

# Zoom Microfinance

## An ever greener microfinance industry: trend or fad?

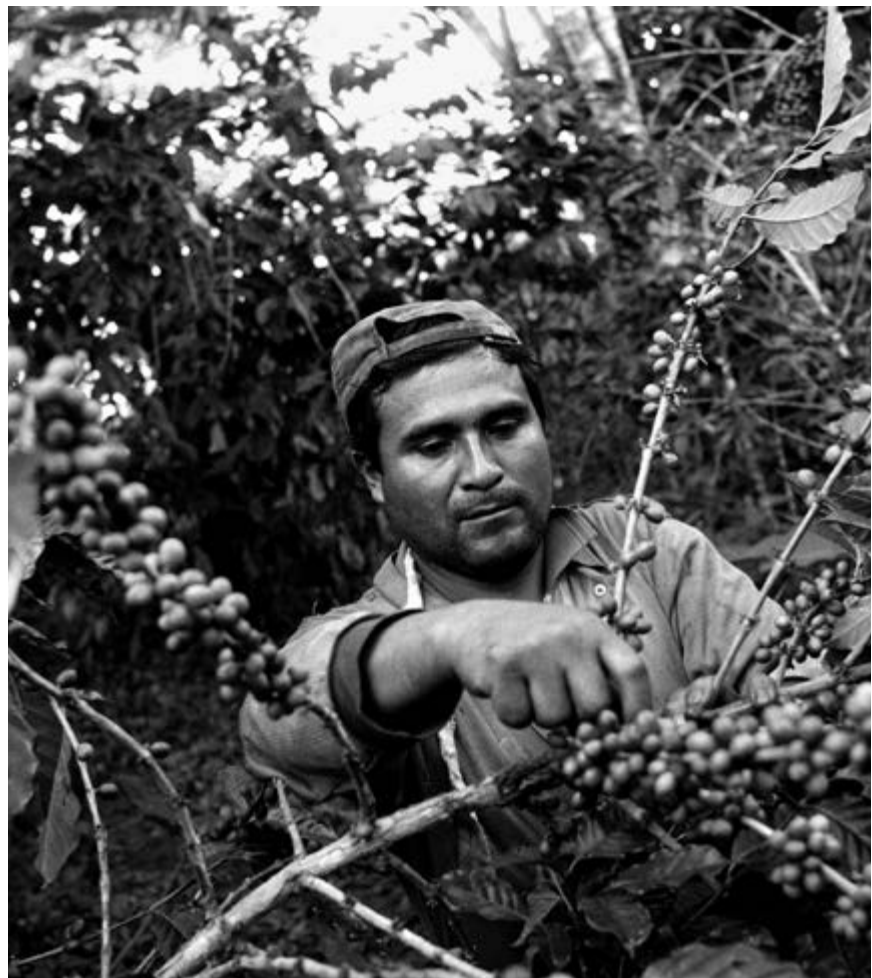
The emergence of green microfinance

Green microfinance – why MFIs do it

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The microfinance industry consolidated in the 1990s and early 2000s with the dual aim of being financially viable and demonstrating that it could have a real social impact. It is only in the past 10 years that voices have also been raised in support of the third pillar of development, the environment. Since that time, talk has been of the “triple bottom line”, initially spurred on by some in the industry, such as funders and service providers.

## The emergence of green microfinance

This concept of green microfinance began to emerge in a context marked by two striking developments: first, following a number of crises, questions were being asked about the impact of microfinance on clients; secondly, the existence of an increasingly competitive relationship between microfinance institutions.

According to the three-dimensional approach, the success of an MFI is based on its behaviour regarding profit (financial), people (social) and the planet (environment), as shown in the figure below<sup>1</sup>

Types of Returns		
Financial	Non-Financial ("societal" or "social")	
	Social (People)	Environmental (Planet)
	<ul style="list-style-type: none"> <li>• Economic</li> <li>• Health</li> <li>• Education</li> <li>• Other</li> </ul>	<ul style="list-style-type: none"> <li>• Energy</li> <li>• Carbon Reduction</li> <li>• Natural Resources</li> </ul>

Linking microfinance and concern for sustainable development can be done in different ways:

- ☛ Funding so called green activities: organic farming, agro forestry, ecotourism, waste management and recycling, composting, installing renewable energy equipment.
- ☛ Reducing the environmental footprint of the microfinance institution itself, which like other companies decides to improve its own environmental performance.
- ☛ Limiting customers' environmental impact, for example, by excluding certain types of credit.
- ☛ Delivering customers non-financial services in order to raise awareness of environmental issues and to train them in environmentally friendly strategies.

1: MicroRate "A Guide to Responsible Investing", December 2013 - [www.microrate.com](http://www.microrate.com).

## Green microfinance - why MFIs do it

As part of his doctoral thesis "Microfinance et environnement," Marion Allet<sup>2</sup> describes the three main motives that may lead an institution to branch out into this area (Bansal & Roth - 2000<sup>3</sup>):

- ☛ **The need for legitimisation:** an MFI might feel compelled to go green because there is pressure from other stakeholders such as investors and donors.
- ☛ **Strengthening competitiveness:** the phenomenon of microfinance becoming more commercially-minded has resulted in greater competition in some markets, which may push MFIs to develop competitiveness in new products for new customers, but also to access new sources of funding.
- ☛ **Social responsibility:** this clearly ties in to the institution's social values. As the microfinance sector was founded on a social mission to provide financial services to those excluded from the traditional banking system, this is, à priori, a potentially significant motivating factor.

If the last motivation is more ethical, the first two are clearly more pragmatic.

Marion Allet's research (which 160 MFIs contributed to) concludes that for MFIs, social responsibility is the issue, which plays the most important role in the drive to green microfinance. This is therefore a positive process, which more often than not couples with green product development (enhanced competitiveness) and the non-financial work of raising awareness amongst and training customers.

SOS Faim is part of the broad donor community involved in supporting the microfinance sector, especially in the rural and agricultural spheres. To date, SOS Faim has not considered environmental credentials as a condition of entry into a microfinance partnership, but each time a partner has wanted to branch into or consolidate in this area, support has been provided. This was particularly the case with regards to access to green power in Ethiopia and the development of organic farming in two Andean countries.

2: PhD thesis "Microfinance et environnement", Marion Allet, Université Libre de Bruxelles, SBS-EM, CEB, CERMI – Université Paris I Panthéon Sorbonne, IEDES, UMR 201 "Développement et sociétés" – 2012-2013 academic year.

3: Bansal & Roth (2000) "Why companies go green: a model of ecological responsiveness" - *The Academy of Management Journal* 43 (4); 717-736.

## Green energy in Ethiopia

The awarding of loans to purchase renewable energy equipment is probably the most frequently cited of examples in green microfinance.

In 2013, two SOS Faim partners in Ethiopia, Harbu and Buusaa Gonofaa expressed interest in developing renewable energy product offerings. Micro Energy International was approached for technical support<sup>4</sup>.

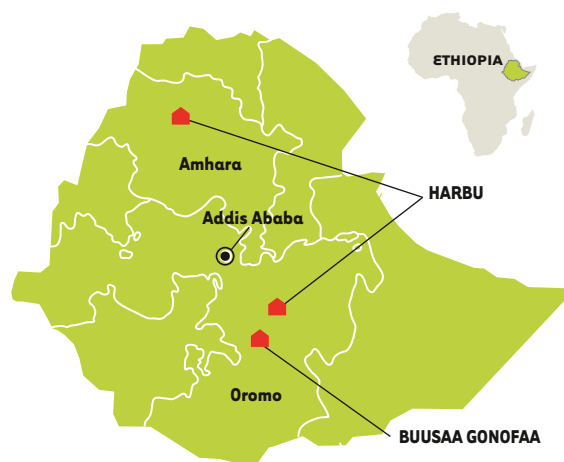
On the one hand, the energy sector in Ethiopia is largely dependent on traditional biomass-based sources, which is why the country ranks among the lowest electricity consumers in the world. In rural areas, only 1% to 2% of Ethiopians have access to electricity. While the government has provided a framework for the transition to renewable and more efficient energy, the lack of financial resources and technical assistance hinders progress already made in policy.

On the other hand, the Ethiopian microfinance sector is experiencing rapid growth. The sector has more than 2.7 million active borrowers for a loan portfolio of US\$600 million<sup>5</sup>.

BUUSAA GONOFAA and HARBU have headquarters in Addis Ababa and are primarily active in the Oromia and Amhara regions and not only want to develop a range of clean energy products, but also want to engage in a more comprehensive green strategy.

The project, which is set to run from 2013 to 2016, has Micro Energy International's support:

- ☛ An identification phase took place in late 2013 to assess the energy needs of current and potential customers of both MFIs and the potential for successfully linking the energy and microfinance sectors.
- ☛ The implementation phase: development of green financial products; development of the supply chain of green products and services (importance of a seamless chain from production to sale, distribution, in-



**For MFIs, social responsibility is the issue, which plays the most important role in the drive to green microfinance.**

stallation and after-sales service); completion of a pilot phase in 2014; amplification of the process as of 2015.

The preliminary identification phase allowed a number of potential products to be researched:

- ☛ Solar-powered technologies - pumps, lighting (main need identified among BG's customers), domestic solar power installations
- ☛ Better stoves - this technology would provide customers with the greatest economies, according to loan officers from both MFIs
- ☛ Biodigesters - where financial support is available as part of government policy

Equally, it gave both MFIs time to see whether they were able to implement a green strategy (in particular, assess management's and staff's identification with the strategy) and to set out the steps and hurdles on the road to success - identify the target market, do detailed analysis of the project's economic viability, ensure adequate human resources.

<sup>4</sup> "Evaluation of the potential to develop a micro energy program"; December 2013; Micro Energy International GmbH.

<sup>5</sup> Source: MixMarket, July 2014.

## “Green” financial tools

Farmers associations in Bolivia and Peru create green financial tools

### Coffee producers create their own financing instrument.

In 2003, La Florida cooperative of coffee farmers in Peru took steps to transform its internal loan management department into an independent savings and credit cooperative. From the outset, the new cooperative immersed itself in green finance, as the parent structure had decided to encourage its members to switch to organic farming. Indeed, this niche export market offered better prospects for the economic viability of family plots.

A decade later, the CREDIFLORIDA cooperative has successfully built itself up and has in particular devoted a major part of its resources to green (i.e. organic) agricultural loans.

Currently, 25% of members are women.

Sight savings earn 4%; for term deposits (1 year), the cooperative offers a yield of 11%. Seasonal loans cost between 20 and 22% per year and the cooperative funds only up to 60% of a season’s budget.

The cooperative organizes its work using information collected through the excellent relationship it has with farmer organisations and cooperatives (about a dozen of them). As these have mostly opted for organic production, the cooperative is following the trend. In addition, collaboration with organized groups is an im-



portant factor in risk mitigation (social pressure and more stable markets).

The loan portfolio is 95% invested in agriculture. Organic farming accounts for about 90% of the overall portfolio.

### A specific product for the renewal of coffee farms:

The cooperative finances up to 100% of farmers’ needs or 28,000 soles (equivalent to € 7,442) per hectare all costs included, over 4 years, and provides technical assistance. A tailored repayment plan is established based on the characteristics of each plot and the total revenues of the family farm. In 2009, a pilot programme covered 50 hectares, and had a 100% recovery rate. Cur-

### Growth over the last 4 years

	2010	2011	2012	2013
Assets (€)*	1,366,546	1,417,658	2,382,444	2,373,339
Members	2,204	2,520	3,040	3,265
Member deposits (savings) (€)	2,080,513	3,050,281	3,557,319	3,606,904
Loan portfolio (€)	4,405,994	5,986,766	8,039,117	7,255,830
Staff	21	22	21	27
Income (€)	157,920	243,949	564,415	27,054

\* The exchange rate used is 3.7624 Peruvian soles to €1.

rently, loans are being made for 250 hectares, of either coffee (150) or coffee combined with bananas (100). In each community involved, leaders are initially given priority with a view to facilitating replication of the process. The cost of this product is 15% in dollars and 17% in soles. An additional 2% commission covers technical assistance, the acceptance of which is a condition of the loan. Real guarantees are required: deeds to plots with their valuation.

In terms of results, the existence of technical support means yields gradually increase from 10–12 to an average of 25 quintals per hectare.

In addition to increased productivity, technical assistance promotes better management of the farm, including through reforestation (200 trees other than coffee are planted per hectare). This leads to higher value added (not to mention the environmental criterion). This is a type of intensive agriculture, which, nonetheless, protects the environment.

Since these loans are relatively long-term (4 years), the cooperative has negotiated external funding of comparative duration, as members' savings are rarely blocked for such long periods.

Another feature of the programme is its hands on approach: a preliminary visit of the plot in question is carried out. How well the plot has been managed is a decisive factor in the decision to award a loan. In addition, the loan officer takes into consideration all the different sources of income the family has (their financial flows and repayment capacity). Once the loan is disbursed, monthly monitoring visits commence. Each loan officer manages a portfolio of 200 loans and spends over 80% of his time in the field.

A significant limitation of the model, nevertheless, is the degree to which CREDIFLORIDA is tied to a single product, coffee. This poses risks, not only in terms of changes in world market prices, but also of disease outbreaks. In 2013, a significant portion of funded plots were affected by coffee-leaf rust<sup>6</sup>, resulting in a reduction in the size of the loan portfolio and income in 2013, with 30% of loans having to be restructured.

It was this tremendous exposure to coffee that led to the creation of a special risk management unit, in 2010.

A risk committee that reports to the Board of Trustees was established. It recommended diversifying credit risk (oranges, pineapples, cocoa etc.). Though coffee still accounts for 87% of outstanding loans, the goal is to get it down to 70%.

### Two examples of successful diversification.

#### **The Ochoa family - father and son (Luz-Maria - Perene): from coffee to oranges**

The Ochoa are members of a farmer organization that has 55 members. The father's farm is at an altitude of 1200 metres above Luz Maria (in Perene district). He cultivates 2.5 hectares of organic coffee and bananas. He took a seasonal loan of 10,000 soles (€2,658). The son owns an organic oranges farm in a lower ecological zone (650 meters). Production stands at nearly 80 tonnes from 3.5 acres. Approximately one third of his production is for export as certified product, the rest is sold in Lima at the same price as conventional oranges. The organic market guarantees him a turnover of 24,000 soles (€6,379) per year. For each of the last 5 years he has taken out a seasonal loan of 15,000 soles (€3,987) mainly to fertilize his land with guano.

#### **The Fundes family (in Grau)**

The Fundes family switched to organic coffee production as of 2000. Not simply because the market had grown, but also in response to health problems associated with the use of fertilizers and toxic pesticides. The family plot was affected by coffee-leaf rust and the family was able to access an emergency loan of 10,000 soles (€2,658), which was sufficient to fund 50% of the cost of replanting with coffee-leaf rust resistant varieties. However, the family's ability to survive, was equally attributable to its foresight in diversifying its agricultural production, with bananas (in combination with coffee) and cocona<sup>7</sup> but also livestock (22 cows and 200 guinea pigs).

CREDIFLORIDA executives also emphasize a clear link between the quality of the portfolio and the level of diversification: this is particularly the case in one of the cooperative's areas - Pangoa.



6: A disease caused by the fungus *Hemileia vastatrix*.

7 The cocona is a fruit-bearing plant that grows in the Andean zone, it is of the solanaceae family, as are potatoes and tomatoes.

### Three Bolivian organic organizations work together.<sup>8</sup>

In 2013, a specific statute was written into the Bolivian financial services law recognising community financial entities (CFE). This was done as part of the implementation of a model of national economic development, based on the productive sector, in particular smallholder farming.

Farmer organizations in Bolivia created three such entities. In 2011, they united as an umbrella organisation called FINDEPRO - the national organization of farmer community financial entities.

The main comparative advantages of these entities are clear:

- ☛ their proximity to farmers and the knowledge and understanding of their production system;

- ☛ their ability to influence farmers' practices;
- ☛ their control by the parent association.

These three entities are heavily involved in green funding because they were set up by farmer organizations that shifted to organic production, initially for economic reasons, i.e. a niche market existed for products such as organic coffee, cocoa and quinoa.

#### FINCAFE

Founded in 1998 by 25 farmer organizations, the entity serves both individual farmers (renewal of coffee plots and seasonal loans) and farmer organisations and cooperatives (coffee processing, marketing and export).

269 individual loans are outstanding, mainly for the renewal of coffee farms, meeting significant need in this area. €1,271 is lent for an area of 0.5 hectares. The peculiarity of the approach is to combine a financial institution (FINCAFE) and a technical assistance provider (Association of Organic Farmer Organizations of Bolivia - AOPEB). The interest rate charged is 16% per year. Loans are granted for periods of 2 to 3 years.

A complete technical package is available to growers with organic arabica coffee crops under forest cover, which diversifies and complements the family income. The approach is individual, tailored, based on an analysis of the characteristics and potential of the plot concerned. SOS Faim covers the cost of technical assistance provided by three AOPEB experts, through a coffee farm renewal programme.

#### AFID

The El Ceibo union of cooperatives, founded in 1977, currently comprises 49 cooperatives and 1,131 members. Its core activity is the production of organic and fair trade certified cocoa. It also produces chocolate, liquor and cocoa butter. In 2008, El Ceibo set up a technical assistance unit for its members. The technical support



Parent Association	CFE	Product	Location
Federation of Coffee Exporting Producers of Bolivia – FECAFEB	Servicios financieros cafetaleros – FINCAFE	Coffee	La Paz - Yungas
Regional union of cooperatives El Ceibo	Alternativa financiera para el Desarrollo – AFID	Cocoa, bananas, lemons, oranges.	La Paz - Alto Beni
National Association of Quinoa Producers – ANAPQUI	Financiera Asociación Agropecuaria del Altiplano Sur – FAAAS	Quinoa, camelids	Oruro, Potosi

<sup>8</sup> This part of the article is based on a document prepared by the Bolivian organization PROFIT-RURAL which provides FINDEPRO with a technical secretariat.



provided to members has revealed the need for accessible and flexible financing with the goal of improving the productivity of plots. In 2011, the decision to create a financial arm, AFID, was therefore taken not only to improve cocoa farming but also to encourage diversification with products like bananas, yucca, papayas, lemons and oranges.

As the financial arm of El Ceibo, AFID carried over the policy of promoting organic farming that its parent organization had implemented. Organic certification is therefore a condition of access to finance.

The current loan portfolio stands at €1.5 million for 770 farmer lenders (average loan size of approximately €1,948). The portfolio is almost entirely invested in production loans, with a basic interest rate of 18% which can be reduced to 16% for affiliates with solid credit records.

### FAAAS

FAAAS (Financial Association for Agriculture and livestock in the Southern Altiplano) was founded in August 2010, by nine regional quinoa farmer organisations all from the same area. They came together as a federation called ANAPQUI (National Association of Quinoa Producers).

FAAAS, the financial arm, is connected to ANAPQUI's technical assistance programme, PROQUINAT, which was set up in 1992 and promotes the production of organic quinoa.

End 2013, the portfolio of loans granted by FAAAS stood at just over €1.5 million, distributed among 458 clients. Loans have been both for organic quinoa production (field preparation, sowing, harvesting), but also for breeding sheep and llamas.

Interest rates charged are 13% for members of organisations affiliated to ANAPQUI and 16%-18% for non-members.

### Commonalities

These four cases from Peru and Bolivia have several things in common:

- ☛ They are relatively small-scale in terms of number of loans and portfolio size. On the other hand, average loan sizes are quite large because there is often an investment dimension to the activities.
- ☛ They all have a relatively small regional focus.
- ☛ They were all set up by a farmer organization or cooperative, which decided to create its own financial arm because other financial institutions were not serving their needs. As such, the organic farming priorities of

parent organizations have clearly determined the choice of financial arm put in place.

- ☛ The loan portfolio of each of these financial institutions is weighted towards a single sector (coffee, cocoa, quinoa), making them vulnerable to various factors (weather, disease, price fluctuations, etc.). The coffee rust that led CREDIFLORIDA to have to refinance 30% of its portfolio is an example.

- ☛ In all cases, loans are tied to a technical assistance programme. In some cases, subsidies are obtained in the framework of international development aid; in others, the cost of technical assistance is included in the interest rate of the loan that is granted.

- ☛ In general, these financial arms set up by producer organizations offer loans on better terms than those from traditional microfinance institutions in either country.

## Conclusion

As stated, green microfinance is still in its infancy. However, its growth is in little doubt.

On the one hand, this is because most microfinance institutions are born of a social purpose, which means they are attuned to their social responsibilities and therefore motivated to participate in the resolution of problems encountered by the community, as in the case of environmental degradation and climate change.

On the other, this is because, as the few cases described show, green microfinance addresses an existing demand among borrowers. The products on offer, either for green energy or for organic agriculture, are of interest to clients from both an economic and social point of view.

In addition, they do not seem to affect the sustainability of the institutions that offer them.

This issue of *Zoom Microfinance* was written by Marc Mees, head of knowledge management at SOS Faim.

## SOS Faim and microfinance

For several years, SOS Faim has supported different microfinance institutions in Africa and Latin America. As with all development tools, we have to analyse the aims, models and implementation conditions of aid to farmer organizations. It is with this purpose in mind that SOS Faim publishes *Zoom Microfinance*.

This publication is available for download in French, English and Spanish on SOS Faim's website: [www.sosfaim.org](http://www.sosfaim.org).

SOS Faim is a member of the European Microfinance Platform [e-MFP] and the Luxembourg Round Table on Microfinance (LRTM).

Apart from *Zoom Microfinance*, SOS Faim publishes another newsletter, *Farming Dynamics*, which deals with the development challenges farmers' organisations face. This publication is available for download in French and Spanish. SOS Faim's website: [www.sosfaim.org](http://www.sosfaim.org).

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