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Tiny Loans Seen as Big Way to Invest in Developing Nations' Poor

Microcredit programs offer borrowers as little as \$30 and are credited with improving lives

By Evelyn Iritani, Staff Reporter

It was at the end of a long, dusty road in Guatemala that Mike Galgon, a Seattle tech entrepreneur, became a believer.

He met a woman who used a \$50 loan to buy a simple metal-bending machine, allowing her to increase her daily production of buckets from two to 10. By selling the extra buckets, she was able to buy medicine for an ailing daughter, send several other children to school and purchase a second machine to expand her business.

"At two buckets, you can't save anything," said Galgon, 38, co-founder of AQuantive Inc., one of the nation's largest online marketing firms. "But with 20 buckets' worth of income, for the very first time she could save money.... It was a miracle of economics."

Microcredit programs that deliver money to poor people have been one of the fastest-growing tools in the anti-poverty arsenal, spurred by a generation of high-tech entrepreneurs attracted to its "hand-up, not a handout" philosophy, said Sam Daley-Harris, head of the Microcredit Summit Campaign.

The Washington-based group has set a goal to have loans as small as \$30 granted to 175 million of the world's poorest families by 2015.

That effort got a boost with the recent news that Microsoft Corp. founder Bill Gates and his wife, Melinda, planned to devote more of their philanthropy to areas such as microlending.

At a conference with investor Warren E. Buffett, who is giving the bulk of his wealth — about \$31 billion — to the Bill & Melinda Gates Foundation, Melinda Gates said poor people, particularly women, needed better ways of getting the money necessary to move beyond mere survival.

Bangladesh is often cited as a microcredit success. That's where pioneer Grameen Bank and other providers of small loans are credited with 40% of the reduction in "moderate poverty," according to a 14-year study by the World Bank. The loans have translated into a dramatic improvement in the quality of life there, including lower infant mortality rates and improved education levels.

This month, BRAC, a leading Bangladesh microcredit provider, sold off \$180 million worth of loans to investors. RSA Capital and Citigroup were among those participating in the deal.

Microcredit providers have found that women, who receive the bulk of these small loans, are better credit risks and more likely to spend their additional earnings on their families.

Backed by a multibillion-dollar purse that dwarfs the annual budgets of many governments, the Gates Foundation has already reshaped the global health arena, spurring innovative research and marshaling treatment of long-ignored diseases such as malaria that kill millions of poor children each year.

If the Gates Foundation chooses to apply itself to microfinance full force, "it'll be another tectonic shift in financial services," said Bruce MacDonald, a spokesman for ACCION International, a Boston-based organization that received a \$5.8-million grant from the foundation to expand microlending in West Africa and India.

Shari Berenbach, executive director of the Bethesda, Md.-based Calvert Foundation, manages a social investment fund that placed \$20 million in microcredit programs in 2005, double the level of 2004.

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She said the Gates Foundation was making small, targeted grants in an effort to “move the whole field of microfinance forward” without undermining existing programs.

The Gates Foundation gave Freedom From Hunger, a Davis, Calif.-based anti-poverty organization, \$6 million to develop a program that would provide poor borrowers in five countries, including Burkina Faso and Bolivia, with a variety of healthcare services including low-cost insurance and doctor referrals.

Christopher Dunford, the organization’s president, said his group hoped to demonstrate that healthier borrowers were more likely to repay their loans and be loyal customers.

“By working with the Gates Foundation, we have an opportunity to push the envelope,” Dunford said.

Roger Frank, managing director of Developing World Markets, said investors were starting to figure out that putting money into poor communities could be profitable, in part because the borrowers are highly motivated to repay their debts.

Frank, a former Wall Street banker, said his Connecticut firm recently closed a deal in which it pooled \$60 million worth of loans to microfinance institutions. By blending money from “socially motivated” individuals with more traditional sources of capital, the firm has also helped other groups raise \$140 million for microcredit programs.

One of those groups, Seattle-based Global Partnerships, has \$9.5 million invested in two microcredit funds and is about to launch a third. Its funds are loaned to groups such as FAMA, a Honduran group that provides low-interest financing to about 14,000 poor clients, 78% of whom are women.

Eloisa Acosta, FAMA’s executive director, said that those loans range from \$30 to \$150 and that her organization has a 95% repayment rate.

To protect its investors, who expect to be fully repaid with interest in five years, Global Partnerships evaluates and monitors its recipients closely, including making on-site visits, said managing director Gary Mulhair.

“This is not a philanthropic endeavor,” he said. “Our investors are all socially motivated. But they want their money back.”

Annual interest rates on the loans can exceed 30%, which sounds high, but in developing countries the rates can be low compared with alternatives.

Mulhair said the group had talked to the Gates Foundation but has not yet received any funding. However, Global Partnerships’ founder, Bill Clapp, is working with Bill Gates Sr., co-chair of his son’s philanthropic arm, on a campaign to build business support for global anti-poverty programs.

After returning from Guatemala, Galgon, the Seattle tech entrepreneur whose company owns the Avenue A/Razorfish agency, joined Global Partnerships’ board and has invested \$50,000 in one of its funds.

“We need to do something to share our fortune,” said Galgon, a former Navy officer and Harvard Business School graduate. “But we need to share in a way that moves people ahead, not just that feeds them today.”