Is Combined Microfinance an Instrument to enhance Sustainable Pro-Poor Public Policy Outcomes?

Koen Rossel-Cambier

Product diversification involving simultaneously microcredit, savings or insurance services – also called combined microfinance (CMF) – can both leverage and challenge policy outcomes. This paper reviews two complementary questions in this regard: Which are the possible effects of CMF on public policy?; and; How can public policy influence CMF outcomes? A literature review, findings from qualitative assessments and a case study in Barbados highlight the increased challenging environment when supervising, regulating and promoting CMF. When preparing regulation, one has to ensure that the necessary technical and organisational capacity is in place to ensure proper monitoring and oversight. When supporting CMF, policy makers should strive at enhancing smart ways of subsidizing. CMF may stimulate economic and outreach policy outcomes. Still, as it can have adverse effects on the depth of poverty outreach, pro-poor and gender specific policy measures need to be put in place to accompany MFIs engaging in CMF. This paper calls for a more ambitious research agenda to accompany the increasingly complex demand and supply side elements relating to CMF public policy oversight.

Keywords: microfinance, microinsurance, microcredit, microsavings, public policy

JEL Classifications: C12, G21, G22, L31, O54

CEB Working Paper Nº 11/013
2011
Is Combined Microfinance an Instrument to enhance Sustainable Pro-Poor Public Policy Outcomes?

Koen Rossel-Cambier

Abstract:

Product diversification involving simultaneously microcredit, savings or insurance services –also called combined microfinance (CMF)- can both leverage and challenge policy outcomes. This paper reviews two complementary questions in this regard: Which are the possible effects of CMF on public policy?; and; How can public policy influence CMF outcomes? A literature review, findings from qualitative assessments and a case study in Barbados highlight the increased challenging environment when supervising, regulating and promoting CMF. When preparing regulation, one has to ensure that the necessary technical and organisational capacity is in place to ensure proper monitoring and oversight. When supporting CMF, policy makers should strive at enhancing smart ways of subsidizing. CMF may stimulate economic and outreach policy outcomes. Still, as it can have adverse effects on the depth of poverty outreach, pro-poor and gender specific policy measures need to be put in place to accompany MFIs engaging in CMF. This paper calls for a more ambitious research agenda to accompany the increasingly complex demand and supply side elements relating to CMF public policy oversight.

**Keywords:** microfinance, microinsurance, microcredit, microsavings, public policy

**JEL:** C12, G21, G22, L31, O54
1. Introduction

In many countries, national and regional pro-poor public policies allow both protective and promotional measures to improve the living conditions of vulnerable populations. While social assistance schemes will always be necessary to assist the most indigent, market-based solutions such as microfinance, can be efficient and fiscally attractive options to meet the financial needs of poor households and small enterprises. Unfortunately, the microfinance sector is also criticized for its ‘history of subsidized credit intended for the poor being manipulated and diverted to the richer and more powerful’ (Rahman, 2004). Hence, from an ethical point of view, public policy makers must, when investing in microfinance, ensure that their interventions achieve their intended pro-poor development results (Hudon, 2008; Atchison, 2004).

When Yunus started Grameen, his focus was not on microfinance but on microcredit (Rutherford, 2005). Moving to microfinance from the narrower goal of microcredit begins with the recognition that poor households want to save and insure as well as borrow. Today Grameen itself, has taken up the cause of savings and insurance with energy and innovation (Collins et al., 2009). Worldwide, one can observe an increased tendency towards the delivery of combined microfinance (CMF), which is the delivery of multiple financial products of different nature such as loans, savings or insurance (Rossel-Cambier, 2009).

This changing outlook may lead to both challenges and opportunities for the public governance of MFIs and various questions can come to one's mind: Does CMF contribute to pro-poor policy outcomes? Can it enhance the sustainability of policy interventions? If CMF effectively enhances the intended pro-poor development results in a sustainable way, it may become a strategic instrument of policy makers for future planning and support interventions.

While selected literature has dealt with public policies on microcredit, microsavings or microinsurance as separate entities, little research has explored the role of policy towards combined microfinance. Public policy –at macro and micro levels- has an interest in enhancing local development and investment (Renneboog et al., 2008), and this can be stimulated through microcredit. Still, CMF may leverage these efforts. Tesar (1991) finds that not only credit, but also savings tends to contribute to economic development. Insurance
policies –including microinsurance- can help enhancing the predictability of socio-economic development (Maccord, 2004). Hence, one can ask how public policy should deal with CMF?

This research will review these two complementary research questions by triangulating various sources of information. It refers to literature on microfinance, a case study in Barbados and builds on previous empirical cross-sectional analysis in Latin-America and the Caribbean.

This paper is organized as follows. The second section presents the analytical framework. The following section reviews the first research question dealing with the possible effects of combined microfinance on economic and social public policy outcomes. The following section looks into the role of public policy on CMF, referring to literature and a case-study in Barbados. The last section draws conclusions and makes recommendations for future action and research.

2. Analytical framework

Little evidence is gathered on the possible effects of CMF on development outcomes and public policies. Still, with the widespread practice of CMF, one has to take stock of past lessons learned. Policy making should not be considered in isolation, but in its relation with the key stakeholders (Rossel-Cambier, 2008). At the microlevel, the main stakeholders are the clients and the microfinance providers, and policy makers have different ways to influence these demand and supply actors. Economic policy results aim at strengthening the situation of supply side actors -MFIs- to make them sustainable at the long term. Pro-poor policies aim at enhancing the breadth and the depth of outreach of the MFI to its clients.

Policy makers generally aim at promoting both social and economic outcomes. While the social outcomes are part of their pro-poor policy objectives, they also have a stake in seeing the MFIs taking on their task in a sustainable way beyond government intervention. This limits their dependence on continuous funding injections and allows fair competition.
This paper aims at gathering evidence if combined microfinance can be an instrument to enhance sustainable pro-poor policy outcomes by reviewing two complementary research questions. In one hand it explores how CMF can have an effect on social and economic policy outcomes. In the other hand it reviews how public policy—in its turn—can influence CMF to enhance these policy outcomes.

Aiming at providing a comprehensive approach to the available knowledge, this research triangulates three sources of knowledge: available literature, quantitative surveys and a case-study. Literature has focused on the role of policy towards microcredit (Gutiérrez-Nieto et al., 2009; Bassem, 2009, Balkenhol, 2007; Labie, 2001), and a rich historical literature exists on savings policies (Mol, 1992; Adams, 1978). Recently, there has been an increased interest on the role of public policy towards microinsurance (ILO, 2010; Churchill, 2006; Fonteneau and Develtere, 2004; McCord, 2004). This research refers as well to a quantitative cross-sectional analysis involving 8500 observations of 250 MFIs in Latin America and the Caribbean, available from the MixMarket\(^1\). It explores how both economic and social policy outcomes can be bridged. Recognising that indicators are limited in their ability to describe a specific situation, this chapter reviews also insights from a case study on policy building around CMF in Barbados. This allows better understanding of the process and reveals complementary qualitative elements. The case-study also brings forward good practices and lessons learned dealing with public policy.

3. Possible effects of combined microfinance on economic and social public policy outcomes

3.1. Social versus economic policy outcomes: literature background

Healthy MFIs have a stake in enhancing both social and economic goals. In one hand, they want to achieve their social mission by reaching out to the unbankable and vulnerable populations. In the other hand, they need to ensure that their activities can be continued over time and hence is economically sustainable. Unfortunately, practice suggests that the reality remains challenging. In a global survey, Christen et al. (2004) observe that MFIs, despite their

\(^1\) See: www.mixmarket.org
vast outreach, only serve a minority of the unbankable clientele they were created for, and many suffer significant limitations, such as financial services unfriendly to clients, weak loan collection, subsidy dependency, political domination, and lack of supply-driven focus on poor clients. Agier and Szafarz (2010) and Labie et al. (2009) suggest that worldwide there exist still various forms of gender discrimination in small-business lending.

Hermes et al. (2007) suggest that there is empirical evidence on a negative correlation between social and economic performance of MFIs. In literature and policy circles there is an ongoing debate between different camps on how to approach this trade-off (Makame and Murinde, 2006). The "welfarists" promote the social performance and outreach goal (Woller, 2002; Rosenberg, 2006) while the "institutionalists" stress the importance of sustainability and efficiency (Rhyne, 1998; Isern and Porteous, 2006). A third group promotes a more balanced view, claiming that both approaches can go hand in hand (Morduch, 2006; Helms, 2006). Applying this debate to the first research question, one can wonder whether the trend towards CMF is part of the expanding commercialisation of MFIs, or does it bring MFIs closer to the needs of low income clients? Or could CMF be an instrument to enhance both the social and economic interests of MFIs?

CMF could be considered as a pro-client factor as it allows clients to access a wider range of products. Still, in practice, the situation is more complex. Research tends to claim that CMF can be good for the sustainability of MFIs (Ahlin and Yang, 2008). Galema et al. (2010) suggests that commercialisation is the driving factor of CMF. Still, too much focus on economic performance can lead to adverse effects for social policy outcomes. Often, guided by financial targets and performances, MFIs can loose focus from their social mission (MacIntosh and Wydick, 2005; Labie, 2004). In the case of “mission drift”, MFIs would increase efficiency by enlarging the average loan size in the process of scaling-up (Mersland and Strøm, 2010; Armendáriz and Szafarz, 2009). The continued pressure for commercialisation may also involve increased profit making and the setting of high interest rates (Ashta and Hudon, 2009). In case of microsavings and microinsurance, various product restrictions can be put forward, which enhance the organisation’s economic performance, but can create a domino effect of access barriers leading to limited outputs for the most unbankable clients.
In summary, CMF can have different effects on public policy outcomes. Policy makers should be aware of the weight they give to economic versus economic outcomes when designing policies. By promoting CMF, they may want to enhance the pro-poor nature of microfinance interventions and aim at tackling access barriers towards vulnerable clients. Alternatively, policy makers can consider financial product diversification as part of a move towards the sustainability of MFIs. In this case, they may want to explicitly prefer –from an institutionalist perspective—supporting sustainability and competitiveness objectives over the inclusion of unbankable clients. Public policies on CMF can also seek the most adequate balance between both social and economic outcomes and hence aiming at achieving both pro-poor and sustainability outcomes.

3.2. Findings from empirical cross-sectional analyses

A review of the presence and characteristics of combined microfinance in Latin America and the Caribbean suggests that the majority, 56%, are combined in nature (Rossel-Cambier, 2009). As there are various ways of engaging in microinsurance, one can make a distinction in function of its ‘intensity’. Next to low intensity insurance (credit insurance only), one can define middle intensity insurance as the delivery of two insurance products and high intensity insurance as the supply of three or more insurance products. The delivery of health insurance, because of its complex nature, can also be considered as high intensity insurance. The review observes that out of the 250 microcredit schemes, 37.6% offer as well savings, 21.6% provide credit insurance; 4.8% medium intensity insurance and 12.4% offer high intensity insurance.

{Insert table 1 here}

A cross-sectional empirical analysis explores the possible effect of CMF on the economic performance of MFIs (Rossel-Cambier, 2010a). Building on 7500 observations of 250 MFIs in Latin America and the Caribbean, the study compares MFIs offering credit only with those combining credit with respectively savings and insurance. By using multiple regression analysis, the research suggests that there is a stimulating effect of savings and insurance on the efficiency of MFIs. These findings can be expressed as follows:

\[ E[O_{e_lh}|W] - E[O_{e,m}|W] > 0; \]  
\[ E[O_{e,hs}|W] - E[O_{e,m}|W] > 0. \]
In the equations (1) and (2), $E[O_e|W]$ is the expected value for efficiency of either a mono-product ($O_{e,m}$) or a combined microcredit scheme offering high intensity insurance ($O_{e,hl}$) or savings ($O_{e,ls}$) in a context $W$.

The survey also suggests that, in case of a microcredit organisation offering savings, the availability of credit insurance also enhances productivity. This observation can be expressed as follows:

$$E[O_{p,hl}|W] - E[O_{p,ls}|W] > 0.$$  \hspace{1cm} (3)

In the equation (3), one can expect a higher value for productivity in case of credit and savings schemes with credit insurance, $E[O_{p,hl}|W]$ in comparison with those schemes with only credit and savings MFIs, $E[O_{p,ls}|W]$, both in the context $W$.

The main reasons for these effects on productivity and efficiency can be attributed to the various dimensions of economies of scope which are generated by the multiple delivery of financial services. CMF can lead to shared fixed costs as well as reduced transaction costs, marketing and outreach. The analysis did not find evidence on the effects of CMF on the sustainability and portfolio quality of MFIs.

Another research, involving 3500 observations from the same region, reviews the effects of CMF on the social performance of MFIs (Rossel-Cambier, 2010b). The study suggests that there are stimulating effects of CMF on the breadth of outreach of MFIs (number of clients), as these respond to more need and hence naturally would attract more customers. This relation can be expressed as following:

$$E[U_{c,lm}|W] - E[U_{c,m}|W] > 0;$$  \hspace{1cm} (4)

$$E[U_{c,hl}|W] - E[U_{c,m}|W] > 0; \text{ and}$$  \hspace{1cm} (5)

$$E[U_{c,ls}|W] - E[U_{c,m}|W] > 0.$$  \hspace{1cm} (6)

In the equations (4), (5) and (6), one can expect a higher value for the number of clients -the proxy for breadth of poverty outreach- in case of respectively middle intensity insurance, $E[U_{c,lm}|W]$, high intensity insurance, $E[U_{c,hl}|W]$ and savings, $E[U_{c,ls}|W]$ in comparison with the value for mono-product MFIs, $E[U_{c,m}|W]$, all in the context $W$. The same study suggests that the combination of credit with savings can lead to a relative decrease in the depth of
poverty outreach, both viewed from gender- and income-related points of view. In other words, the presence of savings is accompanied with a relatively lower participation of poor and female clients. This relationship can be represented as follows:

$$E[U_{\text{DEPTH}_{cs}}|W] - E[U_{\text{DEPTH}_{m}}|W] < 0$$  \hspace{1cm} (7)$$

In this equation, one can expect a lower the depth of poverty outreach when combining microcredit with savings, $E[U_{\text{DEPTH}_{cs}}|W]$ in comparison with the value for mono-product MFIs, $E[U_{\text{DEPTH}_{m}}|W]$, both in the context $W$.

In summary, the three empirical surveys support the strong presence and diversity of combined microfinance in practice. They find empirical evidence of a stimulating effect of CMF on economic performance (efficiency and productivity) of MFIs and also a positive effect on the breadth of poverty outreach. They also suggest that CMF is associated with low depth of poverty outreach, viewed both from a gender and income related lens.

### 3.3. What is the relevance of these findings for public policies?

Public policies aim at both achieving social and economic outcomes. Still, is there a real trade-off between social and economic policy results? A relevant indicator for economic performance is the operational expense ratio (OER), an indicator for efficiency. Social performance, especially its depth of outreach to low-income persons is often measured by the average loan per borrower per gross national income (ALBpGNI)\(^2\). Referring to a database including 250 MFIs in Latin America and the Caribbean (Mixmarket, 2008), chart one presents the distribution of these two variables. Comparing the respective values, one can observe a trade-off between economic and social performance as the higher values of OER are related with the lower values of ALBpGNI and the higher values of ALBpGNI correspond with lower values of OER.

\hspace{1cm} \{Insert chart 1 here\}

---

\(^2\) For definitions of the various variables, see The SEEP Network (2005) and http://www.mixmarket.org/en/glossary
When overviewing CMF, can public policies influence the enhancement of both economic and social performance? The potential of achieving both social and economic outcomes, when engaging in CMF, can be expressed by the following equation (8):

\[
\left[ \frac{E[O_c|W] - E[O_m|W]}{E[O_m|W]} \right] + \beta \left[ \frac{E[U_c|W] - E[U_m|W]}{E[U_m|W]} \right] \geq 0
\]

Here, \(E[O|W]\) is the expected economic performance of either a mono-product \(O_m\) or combined \(O_c\) MFI - measured by the same indicator -, given (or conditional on) the information set \(W\). Similarly for social performance, \(E[U|W]\) is the expected utility of either a mono-product \(U_m\) or combined \(U_c\) microfinance scheme. In case of improved economic performance: \(E[O_c|W] - E[O_m|W] > 0\); and in case of enhanced social performance: \(E[U_c|W] - E[U_m|W] > 0\). The weight, \(\beta\), reflects the level of importance given to social performance in relation to economic performance.

Public policy has a stake in enhancing both social and economic improvements when investing in CMF. From the equations (1), (2) and (3), one can understand that CMF may have stimulating effects on the economic performance of MFIs. Equations (4), (5) and (6) also suggest that CMF has a stimulating effect on the social performance (breadth of outreach). Hence, when applying the equations (1) to (6) on the equation (8) above, one can find an overall positive result on both the economic and social performance of the MFI.

Still, in case of inserting the equation (7) in the equation (8), CMF influences one aspect of the equation positively (economic performance) and the other negatively (depth of social performance). This observation has implications for policy responses, especially if the overall objective of the interventions is to support pro-poor policies. In this case, special attention should be given to the weight, \(\beta\), reflecting the level of importance given to social performance in relation to economic performance. While promoting, regulating or overviewing the sector, policy makers should ensure that CMF schemes continue achieving the right balance between social (depth) and economic performance and the overall equation (8) remains positive, taking into account \(\beta\).

In summary, the empirical surveys suggest that the main issue in the trade-off between economic and social performance is not the necessarily the breadth, but the depth of poverty outreach. If the MFI -by its mission objectives- envisages poverty alleviation or if the MFI is
subsidised for poverty alleviation purposes, a careful balance has to be taken into account. In this context, when governing CMF, public policy may want to encourage additional design features to ensure that cumulative gender and income related barriers are taken into account.

4. What is the role of public policy towards combined microfinance?

One can observe that there has been a shift in focus of public policies on the role of microfinance for more than five decades. In the 1960s and 1970s, many policies focused on loans to support agricultural technology investments. Later, the focus broadened to include credit provision to the rural and urban population engaged in other enterprises, such as trade, handicrafts, and small-scale industry. Also informal savings schemes such as rotating credit and savings schemes (ROSCAs) were progressively recognised (Mol, 1992) and since the end of the 1990s, microinsurance has been defined and considered as a separate issue (Dror and Jacquier, 1999). Presently, public authorities are more proactive on microfinance (Labie and Mersland, 2010) and in many cases consider it as a poverty eradication instrument, contributing to the Millennium Development Goals (Helms, 2006). As these goals deal with multiple social outcomes, MFIs are often encouraged to contribute to various social programmes.

What is the role of public policies towards CMF? From the demand side the findings suggest that CMF should be encouraged to enhance the breadth of outreach of MFIs. Still, as CMF may be accompanied with a relatively lower participation of poor and female clients, policymakers can develop mechanisms to ensure that the neediest also have access to a wide spectrum of financial services (Honohan, 2008).

In the same time, public policies have an interest in economic development. From this supply side point of view, public policy should encourage CMF as it could contribute to the efficiency and productivity of MFIs. It can provide an adequate regulatory framework which allows fair competition, product diversification and gives MFIs the opportunity to grow and expand.
Policy makers could develop various mechanisms to enhance the sustainability and the economic performance of new products being developed by MFIs (Armendariz and Morduch, 2010). From this point of view, public policies supporting the MFIs, have the intention to ensure that they can become more competitive while in the same time protecting the clients and the MFIs from various risks related to CMF.

Public policy can make use of various instruments, both promotional and protective, to enhance social and economic policy outcomes. This section reviews selected literature on the possible policy interventions towards CMF and analyse relevant elements of policy making in Barbados.

4.1. Mechanisms for policy intervention in CMF: literature review

4.1.1. Policy oversight and regulation

The prime objective of regulation is to protect the financial system against harmful practices considered risky (Van Dijck, Nusselder and Sanders, 2004). The role for governments towards microfinance and private sector development has been subject to much public debate, in particular when determining the adequate balance between the liberalisation and the regulation of the financial sector. Some suggest that microfinance has special features that pose unique oversight challenges linked to its client base, lending methodology, transaction costs, portfolio composition and governance which should logically be accompanied with MFI regulations which are stricter than the norm (Rosengard, 2010). Others argue for little regulation and refer to the small size operations of microfinance and the assumption that cost of developing and implementing regulations exceed the benefits accrued from it (Arun, 2005).

Different opinions exist on how policy should respond to its demand and supply side market elements. This research will not enter into this debate. One can observe that today there is a relative consensus that policymakers have an important role in setting appropriate regulation and creating a supportive environment for financial product development (Helms, 2006). Regulation can legitimize the role, improve their professional standards, and ensure accountability to the general public of MFI actors (Mac Abbey, 2008). Public policy should be designed to facilitate the entry of new private actors without abandoning the markets that
could not work without some public support (Hudon, 2006). It should ensure that an environment is created where product diversification, business development and sound competition go hand in hand with the protection of the clients (Labie, 2007). Adequate regulation accompanied by law enforcement and information transparency is a key pillar to ensure this type of environment (Sriram, 2005). Rosengard (2010) promotes the proportionality principle as a framework for making prudent selections among the main MFI regulatory and supervisory options. The latter underscores that Governments have a role to play in terms of regulation and supervision but that both issues are not the same. Regulation entails setting standards and determining rules of the game; supervision is monitoring and enforcing compliance with these regulations.

Regulation can also enhance equity and equality to ensure that possible access barriers are being mitigated. In the insurance sector in the European Union for example, research revealed a number of practices of gender discrimination. As a policy response, the European Council implemented a directive to ensure equal treatment between men and women in the access to and supply of goods and services (European Council, 2004). Similar policies or regulations could be applied and adapted to the microfinance sector.

The evolution from mono-product to combined product delivery of many MFIs offers both challenges and opportunities for policy oversight and regulation. While CMF can allow a number of economies of scope towards development outcomes, it can entail new risks for MFIs such as increased complexity, lack of transparency and covariance risks (Rossel-Cambier, 2010a). The often rapidly growing and quickly evolving MFIs have a plethora of different institutional structures, products and markets, and thus, can have significantly different vulnerabilities that pose myriad risks to their customers and their markets (Rosengard, 2010). The context and legal framework in each country or state may offer a different context, which makes it difficult to draw general recommendations on how, when and where combined delivery of credit, savings or insurances should be regulated.

Cull, Demirgüç-Kunt, and Morduch (2009) and Labie (2007) argue that regulation is critical, especially for MFIs offering deposit services. Prudential regulation generally refers to regulations such as accounting policies and standards of financial structure are intended to protect depositor’s interest and encourage competition in the sector. In many countries, the microcredit institutions are not included under financial regulations which legally restrict
them to engage in providing savings services. Arun (2005) argues for sector specific regulation which allows MFIs to access deposits and refers to complementary regulation such as deposit insurance to mitigate the possible risks involved.

The situation is more complex for microinsurance. Insurance regulation generally refers to reserve regulations, capital requirements, investment restrictions, role of the insurer and policy details (Brown and Churchill, 2000). Many microinsurance providers are operating in legal loopholes, outside the insurance laws. The risks and problems associated with this situation are considerable and in the long term. To correct this situation, MFIs could establish a separate insurance company or develop partnerships with existing insurance companies (Kaplan and Morduch, 2010). They can consider working as an agent but should be aware that there may be specific legal conditions to act as an insurance agent relating to legal status or training certification (Wiedmaier-Pfister, 2004).

Countries need effective, nation-specific regulatory regimes (Hulme et al., 2009). Still, regulating CMF becomes more complex when adapting these to sector-specific conditions (Arun, 2005). Rossel-Cambier (2009) observes the increased diversity when looking at MFIs from a CMF lens. Contrary to NGOs, one can note that cooperatives and banks strongly engage in microsavings and insurance products. Policy responses should hence be adapted to these parameters. Where a more balanced approach towards CMF can be foreseen for banks and mature cooperatives, close monitoring and oversight may be needed for the regulation of NGOs. Care should be taken not to excessively regulate, which restricts innovation and outreach (Mac Abbey, 2008).

Supervision, in itself, can also have an effect on the performance of MFIs. Drawing on a database of 245 MFIs, Cull, Demirgüç-Kunt, and Morduch (2009) suggest that regulation carries costs for the MFIs affecting their economic performance (reduced profitability). They also suggest that supervision is associated with substantially larger average loan sizes and less lending to women, which are indicators of decreasing social performance. In the case of CMF, overregulation or contradicting rules can lead to market inefficiencies.

Often, the know-how and the technical capacity of regulators to adequately overview and supervise CMF may be limited. As quoted from Rosengard by Labie (2007), "One should only regulate what one can supervise; one should only supervise what one has regulated".)
Combining microfinance services of different nature – e.g. credit versus health insurance – means often bringing together different oversight organisations (and their often little complementary internal departments and programmes) with different approaches and technical expertise. The combination of products offers new opportunities but also challenges related to expertise and coordination for public policy bodies. The delivery of the numerous oversight, regulation or promotion functions in distinct government “compartments” for example can lead to weak responsiveness and limited monitoring supervision. In the other hand, the realization that poverty is a multidimensional problem has led many agencies to be working on numerous fronts at the same time which can dilute oversight capacity (Helms and Latortue, 2004).

4.1.2. Promoting combined microfinance

Public policies can support microfinance, and especially CMF, in a number of ways. Historically, governments have been supporting financial services of different nature. Cull, Demirgüç-Kunt, and Morduch (2009) argue that while state-run banks have a generally poor record as lenders, government savings banks and postal savings schemes have proven relatively successful around the world.

The access to CMF for low income people is mainly limited because of a domino effect of access barriers, mostly linked with affordability. Hence, could subsidization be the right answer? Or will this lead to additional subsidy dependency? Subsidization can have different faces. Public funds entrusted to a MFI include soft debt, grants or discounts (Schreiner, 1998).

Microfinance support projects can be also be different in nature. One can imagine a MFI such as a state-owned bank that provides direct services to poor clients. It can take the form of a development fund that finances various MFIs, such as NGOs or private commercial banks. Support can be given through a social fund or community development project that provides revolving credit funds. Also technical assistance can be offered by means of capacity-building, policy or management support (Helms and Latortue, 2004).

Subsidizing combined microfinance schemes can have also unintended consequences. Aniket (2006) finds that subsidising the cost of capital restricts the ability of the poorest to participate in the group lending mechanisms that include saving opportunities. A study in Eastern Europe and Central Asia finds that there is a correlation between the costs of MFIs and the subsidies (Hartarska et al., 2006). CGAP (2006) when evaluating the effectiveness of the portfolio of its most important promoters, revealed that less than a quarter of the microcredit projects were...
sustainable. In a survey on involving 258 health microinsurance schemes, Baeza (2002) observes that 66% of the schemes do not bear the financial risk of the insurance function because of subsidization. Hence, adding new financial products may lead to new forms of subsidy dependency.

Governments can also play a role in providing financial protection for savings or loans. Still, these mechanisms are linked with new risks. Ioannidou and Penas (2010) find evidence in Bolivia that the introduction of deposit insurance can lead to higher risk-taking behaviour of financial institutions. Also partial credit guarantee schemes can be set up by governments. Still, the attractions of these for public policy can be illusory. In practice, the actual fiscal cost of these schemes has varied widely across countries and has represented a high per dollar subsidy in some cases (Tedeschi, 2006).

Similar to regulation, also for promotion one also should take into account the type of MFI which is being supported. Cull et al. (2009), referring to a dataset including 346 MFIs, find that subsidies and non-commercial funding continue to be important to NGOs, while banks rely mainly on social investment and commercial sources of capital.

Armendariz and Morduch (2010) promote the use of “smart subsidies”, carefully designed interventions that minimize distortions, mistargeting, and inefficiencies. One of these market distortions can be the lack of education and information. There is evidence that clients with a poor understanding of insurance are less likely to use it (Patt et al., 2010). Gine and Yang (2009) highlight from a case-study in Malawi that not only income is a factor for the participation in CMF, but also education. Hence, public policies should also enhance transparency, public information and education on the benefits, limits and risks of engaging in microloans, savings and insurance schemes.

Still, it may be difficult to draw general recommendations in this area. Hatarska et al. (2010) highlight that public policies designed to improve MFIs performance to expand their services should take into account regional, organisational and contextual characteristics. Public policy initiatives could support the enhancement of appropriate design of CMF. The design of
products influences adoption and usage-and ultimately economic and social results (Karlan and Morduch, 2010). Drawing from a research-action health insurance participatory decision tool in India, Dror et al. (2007) suggest that involving prospective clients in benefit package design can be done without compromising the judiciousness of rationing choices. Also agents in MFIs must be given incentives to select clients in accordance with the MFI's pro-poor objectives (Aubert, Janvry and Sadoulet, 2009). Public policy could encourage MFIs to follow this road. Prerequisites to this are clear goal setting, realistic pricing and attention to the incentive features of operational design (Tedeschi, 2006; Jain and Mansuri, 2003). Subsidizing new financial products has to carefully take these elements into account.

Microfinance advocates, wary of subsidies, have energetically sought to move microfinance to a commercial basis, free of long-term subsidies (Hudon, 2007). CGAP (2004) suggests that there is a general consensus that subsidies are needed to encourage product innovations. These innovations often go hand in hand with the development of product diversification, and hence can lead to CMF. In this context, there is a need to carefully review if the social return on investment matches the expectations. New microfinance products are being set up but not all achieve acceptable results in terms of efficiency, quality, effectiveness and outreach. If income poverty alleviation is the objective, -from a public policy point of view- there may be alternative instruments to CMF promotion such as social assistance schemes or conditional cash transfer programmes (Abdelmoumni, 2005). Higher performance means that funds entrusted to a new product produces more benefits and less costs for the poor than another social programme (Schreiner, Tin and Sherraden, 2005). Bhattachamishra and Barrett (2010) suggest that there exists little careful evaluations on microfinance support. Still, the situation may even be more complex to appreciate in case of CMF.

4.2. Case-study: public policy and combined microfinance in Barbados

Since independence, Barbados has achieved significant levels of human development. A relatively balanced socio-economic public governance may have contributed to these results (Rossel-Cambier and Romagnoli, 2009). Public opinion in Barbados is convinced that also microfinance –in particular the cooperative movement- has been most instrumental to these socio-economic achievements. In Barbados, microfinance is provided by NGOs, non-bank financial institutions and credit unions. In particular the credit unions, which currently cover
over 80% of all households, are actively combining loan, savings and –to a limited extent-
insurance products.

A case study in Barbados, as presented in Chapter six, observes the stimulating effects of
CMF on the efficiency and productivity of MFIs, in particular relating to marketing and cost-
effectiveness aspects of deposits for loan delivery. It also suggests that CMF contributes to
the breadth of outreach of the cooperative unions. While this chapter recognises various social
advantages, it highlights qualitative information on the possible cumulative exclusionary
effects when providing CMF to low-income groups, especially related to affordability and
access to information.

Taking into account these findings, one can wonder how public policies in Barbados are
dealing with CMF, both in terms of regulation and promotion. This information can lead to
deeper understanding of the possible practical and qualitative issues at stake when governing
CMF.

4.2.1. The Regulatory Framework related to Combined Microfinance in Barbados

Legislation directly and indirectly relevant to CMF in Barbados are the Small Business Act,
the Financial Institutions Act, the Exempt Insurance Act, the Friendly Societies Act and the
Co-operative Societies Act

The Small Business Act (2002) aims at enabling the development of the small business sector
and sets the conditions to access the public credit guarantee scheme (see infra). The Financial
Institutions Act (1997) ensures the regulation of the financial institutions such as commercial
banks, trust companies, finance companies, merchant banks and brokerage houses. The
Exempt Insurance Act (1998) governs the insurance companies which cover risks such as
property insurance, accident and sickness. Insurance can also refer to a number of public and
private liabilities.

The NGOs are covered by the Friendly Societies Act (last revised in 1985). While the
language of the legislation may be outdated, with its first articles dating back from 1905, it
refers to combined microfinance from very early. In its original article 46 for example, it
refers to the limits of small loans which can be given up to a maximum of 50% of the “life insurance value” of the client. Its article 47 describes the conditions on how savings can be used for a microcredit facility.

The Co-operative Societies reviewed Act (2007) governs the registration, management and oversight of cooperative societies in Barbados. It remains most reserved on the combination loans-insurance as it indicates that no credit union can underwrite insurance or act as agent for any insurance company. In practice however, these stipulations don't limit the cooperative unions in developing collaborations with external insurance companies. The cooperative unions are also not allowed to provide cheque services or offer credit card services. The relationship between deposits and loans is monitored on a monthly basis by the Registrar of Cooperatives and it is required that at least 10% of the deposits should remain in liquid form. While the Act went through a number of updates over the years, the IMF (2009) recommended the Government a specialised credit unions law which could better tailor oversight by clearly defining the permissible and prohibitive financial products.

The complexity and interrelationship of the financial services has also an impact on the functioning of the national oversight mechanisms. The regulatory framework of the Barbados financial services sector revolves around the Central Bank of Barbados, the Ministry of Finance and the Barbados Securities Commission. The office of the Registrar of Cooperatives of the Ministry of Commerce, Consumer Affairs and Business Development, is responsible for the regulation and supervision of the credit union system and of non-financial cooperatives.

A study on the regulation and supervision of non-bank financial institutions (Lawrie Savage & Associates Inc., 2005 in IADB, 2007) indicates that the Registrar of Cooperatives lacks technical capacities in financial analysis. The assessment highlights that the agency is weak with relation to risk-based supervision, a most relevant aspect towards CMF policy oversight. During the drafting of this research, the government of Barbados is preparing a merged ‘Financial Services Commission’ which would integrate regulators of the Co-operatives Department, the Securities Exchange Commission, the Business Development Unit of the Ministry of Economic Affairs and Development and the Office of the Supervisor of Insurance and Pensions. The merge and combination of these agencies should allow the country to achieve economies of scope. It could also allow approaching the combined nature of various
financial interventions in a more coherent way leading to enhanced supervisory monitoring and law enforcement.

4.2.2. The government of Barbados as promoter of combined financial products

In Barbados, various programmes support and promote development of the small and microenterprise sector. Such as, The Enterprise Growth Fund provides technical assistance and financing for venture capital, tourism, small hotels, agricultural, industrial investment, employment and innovation. The Youth Entrepreneurship Scheme (YES) targets young entrepreneurs. Various organisations provide management training and technical assistance such as the University of the West Indies, the Caribbean Development Bank, the Barbados investment and Development Corporation and the Small Business Association and Development Centre.

The government is undertaking a number of programmes to directly support microfinance initiatives. It financially supports for example the MFI FundAccess, being its main shareholder and by subsidizing a part of its interest rates for microloans. It also runs the Agricultural Commission which offers subsidized loans for farmers. Some of its previous initiatives such as the Barbados Development Bank or the Urban Enterprise Programme have closed because of lack of financial sustainability.

The fiscal policy in Barbados has promoted savings within credit unions. Until 2010, the government has allowed citizens to claim up to 6500 USD per year in income tax deductions from their savings plan with a credit union. This is in addition to 5000 USD in contribution to a registered retirement savings plan. By limiting the basic personal tax allowance, it aims at relatively give more advantages to low-income groups.

The government is implementing directly financial services through its guarantee schemes which can be considered as an insurance mechanism for loan delivery. The credit guarantee scheme for SMEs of the Central Bank of Barbados aims at protecting financial institutions against protection against losses arising from the failure of borrowers to repay their loans (Central Bank of Barbados, 2010). In the event of loss, the Central Bank will reimburse the credit institutions to the extent of 80% to 90% of the loss sustained, depending on the nature
of the business. A guarantee premium is payable by credit institutions at the rate of 1½ per cent per annum.

In 2006, Barbados set up a Deposit Insurance Fund for the recognised financial institutions (Government of Barbados, 2006). The Barbados Deposit Insurance Corporation (BDIC) is administered by a Board which is independent of the Central Bank of Barbados. The deposit insurance initial contribution was set at 0.05% of the insurable deposits from all member institutions and the Central Bank matches this amount. At present they are fourteen members of the Fund, six commercial banks and eight deposit taking financial institutions. The BDIC guarantees insurance coverage of up to US 12,500 for depositors. During the preparation of this case-study, the credit unions are negotiating with government possible access to the national deposit insurance scheme. From an equity point of view – as the credit unions represent broader and deeper outreach to middle and low-income groups- this could be a justifiable contribution to pro-poor sustainable development in Barbados.

Strongly related to governance is the enabling environment for non-state MFI providers to organise themselves in professional networks and representation groups. Fundaccess for example is member of the Caribbean network of microfinance and the Barbadian Youth Business Trust is part of a network in the Caribbean supported by Youth Business International (Lashley, 2004). The Barbados Co-operative and Credit Union League (BCCULL) was set up in 1957 and represents today the interests of 35 credit unions on the island. It provides technical assistance and capacity building to its members. The BCCULL is also directly promoting CMF services to its members. In collaboration with the Co-operators General Insurance Company, it promotes a mutual benefits plan with three different products: life savings, loan protection and funeral grants (BCCULL and CGIC, 2009). These are microfinance products combining loans or savings with insurance mechanisms. This example shows that social representation groups can be instrumental in enhancing combined financial products through pooled efforts.

4.3. Which lessons can one draw from the Barbados experience?

The example of Barbados brings forward the sensitive exercise that governments must undertake to ensure that it protects clients and in the same time allows organisations to grow
and expand their array of services. This case-study illustrates the complex environment of MFI providers, which are different in nature, objectives and outreach functioning. One can observe in Barbados the limits of further product diversification as cooperative unions are not allowed to provide insurance, chequeing or credit card services. Non-governmental organisations are also limited in offering CMF products.

The government of Barbados has a protective role by regulating the various concerned sectors. It could benefit from a new and specific legislation on cooperative credit unions – opposed to cooperative unions in general- which would establish clear terms on the limits and possibilities of product diversification, taking into account the increased competitive environment between credit unions and formal financial institutions.

The diversity of products offered by the same organisations also requires more informed and comprehensive policy support and review. Taking into account the reported capacity problems at the supervisory level, economies of scope can be achieved by carefully merging the different oversight institutions. The move towards a Barbadian ‘Financial Services Commission’ which will overview the insurance, business development, cooperative and securities sectors could allow the government to merge and consolidate technical capacity which can allow them to anticipate and respond more adequately to the multiple opportunities and risks involved.

The government of Barbados has explored various ways of supporting microfinance. While its experiences with direct implementation and subsidization have had mixed results, its indirect subsidization through fiscal incentives (savings with cooperatives until end 2010) and interest subsidisation (in case of FundAccess) have led to more tangible outcomes. The existing credit and savings guarantee schemes –which can be considered as insurance schemes- could be enhanced to protect more vulnerable target groups. The Government of Barbados offers guarantees for loan products of microbusinesses, but it does not allow credit unions to participate in its deposit guarantee plan. A review of the feasibility to include credit unions in a similar deposit guarantee scheme would be recommended from an equity point of view. After all, credit unions serve over 80% of the households, but only about 10% of the total assets of the Barbados’ banking system. Still, in the current climate of high loan delinquency and rising public debt, all elements should be taken into account.
The case-study illustrates the importance of stakeholder representation. Barbados has an enabling environment for professional representation of the various microfinance providers. This allows social dialogue, networking and continuous review of regulation. In collaboration with an insurance company, the representation group of the credit unions promotes to its members combined savings and insurance products. By means of this pooled efforts, it aims at achieving economies of scope and scale when delivering specialised CMF products.

The experience in public governance supports the position that combined microfinance is more adequately supported through regulatory and promotional support balancing carefully pro-poor government intervention and creating an enabling environment for private initiatives. Appropriate regulation, indirect subsidization and social representation can enhance social and economic outcomes by means of CMF.

5. Conclusions and recommendations

This paper has reviewed evidence if combined microfinance can be an instrument to enhance sustainable pro-poor policy outcomes.

Initially, the paper has looked into the question: How can CMF have an effect on social and economic policy outcomes? When considering a stakeholder framework, one can observe that CMF can influence supply and demand factors while respectively enhancing economic and social policy outcomes. CMF can enhance various economies of scope which lead to a better efficiency and productivity of the MFI, and can be stimulating for the broadening of client outreach. Unfortunately CMF can lead to cumulative exclusionary mechanisms which negatively impact its depth of outreach to low-income and gender sensitive groups. Hence, it is not the breadth, but especially the depth of outreach is the main issue of trade-off between economic and social outcomes when introducing CMF. CMF can have positive effects on socio-economic results of MFI interventions, but public policy should pay special attention to its possible effects on pro-poor and gender sensitive outcomes.

This paper has also explored how public policy can influence CMF to enhance these policy outcomes. Building on a literature review and a case study in Barbados, this research notes
that combined financial services have additional challenges for transparent pro-poor public policy. Diversity in the delivery of financial products leads to corresponding complexity for the regulation, overview and support for these MFIs. When preparing regulation, one has to ensure that the necessary technical and organisational capacity is in place to ensure proper monitoring and oversight. When supporting CMF, policy makers should strive at enhancing smart ways of subsidizing, allowing both pro-poor targeting and sustainability objectives to match. This involves carefully balancing the cost-effectiveness and fairness of possible and existing regulatory and promotional measures.

When one examines the relevance of combined microfinance from a stakeholder perspective, one can consider a number of recommendations for policy development.

Public policies should be pro-poor, non-discriminatory and client-centred when dealing with CMF. Beyond loan delivery for business development, low-income households have multiple socio-economic needs such as education and training, emergencies, assets, insurance services or health prevention (Collins et al., 2009). Public policies can initiate appropriate regulation and measures which limit market distortions such as information asymmetry. In this way as many as possible persons are fully informed on the costs, limits and the characteristics of the various financial products offered. Public intervention should support MFIs to ensure that the design of CMF allows the necessary flexibility and conditions to allow maximum access for vulnerable or unbankable persons.

The various sources of information of this study all suggest that combined microfinance can have a stimulating effect on the efficiency and productivity of MFIs. As highlighted by Balkenhol and Hudon (2010), efficiency assessment is a key criterion for policy makers and donors to appreciate the economic performance of the myriad actors in the microfinance sector. Hence, when embracing this new paradigm for efficiency, one should reflect on performance indicators relating to both loan, savings and insurance services in order to more accurately appreciate the relationship between changing input with output elements.

The diversity of CMF increases opportunities for partnerships between the various stakeholders. The literature (Kolk et al., 2008) as well as the Barbados case-study underline the potential of public-private partnerships. Mladovsky and Mossialos (2008), when reflecting on the promotion of microinsurance schemes, suggest that elements such as solidarity, trust,
civil society links, and state-society relations can enhance results. Also Mac Abbey (2008) supports this observation suggesting that the key role of civil society organizations is to develop community capacity to link with formal sector institutions.

The current paper calls for a larger and more ambitious research agenda, building on these first findings. There is a rich ‘acquis’ in the existing literature on savings, loan delivery and more recently insurance. Still, many issues, related to CMF remain untouched.

Research should look into the potential of the wide range of complex interactions imaginable between the various financial product areas. This paper has approached combined microfinance from the point of view of the microcredit organisation which also can offer savings or insurance services. Still, one could also explore the research question from the point of view of respectively microsavings or microinsurance. Many formal insurance companies for example have a large experience in sustainably providing savings products and engaging in private investment and one can imagine that some elements of this model could be translated at the microbusiness level. This research could build on the rich historical literature of microsavings, especially in the rural sector.

Research should focus on the various public policy instruments which could enhance and protect combined microfinance. For example, what are the institutional preconditions for microfinance to succeed in combining diverse financial product areas? Are these the same as for other financial institutions? Should combined microfinance be regulated differently, if so, in what way? In the case of those institutions that provide deposit accounts, should these be covered by the deposit insurance system? Should loan insurance be mandatory to financial portfolios? Should pro-poor MFIs providing CMF have access to special conditions with the central banks? Can models be developed to anticipate the possible impact of public policy regulatory, fiscal or subsidy interventions for savings, loan delivery and/or insurance products leading to socio-economic outcomes?

Future research should support policy makers in developing monitoring and oversight mechanisms which take into account performance indicators dealing with both loan, savings and insurance products. Public and private actors need to continuously question the effectiveness of their intervention. Many reporting and evaluation initiatives are made in a context of project justification but cannot be considered as evidence-based or critical assessments (Rahman, 2004). There is a need for consistent and rigorous evaluations of microfinance (Servet, 2006), and this should include all its financial product areas. Applied
research, formative evaluation and public policy oversight advocates may need to engage in innovative partnerships to ensure that the results of MFIs are sustainable and pro-poor, in line with the intended policy orientations.

Poverty alleviation should not only be viewed from an income-generating perspective, but more as a progress to the achievement of a wide array of freedoms (Sen, 2000). Multiple financial services can widen the array of pathways to work towards the achievement of these freedoms. The ultimate goal of pro-poor public policy is hence –in a sustainable way- maximising leverage allowing MFIs to reach out to vulnerable clients in their efforts to achieve their most fundamental human development aspirations.
References


BAEZA C., (2002), Extending social protection in health through community-based health organizations, ILO STEP-Universitas, 80 pages.


CGAP, (2006), Aid Effectiveness in microfinance: evaluating microcredit projects of the Worldbank and the UNDP, Focus Note 35, 12 pages


MCCORD M.J., (2004), L’attrait, le piège de la microassurance: pourquoi les IMF devraient travailler avec les assureurs, ADA Dialogue, pages 3-30


ROSSEL-CAMBIER K., (2010b), Does Combining Credit with Insurance or Savings Enhance the Organizational Performance of Microfinance Institutions?, Working Paper Centre de Recherche Warocqué - CERMI, Université de Mons, 2010/6, 32 pages.


RUTHERFORD S., (2005), What is Grameen II? Is it Up and Running in the Field Yet? MicroSave Briefing Notes on Grameen II # 1, Nairobi, 2 pages.


SCHREINER M., (1998), A Framework for the Analysis of the performance and Sustainability of Subsidized Microfinance Organizations with Application to Bancosol of


Table 1. Effects of CMF on the economic performance of microfinance institutions (Source: Rossel-Cambier, 2010a)

<table>
<thead>
<tr>
<th>Type of CMF</th>
<th>Sustainability /Financial performance</th>
<th>Efficiency</th>
<th>Productivity</th>
<th>Portfolio Quality</th>
</tr>
</thead>
<tbody>
<tr>
<td>DCI</td>
<td>0</td>
<td>+</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>DMI</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>DHI</td>
<td>0</td>
<td>+</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>S</td>
<td>0</td>
<td>+</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>C</td>
<td>0</td>
<td>0</td>
<td>+</td>
<td>0</td>
</tr>
<tr>
<td>AGE</td>
<td>0</td>
<td>+</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

Legend: effect of the variables (vertical column) on economic performance indicators (horizontal column)

0: No significant effect
+ : Significant positive effect
- : Significant negative effect
0- : Limited possible negative effect

Table 2. Effects of CMF on the social performance of microfinance institutions (Source: Rossel-Cambier, 2010b)

<table>
<thead>
<tr>
<th>Type of CMF</th>
<th>Breadth of Outreach</th>
<th>Gender specific outreach</th>
<th>Depth of outreach</th>
</tr>
</thead>
<tbody>
<tr>
<td>DCI</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>DMI</td>
<td>+</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>DHI</td>
<td>+</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>S</td>
<td>+</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>AGE</td>
<td>+</td>
<td>0</td>
<td>-</td>
</tr>
</tbody>
</table>

Legend: effect of the variables (vertical column) on social performance indicators (horizontal column)

0: No significant effect
+ : Significant positive effect
- : Significant negative effect
Chart 1. The trade-off between economic and social performance: distribution of Operational Expense Ratio (OER) towards Average Loan per Borrower per Gross National Income (ALBpGNI) (N= 245)