



Microfinance: Markets, Missions & Mendacity

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Thank you for the generous introduction and thank you for inviting me to this wonderful institution of global leadership.

As a neophyte member of this academic community, allow me to open my talk with a promotional advertisement:

The search for economic justice and for better solutions to poverty is a collaborative, community-wide responsibility. In the fight against poverty, there are no second class citizens. For those who want to learn more about my own social justice work or – even better – get involved with me, I hope you will visit my website www.IonPoverty.com.

In this room, we are kindred spirits. We are part of an international community of global citizens, activists, social entrepreneurs, philanthropists, scholars, and policy-makers -- all of us working together – to combat the disgrace of grinding poverty.

As a community, we don't accept a world in which half of our neighbors survive on \$2.00 a day or less – roughly, \$700 a year. We don't accept that if you keep your food in a refrigerator and your clothes in a closet, you are richer than 75% of the world's population. We don't accept that if you have a roof over your head and a bed to sleep in, you are also richer than 75% of the world's population.

We don't accept a world in which 1 out of 7 people are hungry – without the basic *daily calories* needed to survive -- slowly starving to death in a global concentration camp of hunger.

You don't have to be a pessimist to believe the poor will always be with us. You do need to be ashamed enough to do something about it.

BUT I am *not* here to guilt-trip you or to appeal to your conscience, although if conscience does not move us to action, nothing can and nothing will.

Instead, I want to share a secret with you. For social entrepreneurs, fighting the good fight is *personally* rewarding, *intensely* gratifying and *utterly* fun. Tackling big challenges is heady stuff.

You may not know this, but social entrepreneurs and activists are smarter. We're better-looking. We get the best restaurant tables. And, *we have the best posture*. In the words of another bearded public speaker, Abraham Lincoln: "A man never stands so tall as when he leans over to help a child."

In addition to raising our families, pursuing our careers and meeting our civic responsibilities, social change work completes us as individuals. In the words of Horace Mann: "Be ashamed to die until you have won some victory for humanity."

It is now within our economic power to roll back the scourge of poverty. At the turn of the last century, the Industrial Revolution became the single biggest anti-poverty program in the history of Humankind. In the next century, government public health departments backed by government funding of scientific research extended the life expectancy for the average American by 30 years. In our own time, Chinese capitalism has lifted 300 million people out of rural poverty.

Now it is our turn – your turn. With social entrepreneurial skills at the ready, we can change the poverty paradigm.

Whether financing a well-established social venture in Berkeley or a start-up in Bogota, we have to be high-minded without being soft-headed. We have to realistically respect the critical differences between textbook market conditions and the myriad of market imperfections which plague the poor:

In functioning markets, capital flows to its highest and best use. Risk and reward is measured to the single basis point. But where the poor live, capital is rare and expensive. Indeed, microfinance was invented because mainstream banks -- historically and enthusiastically -- had ignored the working poor.

In functioning markets, prices are set between willing buyers and willing sellers. Competition brings down prices, improves products and extends markets. But where the poor live, scarcity and monopoly live side-by-side. The poor are captive consumers subject to predatory pricing.

In functioning markets, consumer protection and financial transparency are enforced by governmental policy and a court of law. But where the poor live, property rights depend upon social norms or brute force. The poor are powerless.

In functioning markets, a distinction is made between public and private goods, between street cleaners and vacuum cleaners. But where the poor live, private investment is often the *only* investment. The market is the sole provider of the common good which means the fiduciary standard of care for social entrepreneurs *has* to be a lofty one.

In functioning markets, survival of the economic fittest is a necessary consequence of progress. Some businesses succeed, some fail. But where the poor live, the *only* ethical economic policy is not creative destruction, but creative opportunity.

As we cannot bomb our way to peace and prosperity, we cannot finance our way to economic justice. In the end, the poor must have the power to speak up, speak out and speak for themselves.

At the sharp edge of smart philanthropic giving and social investing, we want our dollars spent wisely. It is not enough to be well-intentioned. Well-motivated is not the same as well-run.

Thanks to the miracle of microfinance, we now think it is possible to marry profit margins to social missions. Beta-tested in the flood plains of Bangladesh and the mountainous Andes of Bolivia, microfinance achieves what economic development experts call "sustainability" and what business people call "profitability."

Recently, critics -- many of them academics -- are starting to smell the odor of malfeasance and a whiff of hypocrisy. Microfinance stands accused of being exploitive and predatory, charging exorbitant interest rates to ignorant, desperate women and abusing marketplace mechanisms to promote economic opportunity *without* full disclosure to *either* the poor *or* to financial donors and investors.

To correct abuses and to document its many benefits, microfinance deserves greater scrutiny -- not the shrill voices of the uninformed, the ideologically pure or the politically correct.

Today I would like to discuss three misunderstandings about the microfinance mission, its role in the marketplace and the recent charges of mendacity.

Misunderstanding #1 - Microfinance is not lifting people out of poverty.

Of course, microfinance is not a poverty silver bullet, not the next Industrial Revolution and not a cure-all for 10,000 years of economic and gender discrimination. Microfinance is not an economic development elixir. It doesn't build roads, schools or clinics, it has not stopped a war or cleared a mine field, nor does it preserve pristine rivers or protect endangered species.

In the words of Sam Daley-Harris, founder of the Global MicroCredit Summit: "Poverty is much too complex to be cured by one intervention. We don't ask if basic education *alone* ends poverty. We don't ask if vaccinations *alone* are ending poverty."

What microfinance does do is open up financial services for the poor and push loan sharks out of the hidden hamlets and alleyway slums where the poor struggle to survive. At its best, microfinance means opportunity and hope -- providing an impoverished person with choices: the choice to feed a child, pay a medical bill, fix a leaky roof, buy a metal pot or a warm coat. Not bad for a program that can become wholly or partially self-financing.

Acknowledging microfinance is hugely guilty of hype, hubris and deplorable short-hand marketing slang, we should realistically ask ourselves what can be accomplished with a tiny business loan. Twenty cents more a day may seem paltry to us, but what does a 20% increase in annual income mean to mother with hungry kids? For the most desperately poor, microfinance is an *urgent* engine of economic survival.

How much money must that mother earn to satisfy the critics? What other on-the-ground, village-level interventions are deployable *right now* -- today -- the day that she is not feeding her kids?

But microfinance should be about more than just money. None of us in this room would accept living in a community with bad schools, little healthcare, no electricity, filthy water, but with a great bank. Because poverty is a multi-disciplinary problem, multi-disciplinary solutions are needed.

Misunderstanding #2 - What the poor really need are savings accounts, not more and more debt. As microfinance has successfully extended its reach, the poor -- it is said -- are incurring a measure of over-indebtedness and falling into a kind of microfinance debt bondage.

In lieu of health insurance, social security and other safety nets, the poor do *indeed* need safe places to keep their money to cover life's uncertainties. Poverty is the

tyranny of the unexpected -- the unknown. It means *not having* money, but also *not having* it when you need it.

But credit and savings are not mutually exclusive. The choice is no choice at all. Not savings versus credit, but both.

Misunderstanding #3 - The poor are misusing microloans for consumption and other non-productive uses.

To state the obvious, poverty is the absence of money. *Of course*, the poor use microloans for non-business purposes. Money is fungible.

Microfinance provides the poor with money to start businesses, pay medical bills, cover marriage costs, put up a fence or even buy a bit of entertainment. It is the credit card most of us carry and use every day.

Local microfinance institutions – like all lenders – should employ stringent client selection criteria, but what the poor don't need are Western debt wardens to monitor over-indebtedness, police the use of loan money or treat them like children with an allowance. Empowerment includes the poor making decisions over their own financial affairs.

The buzz about microfinance ranges from “a miracle, self-sustaining poverty reduction program” to “a new asset class suitable for investment portfolios.”

While private capital in the service of the poor – or, inversely, the poor in the service of private capital – may or may not be ideal, it is understandable why the microfinance community has embraced private markets. At its operational core, microfinance is thematically aligned with capitalism and market solutions.

But the true argument for mobilizing private microfinance capital is one of pragmatic desperation. Government funds, foundations and donors are often parsimonious, cumbersome and unreliable. With so many poor people still unbanked, well-respected microfinance leaders are understandably pushing hard to “achieve scale” or – in simple English -- reach more poor people.

The most radical policy driving microfinance programs is the expectation that they must become profitable or – in economic development terms -- sustainable. This is not a standard typically used for other public goods and services. Most anti-poverty programs – from health clinics to environmental clean-up, from water projects to schools – are budgeted with long-term external subsidies.

In contrast, microfinance funders expect the poor to bootstrap themselves into profitability. If local microfinance programs don't increase microloan interest rates to at least cover costs, development funders and commercial markets soon look away.

The common sense concern -- and fair question -- then becomes: Is the microfinance model an anti-poverty tool for the impoverished or a pro-profit tool for investors?

Results -- not ideology -- are what count. A drowning person doesn't care, or ask, how the life preserver was financed. Doesn't care, or ask, whether a taxpayer, a shareholder or an NGO paid for the lifeguard. Ideology and economic theory are not the urgent work of social entrepreneurship. Saving lives is.

No economic theory and no marketplace -- whether functioning or failing -- can change a basic truth. As individuals, we are each blessed and burdened with a moral compass.

Free markets mean that each one of us has the *freedom* to make ethical choices. It means we have the *freedom* to take sides in the fight for economic opportunity for all. Is social entrepreneurship about creating a viable asset class to make money while doing good or about building a social movement for economic justice? Are we advocates for the poor or advisers to the well-off?

Who is going to be our role model? Don Quixote? Noble, but uselessly tilting at windmills? Don Corleone? Wielding power to benefit the few? Don Diego de la Vega? Zorro, fighting for the underdog? In the words of the poet: "A wise man should have money in his head -- not in his heart."

We know that reversing 10,000 years of free market bad behavior -- from slavery to debt bondage, from company towns to global cartels, from discriminatory banking to predatory pricing -- is not within our near-term grasp. But in our hearts, we know we have to try.

Serving the bottom of the economic pyramid is not just a market opportunity. It is an existential statement about our values -- your values -- our shared global citizenship.

A few years ago at my son's graduation from Columbia University, the college chaplain challenged the 30,000 assembled graduates and their families with these words --- words which should be the daily mantra for every social entrepreneur:

"Be a maker of peace,
A steward of mercy,
A voice of reason,
Be the hands and feet of justice."

Thank you for your time. Thank you for your commitment to a better world.