

### **Speech before the European Parliament on 2 December 2010 The European Progress MicroFinance Facility**

Thank you for having requested my view concerning the new European Progress Microfinance Facility that joins the existing "JEREMIE" and "JASMINE" initiatives. Progress, endowed with 200 million euros of funding by European authorities, constitutes a major step forwards for the financing of microfinance institutions in Europe. However, there still remains much to be done to create an institutional framework that is favourable for microfinance in Europe.

After a short analysis of the situation for microfinance in the European context, I will share some thoughts on microfinance practices and, to conclude, what is expected from Progress and its limits.

#### **BNPP and microfinance**

BNP Paribas' experience in microfinance is relatively unique, to the extent that it is oriented both towards Europe and towards countries in the Southern hemisphere, combining sponsorship, volunteer work and banking activities. BNP Paribas is one of the oldest players committed to microfinance in Europe: indeed, from 1993 onwards BNP, on the one hand, and Paribas, on the other, both started to back ADIE.

Our microfinance activity is based on three areas:

- **Corporate philanthropy in France**, with financial support of around one million euros per year for ADIE and, in particular, its support since 2005 for the *Projet Banlieue*, a social programme focusing on underprivileged urban neighbourhoods.
- **Skilled voluntary work**, with two associations counting around 150 volunteers each. Both these associations supported by the bank are open to BNP Paribas' current and retired members of staff. One (called *Bénévolat de Compétences et Solidarité*) is particularly active in France, where as a gesture of solidarity its members volunteer their skills to help ADIE's micro-borrowers. The other (*Microfinance sans Frontières*) provides technical assistance to microfinance institutions worldwide.
- **Banking activities** that seek a social impact at the same time as fulfilling our job as banker or investor. These activities comprise first and foremost financing (9 million euros for ADIE and 50 million euros for 17 microfinance institutions in 8 Southern Countries, having a social impact on around 300 000 borrowers). Then comes investment in microfinance funds for individuals and institutionals.

BNP Paribas Fortis and ADIE have joined together at the end of this year to create a common structure called MicroStart, which will grant micro-credits in Brussels to begin with and then throughout Belgium. This new structure, which should begin operations at the beginning of 2011, will be one of the first beneficiaries of the Progress Facility managed by the EIF.

#### **Microfinance in Europe and the world**

The European microfinance context is very specific compared with Southern Countries, where microfinance was developed from the 1960s onwards. In Europe, 95% of the population has access to banking facilities whereas in the Southern Countries 95% of the population does not have access to banking facilities.

In the global microfinance universe, Europe is almost invisible. On the basis of statistics from the European Microfinance Network for 2009, European microfinance represents 136 000 micro-

borrowers and 784 million euros of capital, which respectively represent less than **0.1% of the borrowers worldwide and 2% of the capital**.

Although European microfinance is still microscopic, its growth potential is enormous. In 2007, the EIF estimated the potential demand for microfinance in Europe to **700 000 borrowers and 6.3 billion euros of capital**. These figures appear ambitious compared with the current situation (borrowers multiplied by 5 and capital multiplied by 8). This estimate is based on a very conservative figure of 3% of people interested in creating their own business actually taking action and realizing their project. **Due to the social crisis in Europe, demand is probably much higher now than this 2007 estimate**. In fact, 79 million Europeans live below the poverty line, that is to say 17% of the European Union's population, and only half of them are working or looking for work. In addition, unemployment affects almost 10% of the workforce or, in other words, 24 million European citizens.

In such a crisis situation, microfinance as a social policy tool effectively meets a need. **The existence of a demand is undeniable**. The question is how to satisfy this demand in a context of public budget constraints.

### **Three reflections on current practices**

It is a fact that **the least developed countries are the ones where microfinance is the most developed**. Latin American and Indian countries can draw on over 40 years' experience that may be useful for Europe. I would like to highlight three areas of reflection.

**1) On the economic model and interest rates:** this point appears to be the main obstacle to the development of microfinance in Europe. In many European countries, it seems almost inconceivable to make poor borrowers pay high interest.

As early as the 16<sup>th</sup> century, a moral and theological debate opposed the Dominicans and Franciscans on the question of whether the newly created *Monte di Pietà* in Italy could morally charge interest to the poor they was financing. The Council of the Lateran settled the matter in 1515, ruling that management costs had to be covered but that the interest rates must be reasonable. Our debates in Europe are often new echoes of this ancient quarrel.

**In the Southern Countries, the average interest rate practised worldwide in microfinance is 30%**. These rates must be compared with those practised by moneylenders that can reach 20% a day in the Philippines and 200% per year in India! In the United States and Great Britain, pawnshops practise interest rates ranging from 200 to 400%. Interest charged on revolving consumer credit in Europe is around 20% for a much lower risk than that on microfinance.

Just as in the rest of the world, microfinance in Europe implies **high costs** due, amongst others, to the allocation of small amounts, risk cost, qualified personnel, and measures to assist and accompany clients. According to the European Microfinance Network survey on microfinance in Europe, published in June 2010, only 60% of the institutions polled cover their costs, with a risk portfolio standing at 16%. Such a situation is not sustainable over the long term.

Interest rates of 25% in microfinance shock Europeans, with the exception of the British and Eastern Europeans who are used to such rates. A 5% interest rate is certainly preferable to 25%, but is not realistic without subsidies. **Reflection on an acceptable interest rate is essential since zero cost does not exist:** at a given moment, all public or private sponsors must ensure the sustainability of their model, for example by subsidising measures to assist micro-borrowers or by mobilizing volunteers as we do at BNP Paribas with ADIE, which enables the wage base to be reduced.

## 2) Supervision, regulation and self-regulation

In Southern Countries, microfinance institutions have often created their own rules in the absence of appropriate regulations. Products of the informal world, they often finance people with no identity papers, or no title deeds for their home or business.

Microfinance institutions have often made the **regulatory framework change**, in both the Northern and Southern hemispheres. The case of ADIE in France is exemplary with the abolition of excessive interest rates, exceptions made to the banks' monopoly to lend, and the authorization for microfinance associations to borrow for lending.

In September, the **Basel Committee** published a paper on microfinance, that seems to have gone almost unnoticed in Europe. For the Basel Committee, microfinance does not constitute a systemic risk for the financial system, so very detailed regulation and supervision is not justified. On the other hand, a certain amount of expertise is necessary at the supervisor level to ensure understanding of this sector that is very different from that of classic finance.

In this respect, **France** is exemplary as regards regulation and supervision, with the creation of a microfinance research institute by the Banque de France, and a report submitted to the Tax Inspectorate after the consultation of around a hundred experts. The existence in France of an emblematic organization, the ADIE, and of a banking community that supports microfinance, contributed to creating this favourable institutional framework.

Beyond the importance of regulation, the **importance of self-regulation** must be emphasized. The microfinance crisis in Morocco in 2008 and the situation in Andhra Pradesh in India are currently drawing attention to the risks of deviation in microfinance as the original social objectives are forgotten or borrowers become overburdened with debt. The lessons from these crises apply to Europe: self-regulation and the exchange of good practices constitute the best guarantees for responsible microcredit.

## 3) Microfinance and European citizens

The success of microfinance in Europe depends on **raising the awareness of European citizens, who are also investors** increasingly interested in investing with responsibility and solidarity. From this viewpoint, two different avenues can be explored:

- **With websites such as Kiva in the United States, and Babyloan and MicroWorld in France, the Internet** enables individuals to take action with amounts starting from 20 euros and to personalize their loans (choice of country, institution and project). Babyloan and MicroWorld have both been accredited by the Banque de France insofar as they deal in interest-free loans and therefore not in investment. Together with ADIE, Babyloan has obtained a change in the French Monetary and Financial Code, thereby allowing Babyloan to lend to ADIE's borrowers in France. In order to protect individuals effectively, the supervision of this type of website is essential.
- **Microfinance funds** are currently reserved for institutional investors, with the exception of two countries in the European Union – the Netherlands and Luxembourg – and of Switzerland. However, over the last 30 years, these funds that lend to microfinance institutions have proved that they have a significant social impact, that they control risks and that they have a satisfactory profitability. At best, individual investors can invest in diluted funds (with a maximum of 10% invested in microfinance), which dilutes the social impact accordingly. The European Microfinance Platform's working group, that I initiated two years ago with several banks and specialized funds, has put forward specific proposals on the need to define a regulatory framework for these funds at the European Union level.

## **Conclusion: what can we expect from Progress?**

In the context of social crisis in Europe, microfinance as a tool for financial inclusion corresponds to a **real need**. The initial estimate of 700 000 borrowers and 6 billion euros of credit is probably exceeded today given the extent of the crisis in Europe. The essential issue is to find an economic equilibrium for European microfinance that will enable it to **cover its costs** on a lasting basis. This implies an adaptation of its legal framework requiring consciousness-raising among regulators and supervisors. The regulation of microfinance websites and funds – that increase European citizens' awareness of microfinancing – also constitutes an important issue.

In this context, what can we expect from Progress? Expecting too much risks causing considerable disillusionment. Excess liquidity from Brussels or Luxembourg could have a damaging effect. The success of Progress will depend not only on the mobilization of European authorities, in particular the European Investment Fund, **but also on the capacity to mobilize partners at the level of member States**: local financial players becoming involved to top up European funds, as well as regulators and supervisors in order to improve the institutional framework.

From this viewpoint, the more than 17-year old cooperation between BNP Paribas and ADIE can serve as an example, as can the new partnership between BNPP Fortis, ADIE and the EIF in Belgium.

I thank you for listening and will be happy to answer any questions you may have.