the urban region, it now operates in secondary cities and rural areas within 150 kilometers of Bogota.

Actuar Bogota's vision is broader than financial services alone: it aims to demonstrate that a wide range of important services can be delivered profitably to the informal sector. This is reflected in the relative importance Actuar places on business and technical training and in Actuar's *Centro de Servicios Basicos* (Basic Service Center), a wholesale depot at which borrowers can purchase inventory and raw materials at lower prices -- and more conveniently -- than they can elsewhere. Future services envisioned include savings services, a wider range of loan products, housing, health care, insurance, and recreation. Actuar plans to create an elaborate structure of for-profit subsidiaries to provide these services. It has taken the first step by creating Finansol, a non-bank financial institution that has begun to take over the financial side of Actuar's operations, lending and raising funds. Even though Actuar is the newest of the organizations highlighted in this study, it has revealed a strong potential for continued growth.

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5 Several microenterprise finance organizations in other cities in Colombia also use the name Actuar, but they are entirely independent of Actuar Bogota. To avoid confusion with these other organizations, Actuar Bogota recently changed its name to CorpoSol. However, as this monograph discusses Actuar only up to the creation of CorpoSol, the name Actuar will be used throughout.

I.D. Levels of Achievement

The institutions profiled here have demonstrated significant achievements, which are illustrated by their performance in several areas of financial intermediation (the number of clients, the size of the lending portfolio, savings, and delinquency levels), in the provision of other services and in the measure of impact on clients — each with varying degrees of importance to the organization.

Lending. Because these institutions started as credit institutions, the numbers of active borrowers demonstrate their achievements most conveniently. The two Asian giants, Grameen Bank and BRI, are each approaching two million borrowers (1.6 and 1.9 million, respectively; see Table 2) which they serve through more than one thousand locations, providing nationwide coverage. Because BRI makes much larger loans than Grameen, its total active portfolio (loans outstanding) of US$931 million is far larger than Grameen's US$180 million. BancoSol and Actuar Bogota, which are newer and not yet national in scope, are small in comparison to the two Asian programs, but still unprecedented in scale compared with most other programs. BancoSol and Actuar have 46,000 and 37,000 borrowers, and active portfolios of US$24.8 million and US$8.2 million, respectively.

To place the scale reached by these four institutions in context, it is important to note the population of potential clients in the geographic area of focus and to compare these programs to other programs internationally. Institutions in small countries will naturally attain a smaller scale than those in large ones, and institutions will first set scale goals in a limited geographical area before expanding. These differences account for most of the variation in size of these four institutions. Among other noteworthy institutions, ADEMI, which has achieved nationwide outreach in the Dominican Republic, had an active portfolio of US$11.5 million in December 1993 and serves 13,500 active clients, about one third the number served by Actuar (See Box 1).

The BKK of Central Java, Indonesia, in operation since 1972, had an active portfolio of US$23.6 million in 1992 and reaches about half a million borrowers (see Box 2). (Pearson and Garland, 1993: Table 1) Its average loan size hovers around US$50. The credit union system in Cameroon had an active portfolio of US$21 million in 1991 with 20,000 outstanding loans. The FINCA village bank system in El Salvador has nearly 30,000 clients. The Small Enterprise Foundation in South Africa, with an active portfolio of more than US$200,000 and nearly 2,000 clients, is much smaller than the other programs, but has grown quickly in its two years of operation. Box 2 reviews the achievements of three programs.

TABLE 2

ACTIVITIES AND ACHIEVEMENTS OF MICROENTERPRISE FINANCE ORGANIZATIONS

	GRAMEEN BANK (June 1993)	BRI UNIT BANKING SYSTEM (October 1993)	BANCOSOL (December 1993)	ACTUAR BOGOTA (October 1993)
Volume of loans outstanding (US$ million)	180 (all loan types) 60 (housing) 115 (general)	931	24.8	8.2
Number of active borrowers	1.59 million	1.86 million	46,428	37,482
Percentage of female borrowers	94	24[a]	71	48
Average outstanding loan size (US$)[b]	$114 (all loan types) $73 (general)	$502	$534	$220
Average duration (months)	12	3-24	5 (approx)	4-5 (group lending) 12 (individual)
Effective interest rate (percent per annum)	20 percent (general)[c]	33 percent	53 percent (loans (in bolivianos) 31 percent (loans in US$)	71 percent (includes fees)
Local inflation (percent per annum)	7.8 percent[d]	9.9 percent[e]	15 percent[f]	22.6 percent[g]
Overdue loans • Institution's own past maturity	1.4 percent full value of loans over one year over outstan-over outstan-ding portfolio	7.5 percent value of install-ments past due past due ding portfolio	2.7 percent full value of loans one day past due over over outstan-ding portfolio	2.9 percent full value of loans one day outstanding portfolio
Long-run loss rate (institution's own estimate or provision taken)	3.6 percent[h]	3.1 percent	1 percent[i]	less than 1.5 percent
Volume of savings and deposits (of clients)	$171 million[j]	$2.1 billion	$3.1 million	not applicable

TABLE 2

ACTIVITIES AND ACHIEVEMENTS OF MICROENTERPRISE FINANCE ORGANIZATIONS (cont'd)

	GRAMEEN BANK (June 1993)	BRI UNIT BANKING SYSTEM (October 1993)	BANCOSOL (December 1993)	ACTUAR BOGOTA (October 1993)
Number of active savers	1.59 million[k]	11.2 million	not available	not applicable
Number of retail units	1,030 branches	3,235 units 635 village posts	18 branches	13 branches
Country population (1990)	108 million	178 million	7 million	32 million
Exchange rate to US	$39	2,000	4.47	813.28

SOURCES: The institutions themselves; Khandker et al., 1993; World Bank, 1992.

a Survey data for 1989. (Holt, 1991)
b Based on outstanding portfolio. Average initial loan size is larger due to differing stages of amortization.
c Does not impute cost of forced savings in Group Fund or Emergency Fund. Some observers consider these amounts as raising the effective rate
d Average rate of inflation, 1988-92..
e 1992 annual rate.
f Average rate of inflation, 1990-93.
g 1993 annual rate.
h 1992 estimate
i Represents provision negotiated with the Superintendency of Banks, not actual loss, which is lower.
j The majority of these savings are held in accounts off Grameen Bank's balance sheet.
k All borrowers have savings; Grameen also accepts deposits from non-members, but this number is not available.

Savings. The institutions profiled here have different approaches to savings, but this element of financial intermediation is becoming increasingly important at each. The voluntary savings instruments of the BRI unit system have been stunningly successful in mobilizing savings. The unit banks now count more than 11 million savings accounts, amounting to US$2.1 billion, more than twice their volume of loans. Grameen Bank requires compulsory savings, in the form of required weekly contributions to group and emergency funds. As these funds are not returned to members unless they withdraw their membership, the various forms of savings accumulate steadily. Grameen also offers deposit services to the public, although these deposits are not a significant source of funds. In June 1993, savings and deposits amounted to US$171 million or 95 percent of the total outstanding portfolio. Having dropped its original compulsory savings requirement, BancoSol is currently testing a voluntary savings instrument adapted from the BRI model, which it plans to implement throughout the bank in 1994. Actuar Bogota has also dropped compulsory savings requirements from its group-lending methodology, but as an NGO, it has not been legally permitted to accept deposits. However, its new non-bank financial institution, Finansol, has a license to take deposits and plans to develop a voluntary savings program.

Among other programs referenced here, only the credit union systems are fully savings-based. BKK has a savings program, yet with US$6 million in client deposits in 1992, it draws in only about one-fourth of the amount it lends out. ADEMI, which as an NGO cannot legally accept savings, has created a financial product whereby clients can "lend" money to ADEMI at 18 percent per year. Such funds are treated as deposits and amounted to more than US$1.5 million as of September 1993. ADEMI also actively encourages clients to save at the commercial bank that handles their loan accounts.

Delinquency and Default. None of these institutions could have achieved its current scale without keeping delinquency and default to manageable levels. Definitions of delinquency and default differ from one institution to another, but it is clear that each of the four highlighted institutions has been able to keep arrears from threatening the stability of the lending program (i.e., well under ten percent, if not below five percent) and has dealt effectively with the specific situations in which delinquency has become a problem. Long-run loan losses have been below four percent -- even well below -- at all four institutions (based on the organizations' estimates, see Table 2), amounts that the organizations build into their cost structures through provisioning.

Other Services. In addition to basic financial services, several of these institutions offer other services. Over nine percent of the value of loans disbursed by Grameen Bank between 1984 and 1993, for example, were housing loans. As of December 1992, over 150,000 housing loans had been made. Grameen also keeps track of its social achievements, citing creation of some 16,000 informal schools, the distribution of over five million seeds, and responsibility for eliminating dowry in 19,000 marriages. (Khandker et al., 1993: Table 3.11) Actuar Bogota provides substantial amounts of training to all its clients; it maintains a large wholesale depot where microenterprises can buy inventory and raw materials on good terms, and it envisions a range of additional services. Similarly, ADEMI offers courses in marketing, accounting, and management on voluntary, fee-based terms. K-REP also offers training and technical assistance. BRI's relatively few additional activities include offering savings accounts to local organizations and carrying out simple money transfers and payment transactions. However, for all these institutions, the basic lending operation -- and, for BRI, lending and savings -- is by far the dominant activity and provides a platform for secondary activities.

BOX 1

THE *ASOCIACION PARA EL DESARROLLO DE MICROEMPRESAS, INC.* (ADEMI) / SANTO DOMINGO, DOMINICAN REPUBLIC

Founded as a non-profit organization in 1983, ADEMI is now one of the largest micro-credit programs in Latin America. As the brainchild of Camilo Lluberes, Pedro Jimenez -- its president and executive director, respectively -- and Stephen Gross of ACCION, ADEMI was the first ACCION-affiliated institution to reach large scale and high degrees of financial self-sufficiency, and carried an active portfolio of over US$11 million in December, 1993. Its philosophy emphasizes enterprise and employment growth, with a strong belief in the contribution of informal entrepreneurs to "economic democracy." In contrast to other institutions highlighted here, ADEMI's clients are more likely to be involved in manufacturing than in commercial activities.

Operating in 23 locations (eight offices and 15 smaller posts) in both the *barrios* of Santo Domingo and in the interior regions, ADEMI lends to individuals for both working capital and fixed asset loans. Using the principle of "scaling up" credit amounts, initial working capital loans are granted within the range of US$50 to US$500, and carry short terms. Borrowers who pay back their loans on time are assured of subsequent loans, which are incrementally larger and longer term. In 1991, ADEMI established a small business loan program to meet the demands of entrepreneurs for larger, longer term credit. To date, they have disbursed over one hundred such loans, the bulk of which range from US$28,000 to US$40,000. Nearly all of the clients who have taken out loans under this program were formerly microenterprise clients, reflecting ADEMI's ability to meet the changing needs of its clients. The small business program now represents 25 percent of ADEMI's outstanding portfolio (March 1994). In addition to its credit program, ADEMI offers non-financial services including technical assistance on an individual basis, and business courses for clients.

By early 1994, ADEMI's staff had grown to over 160, including 86 loan officers (*asesores*). With responsibilities including the recruitment and assessment of clients, loan follow-up, technical assistance, and preventing delinquency, each *asesor* is expected to carry an average of 130 clients. ADEMI is a highly competent institution that has made significant achievements in microenterprise finance in Latin America, and now stands at the forefront of small business lending as well.

SUMMARY OF ADEMI ACHIEVEMENTS (year-end 1993):

	Microenterprise Program	Small Business Program	Total Portfolio
Number of outstanding loans	13,543	78	13,621
Amount of outstanding loans (US$)	$9,030,000	$2,360,000	$11,390,000
Average size of loans outstanding (US$)	$670	$30,260	$836
Percent of female clients			39
Number of offices			23
Number of staff			165

BOX 2

OTHER NOTEWORTHY MICROENTERPRISE FINANCE ORGANIZATIONS

Badan Kredit Kecamatan (BKK)/Central Java, Indonesia

Established in 1970 by government initiative, the BKK is a banking system that provides financial services at the village level in the province of Central Java. It is the largest of seven separate, provincial-based institutions established in each of the other most populous provinces. In general, BKK and its cousins reach a smaller scale and more remote clientele than does BRI, though there is certainly overlap and direct competition between institutions. BKK has achieved considerable outreach in Central Java: operating through over 500 separate institutions, at year-end 1992, the system had a collective outstanding portfolio of US$23.6 million in nearly 500,000 loans, and had generated US$6 million in client deposits. (Pearson and Garland, 1993) Most lending is done on a short-term basis, and repayment is motivated by guaranteed eligibility for repeat loans. BKK is well known for maintaining a very low average loan size (US$25 in 1989; US$47 in 1992).

Kenya Rural Enterprise Program (K-REP)/Nairobi, Kenya

Founded in 1984 and incorporated as an NGO in 1987, K-REP is both an intermediary financial institution with its own credit programs, and a support and funding organization for other NGOs doing informal sector lending. K-REP serves its clients directly through two schemes: *Juhudi*, which uses a group-based methodology loosely modelled after Grameen Bank; and *Chikola*, which offers loans to preexisting rotating savings and credit associations (ROSCAs) and informal business associations. Four branches throughout Kenya currently offer the *Juhudi* program. Each branch has ten staff, including six credit officers who jointly carry an average of 1,800 borrowers. From 1990 to 1993, a total of 3,900 loans had been disbursed through these branches. (Mutua, 1993) In addition to its direct credit operations, K-REP lends to and assists other microfinance NGOs, conducts research and evaluation projects in the area of small enterprise development, and facilitates policy dialogue between the public and private sectors on issues of concern to clients.

The Small Enterprise Foundation (SEF)/Tzaneen, South Africa

Founded as a non-governmental organization in 1991, SEF provides finance to microentrepreneurs in the rural areas of the Northern Transvaal of South Africa. Since the first disbursement in early 1992, SEF has made more than 4,500 loans, mostly to impoverished women, and has a current active portfolio of over US$200,000 (March 1994). Largely modeled after the Grameen Bank, SEF employs a group lending methodology that allows for fortnightly repayments and avoids cash transactions for field workers. The Foundation's most remarkable achievement to date is the maintenance of a 100% repayment rate, reflecting the fact that no loan has ever been overdue for more than a few days. While SEF cannot currently accept client deposits, it does encourage participants to save at a local bank. Currently operating in one main area with some twenty staff members, SEF plans to expand into three "zones" by late 1995.

Impact. Although impact on clients is extremely difficult to measure, careful survey research indicates that these institutions make a significant difference in the lives of their clients, both economically and socially. Data from a 1988 survey of BRI unit clients led to estimates that 187,000 families were able to move out of the "seriously poor" category as a result of program participation. The survey also indicated that over three years of participation, household income increased 76 percent, as compared to a 12 percent increase in rural Indonesia generally. Dramatic increases in employment and labor hours (65 and 84 percent, respectively) were also reported. (Sutoro, 1990) Participation in Grameen Bank appears to increase the chances that a woman will use contraceptives, drink safe water, grow vegetables, and send her children (especially girls) to school, as well as leading to increased family income. (Schuler and Hashemi, 1993; Khandker, 1993) The introduction of housing loans in 1984 has triggered the legal transfer of home ownership to thousands of poor women in rural areas in Bangladesh. (Khandker et al., 1993)

Strong growth in demand and continued client participation at all these institutions confirm that they provide services their clients value highly.

I.E. Recognizing Competent Institutions

This brief description of major microenterprise finance institutions and their achievements allows a preliminary step towards describing competence in microenterprise finance. The monograph defines its scope of concern as microenterprise finance institutions that can and do achieve large scale, financial self-sufficiency, and prospects for longevity, while providing financial services to previously excluded groups. To begin to flesh out at least the scale and outreach, we have found that the leading institutions have active portfolios that reach from well over 10,000 clients up to more than a million, and range from several million dollars to nearly one billion — in loans averaging less than US$550. The basic lending methodologies are well tested and stable. Delinquency and default are tightly controlled. Scale in savings services is a lagging aspect of this portrait, with initiatives ranging from pilot plans to a fully operational large-scale savings program. Savings will become an increasingly important element as these organizations continue to grow

This is not to say that institutions must achieve scale before they can be classified as competent. Rather, institutions committed to scale of outreach should begin to aim at reaching levels that attempt to make a major contribution to their region or nation. Accordingly, it is important to recognize that scale is a function of local context and that individual organizational goals will differ between countries and between rural and urban programs.

These competent organizations have a strong sense of mission, and their basic credit and savings services are complemented by other services as an outgrowth of their vision. These institutions and their services are highly valued by clients and appear to make a significant difference in their lives. The rest of this monograph is devoted to understanding the institutional strengths that have allowed them to achieve such scale and outreach.

CHAPTER II

FINANCIAL STRUCTURE AND INSTITUTIONAL TYPE

The microenterprise finance institutions analyzed here have a variety of origins and now take on a range of institutional types. The BRI units are a part of a government-owned bank; BancoSol is a commercial bank arising out of an NGO; Actuar is an NGO that owns a for-profit finance company; and Grameen Bank is a specially chartered, member-owned bank, arising from a university and government project. These differences in origin and institutional type are particularly important in determining the sources of funds these programs use. The organizations highlighted here have all instituted transformations in their financial structures and legal status to bring them greater access to important sources of funding, allowing each to become increasingly financially independent.

These institutions demonstrate that a high degree of financial viability is necessary for the achievement of large scale. Each of these institutions required large initial investments (subsidies) to begin operations, but each has followed a path toward increasing financial viability. The BRI unit system leads all the other institutions here, as it is clearly profitable, covering all costs of operations and financing from revenues. Start-up grants and concessional funding have been superseded by subsequent profits. BancoSol has also crossed the threshold of fully commercial operations. The other institutions retain some element of concessional funding, while generating operating surpluses.[6]

II.A. Institutional Transformation to Gain Access to Funds

For each institution, the path to financial self-sufficiency and large scale is shaped by its institutional form, which, in turn, determines the sources of funds

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[6] Financial viability has internal and external aspects: the internal aspect involves achieving profitable (unsubsidized) operations, while the external aspect involves gaining access to increasingly unsubsidized sources of funds. Operations will be discussed in more detail in Chapter III, while this chapter comments on financial structure and sources of finance.

the organization can tap. Those organizations beginning as new NGOs (Grameen, PRODEM and Actuar, as well as K-REP and ADEMI) have had to focus a great deal of time and energy on resource mobilization in order to be able to expand. Traditional NGO fundraising from donors and government requires extensive senior staff commitments for limited and often poorly timed grants. Most NGOs spend several initial years in a resource-constrained state. The drive for larger and more reliable sources of funds led all four of the featured institutions to become more formal financial institutions. BancoSol and the BRI unit system, which began as banks and built upon existing human, physical, and financial investments, have been able to expand and to reach financial viability more quickly. However, it is important to recognize the extensive time and energy devoted to fundraising (in the form of deposit mobilization) that these organizations experience as well. However, deposit mobilization, unlike fundraising, is fully integrated into basic operations.

PRODEM, the precursor of BancoSol, began life as a non-governmental organization funded by grants from a range of sources: the Bolivian government and private sector, the U. S. Agency for International Development (USAID), and the Calmeadow Foundation. As it expanded, it gained access to additional grants and, in a significant step forward, commercial loans from local banks (backed by partial guarantees). However, with these sources of funds, PRODEM could not grow fast enough to keep up with its client demand and institutional capability, and thus PRODEM found itself rationing credit to clients. To gain access to the levels of funding it desired, PRODEM established BancoSol, a licensed commercial bank with a financial structure that is fast approaching that of any sound commercial bank.[7] As a bank, BancoSol can access several sources of funds closed to PRODEM: for-profit equity investors, the interbank market (more convenient than borrowing from banks as a non-bank client), central bank refinancing facilities (potentially), and the savings deposits of clients and the public at large. A critical aspect of the transformation into BancoSol was the establishment of an equity base, with shareholders who seek a commercial rate of return. The involvement of active equity investors (not just equity capital) enabled the new institution to meet government banking requirements and gain access to commercial markets.

Actuar Bogota envisions a similar progression from NGO to investor-owned financial institution. Unlike PRODEM, however, Actuar Bogota was able to finance its start-up lending entirely from borrowed funds (with help from ACCION loan guarantees), rather than grants, and thus has had a greater tradition of formal financial management and commercially inspired operating procedures from the beginning. Although Actuar has had access to bank loans since it began, it too has faced constraints. Among these have been (1) the high management time cost of negotiating individual loans with large numbers

7 For more detail on the transition from PRODEM to BancoSol, see Amy J. Glosser, "The Creation of BancoSol in Bolivia," in Otero and Rhyne, eds., 1994.

of banks, up to 12 at once; (2) banks' regulatory constraints on the amounts they could lend to Actuar, particularly given Actuar's lack of tangible collateral (despite a willingness by the banks themselves to consider Actuar's portfolio as a suitable guarantee); and (3) the high interest cost of loans relative to other forms of financing, although a portion of Actuar's portfolio has been financed with reduced-cost loans through IDB-funded rediscount facilities. Actuar's solution to its financing constraints was the purchase of a finance company, which it renamed Finansol. As a formally licensed financial institution, Finansol has access to a variety of sources of funds and can carry out most operations of commercial banks (except for checking accounts). The most readily available source of funds, which immediately released constraints upon Finansol's start in November 1993, is the sale of certificates of deposits — and later, bonds — through the stock market to major local institutional investors such as pension funds. Finansol's more permanent strategy will be to offer deposit services to small savers. As different from BancoSol, Actuar does not intend to turn over its operations to Finansol, but to maintain the NGO, now called CorpoSol, as the source of client contact, while Finansol will be the financing arm.

Grameen Bank has also progressed toward being an independent financial institution. Grameen began as a project, first of a university and then of the government, funded by private donors and government grants. A special government ordinance in 1983 paved the way for the creation of Grameen Bank as a financial institution. The ordinance contained certain features which set Grameen apart from other commercial banks, including provisions regarding levels of capital (authorized capital of US$2.7 million and paid-up share capital of US$1 million), as well as an ownership pattern which allows borrowers to be shareholders. Since its inception, Grameen Bank has had access to a mixture of soft loans and grants from international donors and soft loans from the Bangladesh central bank, but over the course of the last decade, it has moved in the direction of greater financial viability while maintaining dramatic rates of expansion. These trends have also brought new sources of financing to Grameen, including member savings, some non-member deposits, and non-subsidized loans from banks in Bangladesh.

During the same period, Grameen Bank's ownership structure has changed from being largely government-owned to being majority-owned by members (60 percent during the late 1980s and 88 percent since late 1990), as members gradually "purchase" the Bank through savings deposits of one taka (about two cents) per week. While Grameen does not have equity investors who strive to earn a market rate of return on their investment, it does have member-owners. These representatives of the entire Grameen client base constitute nine out of thirteen members of the Board of Directors and manifest an interest in the long-run survival of the institution. Given Grameen's abundant access to international donor funding, it has chosen to continue using concessional and grant funds where possible, to keep interest rates to borrowers low (though at present they are somewhat higher than commercial bank rates), and to finance rapid expansion. In Grameen's case, continued use of soft money has coexisted with a drive toward high productivity and efficient operations, as subsequent chapters will show.

ADEMI also maintains continued access to international sources of funds. In addition to having significant support from both the Dominican private sector and government from the beginning, ADEMI has also received soft loans from the Inter-American Development Bank (IDB), USAID, and the German government, among others. These funds include credit lines and long-term loans that range in financial cost from 1 to 22 percent per year. Despite retaining dependence on low-cost funding sources, typically a recipe for an unsustainable program, ADEMI management has used its external subsidies to capitalize itself, rather than passing them to its clients. Few other institutions have enjoyed the access to concessional funds of either Grameen or ADEMI, and it is worthwhile to note that in spite of this continued access both have managed to maintain a strong focus on efficiency.

BRI's history reveals a unique pattern of financial growth. As part of a bank, the unit system moved quickly toward self-financing through deposit mobilization. When BRI introduced KUPEDES lending in 1984, the units were financed in the short term from their preexisting loan portfolios (mainly from the programs known as Kredit-Mini and Kredit-Midi), as well as through a combination of initial capital deposits, borrowings from the BRI branches, and retained earnings during the year. However, as soon as KUPEDES had taken hold throughout the system and was beginning to break even, the SIMPEDES savings program was introduced nationwide in 1986. By 1989, the units were fully funded by their own savings deposits.

II.B. Comparison of Balance Sheets

The diverse paths each of these institutions has taken is reflected in a comparison of their current financial structures (Table 3). On the asset side, Grameen, BancoSol, and Actuar Bogota are similar, with most of their assets in their loan portfolios. BancoSol shows the strongest concentration of its assets in loans because its portfolio is BancoSol's best income earning opportunity. In addition to its loan portfolio, Actuar's assets include its Basic Service Center. Grameen's figure is lower in part because Grameen Bank maintains large deposits (from soft loan sources) in financial institutions on which it earns income applied toward operating expenses, and because of investments Grameen has made in other types of rural development projects with which it has experimented. The BRI units have only 38 percent of their assets in loans, while 58 percent are held as deposits with the main BRI branches, due to the excess capital relative to loan demand. The BRI branches use the deposits as a source of capital for their (larger) non-unit-system loans.

Differences among the institutions are more striking on the liabilities side because each institution has a unique mix of sources of funds. Funds of the BRI units come almost exclusively (90 percent) from savings deposits. This structure puts BRI alongside credit union systems in terms of sources of funds. Grameen is significantly funded by savings with the combination of client savings and deposits amounting to 19 percent of total assets. Grameen Bank has mobilized sufficient savings to fund 95 percent of its loan portfolio. However, the majority of these savings are held in accounts not part of Grameen's balance sheet. The remaining sources of Grameen's funds are largely donor and bank loans. By contrast, Actuar Bogota and BancoSol have few deposits from clients, though the expectation is that this will change dramatically in the coming years. BancoSol and Grameen, as banks, can access a diverse range of funding sources, with BancoSol's sources having a distinctly more commercial flavor. Actuar Bogota, pictured in October 1993, the final month before Finansol opened, was still constrained to raising funds by taking loans, as are other NGOs, such as K-REP and ADEMI. However, rapid change in Actuar's liability structure will occur now that Finansol is operational.

Finally, the nature of equity differs considerably among these institutions. BancoSol is owned by investors who maintain an expectation of earning a commercial return. However, this mix of investors is somewhat unconventional, including, in addition to private Bolivian businessmen, an NGO (PRODEM), and the private sector arm of the Inter-American Development Bank (the Inter-American Investment Corporation). PRODEM's share of equity represents the exchange of PRODEM's original loan portfolio for shares of BancoSol. Grameen's equity consists mainly of capital grants as well as the shares of its 1.6 million members. As of October 1993, Actuar Bogota's equity was not held by investors, but was the accumulated result of grants and retained earnings.[8] Finally, BRI's units have no equity attributed directly to them because they are a division of a larger bank.[9]

None of the institutions are as highly leveraged as commercial banks where international standards suggest equity of at least 8 percent of assets. The equity of BancoSol, which is increasing its leverage as it expands, represents 16 percent of its total assets, while the comparable figure for Grameen is 37 percent. The international commercial bank standard for capital adequacy is 8 percent.

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[8] Finansol has investor equity of US$4 million, 70 percent of which is held by Actuar Bogota.

[9] The capital adequacy of BRI itself, as well as other Indonesian state banks, has been the subject of financial sector reform efforts during the past several years. However, that subject does not bear directly on this monograph.

TABLE 3

SIMPLIFIED BALANCE SHEETS OF MAJOR MICROENTERPRISE FINANCE INSTITUTIONS
(million US$)

	Grameen Bank (December 1992)		BRI Units (September 1993)		BancoSol (December 1993)		Actuar Bogota (December 1993)	
	amount	percent of total	amount	percent of total	amount	percent of total	amount	percent of total
ASSETS								
Loan portfolio	113.4	64	824.0	38	24.5	71	7.5	60
Other financial assets								
•Deposits with Central Bank							0.1	1
•Deposits in financial institutions	33.4	19	1,238.7	58	2.7	8	0.1	1
•Cash and receivables					3.5	10	1.20	10
Fixed and other assets	29.7	17	89.6	4	3.7	11	3.7	29
TOTAL ASSETS	176.5	100	2,152.3	100	34.4	100	12.6	100
LIABILITI ES & EQUITY								
Loans	48.2	27					9.8	78
Deposits[a]	3.5	2						
•Interbank			71.5	3	12.1	35		
•Corporate					12.5	36		
Client savings[a]	30.7	17	1,937.5	90	3.1	9		
Other liabilities	28.7	16	143.3[b]	7	1.2	3	1.0	8
TOTAL LIABILITIES	111.0	63	2,152.3	100	28.9	84	10.8	86
Equity	65.5	37	n/a		5.4	16	1.8	14
TOTAL LIABILITIES & EQUITY	176.5	100	2,152.3	100	34.3	100	12.6	100

[a] For Grameen Bank, the majority of member savings and deposits are not part of the balance sheet.

n/a = not applicable

[b] Includes current earnings and a small amount of long-term designated capital.

II.C. Conclusion: The Underpinnings of Competence — Institutional Type and Access to Funds

The review of financial structure and institutional type offers a first look inside organizations to begin to distill the elements of competence in microenterprise finance. We have found multiple origins for successful microenterprise finance organizations, but also a common evolutionary trend toward becoming more formal financial institutions, driven by the need to access more plentiful and reliable sources of funds. These changes often require complex transformations of legal status and institutional type. Mature microenterprise finance organizations of large scale rely for most of their funding on deposits from the public (clients) and the local financial system and have developed strong equity bases. Use of international funding sources shows a downward trend over time for each institution, and institutions with the highest financial viability have lower reliance on international sources. They access the local system, at the least, by borrowing from commercial banks, and at the more sophisticated end, by participating in money and capital markets. Implicit in these achievements is strong, professional-level financial management capacity, as well as efficient operations, which merit the confidence of private sector funders and the public. We now turn, for the remainder of the monograph, to those operations.

CHAPTER III

THE SKELETON:
ORGANIZATIONAL STRUCTURE AND PRODUCTIVITY MEASURES

III.A. The Shape of Microenterprise Finance Systems

The organizational charts of large microenterprise finance organizations reveal a simple, characteristic pattern: a set of small retail outlets that do the front line work, linked by a superstructure that provides higher level services and oversight to the units (see Box 3).

This pattern is one of the striking commonalities among successful microenterprise finance institutions. It is derived from one of the most basic principles involved in providing financial services to the poor: that financial services for the poor must be located close to clients, whose ability to spend time and money obtaining banking services is limited. This principle necessitates a wide dispersal of outlets and at the same time limits the maximum size of each outlet according to the population of its effective geographic range.

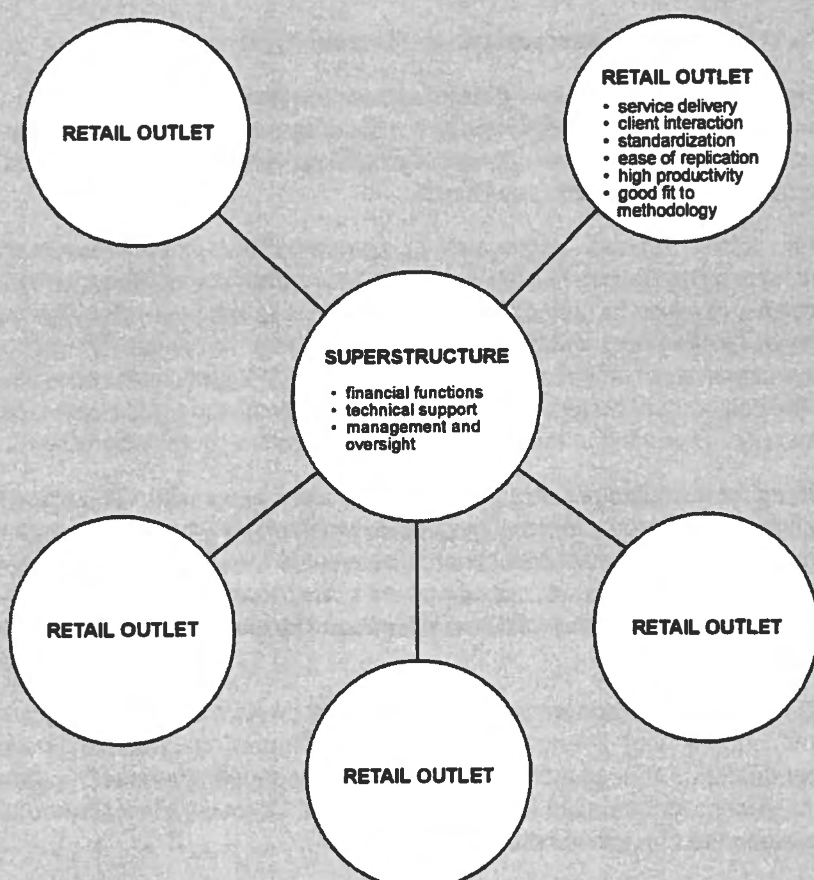
Strong retail outlets are also the key to successful expansion of outreach. Each of the four institutions under detailed review here grows by replicating retail outlets, with the new outlet bearing essentially the same shape as every other. To date, most growth has come from the replication of units rather than from unit growth, and this replication is facilitated by the use of a standardized retail outlet formula.

This characteristic pattern is further defined by the fact that individual units would not be very strong alone without the functions provided by the superstructure. These functions fall into three categories: financial functions, management and oversight, and technical support. There are some economies of scale in the provision of these services.

While the basic pattern illustrated in Box 3 appears throughout the field of microenterprise finance, there are several important variations which are related to different service delivery methodologies. In credit union systems, for example, each retail unit is a separate organization, and in BKK, each cluster of units belonging to the same sub-district is independent. However,

BOX 3

FUNCTIONS AT THE SUPERSTRUCTURE AND RETAIL OUTLET LEVELS



the well-functioning credit union systems and BKK have external superstructures such as national federations which provide many of the same functions that are provided internally in the institutions reviewed here. Village banking programs offer another variant in which each village bank, rather than the sponsoring organization's field staff, might be considered the retail outlet.

Although these variations involve some key differences, they have much in common with the basic model: the pattern of retail outlets linked by a superstructure; the need for high productivity and ease of replication at the retail level; and the need for a superstructure that provides financial, technical, and managerial functions. These elements can be considered the skeleton for successfulinsert box 3 microenterprise finance institutions with the potential to expand. The remainder of this chapter describes how Grameen Bank, BRI's unit system, BancoSol, Actuar Bogota, and others embody this model and how they refine it according to their own needs. In so doing, the chapter elaborates each of the concepts listed in Box 3, thus exploring the basic model in depth.

III.B. Retail Outlets and Service Delivery Methodologies

The basic building block of a successful microenterprise finance institution is the retail outlet, which is responsible for providing nearly all of the financial services. The local retail outlet is likely to be the only portion of the institution clients interact with directly, and its performance makes a major contribution to the public image of the institution.

Organizations that have been able to expand have developed a good fit between the shape of the retail outlets and the service delivery methodology. The outlets are the units of production of services and their structure and activities must be built around delivering high-quality services efficiently. Thus, differences in service delivery methodology are reflected in the structure and activities of the retail outlets. Profiles of average retail outlets for the four institutions are shown in Table 4.

Retail Outlet Structure. The 3,235 BRI units have small staffs (an average of five people) that operate as integrated teams. Each staff person performs a different function. The standard formula for a BRI unit begins with four people: unit manager, credit officer, teller, and bookkeeper. (See Appendix for organizational charts of retail units at various institutions.) If the level of activity is large enough at a unit, additional staff are added until the total reaches eleven, at which point the unit is split in two.[10] To operate in locations without sufficient demand for a separate unit, some units also operate service posts in neighboring towns, staffed by a teller and a bookkeeper, for carrying out cash transactions. These posts (numbering 635) are considered part of the parent unit. They are generally open less than the full week.

[10] See Chapter VI for a discussion of retail unit replication.

The structure of the BRI units reflects the strong emphasis given to savings services. While all members of the staff are involved in both credit and savings, the credit officers are mainly devoted to lending and the tellers are mainly devoted to savings. In the other three programs, loan officers far outnumber tellers (in two there is no separate teller function), but in BRI, the numbers are more nearly equal. The structure of the units also reflects BRI's philosophy that the units are mini-banks and have the potential to add new services as time goes on. Thus, the staff configuration is a scaled-down version of a formal sector bank branch. It is also clear from the BRI unit configuration that each member of the team must perform his or her function well if the unit is to perform well, and this fact pervades BRI's approach to performance monitoring, as discussed in Chapter IV. The differentiation of function also conforms to BRI's emphasis on the development of client identification with BRI as an institution more than identification with a particular staff member.

TABLE 4

ACTIVITIES OF TYPICAL RETAIL OUTLETS

	Grameen Bank Branch (June 1993)	**BRI Unit**[a] (October 1993)	**BancoSol** Branch (December 1993)	**Actuar Bogota** Branch (October 1993)
Number of staff	9	5	9	13
Outstanding portfolio[b]				
• number of loans	1,540	570[c]	2,580	2,880
• amount ($)	175,000	288,000	1,376,000	631,000
Savings and Deposits				
• number	not available	3,460	1,680[d]	not applicable
• amount ($)	166,000	649,000	196,000[d]	not applicable
Number of loans disbursed per month	128	42	454	412
Number of loans outstanding per outlet staff	180	115	269	226

[a] Based on general loans (i.e., excluding housing).

[b] Counts village posts as part of parent unit.

[c] Note that BRI units handle an average of 3,400 savings clients each.

[d] Based on reports from the pilot project in Villa Fatima branch only. Figures do not representan institution-wide average.

The retail units of BancoSol (23 branches as of April 1994), Actuar Bogota (10 branches), and Grameen Bank (1,030 branches) are quite similar to each other and reflect their relative focus on the lending program. The average size of the staff of Grameen Bank and BancoSol branches is the same (nine) although BancoSol has three large branches and several smaller branches with only four staff members. Actuar Bogota branches have an average of thirteen people. Most of the staff in all these outlets are loan officers. Grameen's structure is the simplest. Each branch consists of a branch manager and field workers. Larger branches often have an assistant branch manager. Branch managers and assistant branch managers oversee the field workers, handle all disbursements, prepare documentation of branch activities, and act as the focal point for communication between the branch and the superstructure. The field workers are responsible for nearly all the functions associated with their clients, including forming borrower groups, attending weekly center meetings (at which new loan applications are discussed and repayments collected), maintaining bookkeeping entries for all client transactions, preparing loan applications for approval, following up delinquent borrowers, and working toward social development goals. In some respects, these field workers, rather than the branches, are the fundamental units of Grameen Bank operations.

Grameen's simple branch structure probably derived primarily from the need to bring services extremely close to rural clients located in networks of tiny villages, most of whom lack access to transportation other than by foot. It is more efficient for both Grameen and clients for field workers to circulate to those villages (usually by bicycle) than for clients to come to the branches, and thus, field workers need to be able to carry out as many functions as possible in the village. In general, clients visit Grameen branches only for disbursements. All other functions are carried out on site at center meetings. This structure also implies an emphasis on the personal relationship between clients and field worker, in addition to strong client identification with Grameen Bank.

BancoSol's agency structure lies between BRI's and Grameen's. While emphasizing field workers (called *asesores*, or credit counselors) as the backbone of the retail outlet, BancoSol separates the money-handling function by adding one or two tellers to the branch. Operating in densely populated urban areas, BancoSol's branches are located where clients can easily access them. The use of cashiers to collect and disburse was already built into PRODEM's methodology, and BancoSol's need to meet bank supervisory standards for cash management has further formalized this requirement. BancoSol's methodology strongly emphasizes the personal relationship between each client and the field worker and depends on that relationship as an important repayment motivator.

Even though Actuar Bogota outlets are significantly larger than those of the other institutions — averaging 13 staff, most of whom are *asesores* — they otherwise resemble those of BancoSol and Grameen Bank, with several points of note. First, Actuar Bogota outlets do not handle money and have no cashier. Those functions are carried out by banks to whom Actuar Bogota pays fees. Second, because of Actuar Bogota's strong emphasis on training, each branch includes one or two permanent trainers, who provide training and organize training events using outside instructors.

Third, while Actuar Bogota in its current shape conforms to the basic microenterprise finance model, its vision for the future involves a significant departure from that model. Actuar Bogota intends eventually to provide a full range of services to microentrepreneurs, including credit, training, savings, insurance, wholesale services, and even housing, health care, and recreation. As Actuar Bogota develops these additional services, the retail outlets will clearly be affected. While it is too early to predict how they will change, Actuar currently envisions that it will maintain the retail outlets as the primary point of client contact, and the locus of much of the service delivery. However, Actuar's subsidiaries will provide many of the services separately. Such is already the case with Actuar Bogota's Basic Service Center, which is run by an independent staff. Actuar branch staff publicize the services of the center.

ADEMI maintains two different types of retail units. Those located in the capital city, Santo Domingo, resemble Actuar's in that both are located in dense urban environments, and thus tend to be large (12 to 15 loan officers). Like Actuar, ADEMI also relies on banks to handle all cash transactions, and thus has no cashiers in branches. ADEMI's loan officers focus their efforts on client assessment, follow-up, and general business advice. Administrative assistants and the central legal department play a significant role in assisting loan officers with delinquent clients. At ADEMI's interior branches located throughout the country, loan officers are organized into large groups overseen by a regional manager. Within these groups, teams of one to three staff members maintain posts, often using offices of a local community organization. The members of these small posts function more like a team than do the branches in the capital, where there is greater differentiation of function. Furthermore, the geographic dispersion of the clients in these regions obliges the loan officers there, like the Grameen field workers, to circulate to clients, rather than for clients to travel to the branch office. A significant difference is that ADEMI *asesores* can travel large distances by motor vehicle, while most Grameen field workers travel by foot or bicycle. ADEMI can thus serve a much larger geographical radius with a sub-branch than Grameen can serve with its village unit.

The Group Credit Company (GCC) in South Africa recently created teams, based loosely on the BRI units, including a unit head, two to three field officers, an administrative officer, and a client service clerk. These teams are kept small to allow for efficiency, replicability, and easy on-site training. In contrast to many other organizations, but much like ADEMI, the portfolio of seriously delinquent clients is transferred to a distinct collections department operated out of the head office.

Standardization. Retail outlets at each of these institutions are highly standardized. The functions of each staff member are so clearly defined that staff transferred from one unit to another are quickly able to carry on effectively. Daily and weekly schedules of activities are also made routine. For example, at PRODEM, Monday was repayment day, Tuesday was disbursement day, and the remainder of the week was devoted to client visits. BancoSol has changed to a daily rather than a weekly schedule. At Grameen Bank, loan officers devote mornings to attending center meetings, midday to recording transactions, and afternoons to disbursements. ADEMI *asesores* normally spend the mornings in the branch office reviewing repayment records and assessing applications, while the afternoons are used to visit clients. Actuar Bogota's *asesores* develop a careful schedule for each month to allow for monthly visits to each client. Similarly, the Small Enterprise Foundation (SEF) operates on a fortnightly routine; the first Monday is reserved for administrative affairs at the head office, while the other eleven work days are used for regular center meetings. This level of standardization is essential for the ability of the institution to expand quickly and to monitor performance. Such routines are also easy for clients to understand because they match local work habits and schedules.

The level of standardization displayed here may appear to some to be incompatible with local initiative or client participation. However, intensive interaction at a local level is woven into each of the methodologies. All the programs depend on field workers who know their clients and the local scene very well, and the group lending programs all have some element of client participation in day-to-day activities. Moreover, as will be discussed in Chapter IV, most of the institutions make an effort to listen to field staff, in a search for better procedures. In addition, as mentioned earlier, retail units must be close to the clients, not only in the physical sense, but also in terms of becoming part of the local community. The smallest units often rent or borrow space in government buildings or in the offices of other organizations. ADEMI often uses space donated by a local Chamber of Commerce or another community group. Normally, a unit can then position itself near the local center of economic activity, close to the market, or along a trading route. Such a location often affords the team access to community leaders and helps it to integrate into the local community.

That said, the requirements of managing scale efficiently leave little room for variation in unit activities if they involve departures from the basic tasks of providing savings and credit services according to an organization-wide methodology. There is some room for additional, non-core activities that are important to a locality, as evident from Grameen Bank. Grameen directs loan officers to take the initiative to reduce rural poverty in any way they can, and this leads to a proliferation of small local activities and experiments. For example one branch, or a group of branches, might begin promoting beekeeping. Grameen's client centers are another vehicle for local initiative because the centers often decide to make collective investments or carry out joint activities, such as starting informal center schools. However, even at Grameen, such activities do not detract from the core business of providing credit, and each Grameen branch carries out its credit operations the same way. A general conclusion is that local variation beyond a certain tolerance is not compatible with scale.

III.C. Productivity Levels at Retail Outlets

Given the expense of making very small loans, it is essential for the financial viability of the lenders that retail outlets be highly productive. Each of these institutions continually reviews the operations of the retail units to ensure that all are performing well and to identify ways to increase efficiency.

Because of the differences in setting and methodology, measurements of productivity across institutions are not precisely comparable, but they do illustrate important principles. As shown in Table 4, the active portfolio (volume of loans outstanding) at typical retail outlets varies over a wide range, with the highest (BancoSol at US$1.4 million) being almost eight times that of the lowest (Grameen Bank at US$175,000). Much of this difference can be attributed to differences in loan size, since the average loan at Grameen is roughly US$115, versus US$534 for BancoSol. Number of clients per outlet varies over a narrower range, from 570 at BRI to 2,880 at Actuar Bogota (highest is five times lowest). However, some of this variation is caused by the staff size of the outlets, with BRI outlets just over half the size of Grameen and BancoSol outlets, and Actuar outlets still larger.

The most directly comparable indicator of branch productivity is the number of loans outstanding per outlet staff (Table 5). The similarity of these numbers is more striking than the difference, with the highest number (BancoSol, at 269 loans per outlet staff) being only 1.5 times the lowest (Grameen Bank, at 180 loans per outlet staff). As each of these institutions can be considered highly competent, this figure gives one of the important ranges in the field of microenterprise finance: at present, well-performing retail units can handle from roughly 180 to 270 active borrowers per outlet staff member.[11] A survey of African credit unions revealed a somewhat lower range of productivity, figures ranging from 74 clients per staff in Cameroon to 158 in Rwanda (Yaron and Gurgand, 1993), while ADEMI granted an average of 108 loans per average outlet staff in 1993.

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11 These figures are based on total retail outlet staff rather than number of loan officers or field workers, to emphasize that the retail outlet as a whole, not individual workers, is the relevant unit of service production, and to use figures that allow greater cross-institution comparison because institutions divide tasks differently.

TABLE 5

STAFF PRODUCTIVITY MEASURES

	Grameen Bank (June 1993)	BRI Units (December 1993)	BancoSol (December 1993)	Actuar Bogota (October 1993)
Number of clients				
• per total staff	152	104	171	169
• per outlet staff	180	115	281	226
• per superstructure staff (regional plus head)	982	1,163	442	670
• per head office staff only	3,813	25,135	1,326	670
Active portfolio (US$)				
• per total staff	$17,000	$46,000	$91,900	$40,000
• per outlet staff	$20,000	$51,000	$150,000	$53,000
• per superstructure staff	$112,000	$582,000	$236,000	$146,400
• per head office staff only	$433,000	$11,149,000	$708,000	$146,400

Many of the remaining differences in levels of productivity can be attributed to methodology and setting. BRI, for example, has a greater emphasis on collection of savings than the other institutions. Much of a unit's staff time is taken up by providing services to the 3,400 savings clients (692 per unit staff member) it averages. Allowing that borrowers also hold a savings account, BRI unit staff are likely to handle, on average, close to 580 clients each, a larger total number of clients than at any of the other institutions. Moreover, BRI does a slightly more elaborate loan appraisal, especially for larger loans, and makes loans to individuals rather than groups. These aspects of BRI's methodology tend to limit the number of loans a unit can handle.

The level of productivity of BancoSol is quite impressive, especially given BancoSol's youth and the fact that BancoSol's three-month loan terms require frequent renegotiation of loan contracts. BancoSol staff carry very large caseloads, particularly in comparison with Grameen Bank, for several reasons. BancoSol's clients are located in very dense urban areas, so that most loan officers can visit their clients with little time spent in transport (the main cost of transport being staff time, not travel expense), and BancoSol repayments are weekly and monthly, compared to only weekly repayments at Grameen Bank, reducing somewhat the volume of repayment transactions that must be managed. Time spent per transaction quickly adds up, and Grameen has managed to develop very effective ways of minimizing that time, e.g., devolving some of that responsibility to the groups and centers (which might not be possible if Grameen used a teller system), but still faces a very high volume of transactions. Actuar's productivity closely parallels that of BancoSol, as would be expected, given that they use closely related solidarity group methodologies and work in similar urban environments.

For each of these institutions, the ability to reach more people and to survive financially depends on maintaining the high levels of productivity they now have and on developing practical innovations to increase that productivity.

III.D. The Superstructure

As efficient as the retail outlets may be, their survival depends on the existence of a competent superstructure which performs important functions that would be difficult or impossible for units to provide for themselves. The superstructure for each institution consists of the central office, with the addition, for BancoSol, of the regional offices, and for the two Asian giants, of both regional and area offices. The regional function at Actuar consists at present of three staff based in the central office.

Functions. Central functions fall into three broad categories: management, technical support, and finance. First, management functions include a number of essential routine operations — accounting and budgeting, systems development and operation, staff recruitment, financial control, asset and liability management, administration (e.g., procurement and oversight of premises) — as well as the higher-level managerial functions of policy setting, maintaining corporate culture, and external relations. Supervision of operational performance is a crucial management task. Second, technical support functions include staff development, marketing, and various types of research and development activities.

Third, financial functions involve movement of funds to support the delivery of financial services. For BancoSol, Grameen Bank, and Actuar Bogota, the main financial function of the superstructure is raising funds from external sources, while for the BRI units, the superstructure provides a way to invest surplus funds. In all cases, the superstructure helps manage liquidity and diversify risk by linking the units financially. Thus, losses in one or more units can be balanced by the success of other units. Credit union systems in Benin, Rwanda, Cameroon, and Togo link branches to central finance facilities managed by national federations. The national superstructure allows for a transfer of funds from areas with excess savings to those with excess demand for loans. (Yaron and Gurgand, 1993)

Many of the functions of the superstructure can be seen as services consumed by the retail outlets. The superstructure provides many of the essentials that retail units need to do business — from the initial setup of premises, computer systems, trained staff, and technical guidance to the daily requirements of supplies, management information, and in some cases funds. At BancoSol the center strives to see itself as service-oriented, with the units as its customers, and this effort is thought to improve the performance of the service functions.

However, the center also unavoidably plays a controlling role. It sets policy in order to achieve the organization's objectives. It must monitor how well the units are performing along several dimensions — achievement of output targets, control of costs, maintenance of portfolio quality, and protection against fraud — and it must take action when performance falls below standards. The two postures of the center, service and control, do not always fit well with each other, and organizations must make clear efforts to ensure that control does not become the dominant theme in relations between the units and the center. They must also ensure that control functions are informed by the voices of the units, as Chapter IV will discuss.

Superstructure Productivity. Just as retail units must be productive (discussed above), so must superstructure units. While productivity at the superstructure level is a somewhat less obvious concept, one way of viewing it is to examine the ratio of superstructure employees to retail unit employees to see whether an organization is top-heavy (Table 6). The number of clients per superstructure staff, as shown in Table 5, is also relevant. On these measures, BRI is the leanest organization, with less than 10 percent of its unit system employees outside the units themselves. Grameen Bank also has a relatively lean superstructure, with only 15 percent of its staff outside the branches, followed by Actuar with 25 percent.[12] BancoSol shows the largest superstructure, with a comparable figure of 39 percent.[13] The figures imply that, as organizations mature and expand, branches may focus more on service delivery, and that economies of scale may be increasingly available in the provision of central functions. Thus, one would expect that as Actuar and BancoSol grow, they will add unit staff faster than they add center staff.

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[12] The Actuar figure understates the percentage of employees at the center because it does not include employees of Finansol, most of whom are devoted to Actuar's current operations.

[13] These figures are not fully comparable because organizations divide some of the labor differently. For example, Actuar considers its trainers as part of the branch staff, while BancoSol maintains its trainers at headquarters.

TABLE 6

DISTRIBUTION OF EMPLOYEES BY OFFICE LEVEL

	Grameen Bank (November 1993) number	%	BRI Units (December 1993) number	%	BancoSol (January 1994) number	%	Actuar Bogota[a] (February 1994) number	%
Head office	435	4	74	0.4	35	13	56	25
Regional offices, of which:	1,222	11	1,525	8	70	26	n/a	n/a
• Regional	591	(5)	400	(2)				
• Area[b]	631	(6)	1,125	(6)				
Retail outlets	9,099	85	16,135	91	165	61	166	75
Total[c]	10,756	100	17,734	100	270	100	222	100

[a] Excludes staff of Actuar's Basic Service Center and Finansol. n/a = not applicable

[b] For BRI, branch offices.

[c] Percentages do not add to 100 due to rounding.

In interpreting the BRI figure, it should be recalled that BRI's unit system differs from the other institutions because it is part of a larger organization, and the relationship of the unit system to the BRI's mainstream operations carries different implications. The unit system as a whole is defined as a strategic business unit (known by the acronym BUD) of the BRI. There are BUD staff at each BRI level — central, regional, and area (branch). The branches of BRI are the main retail outlets for BRI's larger scale customers. Thus, unlike the area offices of Grameen, BRI branches have a life of their own beyond providing oversight and support to the units. This at times causes conflicts of interest between branches and units, such as competition for loan funds, or even, at the upper end of unit operations, competition for borrowers. The position of BRI's unit system also means that some superstructure functions are performed not by the BUD system, but by BRI's mainstream offices, as direct charges. Supervision (at branch, regional, and headquarters levels), leasing costs, and expenses of the units' five regional training centers are charged against the units' overall operation, although they are not allocated to individual units. A major role of the BUD superstructure is to identify the needs of the units and demand services from the main BRI superstructure. This relationship greatly simplifies unit system operations but occasionally causes problems. For example, staff recruitment is done by the mainstream BRI regional offices, and the unit system has had difficulty persuading the regions to fill unit positions, for reasons internal to the mainstream part of BRI.

Despite the difficulty of measuring the productivity of an individual organization's superstructure, the experience of major microenterprise finance institutions suggests that the achievement of economies in the provision of central functions could be a significant means of increasing overall productivity for the organization as a whole.

Decentralization. As organizations grow, many of the superstructure functions can be decentralized to regional and area offices. These intermediate offices take on many of the day-to-day superstructure functions. By decentralizing, the organizations can provide services to the units more responsively, monitor unit performance more closely, and avoid bottlenecks that develop when the center is overstretched. BRI, as the largest organization, has gone farthest in decentralizing, with 95 percent of its superstructure employees in regions and branches, rather than headquarters. Grameen's ratio is nearly three regional/area employees to every one head office employee, while BancoSol's is about two to one.

Actuar Bogota has not decentralized to any significant degree. Its only explicit regional function is embodied by three staff members each supervising the performance of several unit offices. Actuar's geographic concentration in one city and its vision of providing a variety of different services, currently makes the creation of regional offices less relevant. Similarly, ADEMI has only one staff person with a regional function. However, as both organizations continue to expand, they may further decentralize many superstructure functions.

At Grameen Bank, the philosophy of decentralization is becoming increasingly explicit. Some observers and staff describe a vision in which the 15 Grameen regions become semi-autonomous regional banks. The very formulation of this concept suggests that Grameen is reaching a stage in which day-to-day operations do not require constant top management involvement. It should be noted, however, that while Grameen is clearly decentralizing functions and, to some extent, authority, decentralization takes place within limits. Each institution has a hierarchy of actions that can and cannot easily be decentralized, and this hierarchy is applicable across institutions. For example, staff placement at Grameen and BRI has become a regional function, but staff training, with its key roles of inculcating corporate culture and lending methodologies, remains at the center. Plans for opening new branches and expanding existing ones are formulated at area and regional levels, but these are subject to final approval at the top. If the regional bank vision were ever to be realized at Grameen, the center might retain only these top management functions: policy, corporate culture maintenance, external liaison, and technical support (e.g., research and development). These are the functions that maintain the unity of the organization. Without them, there would be several increasingly distinct institutions.

Loan Approval Authority. Most microenterprise finance programs feature highly decentralized loan approval processes as part of the basic structure of retail operations. The highlighted institutions allow experienced field workers to make general recommendations about their clients, subject to final approval by the retail unit manager. Unless the amount requested is unusually high, the approval is usually granted, and the real responsibility lies with the field worker. In some cases, such as Actuar, final approval is given by a credit committee that meets daily and is made up of the unit manager and one or more field workers.

At Grameen, an application must pass through three levels, the center, the branch, and the area office. After the field workers write recommendations, the branch manager compiles a group of proposals into a single package, which is then sent to the area office. There, a program officer reviews the proposals, and the area manager gives final authorization. While this may be the least decentralized of the programs, Grameen field workers still retain much of the responsibility in fact, if not formally.

The decentralization of loan authority is essential to the credit methodology of each institution, as it decreases client waiting time for loan approvals, as well as decreasing staff time, and enhances accountability at the appropriate level, i.e., among staff closest to clients. Thus, it is an important aspect of the methodology of serving low-income clients profitably.

III.E. Productivity, Operating Costs, and Financial Viability

This chapter has so far considered organizational productivity without regard for cost. However, the effect of productivity on institutional viability cannot be known until costs are factored in.

Operating Costs and Productivity. One way to place operating costs into comparative perspective is to view them as percentages of the loan portfolios they maintain (see Table 7). This measure is also highly relevant for each institution: it determines the *spread* over financing costs the institutions must charge in order to break even financially. Most microenterprise finance institutions are continually engaged in an effort to increase outreach while keeping the spread at a level that allows pricing for client acceptance and financial viability.

However, even at the most efficient microenterprise finance institutions such spreads are high because loan sizes are so small. Even the best microenterprise methodology, operating in the most favorable circumstances, cannot fully avoid the arithmetic of retail banking: unit costs cannot drop as fast or as far as loan size.

Practitioners in the field of microenterprise finance have sought to determine what spread could be considered an "industry standard" — a level which, if achieved, would show that an institution was operating efficiently. Such a figure has been elusive, however, as the institutions profiled here show. Operating costs for lending range from 12 to 25 percent of portfolio. A closer look reveals that spreads are determined by three major factors: productivity, salaries, and loan sizes. Thus, one would not expect all spreads to be alike, as institutions face different conditions and make different choices. We now examine each of these factors in turn, beginning with productivity.[14]

TABLE 7

NON-FINANCIAL COSTS AS PERCENTAGE OF AVERAGE ANNUAL LOAN PORTFOLIO

	Grameen Bank (1992)	BRI Units[a] (1993)	BancoSol (1993)	Actuar Bogota (1989)	BKK (1989)	ADEMI (1993)
Salary costs	11.2	5.0	15.2	16.9	7.0	9.0
Other administrative costs	5.7	2.1	10.4	4.5	7.3	11.4
Loan loss reserve	n/a	4.6	1.6	3.6	n/a	n/a
Total	16.8	11.7	27.2	24.9	14.3	20.5
Salaries as percentage of non-financial costs	66	44	56	68	49	44

SOURCES: Actuar Bogota; ADEMI; BRI; BancoSol; Khandker et al., 1993; Yaron, 1992; Hook and Patten memo, 1994.

[a] Expenses allocated to lending operation only, as percentage of average annual loan portfolio. Excludes cost of savings mobilization, for comparative purposes. n/a = not available.

Operating Costs and Productivity. At first glance, spread may seem to be largely a function of efficiency or productivity, and productivity may seem to be a matter of number of clients per staff. However, the preceding section showed that BancoSol and Actuar Bogota, which have high levels of operating costs, also have very high ratios of clients to staff. These ratios are higher than those of the Asian programs even when superstructure staff are included.

[14] This section looks only at the costs of lending. Thus, for BRI, it omits a major portion of activity, namely, deposit mobilization, which has its own operating cost dynamic. Adjustments have been made to the BRI units' total costs to separate out the costs of deposit mobilization.

Thus, although high productivity is essential for microenterprise finance programs, it alone does not guarantee low operating costs and does not explain differences in costs among top-performing institutions.

Operating Costs and Salaries. Salaries and related personnel costs explain more of those differences. Salaries are singled out because they are the largest component of operating costs, constituting from 44 percent of non-financial costs in the BRI unit system and ADEMI to 68 percent at Actuar Bogota. All other administrative costs — premises, transport, computer systems, supplies, and contractors—total significantly less than salaries, and the third non-interest cost category, loan loss provisions, while important, is also smaller.

Among the institutions profiled here, Grameen Bank operates in the country with by far the lowest per capita gross national product (GNP) (see Table 8), and formal sector jobs of the type that Grameen Bank offers are not plentiful. The low salaries Grameen Bank can afford to pay (which at one-ninth of those at Actuar, for example, are low by international standards, but, at three times the per capita GNP, are high by local standards) are crucial for reducing per loan costs to a level that will allow Grameen to offer very small loans. Salaries are significantly higher at BRI, as throughout Indonesia, but they are still well below salaries in the South American programs and alternate employment is again in short supply. Thus, BRI also enjoys relatively advantageous conditions.

TABLE 8

WAGES AND NATIONAL INCOME LEVELS

(US$)

	Bangladesh (Grameen Bank)	Indonesia (BRI Units)	Bolivia (BancoSol)	Colombia (Actuar Bogota)	Dominican Republic (ADEMI)
Annual GNP per capita (1990)	$210	$560	$630	$1,260	$820
Average annual salary at institution (1993)	$687	$3,506	$5,472	$6,023	$5,088
Ratio of salary at institution to GNP	3.1	6.2	8.8	4.8	6.2

SOURCES: World Bank, World Tables, 1993; Economist Intelligence Unit, Country Profiles, 1992; profiled institutions.

In Bolivia and especially Colombia, prevailing wages are higher. BancoSol pays salaries nearly nine times higher than GNP, while Grameen pays only a multiple of three times GNP. The need for BancoSol to pay such high salaries may result from the structure of the labor market in Bolivia, particularly at the upper end from which BancoSol recruits. Latin American countries are known for greater ranges in wage levels than are most Asian countries, and the ACCION-sponsored institutions have chosen to recruit well-credentialed staff.

Faced with a similar wage/credential situation, some programs in South Africa have chosen to recruit field staff with fewer qualifications, at lower salaries. Similarly, many credit unions are run by staff volunteers, frequently with significant savings on salaries and benefits. Village banking methodologies may also be able to reduce relative salary costs by relying on the efforts of members. However, the use of unpaid and relatively uneducated staff poses its own set of challenges, and each institution must make choices in the context of its own needs and opportunities.

The high volume of salary expenses in total operating costs suggests that microenterprise finance institutions are highly vulnerable to changes in wage rates. This vulnerability is illustrated by Grameen Bank's experience in 1991, when the Bangladesh government increased civil service salaries by 50 percent. Grameen had already pegged its salary level to the civil service pay scale, and it had also been affected by the labor agitation sweeping the country that year. Accordingly, Grameen had little choice (if it wanted to maintain employee goodwill) but to increase salaries by a like amount. This change necessitated an increase in interest rates from 16 to 20 percent for general loans and from 6 to 8 percent for housing loans. Abrupt changes in salary structures at any of these institutions will also require changes in interest rates.

Loan Sizes and Operating Costs. If institutions have limited control over salary levels, they can more easily turn to the third key variable in determining operating spread — loan size. It is far easier to reduce costs as a percentage of average portfolio by increasing loan size than by cutting salary costs or increasing productivity. Thus, as programs strive for financial viability, the temptation is great for average loan size to drift upward. Each of the institutions reviewed here has shown some such upward movement in loan size in recent years. The movement was particularly significant at BancoSol, where the average size of loans disbursed doubled from January to December 1993. Even Grameen Bank has begun to increase loan size indirectly by offering seasonal loans to existing borrowers on top of the regular loans those borrowers already hold, thus quickly increasing its portfolio size without adding new clients. Grameen's larger housing loans have also been shown to be an important element in branch productivity. ADEMI, whose average outstanding loan in 1986 was about US$300 now averages between US$600 and US$700. This change is not the result of drift, however, but a reflection of ADEMI's increasing interest in serving small enterprises and in encouraging its microenterprise borrowers to make the transition from micro to small.

While larger loan sizes appear to offer a quick route to higher productivity and lower spreads, they must be carefully considered in light of their effect on client outreach, organizational mission, and risk. Increased loan sizes can be beneficial if they reflect: (1) the release of previous funding constraints (as occurred when PRODEM became BancoSol), (2) growth of the enterprises of existing clients (as is true for many clients at each institution), and (3) a gradual expansion of the range of clients served to increase financial viability.

Problems arise, however, if loan size increases reflect either over-lending to clients (supply-led credit) or a shift away from the original clientele toward a higher-income stratum. These latter reasons for loan size increases can herald a significant change in organizational mission, which should be made as an explicit policy rather than as the result of pressure on spreads. Such changes can also increase default risk. For example, in 1991, the BRI unit system greatly increased its loan limits, resulting in large loans being made to many new customers. These loans had higher default rates, both because the larger customers had not been tested through traditional repeat lending and because the units simply were not as good at making such loans as they were at smaller loans. The lending limits have subsequently been reduced. BRI learned that the units work best when they pursue their particular niche of the market. At BancoSol, loan sizes have gone up recently without explicit directives, and management has begun to analyze whether the increase is a result of the release of funding constraints and client growth or of a shift in client outreach patterns. Once it understands the reasons for the changes in loan size, BancoSol can adopt policies to respond.

In the review of the three main determinants of operating costs, a few important points have emerged:

- First, even among top-performing institutions, the range of operating cost spreads is high. However, an upper bound figure has emerged, at approximately 25 percent. Institutions performing above this level should strive to reach it.
- Second, while high productivity is essential, efficiency alone will not guarantee a low spread.
- Third, microenterprise finance institutions are highly exposed to the prevailing wages in the countries in which they operate. This observation has important implications for programs in countries with relatively high professional salaries, such as in Latin America. At least for programs based on solidarity group lending, high salary costs will require programs to charge high interest rates and/or make relatively large loans. One should not expect to see in Latin America the relatively low interest rates and small loan sizes that are possible in some Asian settings. Other methodologies (credit unions and village banking) may avoid some of these costs by using unpaid labor.
- Finally, increasing loan size will be such an attractive strategy for reducing spreads that policy setters for these institutions should

carefully monitor loan sizes to ensure that changes are made deliberately, with full consideration of the effect of such changes on organizational mission.

III.F. Conclusion

This chapter has drawn the organizational outlines of successful microenterprise finance organizations using the characteristic pattern of small, standardized, and replicable retail outlets delivering services, which are connected by a superstructure. It has begun to generate a picture of productivity and cost levels at these institutions.

Among the observations on the retail level to emerge from the review are:

- The closeness of the fit between service delivery methodology and the shape of the retail outlets.
- Standardization of both staff positions and daily or weekly routines, with relatively little room for local variation

These features set parameters within which the retail units must operate.

These important observations about the superstructure emerge:

- Recognition that it acts simultaneously as a service provider to the units and as a control mechanism
- The potential for many of the routine functions of the center to be decentralized as the organization grows

This chapter has also illustrated the high productivity among successful microenterprise finance organizations, suggesting that the carrying capacity of retail units ranges from about 115 to 280 borrowing clients per unit staff (with potential for the volume of savings clients to be much higher), depending on population density and methodology. This high productivity does not leave the institutions comfortable, however, as they must contend with high administrative costs, which, relative to the loan portfolio, range from 12 to 25 percent. It is crucial to note that the organizations with the higher percentage costs are equally or more productive than those with lower costs. However, they face high salary costs determined by the local setting. These costs illustrate that organizations in countries with higher prevailing formal sector salaries will be hard pressed to make very small loans. On the other hand, organizations should resist the temptation to let loan size drift upward to relieve cost pressure. That pressure should instead drive them to seek still higher levels of staff productivity.

CHAPTER IV

USING INFORMATION TO ENHANCE PERFORMANCE

Information can be viewed as the lifeblood of a financial institution. Just as oxygen-rich blood nourishes all the cells and systems of an organism, a regular stream of high-quality information enables staff, retail units, and the superstructure to perform well and make good decisions. "Oxygen-rich" information is timely, accurate, and relevant to the recipient. The organizations described here are all very competent in their production and use of information. If they were not, none would have survived and grown to their current scale.

This chapter reviews the use of information at these institutions. However, rather than describing the information systems first, this chapter zeroes in on the few most important pieces of information institutions use — key indicators — and discusses how those indicators contribute to one of the recurring themes of the monograph, the drive for high productivity. The analysis of key indicators provided here ties together the productivity issues raised in the earlier discussion of organizational structure, function, and costs (Chapter III), and will set the stage for a discussion of staff motivation in the next chapter. This chapter will then move to the topic of information systems in general.

IV.A. Key Performance Indicators and the Profit-Center Concept

Effective microenterprise finance institutions focus their attention clearly and consistently on indicators that measure productivity. It is crucial to the success of microenterprise finance organizations to base staff motivation on these variables. Organizations where field staff are not thinking about those indicators every day, or where the choice of key indicators is inappropriate, are probably organizations in trouble. Organizations use key indicators in a variety of ways:

- To determine whether targets are being met
- To evaluate staff performance
- As "fever thermometers" to determine whether all or part of the organization is healthy and to give warning of problems

- To tell whether changes being tested are working well
- To help plan future activities and set targets
- To identify areas needing management attention

For these functions to be well served, indicators must closely reflect the goals of the organization and be simple enough for the whole staff to understand. Thus, while each institution collects a wide range of indicators, they differ in their choice of the few focal points for evaluating performance.

For newer organizations, particularly NGOs undergoing transition, rapid growth and high portfolio quality are crucial for survival. Thus, at Actuar and BancoSol, the initial focus has been on two main indicators—the total number of loans and the arrears rate—with a third indicator, the number of new loans, also playing an important role. While a significant number of additional factors are monitored, such as percent of clients who are women and numbers of clients attending training programs, staff throughout Actuar and BancoSol still concentrate most of their attention on these two to three main measures and examine them regularly at the superstructure, unit, and field worker levels. Focusing on numbers of loans rather than loan volume avoids pressure to make larger loans, and thereby reduces the risks of loan loss and moving away from the originally targeted clientele. For the Small Enterprise Foundation in South Africa, while the focus on these two indicators remains important, monitoring of attendance at center meetings has been found to be the most reliable indicator of client performance.

More mature organizations, particularly those with a savings component, can re-orient the way they evaluate performance to focus on self-sustainability and profit making. An emerging trend in microenterprise finance is to treat individual units as profit centers that must maintain their own viability. Thus while BRI monitors numbers of loans and savings accounts, as well as portfolio quality, the preeminent indicator for evaluation is unit profits. BRI is widely recognized as having pioneered this method, and the profit-center concept has been critical to its success, as described below.

The Profit-Center Concept. Every BRI unit operates as a mini-financial institution, in that it raises funds and invests them, while charging a spread to cover its operating costs. Funds are raised from savings deposits and invested either in KUPEDES loans or in deposits with the main BRI branches (on which the unit earns interest income). A unit which is short of funds to meet loan demand may borrow from its supervising branch at a cost set by BRI policy makers and known as the transfer price. Units are also responsible for the operating costs they incur, in the form of salaries, other direct administrative costs, and costs paid internally to BRI for services to the units. Each month, units prepare a profit and loss statement and a balance sheet, showing a bottom line in the form of unit profits.

The focus on profits improves upon a focus on loan volume for two reasons. First, by incorporating costs into the equation, it creates incentives not just for high volume but for high productivity. This places responsibility on units to achieve maximum results for the least cost. When financial viability is the overall institutional concern, productivity becomes more important than volume alone. Moreover, by making each unit a profit center, BRI has decentralized concern for cost control and productivity. Such decentralization delegates responsibility to all levels and allows some measure of flexibility in attaining institutional goals.

Second, the profit-center concept allows for a balance between savings and lending activity. Organizations involved in both savings and lending need a guide to help determine how much effort to devote to each activity. This becomes especially important as more staff perform both savings and credit-related tasks (though clearly there is a significant difference in emphasis between tellers and credit officers.) Focusing on profits, rather than separate credit and savings volumes, allows units to work in a way that results in the best mix of financial services, based on the needs of the local clientele.

Moreover, BRI retains the ability to adjust the relative emphasis of the system as a whole on credit versus savings through the mechanism of transfer pricing. The transfer price is the rate BRI branches pay to the units for deposits. It therefore determines the profitability to the units of generating savings. Because the KUPEDES lending rate is fixed, adjusting the transfer price can change the relative emphasis units give to savings and credit. If the transfer price is set very low, i.e., only slightly above the rate paid to depositors, units receive so little spread on savings collections that they must earn all their income from lending. In 1991, when the Indonesian financial system experienced a liquidity squeeze, BRI set the transfer price very high, so that the rate received for placing funds internally neared the rate received on loans. This encouraged the units to generate savings and turn them over to the main BRI branches, where the return would be higher than if they put them into loans (and thus incurred the costs associated with lending). Accordingly, the growth rate of the lending program halted at that time. The transfer price for units to borrow from the main branches can be similarly manipulated. At present, the transfer price is set low to provide maximum incentives to lend, and lending levels are beginning to increase again.

While the profit-center focus neatly combines many of the most important measures of success, it does not cover two crucial areas adequately: portfolio quality and loan size. Additional attention must be given to these indicators to ensure long-run sustainability. While unit profitability does encompass portfolio quality, as carrying bad loans reduces income and erodes the balance sheet, effective arrears management requires attention from the moment the arrears appear, well before the potential damage to profits is felt.

Similarly, supplemental attention to loan size may be warranted to forestall tendencies for units to take the easy route to higher profits by making larger loans.

The profit-center concept is increasingly being applied in other institutions, particularly at Grameen Bank. Grameen branches receive their lending funds by using the mandatory savings deposits they hold (on which they pay 8.5 percent) as well as by borrowing from the superstructure at 12 percent for general loans, less for housing loans.[15] This price is set by Grameen to reflect a market-relevant cost of funds (though it is higher than Grameen's actual cost of funds) to cover headquarters expenses and to encourage branches to control costs and generate savings. It should be noted that profitability of retail units in any institution is not the same as overall system profitability because transfer prices are set expressly to give policy signals and do not necessarily reflect true costs directly. For example, at Grameen, a 2 percent transfer price for housing loans affords branches a spread of 6 percent, thereby applying appropriate incentives for efficiency by branches that must strive to keep their costs within that spread. However, because Grameen uses subsidized funds for housing loans, the loans do not contribute to Grameen's overall financial self-sufficiency. This is an example of the way Grameen manages to combine the continued use of selected subsidies with a strong drive for efficiency.

BancoSol is gradually incorporating the profit center approach. It currently operates its four regional offices as profit centers and plans to convert its retail units to profit centers when it introduces its savings program bankwide. Actuar also plans to move toward the profit-center approach. At present, it does attempt to incorporate concern with costs by making each unit a cost center. However, as it stands now, cost figures are generated at headquarters through the application of formulas, and thus, the retail outlets may not be fully aware of the effect of their behavior on costs and, ultimately, on productivity.

Setting Productivity Goals. Equal in importance to the choice of indicators is the tracking of those indicators by unit (and, where relevant, by field worker), over time. Most of the institutions determine a target range within which they expect units or staff members to perform. Minimum and maximum goals are set based on factors specific to the methodology of the organization. These targets are generally used as a standard by which to judge performance, but some organizations also use such norms to decide when to open new units.

Grameen Bank, for example, sets maximum activity levels as follows: five members per group, eight groups per center, and ten centers per staff member, for a total of 400 members per field worker. However, it does not expect branches to reach full activity at the outset. In fact, currently, the

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15 At the branch level, member savings are used as loan capital. However, to protect savers, Grameen maintains a central reserve equal to the total savings amount.

average is about 180 members per outlet staff (i.e., field workers plus other branch staff).[16] Grameen categorizes branches by age. Estimates suggest that branches become profitable over a span averaging five years. These expectations thus become norms for evaluating the performance of any given branch. Other analysts have pointed out that branch profitability at Grameen Bank depends greatly on whether housing loans are present, which is explained by the fact that they are larger and longer term (lowering relative administrative costs) while yielding a significant spread for the branch. (Houghton, et al., 1992) Nevertheless, there does appear to be a strong correlation between the age of a branch and its profitability. Grameen Bank argues that the youth of a high percentage of its branches means that its long-run or steady-state level of system profitability is higher than its current performance. BancoSol, which has been expanding at a rapid rate, is also expecting to benefit from maturation of its young units, in the form of higher productivity and profits.

Actuar Bogota operates according to a norm of 60 solidarity groups (approximately 240 clients) per field worker. The norm was established after an extensive study analyzing the use of time by field workers concluded that above this figure field workers would be stretched too thin. Accordingly, Actuar changed its policy to add a new field worker whenever the figures exceed 60. However, in February 1994, Actuar was actually operating above this target, with an average of 257 borrowers per field worker. ADEMI prefers its loan officers to carry from 130 to 140 active clients at any given time.

BRI had set what it calls a "staffing standard" of 600 loan clients per credit officer. However, during 1991, when it suffered an increase in the arrears rate, it reduced the target to 400. BRI's standard is higher than that of the other institutions because of its greater differentiation of function. The loan officer at BRI has the unit chief, bookkeeper, and teller to perform some of the credit-related tasks that field workers in other institutions perform themselves.

Organizations use targets and averages to determine which units or individuals are performing significantly below par. One of the most important potential ways to increase productivity is to bring lagging units up to the target range. Usually the response to poor performance is not disciplinary. More often, such units receive additional management attention and support from their immediate supervisors. Grameen Bank has developed what it calls "fire fighting" teams, which operate out of the training division. These teams move from branch to branch as necessary to respond to perceived problems in the

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[16] Using a Grameen-type methodology, the Small Enterprise Foundation has set similar target levels: 5 clients per group; 4 to 5 groups per center; 16 centers per field worker, for a total of about 350 clients per field worker. Its current coverage per field worker is approximately 165 clients, although this is skewed due to a large proportion of field workers in training who do not carry a full load.

field. The fire fighting teams have been used extensively to develop borrower rehabilitation plans in a region suffering high defaults following natural disasters.

Incentive Systems. Some organizations link monetary incentive systems to their key indicators.[17] These systems reward the individual or unit for arriving at the target indicators described above. Staff incentives in the BRI unit system, where profitability is the key indicator, are based directly on unit profits. At year end, 10 percent of a unit's annual profits is distributed among unit staff, up to a maximum of 1.5 months of an employee's salary. This incentive system is fixed over time and broadly based, as approximately 85 percent of the BRI units earn profits. A profit-based system is always affordable: its cost rises and falls with net profits, unlike systems based on volume measures. It is also a team-based incentive, requiring the joint effort of all of a unit's staff. The team concept is particularly important at BRI, where staff functions are more differentiated than at other institutions. However, other organizations have also chosen to aim incentives at the team rather than the individual in order to encourage cooperation rather than competition and friction among staff working side by side. As BancoSol becomes more cost-conscious and introduces savings services, it is contemplating adoption of an incentive system similar to BRI's.

During its development, Actuar Bogota has run a variety of short-term incentive schemes focused on meeting specific targets that have been useful in achieving specific, time-limited objectives. But, according to Actuar's management, these programs are not effective as permanent management techniques and are not being used at present. Actuar's judgment about the lack of staying power of incentives may be more applicable to the targeted incentives it used previously, than to the profit-based system of BRI, which has become permanently integrated into the institution and provides a general motivator for good performance. ADEMI also relies quite heavily on its incentive system as a way to encourage performance. It is estimated that most loan officers earn about 30 percent of their salary from bonuses based on performance.

While staff incentives have been used to some extent at most strong microenterprise finance institutions, they are by no means universal. Grameen Bank has never used such incentives, believing that they are incompatible with its emphasis on motivating staff on the basis of its social mission.

IV.B. Information Systems

Until now, this chapter has been examining the use of key indicators, the two or three variables on which attention is centered throughout the organization.

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17 For more on incentive systems, see Steams, 1993b.

However, key indicators are not enough for effective management of rapidly growing and changing organizations. Supervisors and policy makers need a full range of supporting information, and front line staff need information to manage their own daily activities.

The information that microenterprise finance institutions need to produce can be sorted into several categories, or subsystems, which connect and feed into each other at several points. The ultimate products of the information systems are the consolidated financial statements (e.g., the income and expense statement and the balance sheet) as well as summaries of program activities, outputs, and (for some programs) impact. Feeding into these consolidated statements are subsystems that enable certain activities to be monitored more closely (e.g., portfolio quality or expenditures) as well as subsystems that manage the information needed at the retail and even individual staff or client level.

While organizations may combine these elements differently, effective information systems must have the following elements: accuracy, timeliness, relevance to management decisions, and availability to the people who need them. In addition, they should be designed such that they do not become an undue burden on staff.

Account Management. The system of control of financial accounts and transactions is at the heart of any microenterprise finance operation. Clients must be sure that the institution keeps accurate records of their account status, and it is important for their convenience that account information be readily available and easy to understand, even when the client literacy level may be low. Clients should not have to wait while the institution scrambles to verify account status. Retail level staff and their supervisors use account-level information to keep track of their own performance and to project future activity levels and cash flows. Management uses reports generated from account-level data as the basis for monitoring program status, setting planning targets, detecting fraud, and for input into the accounting system. It is essential that these systems contain various forms of protection to keep information accurate, guarding against error, mishap, and tampering.

Because not all programs handle cash transactions, accounts management may be divided between two organizations. At Actuar, ADEMI, GCC, and many other NGOs, banks handle all the cash transactions, and thus carry out major portions of this function. When this division of responsibility is built in to the methodology, problems may develop as a result of the divergent interests of the respective institutions. An NGO making the loans and interacting with clients requires up-to-date reports on each account from the bank, and at the same time, must ensure that its own records match those of the bank. On the other hand, the bank may have little reason to prepare statements according to the schedule or in the format most useful to the NGO.

At Actuar, this tension became noticeable when commercial banks, to whom Actuar paid fees for such services, complained about the burden of processing too many small transactions, and in some cases, denied service to Actuar clients. The desire to internalize the account management function was one of the reasons for the creation of Finansol, and, as Finansol expands, it will take over much of this responsibility. PRODEM's dependence on a separate financial institution similarly encouraged the establishment of BancoSol.

Arrears Control. Information on portfolio status, while closely intertwined with account management, requires special attention because of the speed and severity with which an arrears problem can damage a lending institution. Reports on arrears, which are derived from the account management system, can ensure that field workers and their supervisors know immediately when clients have failed to repay, either on the same day or the following day. An essential part of successful microenterprise lending methodologies is that late payers are contacted within the shortest possible interval after they miss a payment. Some organizations have attempted to make arrears monitoring easier by scheduling all repayments for the same day of the month or, in the case of BancoSol, the same day of the week. (However, such a bunching of transactions on one day is not an efficient use of staff time, and as BancoSol introduces savings, it may restructure the schedule of repayments.)

Arrears control systems must also track the aging of arrears, to determine how much of an arrears problem is temporary and how much is headed for eventual write off. As a commercial bank, BancoSol must track arrears according to guidelines issued by the bank supervisory authorities. Grameen Bank, which receives far less regulatory oversight, has developed its own non-standard aging categories. In public documents, Grameen's data on arrears uses a definition of more than one year past due — clearly not suitable for program managers, and not a standard banking definition of arrears. However, internally, Grameen maintains aging of arrears reports that begin tracking clients from the day a payment is missed. This system, which can clearly generate the appropriate information to track and manage arrears, represents another example of Grameen's ability to develop its own unconventional solutions to standard problems.

Other Financial Management Information. Financial managers in these institutions focus on two additional types of information sub-systems; one set covering details of costs and expenditures, and the other set covering cash flow and liability management. While accounting for costs is centralized at the smaller organizations, as these organizations shift to a profit-center framework, decentralization becomes imperative, presenting a significant challenge for information and other control systems.

At the center, each institution must be able to manage its cash flow to greatest advantage. This function involves determining how much of what type of money to raise through external means, such as borrowing from banks, and when to do so. It has a long-term component, which must be developed from projections of growth in lending and savings volume, as well as a short-term (cash management) requirement aimed at ensuring liquidity for the institution. Both components require connections to the account management systems that track the flow of funds into and out of the portfolio, as well as separate sets of information on liabilities, which are not used by other parts of the institution. As organizations move from being NGOs to financial institutions, this function is transformed from what might be called fundraising, with a focus on donors, to asset and liability management, a professional banking function. Such changes require a great transformation in information systems as well as staff skills. Good asset and liability management can save significant amounts of money, and it is thus an important function to perfect. BancoSol is placing a good deal of emphasis on developing this aspect of its operations, which had few antecedents in PRODEM.

Outputs, Activities, and Client Information. For these organizations, it is important to maintain a select number of indicators of output, activities, and data about clients in order to understand how well their clients are being served and to evaluate the achievement of their broader missions. Such indicators begin with measures of retail-level outputs which supplement the key indicators. This type of information, while generated at the unit level, is especially relevant for upper management. For example, both BancoSol and Actuar track the mix between new and existing borrowers in their portfolios, as well as the dropout rate — borrowers who choose not to renew their loans. Such information allows the management of these organizations to determine whether they are building a solid client base for the future. If the dropout rate rises, they can explore why and adjust systems or methodology accordingly. Institutions also track the sizes of loans, savings accounts, and other activities such as training or social development activities.

Organizations also need to maintain data on their clients. The extent of the information required in information systems depends on the organization's mission and on the interests of organizational sponsors, such as donors. Typically, individual loan folders contain a wide range of information about clients, but only a few indicators are recorded in the information system. BRI, for example, with its large-scale and commercial orientation, has found that it needs very little client information for its day-to-day operations. BRI finds it more cost-effective to take occasional sample surveys through which specific issues can be examined in greater depth, particularly for purposes of market research and impact analysis.

Organizations with strong donor dependence must be careful to avoid allowing donor reporting requirements to drive information systems. The information donors seek is often quite different from the information organizations need to manage their programs, and young or weak organizations are vulnerable to a phenomenon of fulfilling donor information interests while neglecting their own. For example, even though donors may only be concerned about long-run default rates, organizations must have immediate information about late payments. The organizations analyzed here have all kept their own needs clearly in mind, even during their early phases of high donor dependency.

Avoiding Information Overload. It is essential that management information systems be simple and easy to use. Unfortunately, it is in the nature of information systems that they tend to become increasingly complex over time, as additional information needs are identified. For example, Grameen Bank's monthly packet of statistical reports has continued to grow such that it now numbers some 70 separate reports, each of which are circulated to all 1,030 branches. It is unlikely that the branches can usefully digest such a large volume of information.

The BRI unit system also faced a creeping volume of information and reporting requirements, until it carried out a complete overhaul of its management information system, reducing the number of reports units must complete from thirty-two to five. These five are the balance sheet, a profit and loss statement, a credit activity report, a cash flow report, and a summary of additional indicators. These reports are useful both to the units, for monitoring their own operations, and to the superstructure, to manage the system as a whole on a day-to-day basis. They contribute to the units' ability to focus on key indicators.

Computerization. It is important to resist the temptation to equate a good information system with computerization. While computers are crucial, even in the early stages, for summarizing and analyzing information at the superstructure level, microenterprise finance institutions can run very successfully and become quite large without computerization at the retail level. Grameen Bank, for example, operates without computers at the branch or area office levels. Information from lower levels is computerized at the regions. Similarly, BKK has long supported a portfolio of 500,000 borrowers without retail-level computers. These and other organizations face the challenge of developing creative techniques to track and monitor a large client base. For example, BKK uses a simple but effective system of account management based on file boxes of loan cards for each client. Daily routines of processing the cards make it immediately clear when an installment has not been paid.

Distinguishing between management information systems and computers makes it clear that it is the design and competence of the information system that is crucial for running a strong microenterprise finance institution. Computers are simply a tool, analogous to the ledger books and calculators Grameen Bank uses or BKK's loan cards. The rationale for using computers is to increase the productivity of the information system, by increasing its capacity and decreasing the time it takes to process transactions. If they are based on strong management systems, computers can increase productivity. Thus, BRI has been gradually computerizing its units, starting with those units that handle the largest volume of transactions. BancoSol, which has had computers at the retail level for some time, is now tying the previously independent unit computers to the central system and decentralizing some of the functions previously performed at headquarters. Teller transactions are now on-line, and BancoSol is moving the systems for producing group loan contracts, checks, and repayment coupons from the center to the units (potentially saving days in waiting time for borrowers).

Many organizations have found, however, that the payoff from computerization may be achieved only in the long term because the process of developing the appropriate software, training staff, and maintaining the system is costly and time consuming. Moreover, after computerization, organizations may become more vulnerable to system interruptions or failures. After all, when a client comes into the unit, loan cards can be read immediately, but if the computers are down, a computer-based system yields no account information. Given the client-based methodology of all of these programs, it is more important to develop simple management tools with reliable access for clients than to institute a technologically advanced system that may fit preferences of higher-level managers.

IV.C. Qualitative Information Sources: Listening to the Field

In addition to the strong quantitative information described above, organizations need qualitative information to provide a complete understanding of how well they are doing. Information must flow two ways, with clear policy signals coming from upper management, informed by a wealth of feedback information coming from the field.

The structure of all these microenterprise finance organizations is rather hierarchical, with clearly defined responsibilities at each level. Policies are uniform throughout the organization, and standardization is emphasized. Some observers see the top-down, standardized nature of these operations as a negative aspect of large scale. To counteract this tendency, organizations must cultivate effective ways of allowing for bottom-up information flows. These organizations succeed because they are able to listen to the field. A number of mechanisms allow for the sharing of information, most of them integrated into the routine operations of the organization. For example, at every organization covered in this monograph, regular meetings are held between retail-level staff and their immediate supervisors in the superstructure to review performance, plans and problems, and such meetings proceed up the chain of command. The planning and budgeting process is a particular focal point for two-way communication. In addition, superstructure staff spend a large share of their time in the field. At Actuar Bogota, the supervisor for four retail outlets spends four days per week at the outlets, and only one day at headquarters. Top management at each organization makes a conscious effort to spend a good deal of time in the field.

Organizations have developed a variety of special mechanisms for sharing information. One of the most extensive is the system of monthly branch manager reports at Grameen Bank. Since inception, Grameen Bank has asked each branch manager to write a monthly report in essay form to the Executive Director covering any topics important to that branch. The reports often cover local economic conditions, the activities of borrowers, staff performance, or any problems the branch is experiencing. These reports bypass line supervisors, going directly to top management, with the intent that branch managers feel free to speak. Until recently, each report was read each month by the Executive Director. Now that the number of branches is so large (1,030), however, they are divided among department heads to be summarized with only the summaries forwarded to top management. Observers have credited this system with ensuring that the policy makers at Grameen have a detailed grasp of the status of their organization. Grameen has also introduced a staff technical journal for sharing ideas about innovations.

On this information-sharing dimension, it is important to judge these organizations in relation to other large organizations in the same country. Local norms of organizational behavior are very traditional. In Indonesia, probably the extreme example, it is culturally appropriate for subordinates to remain quiet in the presence of superiors, to defer to the opinions of superiors, and particularly to avoid statements that could be construed as critical. The same issue exists in every setting to some degree. Each of these organizations makes special efforts to overcome traditional reticence to speak, as it is clear that microenterprise finance policy makers need plentiful, honest feedback in order to stay abreast of the organization's needs. Thus, a frequently heard comment at or about these institutions is that their organizational styles contrast sharply with those of other institutions in their own countries.

IV.D. Conclusion: Information Systems and Productivity

In furthering the definition of the essential characteristics of competent microenterprise finance institutions, this chapter has attempted to show that the appropriate use of information can be a focal point through which organizations motivate their component parts to reach high productivity. The ability to embody organizational goals in a few key indicators is an important tool. At some stages in the life of an organization, the number of loans and the health of the portfolio may be the most appropriate indicators, but as organizations become financial institutions, the focus shifts towards unit profitability (with portfolio quality). Regardless of which stage an organization is in, key indicators can be the basis for performance targets and for incentive systems, both important motivators for staff and management.

Competent microenterprise finance organizations also have systems providing a wide range of financial and client information in a timely fashion to clients, retail-level staff, and management. These systems, focused on accounts management, build up to financial statements. They need not be computerized at the retail level! The best systems are simple to use and minimize non-essential information. The reports generated by such systems can similarly aid an organization in determining how well it is achieving its mission.

CHAPTER V

THE HUMAN DIMENSION: TRAINING AND MOTIVATING STAFF

As service providers, microenterprise finance institutions depend critically on the quality, performance, and job satisfaction of their staff. The role of salaries in determining overall cost structure demonstrates this clearly. This chapter looks at several functions of human resource development: recruiting, training, promoting, and, finally, motivating staff. Most of the emphasis is given to retail unit staff, especially field workers.

V.A. Finding Good Field Workers

None of the microenterprise finance institutions discussed here have had difficulty in finding and retaining strong field staff. They have been aided by prevailing labor market conditions as well as by the fact that these institutions embody some traits that are attractive in any job setting.

All the institutions seem to agree that good field workers are made rather than found, but that a certain level of education and key personal and social traits are essential prerequisites. Without exception, these institutions recruit local young people with little previous job experience. This focus makes sense because these institutions are unique in their countries, or nearly so, and there is little relevant value added by hiring people who have worked elsewhere. Instead, each institution wishes to ensure that new recruits will be receptive to the institution's own mission, corporate culture, and job requirements. At several of the institutions, previous banking experience, particularly in credit operations, is considered a liability or even a disqualifier because bank workers bring preconceptions about formal finance that must be broken. This ban on bankers is not as prevalent at the superstructure level where, in some cases, specialized banking skills may be specifically sought.

These institutions differ in the level of education they require for field workers. BRI and Grameen generally hire field workers who have completed secondary school and (until recently) have recruited separately for branch managers, requiring them to have a post-secondary education. BancoSol requires field workers to have some university education, in any subject, and K-REP requires at least two years of post-secondary training. Actuar and ADEMI recruit university graduates with degrees in specifically relevant fields, such as business or finance. The Small Enterprise Foundation (SEF) recruits individuals with the equivalent of a tenth-grade education to avoid the unrealistic career expectations that many higher educated South Africans might have. These differences from organization to organization may be the result of country conditions, particularly relative to the labor market and educational system. Despite the differences among them, each institution is equally sure that it has made the correct choice of education level necessary for the field worker jobs.

Another common requirement is that recruits be willing to live or spend time in poor and (for BRI and Grameen) rural areas, to work long hours, and to be able to relate well to clients. Attempts are made to recruit field workers from the same areas in which they will work. Each institution also adds its own specific preferences. BancoSol gives strong preference to speakers of the indigenous Amerindian languages used by many of its clients, and many African programs must be sensitive to ethnic considerations. Grameen Bank asks whether applicants can handle some of the practical aspects of rural living. Can they cook, swim, and ride a bicycle? Actuar and BancoSol look for desired qualities through interviews with psychologists and psychological testing. Actuar even includes visits to the family home as part of the interview process.

Issues of social class arise here, because with the possible exception of BRI, field workers tend to come from a higher social class than their clients, or to be members of the same social class who have moved up through education. The two South African programs referred to here have often recruited staff from its client base. Not all job seekers with the requisite educational qualifications will be eager to spend their time in low-status settings. Attitude, then, is as important as education. Accordingly, each institution has a process to weed out applicants. BancoSol accomplishes this at the earliest stage, through extensive interviews and testing. Actuar sends applicants to branches to work with field workers for two or three days before accepting them as trainees. The other institutions make weeding out a part of the longer training and probationary process. At Grameen Bank, between a fourth and a third of all trainees leave during the training period.

Most of the staff at each of these organizations are men, and given that a high percentage of clients are women, the gender of staff is an ongoing concern. Grameen Bank, which operates in the country where women's roles are most culturally restricted and whose clients are nearly all women, faces the most severe challenge. As of 1991, less than 10 percent of Grameen's staff were women. (Houghton, et al., 1992) Among the difficulties Grameen Bank faces in recruiting and retaining women are the general preferences of middle class women not to work, restrictions on working hours imposed by families, travel restrictions (for example, few women ride bicycles), and the cost to Grameen of providing separate accommodations for female staff. The other organizations do not face such extreme situations, but still find it more difficult to recruit women, both for family and security reasons.

Counter examples exist in South Africa, where microlending organizations have discovered that female loan officers are more successful in dealing with their female clients. Because the majority of their clients are female, both SEF and the GCC have made deliberate attempts to hire women, currently a majority of staff.

V.B. Training Staff

Staff training for both new recruits and existing employees generally focuses on two broadly defined objectives, both of which are highly specific to the organization:

- Corporate culture -- ensuring that all staff understand and internalize the mission and corporate values of the institution
- Operating procedures -- teaching staff the standard operating procedures they need to follow in performing their jobs -- and exposing them to the procedures performed by other parts of the organization

A third potential area, developing job-related but generalizable skills (such as project appraisal, financial management, and client relations) receives relatively little attention except as it supports one of the two main objectives. For example, BRI trainees do not learn loan appraisal in general; they learn how to do the type of abbreviated loan appraisal BRI employs. Cost is one obvious reason that general skill training is not emphasized.

On-the-Job Training. Because the focus of training is so job- and institution-specific, the basic challenge of new staff training is to organize an efficient and effective means of transferring knowledge from existing staff (who hold the knowledge) to new recruits. It is not a matter of imparting a self-contained or independent body of knowledge.

Accordingly, each of these organizations uses on-the-job training as the major training vehicle for new staff, supplemented by more formal training provided at the center. New entry training includes a small amount of classroom work (from one to three weeks, depending on the institution) and a longer stint as a trainee in a retail unit (from two to six months). In all cases, the training process mobilizes a large part of the existing staff to participate in the transfer of knowledge, as field workers teach new recruits their own jobs, working side-by-side for several weeks or months. Some have described it as an oral tradition in which most knowledge is passed by word of mouth.

It is important to note that the on-the-job component of training is a part of a structured training experience. For example, after a week of initial orientation, Actuar Bogota recruits are assigned to work with an experienced field worker who already has a full quota of clients (sixty groups). They work together for two months, during which time they are expected to add twenty more groups to their portfolio. When this target is reached, the portfolio is split, giving each worker a set of forty groups, of which about ten are new. Similarly, new ADEMI employees spend two weeks at headquarters for an induction program, followed by four weeks accompanying an experienced *asesor* in the field. After observing the loan officer with his clients, the recruit is expected to start building his own portfolio in an adjacent geographical area within three months, at which point he will go off on his own. The other institutions have similar systems with differences in timing and length of classroom and on-the-job activities.

Classroom Training. If the on-the-job training model is the most efficient and effective form of knowledge transfer, the function of the more formal part of the training is to ensure that the quality of the transfer is high, that the information imparted is standardized across all employees, and that topics of particular importance to the organization receive sufficient emphasis. Thus, at BRI, the classroom training focuses on operational procedures, while Actuar and BancoSol stress corporate mission and team building. The GCC in South Africa has a conflict resolution component in its training program. Finally, many organizations, including BRI, Grameen, Actuar, and ADEMI, require that trainees pass exams before becoming regular employees.

Among these institutions, the training staff have been concerned with finding effective pedagogical techniques. For example, the training staff at BRI attempts to break away from the prevailing Indonesian educational system techniques of rote learning and a lecture format. They train instructors (usually former unit employees) in the use of more active learning techniques such as case studies and group projects.

Grameen Bank has developed several unique training techniques, which appear to serve it well in developing the staff attitudes it desires while focusing on job requirements. For example, Grameen has no formal training manual. Instead, its written training materials contain a list of questions about Grameen objectives and operations that trainees are supposed to answer for themselves while they are in the field. Classroom time is devoted to discussing the answers trainees have found to these questions and comparing field experiences, rather than to the presentation of additional material. This technique places responsibility for learning on the trainees, while keeping them focused on the topics of greatest importance to Grameen.

Much of what Grameen wants trainees to internalize involves its philosophy of poverty alleviation. Trainees are required to do several specific field activities which develop those attitudes and at the same time deepen knowledge of local economies. One particularly successful method to do this involves a case study; trainees are asked to find a poor woman, interview her, and write her life history, considering her economic and social problems and coping strategies. They must also complete surveys of the economic and market activity of a particular village. These devices may contribute to the strong internalization of institutional values that Grameen staff exhibit, even as they generate useful information for the trainee and Grameen Bank.

Another issue for training departments is ensuring that training content stays current with organizations in transition. At Grameen, because the training center discussion revolves around field experiences, there is a built-in mechanism to guard against a detached training program. Trainers in the more formal BRI system, however, must devote considerable time to ensuring that their materials reflect the latest policies. On the other hand, the bottom-up Grameen system makes it difficult to introduce new policies or procedural changes into the training process. A uniform presentation of policy may be better accomplished in BRI's training system, which gives relatively greater emphasis to the delivery of specific content during classroom training. BRI's approach to training was developed expressly to re-orient existing BRI staff to a new set of policies at the time when the unit banking system was overhauled and KUPEDES and SIMPEDES were introduced. Thus, it actively wished to overcome the preexisting tradition and impart a new one. This helps explain its focus on delivery of specific content. Rapidly changing organizations, such as BancoSol and Actuar, need to take advantage of similar tools for ensuring the accurate dissemination of new procedures, and thus may require a relatively strong emphasis on providing specific content in classroom training.

In-service training varies greatly from institution to institution. BancoSol and ADEMI see training as an ongoing process and require staff to spend time each year or two in training. Some of the training is job-specific (e.g., training associated with the use of new computer software or the introduction of savings instruments), but BancoSol's particular emphasis is a series of seminars on team building, personal development, and total quality management. ADEMI offers a variety of courses on subjects ranging from credit analysis to attending to clients. BRI relates training of existing staff mainly to promotions, so that employees are trained in their new responsibilities. Neither Grameen nor Actuar emphasizes in-service training to any great degree.

V.C. Motivating Staff

As Chapter III pointed out, high staff productivity is essential for the long run viability of microenterprise finance institutions. One aspect of maintaining staff productivity is providing staff with the kind of job satisfaction that will motivate them to perform well. These organizations have three main tools to engender staff satisfaction:

- Good career prospects
- The direct satisfaction of doing meaningful work in a good organization
- Attractive salaries and benefits

A fourth tool, responsiveness to the expressed needs of staff, is beginning to be important in some of the organizations. Each of these institutions can offer its staff many of the attributes that make a job attractive, and they are rewarded by low turnover. At Grameen Bank, less than 2 percent of the staff left in 1992, and turnover is 1 percent at BRI (including all reasons for leaving). Only six people left BancoSol's staff in 1993.[18]

Internal Career Paths. Perception of career prospects is determined in large part in reference to local labor market conditions. Most of these institutions operate in countries where good jobs for secondary and post-secondary students are relatively scarce. Well-paid professional jobs are so scarce in Indonesia that BRI does not advertise job vacancies because the crush of applicants would be too great. BancoSol receives several hundred applications each time it recruits. Thus the institutions begin in a strong position. The setting is particularly favorable for the Asian institutions, where staff often enter with the expectation that their entire working lives will be spent in that institution, reflecting both the scarcity of alternatives and the prevailing norms of employers and employees.

Actuar Bogota, and to some extent BancoSol and ADEMI, operate in more fluid labor markets. Young Colombian graduates going to work for Actuar are likely to regard the job more as a stepping stone than as a permanent home. One Actuar staff member estimated that field workers will begin to seek advancement or another job after about two years. Similarly, many loan officers at ADEMI consider the possibility of going into business for themselves after they have saved money and learned valuable skills. Accordingly, both organizations have had to compete actively to retain staff, through attractive salaries and advancement prospects. Conversely, both organizations are more willing to fire workers who do not meet targets than are their Asian counterparts.

For higher level positions, each microenterprise finance institution faces a choice between a policy of hiring at the bottom and recruiting from within, and a policy of hiring the best qualified possible people directly into each level. Defining the recruitment and advancement policy requires significant tradeoffs that involve corporate identity, staff satisfaction, and achieving the proper mix of internal knowledge versus technical skills. The career patterns differ significantly at these institutions.

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18 Turnover figures are reported in interviews with human resource departments at each institution.

Grameen Bank is at one extreme: all but a handful of its more than 400 head office staff members originally served as field workers or branch managers and have since moved into other positions. The handful consists mainly of top management who have been with Grameen from the start, with few indeed who were recruited from the outside (e.g., one or two technical specialists). The benefits of this history include the sense of solidarity it yields among the staff, and the clear understanding superstructure staff have of field operations. One Grameen evaluator wrote that,

> Grameen Bank reliance on senior managers whose career is exclusively with the Bank has real advantages for sustaining the responsiveness of Home Office to what is happening in the field. There is little sign of the alienation or even isolation that can overtake head offices with large field operations. (Houghton, et al., 1992)

Grameen Bank has an impressive tradition of developing its own indigenous solutions to problems, and often these solutions are both effective and ingenious (e.g., the question-based training materials). There are drawbacks, however, primarily in the form of limited experience in learning from the outside world. In some cases, learning from outside might have made for quicker and more effective solutions, particularly in technical areas such as information systems, computerization, and accounting. As Grameen becomes larger, it has more to gain by learning selectively from more formal organizations.

BRI career paths are quite different from those of Grameen Bank and bring their own costs and benefits. Staff of the BUD system can be divided into three groups: front line unit staff (credit officers, tellers, and bookkeepers), unit managers, and superstructure staff. Each of these three groups has a different career path. Competent front line staff, who generally have only a high school education, can expect to progress from bookkeeper (the entry level for most such staff) through loan officer to unit manager, and sometimes to staff positions at the BRI branch (either in the BUD portion, supervising units, or in a position unrelated to the units). The education levels of this group generally prevent them from progressing further than the branch. The second group, recruited as unit managers and entering with stronger educational credentials, may progress slightly higher. However, most of the BUD staff at the center and regional offices come from yet a third group, BRI professionals who are rotated through a variety of branches and departments, staying with the unit system for only one or two rotations. The career aspirations of this group lie outside the unit system. The separation between the lower level staff who have first hand experience of the units and the superstructure staff who do not may constitute a significant source of vulnerability for the BRI unit system, as Chapter VI will discuss further.

It should be noted that before the 1984 restructuring of the unit system, the separation was even greater, with unit staff not considered full-fledged BRI staff. One of the successes of the unit transformation was the placing of unit staff within BRI, which opened greater advancement prospects to unit staff and put them on the same pay scale as other employees. Thus, the current situation represents a significant improvement.

BancoSol and Actuar Bogota face yet another set of human resource development challenges. These challenges stem from the rapid transformation of the organizations from NGOs to financial institutions. As a rapidly growing NGO, PRODEM offered its staff good advancement opportunities. At the time BancoSol opened, PRODEM looked something like Grameen in that most of its staff had been with the organization from the start, and most higher level staff had begun as field staff. However, in becoming a bank, BancoSol has had to introduce a range of new functions very quickly, mostly in various financial management areas, and has been compelled to recruit new staff from the formal banking sector. This external recruitment has undoubtedly enabled PRODEM/BancoSol to transform itself and grow very quickly, to the benefit of its expanding pool of clients. However, this transformation has come at a cost to the institution and its staff. The costs take the form of occasional resentments by original NGO staff, including feelings that their career prospects may have diminished, and the weakening of the shared understanding of corporate values through the introduction of staff lacking prior commitment to PRODEM's social goals or informal sector clients. Both costs are relatively temporary (though hardly minor). As BancoSol expands, its front line staff will be made up of new recruits who do not look back at how it was "before." These staff members will not face a disruption of expectations. Meanwhile, the incorporation of bankers into the staff requires a joint re-definition of corporate values, which BancoSol is addressing through its heavy focus on in-service training and, within that, on team building and corporate identity.

For Actuar Bogota, these are the types of shocks that may lie ahead, now that its new financial institution, Finansol, is operating, staffed mainly by bankers. However, the fact that the NGO will retain most of its former functions while Finansol will be a separate entity will make the dynamics of these shocks different from those experienced at BancoSol.

Each of these institutions has also benefitted from its steep growth curve, which has enabled it to provide career advancement as a performance reward. Continued growth often means lateral opportunities as well as promotions. While such opportunities continue to exist for the newer organizations, as others become larger and grow more slowly (happening now at both Grameen and BRI), advancement prospects lessen, and alternate motivators must be sought.

Meaningful Work in a Successful Organization. From the start, the organizations beginning as NGOs, particularly Grameen and PRODEM, relied on a strong sense of mission and commitment to social goals. Staff and management shared beliefs in improving the lives of the poor through entrepreneurship and saw themselves and their organizations as contributing to that objective. This common commitment motivated the staff to work long hours, often under difficult conditions, and at relatively low salaries. Actuar has had a similar experience, but while social concerns are important in the mission, its shared vision gives greater weight to the potential profitability of providing services to the informal sector. Staff at these new organizations have known they were involved in path-breaking experiments; these organizations were setting out to achieve what others had not been able to achieve previously and that many people doubted could be done. For many microenterprise finance organizations in South Africa, including the Small Enterprise Foundation (SEF) highlighted here, working to alleviate poverty is perceived as a way of contributing to the development of the "new South Africa." Such perceptions can be extraordinarily motivating for staff.

In significant contrast to the NGO vision, BRI's corporate culture lacks the added push of social values. Rather, this culture emphasizes belonging to a large, profit-making, and prestigious organization as a full-fledged contributor. Staff at the units are now encouraged to think of themselves as real bankers, an increase in status over the treatment of the units before the 1984 changes. These values can also be strong motivators for staff.

While retail-level jobs in these institutions involve hard work in difficult settings, they do offer inherent satisfactions. Among these are a fairly high level of autonomy and responsibility, within the parameters set by the organization. Field workers are judged by results rather than by hours punched on a time clock (a favorite reference among BancoSol staff). They have a great deal of responsibility for loan approvals, together with their supervisors, and can become important parts of the economic development scene in their immediate locales. At the unit manager level, some institutions use increases in loan approval limits as a performance reward.

For the most part, these organizations have kept their corporate values strong and operative as motivating devices, though as they grow older and more established some of the motivational edge may wear off. Staff also grow older and become more concerned about their own financial security and quality of life. Thus, over time, an organization that began almost as a social movement, like Grameen Bank, will have to think about staff motivation in more concrete terms. That is, it will move somewhat in the direction of BRI. This does not mean abandoning the sense of commitment, but recognizing that it cannot be sustained at the same intensity as the organization matures. Grameen, which is particularly good at infusing its sense of mission throughout the organization, has already experienced the first example of change in the labor difficulties it faced in 1991 when some staff agitated for creation of a labor union. And as noted above, BancoSol is in the midst of redefining its mission to incorporate profitability and efficiency into its objective of serving the poor. By its nature, institutional profitability is not likely to yield the same beyond-the-call-of-duty response that can come from strong social motivation. Thus, as they mature and become more concerned with financial viability, these organizations are relying more on concrete motivators such as salaries, benefits, and incentive systems.

Salaries and Benefits. As explained in the previous chapter, salaries and benefits are normally the highest component of non-financial operating costs for any of these organizations. Salaries are often set with reference to some external standard. For Grameen Bank, it is the government salary structure; for Actuar, BancoSol, and ADEMI, it is the formal financial sector; for the BRI units it is the salary structure of the mainstream BRI office. Conscious reference to these standards is crucial for establishing a generally stable base for salaries and for ensuring that staff believe they are being paid well, or at least fairly. However, with a reference wage, organizations become vulnerable to the fluctuations in that wage. Grameen Bank has already demonstrated that when the reference rate rises, it has little choice but to go along. Nevertheless, organizations are probably less subject to pressure than they would be without the reference.

Actuar, BancoSol, and ADEMI, which all operate in Latin American labor markets that are more competitive for employers, have announced annual salary increases that exceed the level of increase in their points of reference. They also make a point of exceeding legally required fringe benefit levels, for example by offering housing loans.

Benefit policies that increase the percentage of operating costs designated for salaries will be difficult for organizations striving for financial viability to maintain over time. Thus, the managers of the different organizations have developed alternative ways to appeal to their respective staffs. To deal with its direct labor challenge, Grameen created a staff association (rather than allowing a labor union to form) through which staff communicate their concerns formally to management. Frequent regular staff association meetings are held at all levels, including branches. The issues that have emerged as staff priorities through the staff association include the size of allowances for daily expenses, improved opportunities for promotion, and the transfer of staff to areas near their home districts. Through the staff association, some observers believe that Grameen Bank has successfully diffused the potential labor union threat by creating a genuine means of dealing with the sources of potential differences, in a form that supports rather than challenges Grameen Bank. ADEMI has similarly created a special credit cooperative to help staff with their short- and long-run financing needs. Most employees place their pension plan benefits into the cooperative, which is run by the staff itself. ADEMI also contributes on a matching basis.

V.D. Generating Good Performance

In addition to providing the elements for staff satisfaction, increasing productivity requires methods to focus staff on defining and achieving good performance. The key indicators and incentive systems discussed in Chapter V are a major tool for focusing behavior. More generally, organizations must define levels of responsibility and establish means for evaluating whether responsibilities have been carried out.

Most of the organizations discussed here have found it more effective to define responsibilities at a team rather than an individual level. The profit-center concept makes the idea of teams explicit, but teams are emphasized even in organizations that do not use profit centers. Evaluating performance at a team level encourages those within a team to support each other. Thus, workers at a BancoSol branch report that each *asesor* has developed a specialty for which he or she is known, such as keeping accounts or working with delinquent borrowers. The *asesores* turn to each other for help in these areas. If the *asesores* felt they were in competition with each other, such cooperation might not develop.

Grameen Bank defines responsibilities in a way that connects the different levels of the organization through the use of its "circles in circles" concept. Beginning with the individual borrower at the center, a series of concentric circles is envisioned as follows: borrower, group, center, branch office, area office, region, and home office. Each circle is responsible for the performance of the next smaller circle. A frequently heard illustration of this concept is that if a branch performs well, the branch staff is praised, but if it does badly, it is the area level staff who are called to account.

Many organizations have found that the authority to approve loan applications can provide positive motivation to staff and boost staff morale. As organizations grow, they are less able to offer promotions to front line staff. Thus, delegating an important responsibility can provide alternative means for managers to give individuals a sense of importance in the organization.

Despite formal systems of individual and team evaluation, it must be noted that most of the energy for ensuring good performance comes from the daily interaction between staff and supervisors. For example, at Actuar, the daily regimen of loan committee meetings, at which field workers present loan proposals to their branch manager and another field worker, constitutes a forum for testing field worker skills and reinforcing norms and standards.

V.E. Protecting against Fraud

Organizations must also protect themselves against substandard behavior, including various forms of fraud (e.g., fictitious clients or kickbacks). All microenterprise finance organizations encounter fraud by employees at some point. They respond to the possibility by developing systems of financial control that make fraud difficult to arrange and easy to detect. They also deal quickly and sharply with any employee found guilty of fraud. The following are common methods of protection against fraud:

- Defining and promulgating a simple, clear code of ethics. For example, at both Actuar Bogota and ADEMI, one rule in the code is that no field worker is allowed to receive any type of favor from a client, such as a cup of coffee or lunch. Notably, ADEMI allows *asesores* to buy goods from their clients at wholesale prices, while Actuar does not.
- Developing very formal and transparent processes whenever money is handled, or avoiding handling money as much as possible. At Actuar, field workers handle only checks, which borrowers take to banks to cash, and they are not allowed to receive repayments from clients. These must also be made by the client at the bank. At Grameen, where cash is handled, at least two staff members are present for every disbursement.
- Rotating personnel regularly (e.g., every two or three years) to different units so that improper relationships with clients are not easy to establish.
- Developing multiple cross-checks in financial management and information systems and ensuring that information flows quickly. It is impossible to detect fraud if information systems are not working.
- Establishing clear standards for the determination of interest rates and repayment schedules to prevent kickbacks to loan officers.
- Providing services for employees that lessen the need for them to commit fraud. For example, most organizations provide adequate benefits for their employees. ADEMI gives regular loans to employees in times of need, while Grameen provides housing finance.
- Providing regular supervision. The major burden for fraud detection lies with the supervisors of the retail outlet staff, either unit managers or the superstructure employees with direct oversight of unit performance. The next line of defense is the internal audit system whereby detailed checks are made on individual transactions, including interviews with clients. BRI has an extensive system of internal audits, while ADEMI has an internal auditor on staff.

Each of the organizations reviewed here uses all or most of these methods in some way.

In cases of serious fraud, most of the organizations immediately fire the culprits. In Indonesia, where firing employees is not culturally acceptable, BRI first takes milder steps, such as transfers and demotions. Unlike most

Indonesian organizations, however, BRI is willing to fire employees if their behavior is chronically below par. When K-REP found one of its employees had misused funds, it had a choice between filing a civil case, which would force the return of those funds, and a criminal case, which would result in a prison sentence for the culprit. It opted for the criminal procedure as a warning to others. In a similar instance, ADEMI also pursued criminal charges.

V.F. Conclusion: Worker Motivation as a Key to Productivity

A number of generalizations can be made about the way strong organizations have handled human resource development. These generalizations add to the picture this monograph is developing of the essential characteristics of microenterprise finance.

All of the organizations show a preference for young recruits with good but not outstanding educational achievements and receptivity to the organization's mission. Clearly, the organizations in countries with a plentiful supply of well-educated workers and a soft labor market have an advantage. Organizations train recruits through strikingly similar training programs designed to mobilize the existing staff to convey knowledge through an oral tradition, with an emphasis on corporate values and job-specific procedures. Each organization has a well-defined corporate culture, which it stresses throughout staff development, particularly during training activities including in-service training. In the cases where that culture involves strong social goals, there is an extra motivational factor.

The organizations provide for ongoing staff satisfaction by giving staff responsibility for results, paying good salaries and benefits (from a local perspective), offering good career prospects, dealing openly with staff needs, and, in general, instilling a cooperative feeling among staff. Each organization also employs effective systems for detecting and dealing properly with any fraud by employees. Together, these elements secure the kind of motivated workforce which, when given proper focus, will be highly productive.

CHAPTER VI

THE LIVING ORGANIZATION: MANAGING GROWTH AND CHANGE

The previous chapters have examined the anatomy of competent microenterprise finance organizations, introducing the systems and structures that enable the organizations to deliver high-quality services to large numbers of people. However, like any living organism, the behavior of the organization as a whole is more than the sum of each of its systems. This last chapter looks at the organizations as wholes, particularly as they go through complex processes of rapid growth and change, as they develop new services, and as they face both internal and external crisis situations.

To put the issues of this chapter into perspective, it is useful to consider that the institutions reviewed here have experienced extremely high and sustained growth (see Table 9). Actuar Bogota, for example, more than doubled its number of clients each year for four years in a row, while Grameen Bank's annual growth rates have been over 20 percent (usually well over) every year since 1985. Moreover, several of these organizations have made major changes in their organizational forms and have added new services. That they can maintain strong institutional health while undergoing these changes is evidence that they are extraordinarily competent.

This chapter examines how some of these organizations manage growth and change, after a short review of the leadership, governance and policy making, topics which are closely related to the ability of organizations to progress.

TABLE 9

INSTITUTIONAL GROWTH RATES (1985-1993)

(Percent change in number of clients at year end over preceding year)

	1985	1986	1987	1988	1989	1990	1991	1992	1993
Grameen Bank	26	37	57	44	37	31	22	33	n/a
BRI Units									
KUPEDES	61	19	7	5	19	15	-3	0	n/a
SIMPEDES	1,277	1,046	131	69	62	32	27	n/a	n/a
PRODEM/BancoSol				227	93	112	44	24	56
Actuar Bogota					445	133	132	133	54

SOURCES: Khandker et al., 1993; Robinson 1992b

VI.A. Leadership and Governance

Boards of Directors. The governing structure of BancoSol, Actuar Bogota, and Grameen Bank consists of a board of directors, with implementation led by a strong executive director. While outwardly similar, subtle differences give the organizations different characteristics. BancoSol, Actuar, and ADEMI are led by active boards, made up of prominent local businessmen. In a sense, these organizations were created by their boards of directors.[19] The board members, particularly the chairmen, feel personally responsible for the organizations with which they are publicly identified. Thus, they take an active role, both in overseeing the progress of the institutions and in performing external relations functions for them. While Actuar, BancoSol, and ADEMI have strong executive directors who are genuine leaders, it is clear that the executives work for and answer to the boards.

The BancoSol board is particularly noteworthy. Because BancoSol is an investor-owned institution, its board represents shareholder interests, which is a source of difference in defining the organizational mission: return on investment operates side by side with the goal of reaching the poor. Moreover, many of the members of the board are leading Bolivian bankers, who are positioned to perform three important tasks for BancoSol: (1) guide BancoSol in learning the banking business; (2) bring legitimacy to BancoSol in the eyes of participants in the broader financial sector, including the regulatory authorities; and (3) link BancoSol to sources of funds from their own banks, e.g., in the interbank market and by placing time deposits in BancoSol. It would be much more difficult for BancoSol to do these things from a staff level. The boards of ADEMI and Actuar similarly include prominent individuals from the private sector.

Grameen Bank is not led by its board in the same way or to the same degree as the ACCION-affiliated institutions. Grameen is primarily a management-led institution. Grameen's thirteen-member board is made up of four representatives of the Bangladesh government and nine representatives of its own members. The board did not originate the organization; it was initiated by its executive director, Mohammed Yunus. However, Grameen's board of directors does make major policy decisions. The board's function appears to be mainly reviewing and approving policy proposals developed by management, modifying them if it chooses. For example, in 1991 it agreed to increase the interest rate on general loans from 16 to 20 percent, but only with the promise that Grameen Bank would attempt to increase productivity so that the rate could be reduced as soon as possible. The governmental members of the board may also help secure good relations between Grameen Bank and the authorities of the Government of Bangladesh.

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19 This is not directly true of BancoSol, which grew out of PRODEM, but PRODEM was created by its board. See Glosser in Otero and Rhyne, eds., 1994.

The BRI unit system differs from the other organizations reviewed in this study as well as most microenterprise finance institutions, both because it is not a separate organization and because it is owned by government. BRI's seven-member board of directors is appointed by the government. Each director, except the president-director, is responsible for several of the twenty-two major departments of the bank. Thus, the unit system is the general responsibility of the overall head of BRI, the president-director, and the special responsibility of only one of the remaining directors. These directors are much more operational than the board members of the other institutions, functioning in part as executive vice presidents and in part as a policy-making board. For example, many of them sit on the Asset and Liability Coordinating Committee, which determines interest rate policies throughout the bank. The directors are rotated within BRI at regular intervals and may also be moved from BRI to other government-appointed positions. Accordingly, with the exception of the director currently in charge of the unit system, none of the directors is primarily concerned with that system's well-being. Decisions about the system are made in the context of the broader needs of BRI, and of the Indonesian Government more generally. In fact, the creation of the unit system itself involved extended partnership between the Ministry of Finance, which originated the concept, and BRI. For all these reasons the BRI unit system is less independent than the other institutions and frequently subject to events outside itself.

The Executive Director: Charisma and Continuity. All of the institutions reviewed here have benefitted from having strong executives who have provided leadership and continuity to the organizations. The most notable case of this is Grameen Bank whose success is often attributed to the "charismatic" qualities of its leader, Mohammed Yunus. The unique qualities of Dr. Yunus are often cited in discussions of whether Grameen Bank can be replicated, especially by those who argue that it cannot. The basic premise of this paper is that successful microenterprise finance organizations grow in a variety of settings (i.e., that Grameen Bank, broadly interpreted, can be replicated), provided that institutions develop certain types of competence. After reviewing the most successful institutions, it appears that one important aspect of competence involves a strong leader who provides continuity to the institutions as they develop.

However, in examining the leadership issue, the term charisma may be less than helpful, if it connotes a special mystique not found in ordinary people. Across institutions, one observes no single type of personality or unusual personality trait common to the leaders. Rather, there are functions that the leaders are able to perform. The mystique of leadership is the fact that few people are able to perform equally well in the wide range of areas necessary to lead a microenterprise finance organization (or any complex organization).

Grameen, BancoSol, Actuar, and ADEMI all have such leaders and have had the same leader since the beginning (at ADEMI, there was a break in the mid-1980s). BRI has also enjoyed such leadership in the form of the president-director of BRI, Kamardy Arief, who led BRI's overhaul of the unit system and introduced the "new culture" (but who moved to another institution two years ago) and Sugianto, the director in charge of the unit system. By contrast, BKK, which has lacked clear and continuous leadership, has not grown significantly in a number of years.

This monograph does not attempt to analyze the functions of the executive director in detail. Rather, it points out some of the salient features that appear to be common to the leaders at the institutions under review. Among the traits the leaders exhibit are the following:

- Extremely high devotion to the institution, involving heavy time commitments and strong personal self-identification with the future of the institution
- The ability to maintain an overall vision of where the institution is going, in terms of mission and practical achievement
- Involvement in the details of the organization, including a firm grasp of operations at the field level (for example, these leaders are consistently aware of how the institution is performing with respect to key indicators and targets)
- The ability to work within the local social and political environment (such as, through personal contacts or a strong board) and to interact with govemment bureaucracies
- The ability to motivate staff
- The ability to project the corporate culture of the institution

While it is rare to find someone who is equally strong in all these areas, it also appears that the leaders grow and develop some of these traits on the job, as their organizations evolve.

As the organizations grow, the role of the executive changes and the question of succession arises. Each of these successful institutions has been very fortunate in the continuity of its leadership, and it is a very real question as to how well they will be able to withstand leadership changes.

However, questions of evolution arise first, as organizations are transformed under the same leadership. With increasing size, the leaders find that they can no longer maintain the hands-on involvement with all operations that characterized their role in the early stages. As the organization grows, executives face several challenges: (1) how to delegate increasing responsibility for day-to-day operations to competent senior management, which includes hiring and/or training competent managers; (2) how to formalize systems that may have operated informally at a lower level; and (3) how to maintain corporate culture as the organization becomes larger and more formal. These challenges are not unique to microenterprise finance institutions, but take on a certain character in those organizations.

For entrepreneurial people, who have built organizations from a small size and who excel at managing details, delegating authority is often difficult. At worst, entrepreneurs fear to hire competent top staff because they wish to retain control; more often, top staff do not have the opportunity to grow if the entrepreneur does not delegate. As the microenterprise finance organizations become more formal and particularly as they are transformed into financial institutions, the skills required by senior managers become more technical, calling for intensive learning by top managers and, in many cases, introduction of new high level staff. All the organizations and their leaders appear to be meeting this set of challenges successfully, although not without growing pains.

Actuar Bogota has taken clear steps to transform the role of the original executive director, Oscar Giraldo. In order to pursue the broader vision of building a full range of organizations serving the informal sector, Giraldo has moved from being executive director of Actuar to a new, more all-encompassing position, in which his main focus will be building new organizations and services. This transformation was made possible through the selection several years ago of a highly competent deputy director (now executive director), who has gradually taken over responsibility for Actuar's ongoing operations.

At Grameen and BancoSol, both of which embody a sense of being an extended family, staff express concern over this kind of evolution. They worry that organizational unity and motivation will diminish as the executive becomes less able to interact personally with every staff member. However, this concern is primarily an issue of corporate culture, rather than of effective operations. Grameen Bank has demonstrated that a pervasive sense of corporate culture can be maintained even at a very large scale of operations. At both of these institutions and Actuar, the executive director maintains his role as the embodiment of the corporate culture, even while stepping back from daily operations.

Because much of the business of microenterprise finance organizations is the routine production of services, the executive should strive to hand that responsibility to others, focusing instead on maintaining corporate culture, relating to outside constituencies, setting future directions, and overseeing change and innovation. Most of the organizations reviewed here have made or are well on their way to this redefinition of the executive's role.

However, these organizations have had little experience with an actual change of leadership or succession, and it remains to be seen how they will react to the eventual loss of their original executives. Major determinants of how well succession may proceed include the existence of people in key positions (e.g., top management and boards) who thoroughly understand what makes the organizations work, particularly at the retail unit level, and who are committed to the organization's mission.

K-REP is the only institution reviewed here that has completed a cycle of succession fully and successfully.[20] K-REP began with an expatriate executive. Through careful planning, it laid the groundwork for the transition to a Kenyan director and eventually promoted A. Kimanthi Mutua, one of its early staff members, to that position. Before the appointment, Mutua had served first as finance director and then as deputy director. Thus, a transition was made successfully as the result of long-term planning and training from within.

The BRI unit system, because it is part of a larger bank, has a unique succession challenge. The unit system, KUPEDES, and SIMPEDES were established during the tenure of Kamardy Arief, the president-director of BRI, and Sugianto, the director in charge of the unit system — in conjunction with high-level government leaders. If the directors who have guided the unit system thus far choose to leave the bank, it is unclear who would succeed them. Among head office staff, as described in Chapter V, there are few people who have worked within the unit system, though there are a number who have served in the branches and may have had some responsibility for units then. Many head office staff are rotated throughout other BRI departments and thus may have career aspirations that are not necessarily linked to the unit system. Accordingly, the head office staff with unit system responsibilities cannot be considered the embodiment of either commitment to or knowledge about the unit system.

As a result of both succession and the orientation and experience of the head office staff, there is a potential danger that the future leadership of BRI may not focus or concentrate on the unit system to the same extent as is done currently. And although KUPEDES provides most of the profits for the bank, there is also a danger that the unit system could be sacrificed for other projects. For example, banks with large rural networks in many countries have treated those networks as sources of deposits, but not lending outlets. Thus it is particularly important for the unit system that BRI management continue to have a clear understanding of how the units operate and what their overall relevance is — both for the bank as a whole and for the field of microenterprise finance internationally.

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20 ADEMI saw the departure of an executive director, but this turned out to be short-lived. The original director, Pedro Jimenez, returned two years later. He is currently making a more concerted effort to involve his senior managers in day-to-day decision making.

Policy Setting. One of the key functions of top management at microenterprise finance institutions is setting policy, and a brief comment on how this is done may be relevant here. Policy decisions may involve a variety of topics common to any organization from personnel policies to ethics to procurement procedures. However, microenterprise finance institutions focus on a specific set of financial policies top management uses to direct the basic financial service operations. These include the determination of interest rates and fees, loan size minimums and maximums, eligibility requirements for services, the transfer price for institutions using profit centers, target levels of performance for field staff, and loan approval and collection policies. These policy levers can have a major effect on productivity and profitability, not to mention their direct effect on clients. It is often necessary to fine-tune these policies in response to both internal and external conditions.

At most of these institutions, such policies are set through a formal process involving committees of top management and are communicated through circulars distributed to all staff. Policy decisions are rarely made by one person acting alone. Grameen Bank has three tiers: a lower management committee, which formulates many of the policy proposals; an upper management committee, which makes most of the decisions; and, for the most important policies, the Board of Directors. At BRI, financial policy decisions are made by the Asset and Liability Coordinating Committee for BRI as a whole, including the units. ADEMI vests policy authority in an internal executive Committee comprising senior management, while K-REP's executive committee, comprising board members, oversees policy implementation. Several organizations report that in the range of 30 to 60 policy circulars (on all topics) are written each year, few of which cover major issues. Formal policy pronouncements should be limited to avoid confusing and overwhelming front line staff.

It is also crucial that adherence to policy be stressed throughout the organization. Policies must be clearly spelled out, communicated, and acted upon in daily staff interactions. The president-director of BRI had a well-known habit of dropping in unannounced at units and quizzing staff about policies and procedures.[21] Visitors to BRI often take note of the consistency with which BRI unit staff are able to state current policies accurately. If policies are not well known or are inconsistently applied, organizations lose the ability to respond to emerging situations.

VI.B. Horizontal and Vertical Growth Strategies

All the programs highlighted in this study have as an explicit goal the expansion of services to the maximum possible number of clients. Expansion

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[21] Information based on an interview with Marguerite Robinson, Harvard Institute of International Development.

is an ongoing process that can be achieved either horizontally — by increasing the number of retail outlets, thus widening the organization's geographical distribution; or vertically — by operating more intensively from existing units. Organizations have relied in the early stages mainly on horizontal growth.

Horizontal Expansion. Horizontal expansion is a relatively straightforward method of increasing outreach. To achieve it, each of the institutions has developed its own formula for replicating existing retail units.

One key to replication is keeping the retail units relatively small, efficient, and standardized. At BRI, GCC, and ADEMI's rural branches, the five or so staff members form a team. Thus, staff who have worked for some time as part of a team in one unit can easily be dispatched to create a new unit, with a good understanding of all the functions involved. The small size also requires little physical infrastructure, and thus the creation of a new unit does not require a heavy capital outlay.

Another element central to expansion is the flexibility of staff. Each organization designs staff descriptions to be applicable throughout its entire network. The basic responsibilities of a Grameen field worker, for example, are simplified such that virtually all of Grameen's staff understand the core of Grameen's operations through understanding the job of the field worker. This shared knowledge facilitates organizational cohesion and makes staff rotation easier. On the other hand, it may make it more difficult to add services in the future if those services involve increasing the responsibilities of each field worker.

Formulas for Horizontal Growth. Each organization has developed a clear formula to guide and make the replication of retail units routine. The formula is based on standard assessments of the break-even requirements for units.

Both BRI and Actuar use an amoeba formula: when the retail unit reaches a certain size (as determined by loan volume and number of staff), the unit splits into two equal-sized units that can eventually cover twice the geographic area, client base, and average portfolio. In both cases, the minimum and maximum limits of unit capacity are determined by the costs associated with unit operations; each branch must cover the costs of its own operations, and eventually, the indirect costs incurred by the superstructure for the additional branch. If the demand in a particular area is believed to be too low to achieve this, BRI's local units operate a small service post that has less capacity but also incurs lower costs. Maximum limits are determined at a rate well above the break-even point for the unit. ADEMI has calculated its ideal "block" size to be between twelve and fifteen loan officers, but will create a new block with as few as six staff.

As Grameen Bank strives to increase the number of villages in which it operates, it encourages its branch managers to seek out appropriate localities for establishing new branches. The standardized procedure requires the manager to become familiar with the locality and to prepare a report for the head office concerning the geographic, economic, demographic, and political issues in the area, as well as the level of infrastructure. If the report is approved by the head office, the branch manager will arrange a community meeting to explain the objectives and procedures of Grameen. Then the process of opening a new branch can officially begin. (Hossain, 1988) K-REP follows a similar process. After an initial staff assessment of a new location, a survey determines the demand and location of potential clients, and meetings are held with local leaders and existing savings groups.

The most striking similarity among these examples is the ability of the organizations to simplify—and, especially for Grameen and BRI, to decentralize—the procedures for expanding outreach. Final approval of senior management is almost always required, but it is worthwhile to note the active role played by branch managers, as well as field staff.

Because it involves moving into new and untapped markets, horizontal expansion can produce the high growth rates that many of these organizations have demonstrated, where doubling client outreach in one year is not uncommon (see Table 9). However, as they begin to fill in their geographic coverage, and as existing retail units reach capacity, growth levels off. The BRI unit system, which had nationwide coverage before KUPEDES was introduced, began to see slower growth rates by the time KUPEDES was three years old. Growth on the savings side did not slow as quickly in part because the unit system expanded horizontally into urban areas just as the rural areas began to be fully served (and these urban units have drawn much more savings than loans).

Grameen Bank has recently, after ten years of operation, achieved essentially nationwide coverage, a major accomplishment. It claims to operate in about half of all villages in Bangladesh, with relatively uniform coverage across the country, except in some of the mountainous border regions. Accordingly, since 1992, Grameen has begun to move into a consolidation period, with expectations of slower growth and greater emphasis on vertical expansion. BancoSol and Actuar are still in the horizontal growth stage, where increasing geographic coverage yields very high growth rates.[22] While several years remain before they move into a slower growth phase, they are already beginning to think about the strategies they will need.[23]

The shift from horizontal to vertical growth may be a difficult moment for these organizations, involving subtle as well as overt shifts in organizational focus.

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[22] .Actuar had limited its operations to the Bogota region until recently. It now plans to expand throughout the country.

[23] Eventually, these organizations will have to contend with challenges posed by market saturation and competition. These are subjects for future exploration.

During horizontal growth, the focus is on ease of replication, including all the elements just discussed that allow the replication process to go smoothly. This process is built on a proven set of delivery methodologies and retail unit operating procedures that do not have to be re-thought in each new instance. The focus is on starting new units and bringing them up to target activity levels. As this phase ends, productivity and profitability for the institution as a whole may increase. This arises from the maturing of the units, i.e., fewer units are in their low productivity start-up phase. Grameen Bank appears to be seeing this trend at present.

Vertical Expansion and Market Penetration. As an organization moves into a consolidation phase, the easy opportunities for expansion have been exhausted, and further expansion will come from vertical growth. Vertical expansion relies on increasing the productivity of existing structures, but as explained earlier, there is a limit to how much of this can be achieved. Achieving vertical growth may be difficult because it involves adjusting the retail unit formula that has been the basis for previous growth. One vertical growth strategy is to increase market penetration (ratio of clients per target group) within each unit's geographical area through more intensive outreach. This form of growth is compatible with horizontal growth since it eventually results in splitting units.

It should be noted that market penetration ratios at these institutions are not as high as some might expect. It is estimated that BRI serves about nine percent of potential borrowing clients and that its deposit accounts may meet more than one third of the demand for savings services.[24] Grameen Bank estimates that it serves 25 percent of its market. (Khandker et al., 1993) Consideration of these ratios suggests that for these institutions a strategy involving moderate increases in market penetration would be likely to yield significant expansion. On the other hand, for the microenterprise field as a whole, such figures suggest what the range of expectations should reasonably be. They indicate that not all households or entrepreneurs need or want loans, and that some entrepreneurs can meet their financial needs in alternate ways. In the future, competition will keep market penetration ratios down. This may already be a factor in Indonesia due to the existence of several competent microenterprise finance institutions. Certainly, planners of new microenterprise finance institutions would not want to set estimates of market potential using ratios higher than those achieved by leading institutions.

Vertical expansion can also mean adding new services for clients, thus intensifying the client relationship. Grameen Bank, for example, added housing loans and seasonal loans. The introduction of voluntary savings

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[24] Based on the assumption that approximately two-thirds of the 33 million families living in Indonesia are potential KUPEDES customers. (Richard Hook and Richard Patten, memo, May 1994)

services at BRI, and in the future, at BancoSol and Actuar, can be seen as a form of vertical expansion that may dramatically increase the number of clients. Actuar has an ambitious and well-conceived vision for vertical expansion. It has identified a range of financial and non-financial services for its clients that it believes it can eventually offer, using its comparative advantage in client contact based on credit as its starting point. This type of vertical expansion is difficult and risky, however, and must be approached systematically, as the following section on innovation describes.

VI.C. Managing Innovation

Strong microenterprise finance organizations are not content to remain static. They see the many needs of their clients and attempt to fulfill more of them by developing new services. Yet developing and implementing new services successfully present challenges to the organization that go far beyond the visible steps of defining and testing the service itself. Each new service must be integrated thoroughly into the organization, requiring changes in retail and superstructure operations, training, and the use of information. As the extensive discussions of productivity in earlier chapters have shown, microenterprise finance institutions have limited degrees of freedom in crafting financially viable operations. They must ensure that innovations fit well into the organization's overall operational equation. This section examines the experience of institutions in developing new services, looking first at the development of the basic savings and credit services that form the backbone of their operations, and then at newer, more specialized services.

The Phases in Introduction of Innovations. In concept, three phases can be identified in the development and implementation of any new service. The first phase involves defining the service according to what is known about client preferences, and testing the service to ensure that clients respond favorably to it. This phase answers the question: Is there a viable product? The second phase, which may overlap with the first, centers on fitting the service into the operations of the retail outlets. It answers the question: Is there a viable service delivery mechanism? Finally, the third phase integrates the new service into the operations of the institution as a whole, at both retail and superstructure levels.

The nature, sequencing, and relative importance of these three phases depend on the setting in which they arise. Organizations that grow as their services grow may work on all three phases at once as they develop their basic savings and credit products. Grameen Bank developed its services slowly through years of methodology testing during the late 1970s while it was still an experimental project. Thus, all three phases were developed simultaneously —one might say, organically. Actuar Bogota and PRODEM/BancoSol had the start-up advantage of using an off - the-shelf methodology that had been applied at several other institutions, and were therefore able to borrow not only

BOX 4

PHASES IN THE INTRODUCTION OF INNOVATIONS: THE BRI CASE

Phase I. **Is there a viable product? Market research; adaptation or development of methodologies; and testing client response to pilot services.**

BRI examined the economic and social status of clients and their financial service preferences and matched them with what it knew about service delivery to identify a loan product, KUPEDES, and later a savings product, SIMPEDES. These products, with several experimental variations, were pilot-tested in selected retail units. For example, in SIMPEDES pilot-testing, a variety of interest rate structures were offered, to determine how sensitive savers were to the rate of return. BRI carefully monitored client response, both quantitatively and through interviews, to determine if the products (and which of their features) were attractive to clients.

Phase II. **Is there a viable service delivery mechanism? Restructuring operations of the retail units on a pilot basis.**

This phase was crucial to the transformation of BRI's unit system into a financially viable operation. Nearly everything about the retail units was affected, beginning with their fundamental concept. No longer simply outlets for subsidized credit, they became mini-banks, with activities on both sides of the balance sheet, and responsibility for their own profits and losses. Following this change in concept were changes in the personnel structure of the units, in the basic activities entailed in each person's job, and in accounting and reporting requirements, all designed around KUPEDES and, later, SIMPEDES. Cost analysis was done of the pilot tests to see whether the services could be provided profitably, and to make adjustments accordingly.

Phase III. **Implementation: Introducing the new structure and services throughout the institution.**

This phase was a massive effort for BRI, involving virtually everyone in the organization. BRI's president-director introduced the "new culture," in which the units strive to serve their clients efficiently and profitably, as professional bankers, and emphasize accountability for performance. The new culture pervaded all aspects of the third phase.

A chief focus during this phase was staff retraining. BRI's retraining was led both by the needs to reorient the thinking of the staff towards the bottom line and to teach staff how to do their re-configured jobs — including, for the first time, real (though simplified) credit analysis and loan appraisal procedures that would require loan officers to exercise judgment and take risks. BRI established a large training center, but even so, it took several years before all staff members could take the retraining course. Meanwhile, supervisors were responsible for implementing the new services and procedures. Staff who were unable to adapt were transferred or encouraged to leave, and non-performing units were closed. Also at this time, management information systems were redesigned and implemented throughout the institution.

Because these changes were so far reaching, BRI delayed introducing savings services until the basic restructuring and introduction of the lending programs was essentially complete, to avoid overloading the system. Thus, SIMPEDES lagged KUPEDES by about two years.

the definition of the service, but also many of the institutional requirements needed to deliver it. During the early years, they adapted the methodology to fit their clientele and the service delivery and systems to fit their institutional character. Again, all three phases proceeded together.

BRI, on the other hand, was already a large scale institution when it began the KUPEDES and SIMPEDES programs. It therefore had to take each of these steps more systematically and in sequence (see Box 4). On the lending side, BRI took advantage of some pretested methodologies, developed at institutions such as BKK, the Bank Dagang Bali, and in BRI's own Kredit Mini program, allowing some shortening of the first phase. However, in developing SIMPEDES, BRI was charting new territory and had to go through each phase very carefully.

Similarly, as BancoSol develops a savings program, it is in much the same position as BRI, a large institution with a set of operations that do not include savings. While it can build on the experience of BRI, it must proceed systematically through each phase. At the time of writing, BancoSol is well on its way to being sure that it has a product clients find attractive. BancoSol must be thinking carefully about how the new savings services will change the staffing pattern and daily operations of its branches in a way that will maintain its already high branch productivity. For example, it must ask whether the addition of savings services will affect the loan portfolios of field workers and how to structure the weekly schedule to avoid bottlenecks for the tellers. The third phase will also involve far-reaching changes at the superstructure level.

A major point of this discussion is that introduction of new services has repercussions throughout all parts of an organization and cannot be undertaken lightly. In considering whether to introduce additional services, organizations must assess risks, costs, and benefits carefully. They must particularly be concerned with how the new service will affect the structure of their existing retail-level operations. The following examples show how institutions have handled a variety of innovations.

Grameen Bank. Grameen Bank has a broad concept of its mission, and therefore is willing to contemplate a variety of services beyond its basic formula. However, it faces organizational constraints in doing so. Grameen has made two major innovations in basic services since the original introduction of general loans: housing loans, introduced in the mid-1980s, and seasonal loans, introduced in the early 1990s. These innovations were added without changing the basic routines of the branches or field workers, although they have increased the number of transactions the workers must manage. The reporting requirements of a Grameen field worker have been significantly expanded, for example, even though the clients are the same as for general loans. However, the benefits these services provide in terms of overall branch profitability appear to outweigh the costs of those increases.

Another innovation, of sorts, was the adoption in 1984 of the Sixteen Decisions, a set of social development principles that each member is asked to commit herself to. The decisions can be considered a service product in that they offer something of value to clients. They represent a uniquely successful kind of innovation because they carry few operational costs -- only the time spent talking about them within Grameen and with members.

While these examples did not dramatically affect Grameen's retail unit operations, the complexity and riskiness of introducing new basic services may be one reason Grameen has hesitated to embrace voluntary savings instruments. With its very simple branch structure, featuring little functional differentiation between staff, Grameen faces two choices in adding a new service: it can either add the new service to the tasks of each field worker, forcing a risky revision of the carefully honed balance of field worker tasks, or it can add a different kind of worker to the branch configuration, which might disturb the balance of branch operations. Only innovations that do not alter these balances too dramatically can be accommodated.

Grameen has also been interested in diverging considerably from its familiar financial service territory, in areas such as fish hatcheries and textile manufacturing projects. Many of these projects began as add-ons to local branches, but Grameen has found it necessary to separate them from the branches, and eventually from the Bank itself, to ease the burden on management, systems, and staff and to increase financial transparency. A similar approach may be necessary if Grameen's current explorations of health care are developed into a service product.

At the retail level, Grameen Bank is willing to let its branches innovate, but very few of these projects become bankwide innovations. There are thus a large number of creative projects going on, but they remain localized at the center, branch, or area levels. It may be that Grameen's policy makers, aware of the limits of the Grameen system as a whole, hesitate to tamper with a highly successful formula.

Actuar Bogota. Like Grameen, Actuar has a broad concept of mission and is interested in widening its range of services. It has also followed a mixed strategy of incorporating relatively straightforward innovations into its basic retail structure while setting up new structures for services that might otherwise jeopardize their established retail operations. For example, it has been introducing legal advisory services simply by placing legal advisors at branches, without changing the basic structure of the branches.

However, when it sought to move from urban to rural areas, it developed this focus separately from existing operations, establishing what is expected to become a separate entity, AgroActuar. AgroActuar uses a different lending methodology and serves different geographic areas. Therefore, by establishing it as a separate division, Actuar could allow it to develop without worrying about its effect on urban operations. Similarly, Actuar's wholesale depot is managed as a separate entity, both organizationally and physically and will soon become a separate, for-profit company. Actuar's existing field workers do not actively participate in that operation, though they do promote its services among their clients.

Actuar's vision of even more innovative services results from its recognition of major market imperfections in the way formal markets serve the informal sector, and the conviction that microenterprise finance institutions have a great comparative advantage in identifying and implementing viable services that can attack those imperfections. However, most of the services are as yet untested and few precedents are available to guide their development. Actuar has developed an organizational concept in the form of a series of linked companies for allowing these services to be developed. Because of the highly experimental nature of the contemplated services (in areas including insurance, housing, health care, and social services), Actuar will have to emphasize Phase I, service product development and testing, and should expect that not all its attempts will succeed.

BancoSol/PRODEM. While BancoSol has been involved in developing savings services, PRODEM has been taking on more experimental efforts, particularly in rural credit. The sparse population and poor infrastructure of rural Bolivia means that the methods PRODEM developed for use in urban centers, which now form the backbone of BancoSol's operations, may not be cost-effective in rural areas. PRODEM is in the process of adjusting its methodology, based in part on the experiences of other rural programs. PRODEM has considerable institutional freedom to design a new system based on any methodology it finds effective as it has transferred most of its urban program to BancoSol, and it continues to operate in the subsidized environment of an NGO. As a formal financial institution, BancoSol is not yet able to take on such risky ventures.

K-REP. When K-REP opted to introduce its *chikola* methodology, its management decided to open new outlets, largely to avoid the potential confusion that could be made with its *juhudi* scheme if the two were operated side-by-side at one outlet. The *chikola* scheme lends to larger, preexisting groups, using a method similar to village banking programs, while the *juhudi* scheme requires the formation of new solidarity groups. To retain the distinction between these two programs, new units were opened in different geographic areas.

BRI. After establishing its basic services, the BRI unit system has introduced relatively few new products. Its main innovation has been its move in 1989 into urban areas, which required the creation of new units based very closely on the rural units. With minor adjustments, BRI also introduced a supplier-referred loan but discontinued it after it was found not to fit unit strengths.

In summary, if the appropriate methods are developed, a large number of potentially exciting services can be provided to the clients of microenterprise finance institutions. These institutions are very well placed to develop such services and may feel it is within their mission to do so. However, such innovations are risky and must be implemented systematically and with careful considerations of their effect on existing operations. In general, the number of additional services that can be successfully maintained by the retail units and their supporting superstructure is quite small. Therefore, new services often require separate organizational structures, in the form of either a new set of outlets (as in the K-REP example) or a wholly separate company (as in Actuar's approach), and the need for separation is greater for services that are not closely linked to credit and savings. Integrating additional services into the existing structure requires a great deal of organizational maturity and management competence, along with the recognition that the existing structure can handle only a limited increase in complexity. On the other hand, creating a separate organization requires strong policy-level governance, as well as careful thought about the relationship between the original retail outlets (and their clients) and the new service. Just as the structure of the retail units is closely tied to the methodologies being employed, the way the innovation is integrated into the system must fit the innovation itself.

VI.D. Coping with Crisis

No institution can be sure of its strength until it has been tested in stressful situations. Such stress can be brought on by a range of factors, both internal and external. Both BRI and Grameen experienced severe, externally generated stress in 1991, and are still feeling the ramifications of those events. BancoSol and Actuar have high internally generated stress, brought on by combined rapid growth and institutional change. ADEMI has weathered periods of high and fluctuating inflation. All the institutions have thus far withstood these stresses, often becoming stronger organizations as a result. This section reviews two of these crises as case studies, and then assesses their relationship to overall institutional competence.

Grameen Bank's Labor Cost Crisis. As noted in several places above, Grameen Bank was forced to raise its entire salary structure by 50 percent in 1991 to keep up with similar increases in pay for Bangladesh government civil servants. At the same time, labor union activists from both inside and outside Grameen began calling for the establishment of a labor union at the bank in ways that became at times quite uncomfortable for Grameen leadership. It became clear that Grameen would have to make vigorous responses to these related stresses in order to preserve institutional viability.

While maintaining adamant opposition to the creation of a union, Grameen management parried the labor union thrust by increasing salaries and creating a staff association through which staff complaints could be aired. These actions succeeded because they were credible responses to the underlying issues that generated staff dissatisfaction. Most staff were willing to agree that Grameen leadership would use (and is now using) the staff association in a genuine attempt to understand and respond to specific issues as they arose, in a less confrontational setting than that of a union. This result was particularly important to achieve, given the emphasis Grameen places on employee commitment to the organization.

To be able to make these concessions, however, Grameen was forced to raise its expectations of staff productivity. The immediate increase in salaries required Grameen to raise the nominal interest rate on general loans from 16 to 20 percent, only the second time that rate had changed in the history of the bank.[25] At the same time, the board of directors required that productivity levels increase enough to be able to reduce the rate again within a few years. In response, Grameen changed its standard expectations as follows: the maximum number of groups per center was raised from six to eight, while the maximum number of centers per field worker was raised from eight to ten. The result of these changes would be an increase in the client base of each field worker from 240 to 400, an increase of 67 percent for those at the maximum. These new expectations reflected a change in Grameen strategy from one of horizontal to vertical expansion and coincided with Grameen's achievement of essentially national scale. More recently, Grameen has added seasonal loans, another type of vertical expansion that also addresses the need for higher branch productivity, in which existing borrowers are offered additional short-term loans, thus increasing exposure per borrower.

The institution as a whole responded quickly to these policy changes. The number of members per employee (all employees, not just field workers) rose by 33 percent in 1991 and 38 percent in 1992, and the average number of members per branch jumped 17 percent in 1992 and 15 percent in the first half of 1993. (Khandker et al., 1993) While some of these increases can be attributed to the maturation of young branches, many are clearly the result of the policy changes just described. It became clear that the leading Grameen focus had changed from one of expanding by adding branches to expanding by increasing branch activity. Thus, Grameen Bank was able to turn a difficult situation to its advantage, using it as a springboard for productivity increases and strategic change.

BRI's Response to Indonesia's Financial Sector Crisis. Indonesia's financial sector was subjected to a very tight monetary policy by the central bank in 1991. Liquidity vanished from the financial system, and banks began competing fiercely for deposits, driving up interest rates. Several parts of Indonesia simultaneously experienced a severe drought, which affected the

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[25] A similar change occurred in 1984 when the interest rate was increased from 13 to 16 percent, following other commercial banks.

economic well-being of many BRI borrowers. These events had a significant effect on BRI as a whole and affected the units in a variety of ways.

The units were quickly identified as being a strong potential source of savings, and the BRI superstructure set a very high transfer price for units depositing funds with branches, particularly in comparison to KUPEDES lending rates, which did not change.[26] The increase greatly reduced the relative profitability to the units of making loans. Whereas the units had previously been seen as balanced entities, which raised the money that they lent, they now began to be perceived as sources of cash for the rest of BRI's banking operation.

At the same time, but independent of the liquidity crisis, BRI implemented a new policy that raised the maximum loan size limit at the units. In fact, an error in one of the policy circulars distributed throughout the system inadvertently omitted the requirement that larger loans go only to repeat borrowers. Although the mistake was soon corrected, many larger loans were disbursed during this period, especially because some branches, also facing the liquidity squeeze, were known to pressure units to lend to some of their borrowers.

All these factors combined to produce two effects, particularly in the drought-affected areas. Most importantly, there was a significant increase in the default rate. By the end of 1991 it had reached 8.6 percent, more than double the previous year's rate of 4.1 percent. It stayed above 9 percent for most of 1992. Secondly, KUPEDES lending declined; for the first time, there was a negative growth in the number of active KUPEDES clients in 1991 (-3 percent; see Table 9), and the following two years have seen only negligible positive growth.

The increase in arrears compelled BRI management to implement several policy measures that further reduced the incentive for units to lend. These included direct limits on the percentage increase in lending, interruption of lending at some units with particularly high arrears, a decrease in the maximum caseload of credit officers from 600 to 400, and a directive that credit officers with more than a certain percentage of loans delinquent would be subject to dismissal (a drastic measure in the Indonesian context, and one that had an inhibiting effect on the willingness of loan officers to make loans in the first place). As the liquidity crisis gradually subsided during 1992, BRI altered several of these policies, redirecting incentives back into lending, and has focused a great deal of effort on reducing defaults. Now that the arrears rate has begun to come down (to 7.5 percent in 1993), the transfer price has been readjusted to give maximum incentives to lending. The KUPEDES program is thus growing again and, with the decreasing arrears rate (since mid-1992),

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26 The reader is asked to remember that BRI's units are the retail outlets for KUPEDES and SIMPEDES, while the branches supervise the units as well as make loans to larger scale clients on their own.

it appears that the crisis has been weathered. However, the shift back toward lending has been slow and difficult, a result of both external shocks and internal responses. The policies instituted to cope with the crisis may be compared to strong antibiotics that cure the disease but leave the patient in a weakened state.

The events of 1991 and 1992 at BRI illustrate a number of lessons. First, they show how important it is for institutions to keep track of key indicators, noting trends before they become problems. Because indicators tend to lag behind the events that created them, once a trend is spotted, it is likely to have enough momentum to continue despite the implementation of policies designed to alter the relative incentives. This has certainly been true of BRI's arrears experience. The events also show how sensitive the retail units are to policy changes; even what might appear to be minor policy changes had major effects on lending behavior. And for BRI specifically, where the unit system remains dependent on its parent institution, the events show how the forces operating on the larger bank can have far-reaching effects in the unit system.

The experiences of both Grameen and BRI reveal how a sound institution must be able to react to the inevitable crisis in a flexible manner. In light of the complexities involved in microenterprise finance, all of the institutions in this study will at one time or another be faced with situations that challenge them. The macroeconomic policies of the respective governments, which affect everything from interest rates and inflation to the regulatory environment in which the clients operate, can be a source of external crisis. At the same time, as these institutions become larger and more national in scope, they face internal growing pains that can be just as challenging, as the labor crisis at Grameen and the strains on staff during PRODEM's transition to BancoSol have illustrated. However, competent microenterprise institutions have a depth of skills and resources to be able to withstand many such stresses.

VI.E. Conclusion: The Challenges of Growth and Change

By examining microenterprise finance organizations as they deal with major cross-cutting issues, this chapter has further identified some of the specific traits common to successful institutions. These include strong and stable leadership, i.e., active boards, multi-talented and committed executive directors, and senior managers able to take on increasing levels of responsibility. It has shown that such institutions take a systematic approach to policy making, vesting such responsibility in more than one person and making policy changes through formal channels. Similarly, growth and innovation are carried out in a highly systematic fashion. All the high-growth institutions have very standardized approaches to horizontal expansion through the replication of retail units. In introducing innovations, the institutions move carefully through product identification, delivery system design, and full implementation, and they respect the limits of their retail units in managing increasing complexity.

This chapter has also identified some of the major challenges for the future that face the mature microenterprise finance organizations, one of the most important of which is the evolution of leadership and eventual leadership succession, an issue few institutions have faced. It is clear that successful transition of leadership requires some years to lay the groundwork, and the time to begin thinking about succession is well before it actually happens.

Another challenge, imminent for some institutions, but more distant for others, is the change from a mainly horizontal growth strategy to a more difficult vertical growth strategy as wide geographic coverage is attained. Closely related to vertical growth is the introduction of innovations. Institutions have on their horizons an exciting array of potential innovations, in varying degrees of planning and implementation. These innovations will take the organizations in increasingly diverse directions and must be managed in a way that enhances the existing base of credit and savings activities.

Finally, this chapter has illustrated the dramatic effect external and internal shocks can have on institutions, and noted that quick and well-designed policy-level responses are crucial for responding to such challenges. These microenterprise finance institutions, especially the larger ones, necessarily have elements in their design that limit flexibility in pursuit of high productivity. However, they retain enough flexibility to remain resilient, and, in some cases, to turn external shocks into opportunities for improving operations.

CHAPTER VII

SUMMARY:
ELEMENTS OF COMPETENCE OF MICROENTERPRISE FINANCE ORGANIZATIONS

This monograph has examined the institutional structure of some of the most successful organizations providing microenterprise finance to the poor in developing countries. While the operating environments, missions, and corporate cultures of these organizations are quite different, our analysis has shown that certain characteristics are common across institutions. These elements are underlying principles for the provision of microenterprise finance and the growth of the related institutions. Box 6 summarizes these conclusions.

This monograph has focused on the elements of institutional competence which, along with methodology, allow these institutions to (1) become financially self-sufficient, (2) expand outreach to a nationally significant scale, and (3) survive over time. By comparing the programs highlighted in this study, we have begun to identify some of these elements. The most striking theme developed here is the strong relationship between the service delivery methodology and the institutional structure: retail outlets are designed to fit the chosen methodology of an organization, and superstructure functions are all designed to support the retail outlet pattern described in Box 3. The key to successful expansion and growth is found in the strength and productivity of these retail outlets.

A second theme presented here is that strong microenterprise finance institutions are focused on achieving high productivity. As the institutions become increasingly formal financial institutions, and especially if they introduce savings, the focus on productivity evolves into a focus on profitability. Organizations must be able to maintain a dual focus on their special mission (e.g., serving the poor) and on profitability, a balance maintained only through strong corporate culture.

This monograph has also described how effective information flows and human resource development policies support the achievement of productivity. While productivity and profitability are certainly necessary for institutional growth, this comparison has shown that such goals can be achieved in a variety of ways within an overall framework and set of principles. In comparing institutions, it remains striking that many of these organizations have chosen to tackle crucial decisions of growth and change in similar ways, and that so many generalizations can be made.

BOX 6

ELEMENTS OF INSTITUTIONAL COMPETENCE IN MICROENTERPRISE FINANCE ORGANIZATIONS

I. Scale

- The leading microenterprise finance institutions have achieved active portfolios from several million dollars to hundreds of millions, and serve more than 10,000 clients (up to one million); such levels of outreach constitute a potential vision for other aspiring organizations.
- Delinquency is held well below 8 percent and long-run loss ratios are less than 4 percent, often far less.

II. Financial Structure and Institutional Type

- Microenterprise finance institutions can have many different origins and institutional types, underpinning surprisingly similar operations.
- Mature organizations gain access to funding from the local financial system and from their own clients. They must develop strong financial management in order to achieve such access.
- The development of formal financial institutions is emerging as a trend, and it is often necessary to move from depending on international donors to depending on the local financial system.

III. Operational Structure and Productivity

- ***Retail units*** are designed to fit closely with methodology and usually comprise standardized staff functions and routines.
- The ***superstructure*** functions both as a service provider and a control mechanism, and achieves a careful balance between each.
- Retail units must focus on achieving high ***productivity***. Because salaries are such a high percentage of total costs, profitability depends more on high staff productivity than on cost controls. Currently, unit staffs can handle between 115 to 280 credit clients per unit staff, and many more savings clients if voluntary savings are offered.
- Costs as a percentage of average portfolio range from 12 to 25 percent, with the higher percentages occurring in organizations facing high salary structures. Organizations face pressure to increase loan sizes in order to lower that figure, but must consider whether such a change fits the organization's mission.

BOX 6

ELEMENTS OF INSTITUTIONAL COMPETENCE IN MICROENTERPRISE FINANCE ORGANIZATIONS (cont'd)

IV. Managing Information

- Successful institutions are driven to focus at all levels on a few key indicators of performance. For some, especially growing NGOs, these key indicators are numbers of loans or portfolio quality.
- Evolution to a focus on profits internalizes concern with cost control and provides incentives for high productivity directly within retail units. The profit center focus is supplemented by monitoring of portfolio quality and loan size.
- High quality information systems are timely, relevant, and accurate, and serve all levels of an institution, including clients, field workers, supervisors, and policy makers. Information systems must guard against overwhelming users with too much data.
- Computers are not synonymous with information systems. Good information systems are possible without computers at the retail level. Computers should be viewed only as a productivity enhancing tool.

V. Human Resources

- Successful organizations recruit young people with little prior job experience, who demonstrate the ability to work in the informal sector and to absorb the corporate culture.
- In-house training is a process of passing highly job-specific information from existing staff to new recruits. It relies on oral tradition and learning-by-doing, supplemented by classroom reinforcement that emphasizes corporate culture.
- Successful organizations employ a wide range of staff motivators, including commitment to organizational mission, good prospects for career advancement, organization of units as teams, attractive salaries and benefits, and specific incentive programs.

VI. The Living Organization

- Strong leadership is not a matter of "charisma," but does require extended commitment to provide continuity to the institution, as well as a combination of talents such as operational knowledge, external relations, and the ability to motivate people.

BOX 6

ELEMENTS OF INSTITUTIONAL COMPETENCE IN MICROENTERPRISE FINANCE ORGANIZATIONS (cont'd)

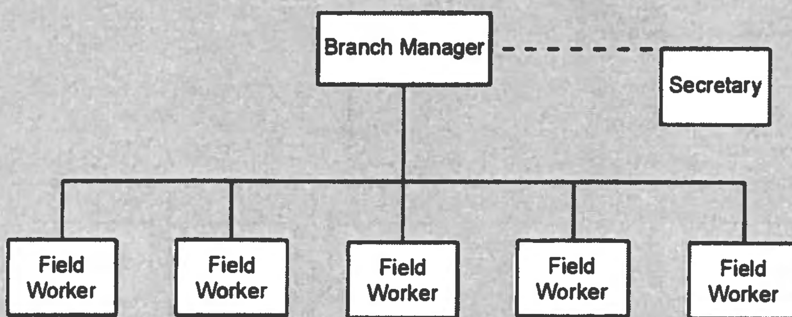
VI. The Living Organization (cont'd)

- Active boards of directors and competent senior staff are essential, particularly as the role of the executive evolves, and leadership succession is faced.
- Organizations have achieved high growth based on "horizontal" expansion into new geographic areas, often consistently above 20 percent. "Vertical" growth within existing areas is more difficult as it challenges their successful retail unit formula.
- Innovation requires systematic attention to three stages: product and market identification; delivery system design; and organization-wide implementation. In considering new services, the limits in capacity of existing retail units must be respected.
- Leading organizations have shown resilience in coping with inevitable crises that any microenterprise finance organizations may one day face. Swift and sure policy-level action is crucial in helping organizations adjust to major shocks.

APPENDIX

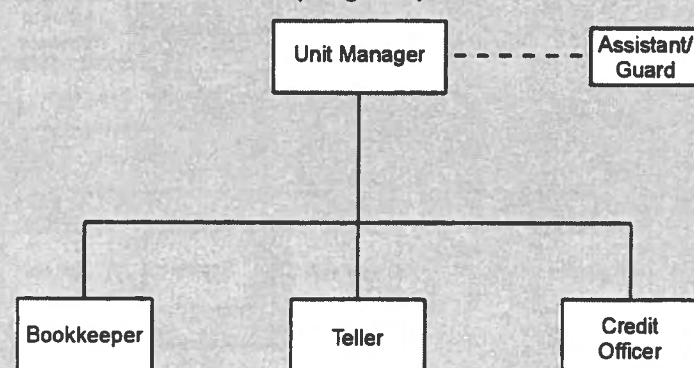
THE RETAIL UNITS OF MAJOR MICROENTERPRISE FINANCE INSTITUTIONS

Grameen Bank (branch)



(up to 9 field workers, larger branches also have assistant branch manager)

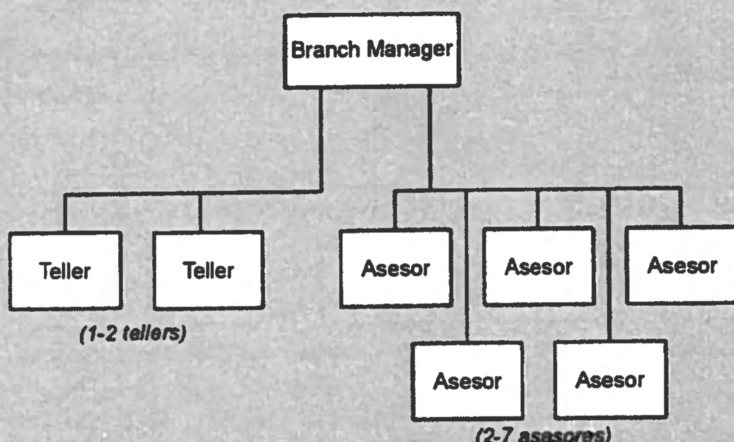
BRI (village unit)



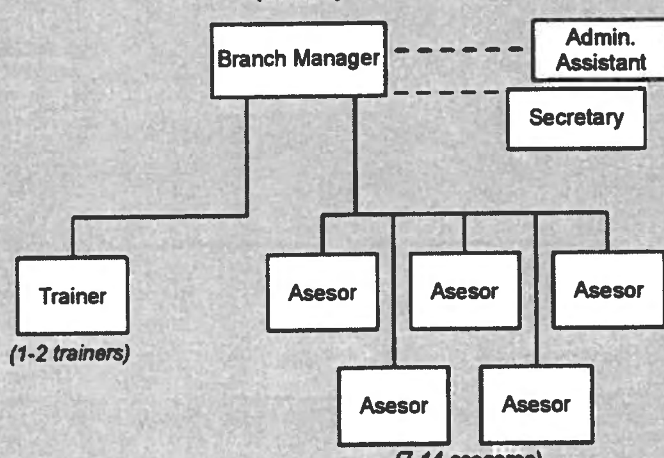
APPENDIX

THE RETAIL UNITS OF MAJOR MICROENTERPRISE FINANCE INSTITUTIONS (cont'd)

BancoSol
(branch)



Actuar Bogota
(branch)



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ACCION's goal is to make financial services available to poor entrepreneurs through permanent, self-sustainable microfinance institutions that are part of the financial systems in their countries. ACCION has played a key role in the creation of a number of fully commercial microfinance institutions including BancoSol in Bolivia, Mibanco in Peru, BanGente in Venezuela and FINAMERICA in Colombia. ACCION's Latin American Network is comprised of 19 affiliated microfinance institutions in 13 countries, including 9 regulated microfinance institutions. In 1991, ACCION brought its microlending experience to the United States to foster economic growth in distressed neighborhoods, and currently works in 12 cities.

From 1991 to 1998, the ACCION Network has disbursed $2.2 billion in loans averaging about $600, providing loans to over 1.6 million microentrepreneurs, over 60% of whom are women.

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