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The cradle of microfinance, Bolivia remains solid

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The cradle of microfinance, Bolivia remains solid. Legislative changes represent a major challenge

What factors have contributed to the growth and sophistication of Bolivian microfinance? Well-managed microfinance institutions (MFI), borrowers using credit in a targeted manner, a good regulatory framework, and access to abundant domestic and international funding. This, despite the emergence of policies that do not always reach their target.

Bolivia is largely considered to be the cradle of modern microfinance, most notably for the 1985 liberalization of the financial system and regulation designed to make room for microfinance. The sector has, on the other hand, emerged from much stronger and healthier from a serious crisis in 1999-2000. Will recent changes to banking regulations harm this success?

This question is worth asking because today microfinance is facing significant headwinds. These are related to growing pressure aimed at moving from a liberal regulatory formula toward a regulatory regimen that caps interest rates for credit, sets interest rate floors for deposits, establishes minimum quotas for MFI interventions in certain sectors, and creates financial and legal disincentives to fund microfinance activities by international actors. Until recently, the banking superintendence had always followed a market-based approach with respect to the financial system and microfinance. The framework had been quite flexible, allowing for financial institutions of different legal forms to offer microfinance products.

But the new financial services law promulgated in 2013 gives a greater role in the financial system to the State. The new law aims to curb corruption, decrease what is perceived to be excessive profitability for the banking sector, and increase access to financial services for those who are most vulnerable. While well-intended, these targeted policies carry the possibility of distorting the market.

Historically speaking, Bolivian microfinance has been able to rely on a solid foundation for growth. This includes a favorable institutional framework for microfinance institutions, microfinance industry associations that contribute to transparency and free flow of information, and excellent bureau coverage that helps to mitigate client over-indebtedness. Price transparency and solid competition have had a direct effect: some of the lowest effective interest rates to micro-borrowers in Latin America. The positive results fostered by the combination of these factors are evident: the percentage of outstanding portfolio investments in the Bolivian financial system was a mere 1.5% at the end of 2013, a historic low. That is even more impressive in comparison to the regional level, which exceeds 5%

Microfinance is an integral part of Bolivia's economic development: Bolivian real GDP growth has averaged 4.9% in the last five years. The Economist Intelligence Unit ranked Bolivia as the second best business environment for microfinance in 2013. Indeed, 37% of assets in the financial system are microfinance assets, held mainly by regulated entities. Bolivia is not only a pioneer in Latin American microfinance, but also has one of the most developed microfinance sectors worldwide.

The impact of these regulatory changes on the Bolivian microfinance industry will play out over the coming years. Given the characteristics of the Bolivian system, microfinance is well-positioned to adapt and thrive.

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