MICROFINANCE IN DEVELOPED COUNTRIES*

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Microfinance in developed economies

Microcredit, an idea which was born in a developing country, is becoming an increasingly useful financial instrument in the current context of developed countries in Europe.

Since the 90's, various entities, including the social programs of some Saving Bank's, pushed for the provision of microcredit in order to contribute to the funding of self-employment projects, in order to promote a working autonomy and to achieve the social integration of those people who may be victims of exclusion or vulnerability.

This first approach, directly inspired by a model which was born in order to drag families out of poverty in developing countries, has required multiple adjustments to accommodate the important differences between the context of emerging countries and developed European countries.

Firstly, the nature of poverty is different in these two contexts: in developing countries, poverty is the deprivation of access to basic resources for survival, whereas in European countries, even though there is a part of the population suffering severe poverty, there are social assistance mechanisms in place which will cover some of these needs. This is why the actual concept of poverty in developed countries will gradually drift to mean a lack of development opportunities for individuals and families.

Due to the economic crisis across Europe, a growing percentage of Europe's population is now in this situation known as "relative poverty". These are families and individuals that were not previously economically vulnerable but have now come to this situation due to job loss.

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While in developing countries self-employment may be the best and sometimes the only alternative for people suffering from exclusion to generate income, in most developed economies being employed by someone else as opposed to being self employed may be the best option and provide more opportunity.

The more competitive economic environment that exists in more developed countries will lead to an increased demand when the time comes to formulate new business proposals. In less developed economies, the will and skill of an individual may be enough to initiate a project of self-employment. However, in more competitive economies, entry barriers such as training, competition, investment, finance, technology and legislation will pose a much greater level of demand. Therefore, without ruling out the fact that self-employment is a good way of creation of employment for vulnerable groups, the above mentioned reality makes this option unreachable for many people who do not have the skills or resources to successfully promote a project in such a competitive environment.

Going beyond the adaptation to the contextual factors that the concept of microcredit has required in its implementation process in developed economies, it has also been necessary to adjust the characteristics of such operations in order to make this tool socially and financially compatible.

The extension of the loan amount to 25,000 euros, while in other developing countries the amount of microcredit only goes from 18 to 250 or 300 dollars, depending on the country, is one of the main changes that have arisen from the higher level of investment required for setting up a business in developed economies.

Investment needs in developed economies require that the full funding is granted at the beginning of the project and the total amount is generally needed upfront. However, in the original model, the funding would be given progressively. Paying back the first amount would the lead to a second microcredit, which will in some cases benefit from a longer period for repayment.

Other characteristic which has had to be modified is the amortization period of operations. For example, in the case of MicroBank, the repayment period is six years, with the option of six additional months of grace already included in this period. On the other hand, countries like Bangladesh, the birthplace of this financial tool, the deadlines would be ascendant, as discussed, ranging from eight weeks to two and a half years without the possibility of period of grace, because in most cases the loan must start to be repaid after one week of issuing the microcredit.

The interest rates are another main difference. In Spain, the interest rate is generally similar to the one applied by commercial banks in their operations or, at most, slightly higher in order to pass on higher operating costs and the implicit premium risk in these operations. One consequence of this is that the margin of these operations in developed economies is so small that the microfinance institution will not be able to assume the cost of accessory services such as counseling, tutoring, weekly payment “at the door”, etc., while microfinance institutions in emerging countries will cover this with the larger margin. In our model, these additional services are provided free of charge by over 420 organizations working with MicroBank.

Another principle of operation that has also needed to be modified is the group structure of the microcredit beneficiaries, which had generally been considered an inevitable requirement in the model applied in emerging countries. When adapting the model to developed economies, the group structure has disappeared, which means that the principle of shared responsibility among the group of vulnerable applicants does not exist, so the capability for repayment will be more vulnerable.

The impact of microcredit on employment generation in developing countries

Even though we often identify the ability to create jobs with large companies and multinationals, 98.7% of European and Spanish companies, are either small companies or micro businesses (businesses with less than 10 employees), and it is precisely in this range where they generate the most employment opportunities. Such businesses employ 49.5% of European active workers[1].

In the present context, the contribution to the creation of new employment opportunities and the permanence of existing jobs becomes vital in the fight against exclusion from employment, a basic requirement (although not the only one) in order to maintain the social cohesion that would be partly responsible for the economic recovery and the progress of our country.

1. Data from the European Statistical Office, Eurostat. Latest report available: June 2008.

Table 1. European businesses by size and other indicators

	Number of enterprises	Persons employed	Value added	Aparent labour productivity
	Share in total (%)			Relative to total (%)
All enterprises	100.0	100.0	100.0	100.0
All SMEs	99.8	66.7	58.6	87.8
Micro	92.0	29.0	21.8	75.3
Small	6.7	20.5	18.6	90.5
Medium-sized	1.1	17.2	18.2	105.3
Large	0.2	33.3	41.4	124.5

Fuente: Eurostat.

Nonetheless, access to bank financing by these microenterprises is especially difficult because, for traditional banks, these small operations entail high of management costs and do not have enough guarantees to compensate the credit risk.

La Caixa bank, after an initial experience in the field of microcredit through its Social Program, in 2007 opted for an ambitious new strategy with the aim of reaching out to provide funding through a financial instrument of great social value, microcredit, but this procedure is now under a new model of specialization which is governed by the principles of rigor and sustainability that one would expect from a financial institution.

MicroBank is the realization of this strategic potential goal. It was created with the objective of contributing to productive activity and job creation, and also to facilitate access to credit for families with limited resources, so they could meet their basic needs for development. Its nature as a specialized bank favours the professionalization of the activity, the evaluation of its sustainability and the progressive adaptation of the range of products and services that our customers need.

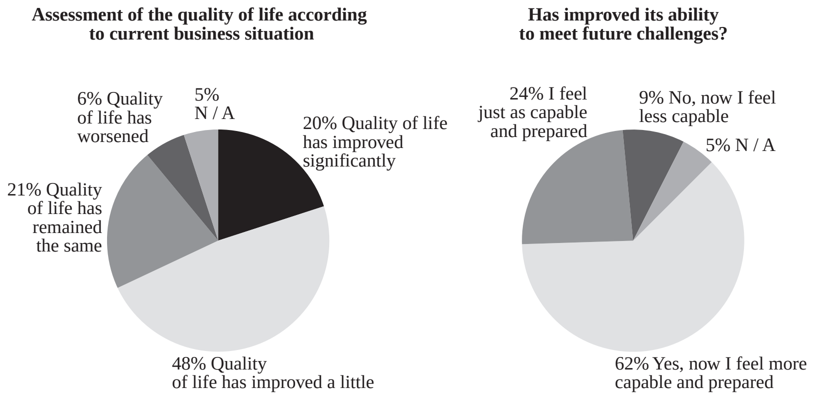
However, MicroBank has not been the only one to consider that microfinance could have a much broader scope than it did in its inception. The European Commission, who has set its maximum amount at 25,000 Euros, also welcomes the concept that microcredit can constitute a useful financial tool in order to facilitate access to credit to freelance professionals and micro-businesses.

It not only shares this view but, acknowledging the impact of these small business sectors in economic development and job creation, and also conscious of the difficulties in obtaining financing from traditional banking system, it has articulated a policy of active support for microfinance activity, especially oriented to those entities that can identify the size of the necessity and provide a sustainability that would ensure its permanence in time.

Last but not least, the access to credit for families who find themselves incapable of generating savings because of their limited incomes is a necessary factor in order to meet temporary or unexpected difficulties, as well as to finance small investments for the development of its members.

Today, Europe has a financial exclusion rate of 19% among the adult population and more than 80 million people live below the poverty line[2], meaning that almost two out of ten people do not have a bank account, nor use any banking services. In the case of Spain, this percentage drops to 8%, but this does not mean that all the people who have access to a bank account have access to credit when they need it. In fact, the level of what we might call "lending exclusion" reaches higher percentages in Spain, where 78% of the population in 2009 reported having trouble getting a consumer loan and 55% found it difficult to get a credit card.

Since its inception, MicroBank has financed more than 116,100 projects with an investment of 733 million Euros, but we are convinced that there is still much progress to be done in the development of this financial instrument, while its effectiveness has been proven already in many countries. The international



2. European Platform against poverty and social exclusion: a framework for social and territorial cohesion. Communication from the Commission to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions. European Commission, Brussels. February 16, 2010, pp. 2.

expansion of microfinance and its impact on economic development and social cohesion have consolidated these small loans as an engine of progress and effective recovery.

According to the study *Social Impact of Microcredit*, developed in 2010 by the ESADE business school and based on a sample of MicroBank operations, the impact of these microcredits, which were awarded based on the confidence in our clients and their projects, played a role which went beyond its value as a financial instrument, by also contributing to social integration. This article analyzes the social and economic impact, as well as the contribution to job creation, that MicroBank's financial and social microcredits have had. The general conclusions of the report point out, among other things, that the business success through MicroBank's microcredit is 77%, that most microentrepreneurs have stated that without microcredit they would have not been able to complete their business project, or that the companies that had been created thanks to microcredit had hired an average of 1.57 workers, showing that this type of loans create employment.

Furthermore, as reflected in the following graphics, obtaining a loan and the consequent financial inclusion improves the expectations of individuals, and 62% of people involved found that their quality of life has improved.