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# FONPRODE AND THE FUTURE OF FINANCIAL INCLUSION FROM SPANISH COOPERATION\*

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In 1998, the Spanish Cooperation launched the microfinance program, through the creation of the Microcredit Fund, managed from the Spanish Agency for International Cooperation for Development.

Since then, FCM has actively contributed to the financial inclusion of hundreds of thousands of people through its credit program to microfinance institutions, the technical assistance programs and the conducting of numerous activities and studies on evaluation, organization and management. From its work during these 13 years, the Microcredit Fund has contributed to establish AECID as one of the major international donors in microfinance and financial inclusion. AECID not only maintains an active portfolio of loans of close to 500 million Euros, but has also strengthened its partnerships with key bilateral and multilateral actors such as the World Bank, Inter-American Development Bank, African Development Bank and the United Nation's Capitalization Fund. Its main area of influence is in Latin America, but has a special interest in increasing the work in sub-Saharan Africa and Southeast Asia.

Similarly, in Spain, AECID has strengthened its viewpoint and its training in micro-management, not only through its work with various NGOs, but also with the academic and the private sector.

Through this experience, the Spanish Cooperation has accumulated an important practical, theoretical and methodological background in microfinance management. However, the past two years have seen a turning point in relation to the approach of the AECID to the financial inclusion. There are several factors that have catalyzed this new period.

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Firstly, the microfinance sector itself and financial inclusion are facing a major debate about their goals, their social impact and their results in terms of development. The evidence of impact on development and poverty reduction of microcredit as an instrument is currently being argued of both theoretical and practical grounds, both in the academic sector and when it comes to public opinion. Indeed, access to credit constitutes “a human right” according to Professor Mohammed Yunus, but the fact that this is necessary to achieve poverty reduction does not necessarily mean it is enough. In fact, indiscriminate and uncritical use can even be counterproductive. The dramatic cases of default in payment and delinquency with microcredit programs, which have arisen in recent months, indicate that a misdirected microcredit program whose risks are not properly calibrated, can not only not help at all to their clients out of poverty, but also eliminate this possibility for several years.

Secondly, the complexity of the microfinance sector itself, which has gone from being led by NGOs and credit unions, to the emergence of microfinance institutions which are professionalized and have a higher level of financial development, being able to identify the “bottom of the pyramid”, not only as an area for action in the fight against poverty, but also as a new sector of the financial markets, with its own dynamics. This has increased the facilities and services offered, such as micro-insurances, micro-savings, or mobile banking, while also attracting sophisticated resources through venture capital funds or the issuance of bonds in domestic and international markets.

Thirdly, the emergence of new sources of funding, especially remittances from immigrants who have managed to become, in many developing economies, the main source of foreign financing. Apart from international remittances, we should draw special attention to internal or domestic remittances, originated in the industrial and economic centres for rural communities. Most of these new funding sources are for families, and in many cases are aimed for direct consumption or investment in housing. They are used for business projects in a much lower percentage.

Fourthly, and as a result of the above factors, the establishment of international standards, guides, social and financial performance, and management mechanisms approved at a national and international level. The systematization of the practice of microfinance institutions requires a process of transformation and professionalization of the management of microfinance initiatives, which require not only performance guides, but also highly qualified professionals to ensure not only their impact in the fight against poverty and exclusion, but also the financial viability of the entities.

These internal factors are compounded by the very process of transformation of the financial instruments of Spanish cooperation. Thus, the creation in 2010 and implementation in 2011 of the Fund for the Promotion of Development has been a significant change in the financial and technical implementation of financial inclusion programs for Spanish Cooperation.

The FONPRODE, approved by law in October 2010, assumed from the beginning of 2011 the work of the Microcredit Fund, and features these projects from a financial functionality, by overcoming the traditional credit scheme that allow microfinance institutions investment operations, through guarantee funds, venture capital, lines of credit and contributions to multilateral institutions.

Several principles situate FONPRODE as a financial instrument for Spanish Cooperation:

Firstly, the acknowledgement that the mere strategic provision of concessional funds is not enough to ensure the fight against poverty. On the contrary, the increase in private external financing in many developing and emerging countries can have a pernicious effect on the price increase, with the consequent deterioration of the purchasing power of the poorest. External financing must be accompanied by adequate financial development in both the regulatory and the financial infrastructure, as well as in the soundness and effectiveness of financial institutions. It is through proper financial development and external funding that we can achieve sufficient results to boost the productive sector, especially in those areas where such funding is most needed.

Secondly, the FONPRODE's adoption of the responsible lending code, approved by its Executive Committee in accordance with the law, imposes the strict establishing of rigorous controls on the social and environmental impact, as well as impact on gender, not only following specific recommendations for the microfinance sector, but also those social and environmental standards that form the key principles of finance for development.

Thirdly, the very instructions of the Committee for Helping Development, which, in terms of funding for microcredit, has strengthened the components of concessionality for loans in a context in which interest rates in developing and emerging countries converge with market and official rates in developed economies, thus questioning the potential additional funds that donor countries could provide to developing countries.

These three factors, strategic orientation, social performance, and new perspectives on the concessionality of funding, define a new framework for

the intervention of Spanish Cooperation in the field of financial inclusion. This is why FONPRODE should, in the following months, develop a new approach to microfinance.

Some thoughts on this new intervention framework could be summarized in the following points:

- When possible, Spanish Cooperation will strengthen partnerships with those institutions and networks that share a similar vision of the microfinance environment. The experience of the implementation of the Microfinance Fund for Africa in cooperation with the African Development Bank and the United Nation's Capitalization Fund, should serve as a test to create synergies, joint action and regional strategic thinking. The AECID is working in the same direction, with other public and private institutions.
- Considering that the primary focus of interventions should be based not only in the provision of funding for microfinance institutions, but also in supporting their strategic and institutional reform, Spanish Cooperation will focus on the contributions of capital and entry into the boards of institutions, promoting modernization of the sector and its institutions through a direct presence in its management.
- Moving forward from microcredit, Spanish Cooperation will extend its scope to the entrepreneurial initiatives related to small and medium enterprises, putting funding where it is most useful in terms of employment generation and productivity. Likewise, new possibilities in terms of banking support, micro investment and micro-savings will be explored, as well as mobile banking initiatives.
- Finally, the management of the microfinance portfolio will be integrated, both financially and technically, with all FONPRODE operations, complementing the whole strategy of support to social productivity, both in technical and methodological terms.

From these issues, AECID now faces a new cycle in its cooperation in microfinance, with the aim of contributing to a broad debate with all parts, networks and microfinance institutions, universities, and bilateral and multilateral agencies on the future of microfinance and financial inclusion. In this sense, the implication of Spain in the Global Microcredit Summit is an excellent opportunity to explore new perspectives for the sector.