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**Small Foundations:  
How to Invest in Microfinance**

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**ABSTRACT**

Microfinance is a powerful tool in fighting poverty throughout the world. Small foundations are a valuable resource in supporting the efforts and goals of microfinance. However, it is important for small foundations to understand their investment options in the marketplace and compare them in order to find the right one for them. This analysis aims to assist small foundations in making that decision by assessing six investment intermediaries including Peer to Peer, Microfinance Funds, Retail, Development Agencies, Microfinance Networks and Large Foundations. The article also examines the financial vs. social returns produced by the various intermediaries and the level of involvement required to help small foundations visualize their investment goals. Finally, trends in foundation investments are evaluated as such investments are moving from charitable to financial objectives and few, but growing number of, microfinance institutions are moving towards a profit-making model.

**About the Authors**

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*(The Microfinance ASP Management 891 course at the Wharton School aims to provide students with a basic understanding of microfinance and equip students with the knowledge and tools that are transferable to a career or a volunteer role in microfinance or international development.)*

**About the Company**

**Social Enterprise Associates** is a consulting firm specializing in triple bottom line enterprises. The company offers clients business acumen, managerial experience, practical research, and affordable services. The company supports entrepreneurs, their organizations, and the industries in which they operate. Specializations include New Ventures, Socially Responsible Business, Microfinance, and Non-Profit Earned Income Strategies. More information is online, [www.socialenterprise.net](http://www.socialenterprise.net).

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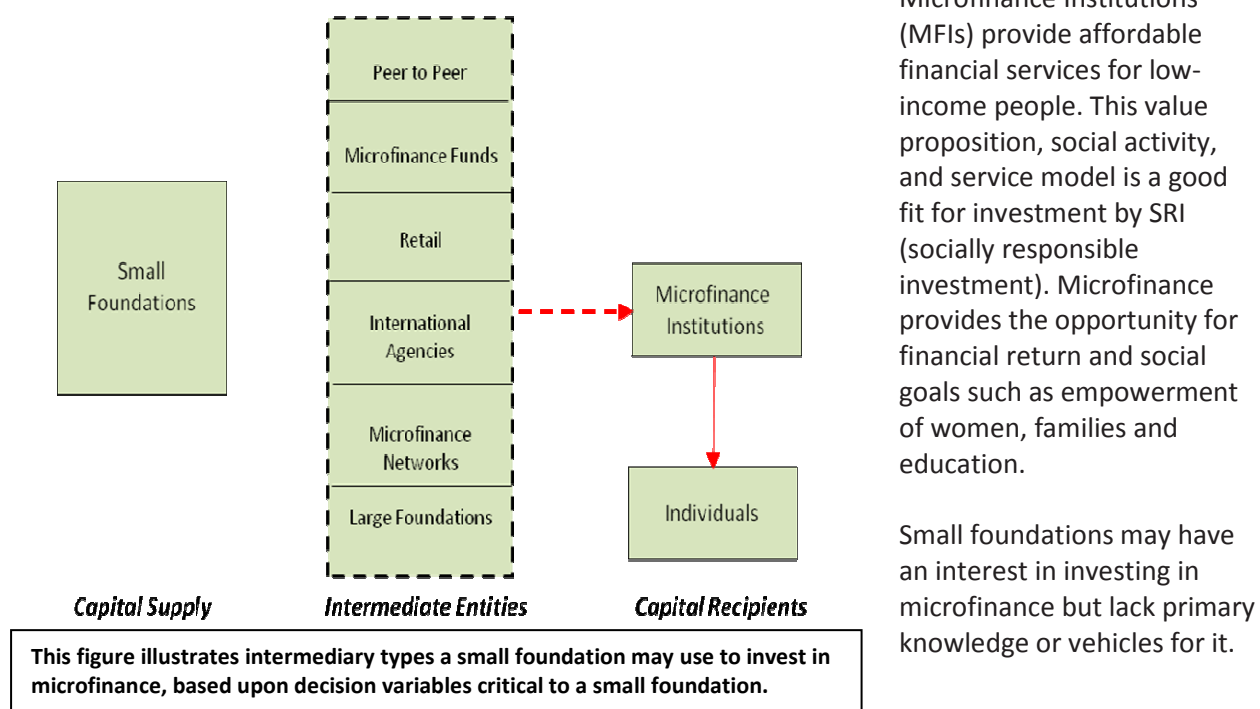
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## Guidelines for Small Foundations Seeking to Invest or Contribute in Microfinance

Microfinance is the offering of financial instruments to the very poor. It can serve as a very rewarding investment target as it not only empowers its beneficiaries, but also offers a permanent solution by offering both employment and business skills. It can also often impact other social initiatives including education, healthcare, and environmental concerns. This article helps small foundations understand the available investment options in the microfinance marketplace as well as how to compare them in order to decide an end target.

The analysis below compares options, taking into account the social goals and investment criteria of small foundations to help make this choice easier. The long-term objectives of small foundations provide tactical decision variables to choose an intermediary in such a marketplace. Small foundations should have a clear view of its objectives and can select a marketplace intermediary based on decision variables such as financial rate of return—categorized by at cost return (0%), small return, or approaching market rate—social goals, level of involvement, donation size, geography, and for-profit or not-for-profit delineation in investment targets. Once the foundation narrows down on the intermediary, several choices exist within each intermediary type, which the foundation can further investigate to make its final decision.

## Marketplace for Microfinance Investments



The research below, conducted by students from the Wharton Business School, University of Pennsylvania outlines investment intermediaries small foundations can use to realize their goals.

### Intermediary 1: Peer to Peer (P2P)

The most direct intermediary is peer to peer, which obfuscates levels of the microfinance value chain providing a direct experience for lenders and borrowers. Players in this space are further categorized by differing financial returns on investments. Kiva.org is a P2P intermediary operating in the international market offering no ROI. Prosper.com, on the other hand, operates solely in the US and has returns. The downside for this choice is that small foundations will find the investing process time consuming and labor intensive, as loan sizes are typically small, and they must do their own due diligence.

### Intermediary 2: Microfinance Funds

For small foundations interested in making larger investments, microfinance funds provide risk-assessed products to allow investors to reach a broader scope. Microfinance funds are institutions that use financial instruments to manage large funds whose underlying assets are based in loans to MFIs. These funds all operate on distinct and unique revenue and business models that need to be investigated individually. They mobilize financial funding to select MFIs based on level of return, cause and geography. They are further distinguishable based on the financial rate of return particularly in three major categories: commercial funds, quasi-commercial funds, and microfinance development funds.

**Commercial funds** have a predetermined financial target rate of return where social returns play a secondary role. The secondary nature of the social returns may dilute the philanthropic aims of the microfinance institution. This objective may not fit with the foundations long-term mission. It might be difficult to understand intermediary's investment decisions and the measurable real effects on social cause.<sup>1</sup>

**Quasi-Commercial funds** like ResponsAbility Microfinance Fund aim to create a balance between the social and financial returns, at times opting for below market returns to satisfy social impact.

**Microfinance Development Funds** e.g. Oikocredit focus as non-profit entities or cooperatives and primarily target the development of microfinance institutions (MFIs) by granting capital at favorable financial rates without necessarily seeking a financial return. Usually, funding is provided below market rates and often complemented by technical assistance. This investor base normally seeks a social return and aims at maintaining its real inflation adjusted capital at maturity.<sup>2</sup>

### Intermediary 3: Retail

For those interested in smaller investments, retail intermediaries provide more flexibility in loan size without eliminating returns. Calvert Foundation and Microplace have partnered to create a portal focused as a retail intermediary where profit-conscious investors can also get involved in microfinance. This intermediary allows investors to invest in a securitized pool of loans to MFIs which means small foundations can use this portal to directly support MFIs, spread its default risk across all lenders at the MFI, potentially handle larger loans and target specific MFI requirements.<sup>3</sup>

### Intermediary 4: Development Agencies

Small foundations can also contribute to other development institutions with large projects or initiatives in microfinance. Development agencies such as CARE International, a leading humanitarian organization

<sup>1</sup> [www.esgalpha.com/publications/uksif-new\\_SRI\\_Instit\\_Opps.pdf](http://www.esgalpha.com/publications/uksif-new_SRI_Instit_Opps.pdf)

<sup>2</sup> [www.dbresearch.de/PROD/DBR\\_INTERNET\\_EN-PROD/PROD00000000000219174.pdf](http://www.dbresearch.de/PROD/DBR_INTERNET_EN-PROD/PROD00000000000219174.pdf)

<sup>3</sup> <http://mindtangle.net/2007/11/06/kiva-vs-microplace/>

aimed to fight global poverty, have partnered with other private organizations to provide financial services to the poor. Care International, for example, has partnered with Max New York Life Insurance, to launch insurance products to microcredit clients.<sup>4</sup> However, since many international agencies fund multiple initiatives, it is harder to measure progress of any donation or investment on any one sector.

### **Intermediary 5: Microfinance Networks**

A small foundation that prioritizes social goals but also wants to impact a large group of MFIs can work with microfinance networks. Women's World Banking (WWB) is an example of such a network (not-for-profit). It was established in 1976, with a mission to provide sustainable financial services to low-income women and their families by building an effective global network of microfinance institutions and banks<sup>5</sup>. WWB partners provide support to over 50 banks and microfinance institutions across Africa, Asia, Eastern Europe, Latin America and Middle East continents. The network also offers management guidance, training, technical assistance, and financial products and services. They work to ensure their member MFIs are operating well according to performance standards and evaluation criteria. They are able to impact entire global regions—for example, they can provide advice on how to impact government policies to create a better environment for MFIs.

Other microfinance networks include ACCION International ([www.accion.org](http://www.accion.org)), FINCA International, ([www.villagebanking.org](http://www.villagebanking.org)), Banking with the Poor ([www.bwtp.org](http://www.bwtp.org)) and the Grameen Foundation ([www.grameenfoundation.org](http://www.grameenfoundation.org)).

### **Intermediary 6: Large Foundations**

Small foundations can invest in larger foundations that have created microfinance initiatives or focus on microfinance. Large foundations such as The Palli Karma-Sahayak Foundation (PKSF) focus on microfinance related causes such as empowerment of women resulting in better lives for families.<sup>6</sup> The operational costs tied to these intermediaries are quite high but their focus on the microfinance industry makes a unique niche for these players in the marketplace.

### **Trends in Foundation Investments**

Besides the intermediaries mentioned in this research, small foundations could choose to invest directly into microfinance institutions. This process requires a high level of diligence so proper resources must be in place for small foundations to attempt this method. Another option is to invest through independent advisory organizations such as Cambridge Associates, which provide advice and research on asset allocation and investment strategies.<sup>7</sup> Organizations such as Social Enterprise Associates<sup>8</sup> also provide valuable help on advancing a social mission.

Overall, the trends in foundation investments are gradually moving from charitable objectives to financial objectives. These financial objectives are achieved by foundations through investment in conventional financial instruments, market rate mission investments and below market rate mission statements. As this trend moves towards the financial objectives, most intermediaries in the marketplace have now started moving towards a model of return on investments. Although the current rate of return on microfinance investments is low, the successful public offerings of Compartamos in Mexico (moving from non-profit to profit) and SKS in India show a strong trend towards this profit-

<sup>4</sup> <http://news.mongabay.com/2005/0525a-poverty.html>

<sup>5</sup> [www.womensworldbanking.org/id,103](http://www.womensworldbanking.org/id,103)

<sup>6</sup> [www.pksf-bd.org](http://www.pksf-bd.org)

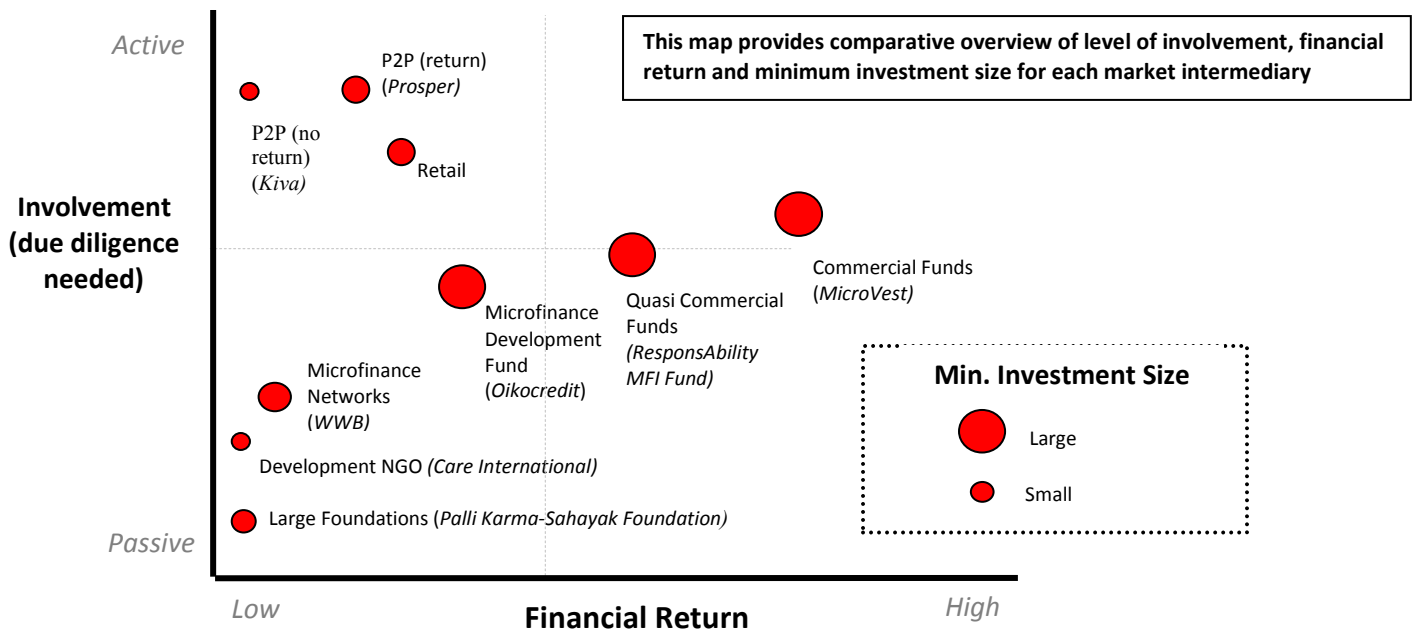
<sup>7</sup> [www.cambridgeassociates.com](http://www.cambridgeassociates.com)

<sup>8</sup> [www.socialenterprise.net](http://www.socialenterprise.net)

making model. The successful merger of social causes with market returns is a definite evolution within microfinance. As a small foundation, opportunities to capitalize on this wave are plentiful.

**Comparative Map of Microfinance Intermediaries**

The map below distributes the various intermediaries based on financial vs. social returns, and the level of involvement required to help small foundations visualize their investment goals and select an appropriate intermediary.



**Conclusion**

Ultimately, the growing arena of microfinance provides a rich set of intermediaries that facilitates involvement in microfinance, in particular for small foundations. These choices allow small foundations to quickly assess their goals based on the key decision variables such as financial return and social cause and choose a mode of participation that best fits their own investment criteria.

**Additional Resources**

For information on these marketplace intermediaries:

- Mix Market ([www.mixmarket.org](http://www.mixmarket.org)) for information such as overview of the organizations, credit reports, objectives on their social and financial performance.
- Microfinance Gateway ([www.microfinancegateway.org](http://www.microfinancegateway.org)) provides publication, articles and is a comprehensive online resource for the microfinance community.
- Social Enterprise Associates ([www.socialenterprise.net](http://www.socialenterprise.net)) provides consulting services fostering triple bottom line solutions and makes publications available for free on its website of value for small foundations and NGOs.