

German savings banks get involved in development cooperation

Social responsibility and profitability

Innovative approaches in the financial sector need not necessarily be new. Very often, tried and tested methods and principles can be adapted to provide modern solutions. This also applies to microfinance in developing countries. In Germany an independent structure within the financial sector has developed over the past 200 years: the Sparkassen and cooperative banks combine social responsibility with profitable business and number among the world's first microfinance institutions (MFIs).

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Photo: Sparkassenstiftung

Mexico's *cajas de ahorro* have a long history and more than 3 million customers.

In Germany, Sparkassen (savings banks) have always been open to low income clients and to small businesses (see box on page 44). They actively encourage people to build up savings, finance 70 percent of all small businesses with fewer than ten employees and finance more than 50 percent of all business start-ups in Germany. Sparkassen and cooperative banks are the only banks operating a full-coverage network of branch offices – 16 000 savings bank branches and 15 000 cooperative bank branches exist, compared to only 5 000 commercial bank branches.

Social responsibility plus professionalism and profitability – this is the framework within which Sparkassen operate in Germany. It is the only way they can provide sustainable access to financial services to all income groups all over the country. As part of their social responsibility for a globalized world, Sparkassen are passing on these principles to partner institutions in developing and transition countries through partnership projects.

Mexico: Restructuring the savings bank sector

Cajas de ahorro, savings banks organized on a cooperative basis, have existed in Mexico for more than 50 years. Today more than 600 mostly small such banks are the

only opportunity their more than three million customers have to deposit savings securely and to obtain small loans. Particularly since most Mexican commercial banks were sold to large international banks, many commercial banks have largely closed their branches in remoter areas. However, as the *cajas* gained in importance, their disadvantages also emerged. They were only subject to the general legislation on cooperatives and were not supervised by the state banking authorities. Staff were often poorly trained, only a few, not always good products were available, and many *cajas* operated at a loss. The result was closures and isolated cases of fraud, which discredited the entire *cajas* sector. That was the situation in 2000, when the Mexican government decided to provide targeted support for the sector.

The restructuring programme for the Mexican *cajas* sector is modeled on the structure of the German Sparkassen in many respects:

- a law was enacted specifically for savings banks (Ley de Ahorro y Crédito Popular, LACP);
- *Cajas* were subject to state banking supervision;
- an authorization process for *cajas* was established;
- federations to support and represent the *cajas* were developed and strengthened.

- ened and supervisory bodies established in association with the federations,
- a central bank was set up for the cajas (Banco de Ahorro Nacional y Servicios Financieros, BANSEFI),
 - cajas were integrated into the Network of the People (La Red de la Gente) by means of a common logo, uniform IT platforms and shared products.

The reform of the savings banks sector is supported by the World Bank. Assistance involves individual restructuring plans for almost 400 cajas. Comprehensive training is being undertaken, new products developed and introduced, work processes made more efficient and many other aspects. International consultants, some of whom are from German Sparkassen and cooperative banks, are advising the Mexican cajas.

The objective of the measures is to reinforce the financial stability of the cajas while retaining the socially oriented character of these financial institutions, and consequently give more people access to financial services.

Vietnam: Loans for women

The Vietnam Women's Union (VWU) has been running a microcredit programme (TYM Fund) for women in the country's poorest provinces since 1993. The Union grants loans to the poorest people: in order to become a member, a woman's monthly income must be less than US\$ 6.50. The loans granted are also small; the first loan rarely exceeds US\$ 50.

Not only do members of the project receive loans, they also save: 20 cents each week, which add up to more than US\$ 10 over the year. This is a lot of money in Vietnam, particularly in rural areas. In addition, every week each woman pays the equivalent of approximately 1.5 cents into a joint insurance fund. Should a woman die, the insurance repays the amount outstanding on her loan and the family receives the equivalent of US\$ 33 towards funeral expenses. In addition, the insurance pays a subsidy on the death of a woman's husband or underage child or if she has to spend time in hospital.

The TYM Fund also goes a step further: at the weekly meetings (at which attendance is compulsory) members are advised not only on money matters, but also on important aspects of daily life such as hygiene, family planning, storage, crop cultivation, livestock husbandry and much more. TYM takes a holistic approach to development, extending far beyond traditional microcredit.

The project currently has 20 000 members, and numbers are increasing con-

stantly. But VWU is becoming a victim of its own success: to date, an internal VWU division has looked after the project, but the steadily growing membership and savings and loan volumes mean that professional banking expertise is required. The decision-making processes are time-consuming, and the management does not have the knowledge to deal with such financial issues. The logical outcome would be to professionalize the structures of the TYM Fund and to separate them from the structures of the association. Since the start of the TYM Fund small loan project, the VWU has modeled itself on a successful microfinance institution in the Philippines – the Center for Agriculture and Rural Development (CARD). The TYM Fund has adopted CARD's loan and savings technology, while CARD has supported the VWU by providing consultants on several occasions.

Through CARD, the VWU eventually approached the German Sparkassenstiftung für internationale Kooperation (Savings Banks Foundation for International Cooperation). A partnership project supported by the German Federal Ministry for Economic Cooperation and Development (BMZ) and involving CARD, the Sparkassenstiftung and the Sparkasse Essen (Essen Savings Bank) has been run-

Germany as a microfinance pioneer

The end of serfdom, the beginning of industrialization in the nineteenth century, together with the introduction of free trade, brought economic freedom and independence to the people. But it also created serious economic and social problems, above all because of migration to the cities and the break-up of traditional family structures. During this time, and building upon private initiatives and supported by municipalities and local authorities, the first Sparkassen (savings banks) were founded, with the specific aim of supporting workers and people in need. Their predecessors, such as «widows and orphans banks», had emerged in the late eighteenth century. In the middle of the nineteenth century, Friedrich Wilhelm Raiffeisen and Hermann Schulze-Delitzsch established cooperative self-help organizations for farmers and tradesmen. And so the first Raiffeisenbank (rural credit associations) and Volksbank (credit unions) were born. In the savings and cooperative banks, which were usually very small and based locally, savings deposits were accepted and micro loans distributed. They were among the first microfinance institutions in the world.

ning for the past eight years. These German partners have helped CARD gradually transform the previously informal microfinance NGO into a licensed bank – the CARD Rural Bank. CARD also targets poor women in rural areas, who normally would not have access to loans, savings deposits or basic insurance. With German assistance, CARD has succeeded in operating profitably. In eight years, customer numbers have increased from 10 000 to over 130 000.

Now VWU would like once again to follow CARD's example. In 2004, a new partnership project was agreed with financial support from BMZ. The aim is to make the TYM Fund independent and to turn it into a «proper» microfinance bank. The Sparkassenstiftung and the Sparkasse Essen are involved on the German side, passing on German savings banks know-how and experiences from the CARD project. CARD itself is involved in the project, no longer receiving assistance but giving advice.

The TYM Fund has a hard road to travel. Its staff know the core business and understand how to work with small loans, savings and micro insurance. Now the challenge is to develop the internal structures and the technical banking expertise which will be necessary to ensure the TYM Fund continues to operate in the long term.

Professional – profitable – socially responsible

The TYM Fund has decided to work professionally in all areas to ensure its long-term profitability. Only in this way can it fulfill its social mandate in the long term. The case of the Mexican cajas illustrates how a lack of professionalism risks resulting in losses and even fraud.

The keys to success – both in the history of the German Sparkassen and for microfinance institutions in developing countries today – certainly lie in a wide range of areas. Professionalizing the management and being integrated into the formal banking sector, including being subject to the relevant supervisory authorities, are certainly important areas. It is essential that the banking supervisory authority creates rules that are adapted to the needs and possibilities of microfinance. This has been achieved in Mexico with the LACP law on savings banks of June 2001 and in Vietnam with the decree on microfinance of March 2005.

Incorporating MFIs into the formal financial sector obliges them to work professionally and profitably. Only by working professionally and therefore profitably can they fulfill their social mandate consistently in the long term.