

"THE DEVELOPMENT OF MICROFINANCE IN BOLIVIA

FUNDA-PRO

La Paz, Bolivia

methodology integrated with their non-

financial services.

On the other hand, the Institute for the Development of the Small Productive Unit (IDEPRO), was founded in 1986 with the objective of providing business development services as a complement to their financial services. IDEPRO started its Financing activities in 1991, several years after its creation.

Also in 1986 PRO-CREDITO was founded, an organization targeting urban centers using the individual methodology. The success of this institution motivated the creation of a specialized financial entity as a Private Financial Fund (FFP)⁶ in 1995, named Los Andes SA., FIE followed this example and created FIE, FFP in 1997.

In 1991 Programs for Women (PRO MUJER) was formed, an institution dedicated exclusively to lower income women in the semi-urban areas surrounding various cities in the country. PRO MUJER introduced the concept of communal banks or associations as a new methodology with the goal of reaching the poorest sectors of the population.

⁵ Institutions which provide microcredit have operated in Bolivia before this date, for example the National Ecumenical Association for Development (ANED), founded in 1978 and operating since 1979. However, innovations in guarantee schemes were started in the year mentioned.

⁶ Private Financial Funds were established through Supreme Decree No. 24000 of April 12th, 1995, which regulates non-banking financial institutions targeting small and micro enterprises.

The development of the institutional, methodological and legal framework aspects relevant to the microfinance sector has converted Bolivia into a model for other countries. The emphasizes the transformation that several NGOs have undergone as they convert into regulated and sustainable institutions (FFPs). This institutional structure focuses on regulating financial intermediaries dedicated to the small and micro enterprise. One special feature is that it permits these institutions to accept deposits, thus allowing the possibility of providing savings services to microenterprises.

However, not all institutions have followed the model outlined above. In 1996 the institution FAS\$IL was formed as an FFP, by a group of private entrepreneurs to offer services to microenterprises in the department of Santa Cruz.

In addition, other methodologies such as institutions have been developed, as in the case of the Foundation for Production (FUNDA-PRO) and the Bolivian National Finance Corporation (NAFIBO SAM). The former has a program of institutional credit since 1993, working with a variety of financial entities, primarily non-banking institutions; and the latter was created as a specialized financial entity in 1996 to attend to the credit needs of regulated financial institutions. Both institutions have established their own methodologies for channeling resources to different economic sectors through intermediary credit institutions. FUNDA-PRO, the oldest institution in this group, has placed emphasis on providing financial services to entities dedicated to microenterprise activities.

Institutional development has taken diverse paths, in addition to the creation of the FFPs and the "second tier" institutions. The NGOs most active in microfinance have organized two associations which provide assistance to microfinance institutions : the Corporation of Private Institutions to Assist the Microenterprise (CIPAME), by institutions which target urban areas, and the Association of Financial Institutions for Rural Development (FINRURAL), focusing on rural areas.

The constitution of FFPs has provided the means of regulating financial intermediation in the microcredit sector. Supervision of this sector falls under the control of the Intendency of Non-Banking Financial Institutions, which in turn forms part of the Superintendency of Banks and Financial Entities.

With respect to the public sector, the government of Mr. Gonzalo Sánchez de Lozada created the Assistance Program of Microcredit and Rural Financing (PAM)⁷, responsible for financial and institutional assistance to NGOs in the microcredit sector. Under the new government which took office in August 1997, the new Viceministry of Microenterprise and FONDESIF work together to attend to the training, technical assistance, and Financing needs of microenterprises. A Microcredit Fund program has been designed which defines the strategy and policies of the government for this sector.

International organisms have played a very important role in the development of microfinance

⁷ Under Supreme Decree No. 24436 of December 13th, 1996, PAM became part of the Development Fund for the Financial System and Support for Production (FONDESIF).

activity, concentrating their assistance primarily on institutional strengthening and credit resources for the majority of the microcredit institutions.

Finally, the document highlights some of the challenges to be overcome in the microcredit sector, including the development of new financial services, equity and institutional strengthening and the development of adequate regulations for these activities.

The Development of Microfinance in Bolivia

I. Introduction

This analysis regarding the development of microfinance in Bolivia describes the advances in this sector with respect to credit technologies, geographical coverage, institutional development, the legal framework and the role of the government and of donor institutions.

The work of various non-governmental organizations (NGOs) has transformed what was once considered "taboo"- lending to the poor and those involved in the informal market - into a flourishing, profitable activity which has had a visible social and economic impact on an important segment of the Bolivian society. In over 10 years of activity, the primary lesson learnt is that the market must respond to the needs of the people, and as a result different technologies have been developed ranging from solidarity groups to individual credit, covering a gamut of schemes which have proved their effectiveness in allowing access to credit.

The development of these technologies has been accompanied by important advances in institutional development, forced -to some extent- by the growing demand and the restrictions embedded in the norms established by the regulatory and supervisory authorities of the financial system. Organizational structures have been modified to improve the management, administration, and credit/financial policies to become more efficient. Throughout this process, various NGOs have decided to create autonomous entities, specialized in microfinancing, with a profit motive, although the aim of providing assistance to the most needy segments of the population remains. The necessity of meeting regulatory guidelines and of covering a wider geographic area of the country has forced many of these entities to increase their equity, and as a result they have their institutions to socially oriented organizations (domestic and foreign) and individuals. This document also highlights the creation of two microcredit associations, one of financial entities that work in urban areas and a second of those in the rural areas, with the goal of offering services of common interest to their members. (Note : Studies are underway to fuse these two associations into a single institution.)

The “boom” in this emerging financial market has also provided incentive to the monetary authorities, mainly the Superintendency of Banks and Financial Institutions (SBEF) to develop a specialized institutional capacity and appropriate norms in order to establish and supervise the activity of microcredit institutions (MIs). As a result, confidence in these institutions has increased and, more importantly, it permits the development of other financial services - for example, the mobilization of savings - demanded by this market.

It is important to note that microcredit in Bolivia initially received a great boost from international cooperation. For example, the participation of USAID was key in the development of PRODEM and the later creation of BancoSol; and the GTZ (German Cooperation) played a prominent role, first in PROCRÉDITO and later in Los Andes, FFP, together with the Swiss Cooperation for Development (COSUDE), the Interamerican Development Bank (IDB) and the Andean Development Corporation (CAF). However, this assistance is limited and, as MIs become sustainable, continues to diminish. The growth of this market provided the catalyst for the development of new institutional structures: institutions which offer financing to bank and non-bank financial entities, who then attend to the needs of the small and micro-enterprise. This new institutional structure has resulted not only from the growing demands of the market, but also from the backing of the government and foreign aid organizations which view these new schemes as an effective means to provide funding to the MIs.

The government played a very limited role in the development of the microcredit market. First the Popular Microcredit Program (PMP) was established to provide grant funds for portfolio and institutional strengthening of several financial NGOs. Subsequently, the Rural Financing and Microcredit Aid Program (PAM) was developed to cover a broader spectrum of financial and non-financial aid, although it was never fully implemented. Finally, the current government has just defined the strategy of a Microcredit Fund to provide financing and institutional strengthening to MIs. Throughout these developments, international donors have had and continue to play a very active role.

To summarize, it is important not to lose sight of the fact that although significant advances have been made in the microcredit sector in Bolivia, there remain difficult challenges to be faced and overcome. Perhaps foremost amongst these challenges are the need to develop new financial services (primarily savings), achieve financial sustainability in the MIs, improve the regulatory framework, train human resources and support programs of equity strengthening.

II. Credit Technologies

In response to the existence of very heterogeneous markets within Bolivia, various types of institutions have developed which apply diverse credit technologies to reach the microentrepreneur. The following is a brief description of the different technologies applied in Bolivia, including an example of an institution in each case. The most general aspects of the institutions examined are summarized in Annex 1.

A. Solidarity Groups

General Characteristics

The technology of solidarity groups is the most well-known, both nationally and internationally. PRODEM was the pioneer of this type of service, which has subsequently been adopted by various other institutions⁴, although in some cases this technology has been combined with others of the individual or associative type, or with other non-financial services as in the case of PRO MUJER, as will be discussed.

The principal characteristic of the solidarity groups is the use of an intangible guarantee, called a community guarantee, although the credit is approved individually. This type of guarantee is based on the compromise of all the members of the group to assume responsibility if one of the members of the group fails to make payment. These loans are not targeted and can be used for any need deemed necessary by the borrower. Finally, these credit lines are sequential, in that the group starts with small loan amounts which can grow over time as the group meets its financial obligations.

⁴ Of ten institutions analyzed in this document, eight use this methodology.

BANCO SOL

Authorized by the SBEF in 1992, BancoSol has become established as the foremost private Bolivian bank specializing in microcredit. The shareholders of the bank are institutions and individuals, both national and foreign. Its mission is to democratize credit and stimulate self-employment. As of December 1997, the institution had 34 branches in the urban sectors of 4 departments (La Paz, Santa Cruz, Cochabamba and Oruro).

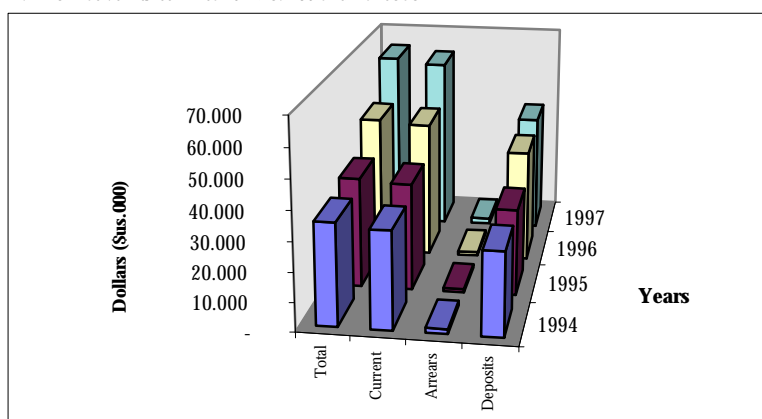
BancoSol has accumulated approximately 10 years of operating experience, if that of PRODEM is included, over which it has achieved financial sustainability. Its success can be attributed to various factors, amongst which is its innovative credit technology (solidarity groups), the quality of its service (efficient and personalized) and effective management of its rapid growth. On average, loans have a term of one and a half years, at an average interest rate of 30% for loans denominated in dollars and 48% for loans in bolivianos, above which is charged a 1% one-time commission on the total amount of the loan at the moment of disbursement.

The following data shows the development of the institution : since 1994 its gross lending portfolio has grown at an average annual rate of 11.9%, less than the average annual growth in its deposits of 13.2% over the same period. Approximately 85% of its lending portfolio is placed in the commercial sector. The average loan amount is around US\$ 600. It is important to note that BancoSol started placing individual credits in October 1997, and as of December 1997 this segment represents 5% of its entire loan portfolio.

PORTFOLIO AND DEPOSITS (In thousands of US dollars)

Year	Total	Current	Arrears	%Arrears	No.Borrowers	Deposits
1994	34.920	33.214	1.706	4,89%	61.255	28.575
1995	37.989	36.857	1.132	2,98%	63.336	29.789
1996	48.658	47.447	1.211	2,49%	71.745	38.917
1997	63.086	61.182	1.904	3,02%	76.215	41.464

Source: SBEF. Informative Bulletin Year 9-Nro. 109 and BancoSol



Method of Operation

In virtually all of the institutions analyzed, the process is initiated when the credit advisors identify potential clients, and give them a brief explanation of the financing characteristics. An invitation is extended to interested individuals to attend an informative session where a more detailed explanation of the methodology is provided, incorporating additional material to assure complete understanding. Once the session is over, groups are formed (between 4 and 8 people) and then present their request for credit.

When assessing the request for credit, the assigned advisors visit each member of the group to verify the existence and operations of their business. This process usually takes a week. If the request is approved, the loan is disbursed to the entire group.

To expedite the follow-up and repayment of the loan, each group designates a coordinator and a secretary who alternate the tasks of distributing the total amount disbursed to the group, collecting the installments and ultimately repaying the loan to the institution. The rotation of these types of loans is very rapid, generally six months on average. If the loan is repaid without problems, the group is able to continue borrowing for larger amounts.

Financial Conditions

The nominal annual interest rates applied fluctuate between 24% and 48% for loans in bolivianos, and between 21% and 30% for loans in dollars. Some institutions charge one-time commissions ranging from 1% to 2.5%, applied on the amount of the loan. The terms of the loans can vary between 1 and 24 months, depending on the activity and on the prior history of the group. Loan amounts span a wide range of US\$ 60 to US\$ 15,000.

B. Individual Credit

General Characteristics

This technology was introduced mainly by the international cooperation, above all that of Germany. Its principal characteristic is an individual guarantee, which allows the clients to formulate their own business plan in accordance with the business activity in which they are involved. This method provides an alternative for those microentrepreneurs who either do not want to or cannot participate under solidarity credit schemes, and whose only funding alternative is through informal mechanisms. This technology is also used for those entrepreneurs who normally need larger amounts of credit than those granted through solidarity groups, and are able to provide other guarantees.

Some institutions which only work with solidarity groups have been forced to introduce the individual technology, as in the case of PRODEM, to respond to the needs of their clients. There are also other institutions, such as Los Andes, which exclusively provide funds using this technology.

Method of Operation

Almost all of the institutions advertise their services, using various forms of communication such as flyers. In other cases, as for example with Los Andes, advertisement is employed only when demand drops.

FIE

The Center for the Promotion of Economic Initiatives (FIE) was founded in 1985, by a group of individuals who currently form the assembly of associates. FIE was established to provide services to support the sustained development of small and microenterprises which have limited access to conventional systems of credit and training.

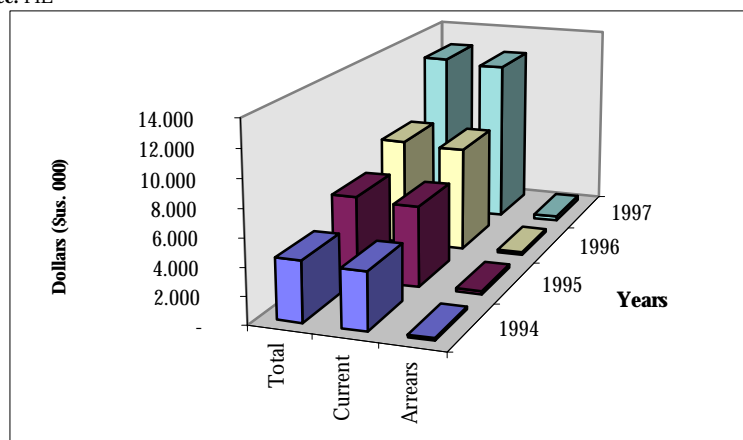
From 1986 to 1988, the institution tested different operating procedures, developed the individual credit technology and also focused operations in urban areas. In 1988, FIE widened its credit program to include producers and artisans in the city of La Paz, and introduced management training programs.

At this moment, FIE has 14 branches in the departments of La Paz, Cochabamba, Santa Cruz, Oruro, Tarija, Chuquisaca and Potosi. Approximately 70% of its loan portfolio is concentrated in productive sectors and the other 30% in commercial sectors and loan amounts average US\$ 550. Annual interest rates are 24% for loans in dollars and 36% for loans in bolivianos, and the institution charges a one-time commission of 2.5%. The terms of the loans range from 12 to 24 months, depending upon the client's business activity.

LOAN PORTFOLIO (In thousands of US dollars)

Year	Total	Current	Arrears	% Arrears	No. Clients
1994	4.338	4.159	179	4.12%	12.754
1995	6.119	5.881	238	3.89%	18.875
1996	7.893	7.694	199	2.52%	14.039
1997	12.451	12.127	324	2.60%	22.086

Source: FIE



In institutions which offer other financial services in addition to individual credit, as in the case of FA\$\$IL, this technology is applied to those clients who initially formed part of a solidarity group, demonstrating their credit worthiness throughout time and due to the growth of their microenterprise activity require larger credit amounts over longer terms and are in a position to offer other types of guarantees.

Commonly these institutions offer informative talks regarding the characteristics of their financing, whose periodicity and duration depends upon the clients cash flow and upon the policies of each institution. Afterwards, interested potential clients can present their request, which is then evaluated by the credit advisors for acceptance or rejection.

In the case of Los Andes, for example, upon receiving loan requests, agents of the distinct regions are assigned to their processing according to the regional breakout established by each institution. The agent in charge visits each potential client in order to analyze the repayment source and prepares a cash flow, and subsequently forwards the request to the credit commission, which ultimately accepts or rejects the loan request.

Financial Conditions

Annual nominal interest rates vary between 36% and 48% for loans in bolivianos and between 21% and 30% for loans in dollars. Some institutions charge a one-time commission, ranging from 1% to 4%. Loan terms fluctuate between 15 and 48 months, with loan amounts ranging from US\$ 20 to US\$ 56,000, depending upon the activity.

C. *Associative Credit*

General Characteristics

The development of this technology is based on an established organization (association or cooperative), whose function is the intermediation of funds given by the financial institution for its members.

In the cases studied, these funds are used by the organization's members, largely producers, mostly in investment capital. This type of financial services is provided by institutions such as ANED, FONDECO, IDEPRO and FADES. In some cases, this credit complements other types of services (such as technical assistance) which can be provided by the same institution or by a separate NGO.

Method of Operation

Once an organization or association of producers presents its request for financing, the financial institution analyzes the request. In some cases, the association must supply a guarantee fund deposited in a bank before the evaluation to gain access to credit, as in the case of IDEPRO.

FADES

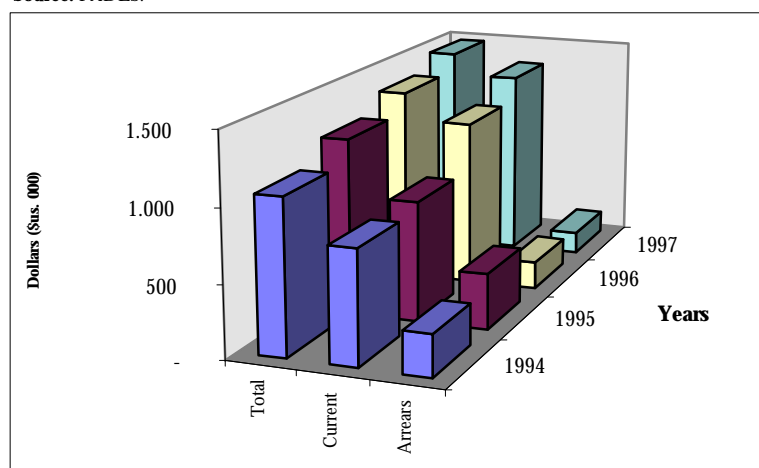
The Foundation for Development Alternatives (FADES) was formed by a group of institutions in 1986 with the aim of supporting the development of the rural sector, especially the poorest segments unattended by other types of institutions. FADES has now expanded to include a network of 20 branches. Annual interest rates are around 30% for loans in bolivianos and 16% for loans in dollars, with an average term of two years.

After operating for almost ten years, FADES has achieved wide rural coverage, with a presence in six departments with the exception of Pando, Beni and Santa Cruz. During 1997, 35% of the loan portfolio was placed in La Paz, 29% in Potosi and 17% in Oruro, departments with greater rural poverty indicators in relation to the rest of the country. Approximately 95% of the loan portfolio is placed in productive sectors (cattle ranching, milk production, etc.), with an average loan amount of US\$ 360 per individual client.

LOAN PORTFOLIO OF ASSOCIATIVE CREDIT (In thousands of dollars)

Year	Total	Current	Arrears	% Arrears	No. Clients
1994	1.065	780	285	26,76%	1.323
1995	1.220	833	387	31,72%	2.430
1996	1.353	1.162	191	14,12%	2.928
1997	1.476	1.322	154	10,43%	3.511

Source: FADES.



In the case of FADES, a credit official is assigned to evaluate the feasibility of the project, in

is composed of two sources; the first, is the savings of the members of the communal bank, which is a requirement to have access to credit, and they are deposited in a bank account in the financial system under the name of the communal bank, and the second source is the interest generated on the external account during the loan cycle of approximately 4 months.

Once the funds of the Executing Institution are received, these are continually relent among the

borrowers of the communal bank, given that the members make weekly payments on both capital and interest.⁸

PRO MUJER

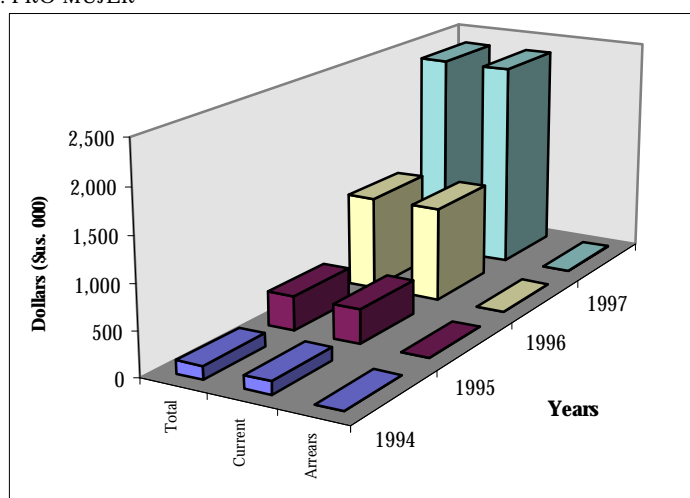
The Programs for Women (PRO MUJER), established in 1990, began credit activities in 1994. This institution's central objective is to empower women with scarce resources as the key to sustainable development. This program is characterized by a combination of training and credit.

In six years of operation, PRO MUJER has become established in the departments of La Paz, Cochabamba, Chuquisaca and Tarija, with a branch in each one. This regional expansion has permitted the growth of the institution's outreach; as of December 1997, 14,266 members received loans totalling US\$ 2.3 million and the arrears percentage is 0.19%. Approximately 80% of PRO MUJER's loan portfolio finances commercial activities and the remainder is allocated to the productive sector. The average loan amount is approximately US\$ 90. The annual interest rate is 48%, and the average term is eight months. All of the loans are given in bolivianos.

LOAN PORTFOLIO (In thousands of US dollars)

Year	Total	Current	Arrears	% Arrears	No.Clients
1994	146	146	0	0.00%	2,075
1995	388	388	0	0.00%	5,940
1996	1,060	1,060	0	0.00%	12,081
1997	2,341	2,336	4,342	0.19%	14,266

Source: PRO MUJER



In Bolivia, the application of this technology is focused mainly on poor women's groups, as in the case of Freedom from Hunger, PRO MUJER and Save the Children.⁹

Method of Operation

⁸ Catholic Relief Services. Seminar Workshop Report: Characteristics and Potentials of the Microcredit Market in the Sectors with Greatest Poverty in Bolivia. La Paz, AGRODATA, 1996.

⁹ MARCONI Ojeda Reynaldo. NGOs and Rural Credit in Bolivia. La Paz, Association of Financial

In general, institutions which offer services via communal banks take the initiative to contact potential clients. For example, PRO MUJER contacts mothers groups to provide information on their services.

Once the communal bank is organized, a training course is given before the disbursement of funds, where in addition to supplying information concerning the credit mechanism and the implications of a group guarantee, each borrower explains the activity in which loan will be invested. In the case of PRO-MUJER, the objective of this training course is to develop a *business plan* to help the borrowers to better manage their money. Freedom from Hunger, on the other hand, trains women in health, nutrition, microenterprise development and basic business administration.

Afterwards small solidarity groups are formed, composed of 4 to 6 individuals. In some cases these groups are already organized prior to their presentation to the communal bank, but this is not a prerequisite. Each group presents its credit request to the communal bank. The credit mechanism is sequential and during the first cycle only small amounts of funds per individual can be requested.

The Executing Institution makes the disbursement to the credit committee of the communal bank, which is then charged with the distribution of the funds to the solidarity groups. Repayments are made in weekly meetings. In the case of PRO MUJER, these meetings take place in *focal centers*.¹⁰

Financial Conditions

The *nominal annual interest rate* fluctuates between 42% to 48% for loans in bolivianos, and is 8% for loans in dollars. The average loan term ranges from 4 to 8 months, with amounts ranging from US\$ 50 to US\$ 600.

E. Credit and Non-Financial Services

General Characteristics

Microenterprises face a series of restrictions, including lack of access to markets, to information and technology.¹¹ Non-financial services are designed to overcome these restrictions and thus improve the performance of the microenterprises. In many cases the services are offered alone, and in others, jointly with financial services. These services are not necessarily a prerequisite to access to credit, as in the case of IDEPRO, an institution which has been able to achieve an integrated operating strategy where the offer of business development services is only a complementary option to the financial services extended by the institution.

Method of Operation

Mostly, the combination of financial and non-financial services offered by the same institution is a result of the market demand. Often market studies are performed to quantify the potential demand. These studies are then used to determine the institution's strategy, and if necessary, the services could be modified to meet the clients

IDEPRO

¹⁰ A focal center is a conveniently situated place where the borrowers get together.

¹¹ GOLDMARK Lara, BERTE Sira and CAMPOS Sergio. Preliminary Results of the Survey of Development Services to the Microenterprise and Case Studies. BID, Washington D.C., January 1997.

The Institute for the Development of the Small Productive Unit (IDEPRO), established in 1988 by various private development institutions, began its activities in 1991 with the goal of contributing to the integral development of the urban microenterprise by providing financial and non-financial services (business training, marketing, information and basic insurance).

The participation of the borrowers in the business development programs is not a prerequisite for access to credit. However, the institution promotes the advantages of these programs principally amongst its financial services clientele. The services provided are as follows:

PROGRAM	CLIENTS	NO.CLIENTS	COST
	ACCUMUL. 1997	1997	
Training	6.400	2.024	2,5 Bs/hour
Business Counseling	1.005	675	15 Bs/Couns.
Market Information	1.715	1,287	7,5Bs/cm/colum.

The costs of these programs are financed by the profits generated by the financial services of IDEPRO and by foreign donors.

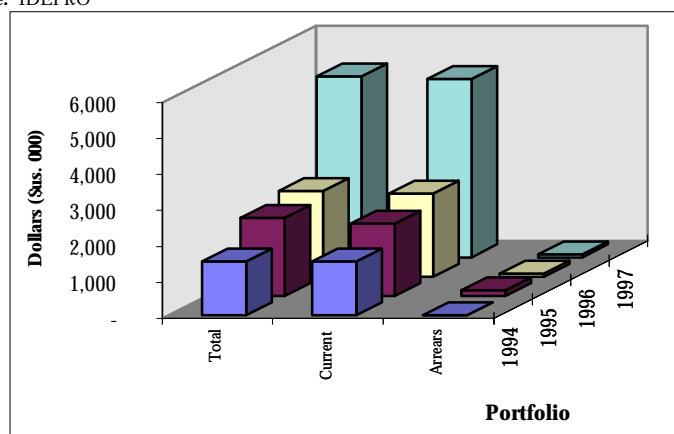
Regarding its financial program, the institution has five branches in the cities of La Paz, Oruro, Potosí, Chuquisaca and Cochabamba. Approximately 57% of its loan portfolio is placed in the productive sector, 35% in commerce and the remaining 8% in services. The average loan amount is US\$ 400.

The large part of the institution's funds (62%) come from loans, 27% are from the institution's own resources and only 11% are donations. IDEPRO, along with other institutions, has applied for authorization to become a private financial fund.

LOAN PORTFOLIO (In thousands of US dollars)

Year	Total	Current	Arrears	% Arrears	No. Clients
1994	1,495	1,494	1.45	0.10%	3,949
1995	2,161	2,013	148	6.85%	4,496
1996	2,382	2,304	79	3.32%	7,721
1997	5,033	4,960	73	1.45%	12,318

Source: IDEPRO



In almost all of the cases studied, non-financial services are not a prerequisite for access to credit.

The majority of the institutions which provide these services charge for them, although the cost to the microenterprise is minimal as in many cases donations from international organizations are used to finance such services.

Costs of Non-Financial Services

The cost of the non-financial services varies according to the type of service provided, the number of clients assisting, the duration of the event and other policies applied by the institution. For example, the cost of IDEPRO's market information program to the public is represented by the cost of a fortnightly publication in a nationwide newspaper. In other cases, microentrepreneurs pay only 10% to 20% of the total cost of the training course, with the remainder supplied by the institution sponsoring the event.

F. Combination of Credit Technologies

General Characteristics

The development of microcredit in Bolivia, has given rise to innovation, not only regarding the development and implementation of new credit technologies to attend to a given client base, but also in terms of an adequate combination of the existing technologies to provide an improved coverage of the services offered. At the same time, these institutions are taking advantage of the new regulations of the SBEF to deepen financial intermediation as they transform into FFPs.

Method of Operation

The diversification of the institutions' credit portfolio is achieved by offering a wider range of financial options to their clients. For example, FA\$IL offers different alternatives to get credit taking into account the financial position of the client.

The National Ecumenical Association for Development (ANED) is one of the oldest institutions, founded in 1978 by a group of private development institutions and a few ecclesiastical organizations, with the goal of offering adequate financial services to low-income segments involved in income-generating activities.

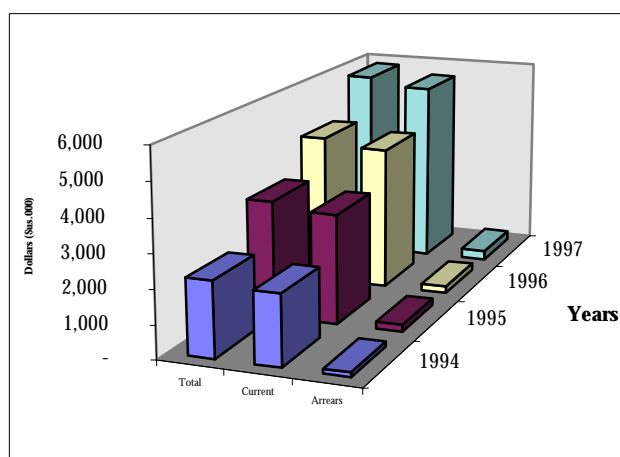
ANED began its operations offering only associative credit, although over time it has begun to employ diverse technologies according to the amount of credit requested, the term of the credit and the guarantee offered by its clients. In addition to associative credit, the institution works with solidarity groups, individual credit and communal banks, and even performs "second-level" operations.

ANED works directly in rural areas and indirectly in urban centers, the later as a result of its "second-level" activities through which it provides financing to other institutions. As of December 1997, the loans were channelled through 17 branches in five departments of the country. The interest rates charged fluctuate according to the technology applied for both loans in dollars and in bolivianos. Loan terms range from 6 months to 3 years.

LOAN PORTFOLIO (In thousands of US dollars)

Year	Total	Current	Arrears	% Arrears	No. Clients
1994	2,228	2,084	133	5.97%	18,473
1995	3,474	3,269	205	5.90%	25,350
1996	4,535	4,327	208	4.59%	27,387
1997	5,808	5,533	276	4.75%	34,731

SOURCE: ANED



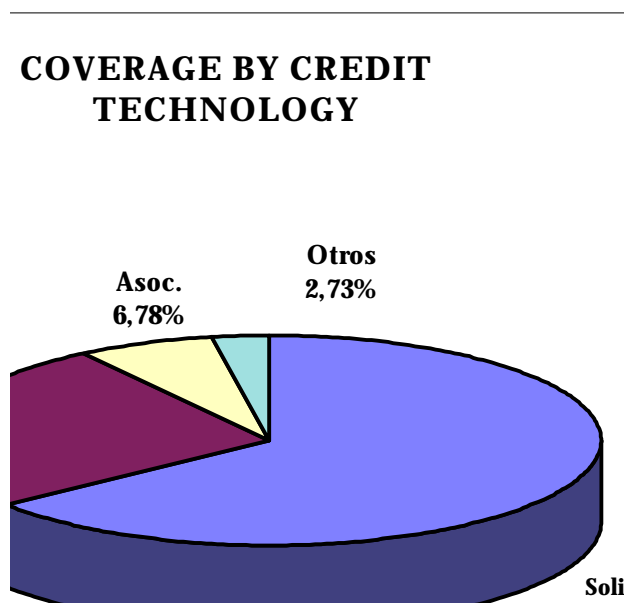
On the other hand, other institutions apply different complementary technologies. ANED considers solidarity credit to be complementary to associative credit, given that the first is used for investment operations and the second for working capital.

Financial Conditions

The financial conditions depend upon the type of technology used and whether the clients are

located in rural or urban areas.

To summarize, of the institutions analyzed the predominant technology applied is that of solidarity groups. Individual credit is gaining importance in the urban area and associative credit is more utilized in rural areas.



III. Second-Tier Institutions

General Characteristics

Second-tier" institutions have developed in response to the financing needs of financial intermediaries, whose loan portfolios have grown rapidly in recent years. Currently there are two institutions which directly supply funds to microcredit institutions, the Foundation for Production (FUNDA-PRO) and the Bolivian National Finance Corporation (NAFIBO) S.A.M..

A. Foundation for Production

General Aspects

The Foundation for Production (FUNDA-PRO) is a private non-profit institution which seeks to promote social and economic development by improving the welfare and quality of life of the Bolivian society. Its mission is to expand credit to those sectors that traditionally have confronted barriers in getting access to this service from conventional financing sources.

FUNDA-PRO was created as the result of the institutionalization of the Market Town Capital Formation (FOCAS) Project, agreed upon by the governments of the United States and Bolivia in 1991.

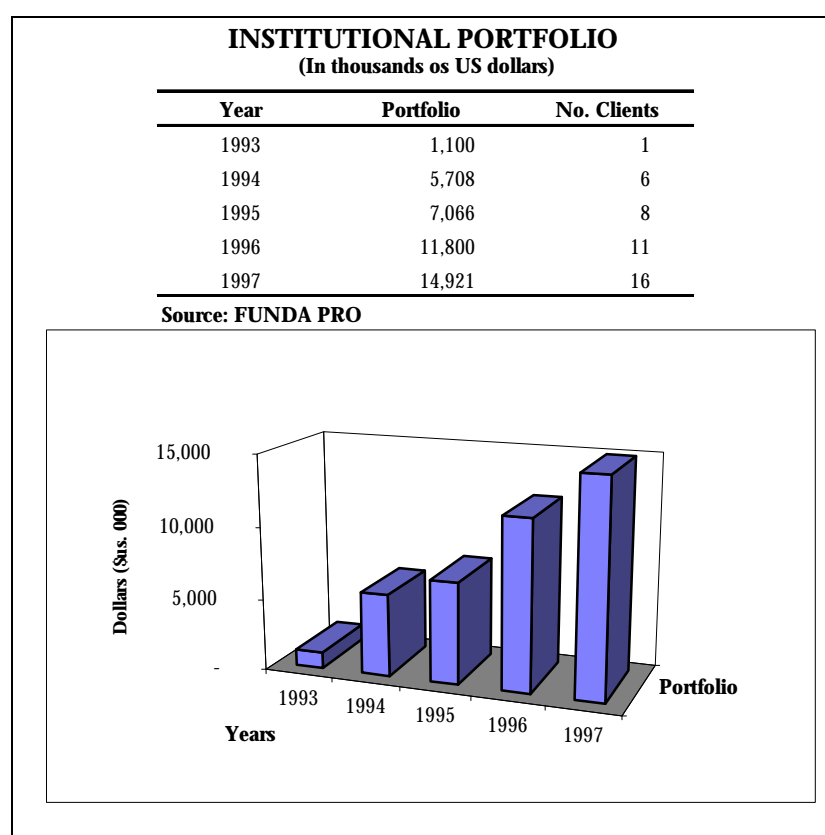
Services Offered

Financing. FUNDA-PRO has two financing programs: institutional and educational. Under the institutional credit program, it channels funds through legally established financial intermediaries with the aim of providing support to the productive activities of the micro, small and medium enterprise which confronts difficulties in accessing credit. Through its educational credit program FUNDA-PRO provides financial assistance for master's degree programs, technical or specialized courses and thesis completion.

Development programs. FUNDA-PRO has developed programs for the strengthening of non-bank financial entities, the opening of new markets, research concerning topics in microcredit and the development of financial services in rural areas.

Method of Operation

Regarding its institutional credit program, FUNDA-PRO has designed a methodology for channeling resources through banks and non-bank financial entities (FFPs, cooperatives and financial NGOs). In its five years of operations, FUNDA-PRO has placed an accumulated amount of US\$ 40.6 million, without incurring arrears. As of December 1997, the balance of its financial operations reached US\$ 28.7 million, distributed amongst 16 institutions which primarily attend to microenterprises in different regions of the country.



The evaluation of loan requests includes an analysis of the pertinent legal, institutional and financial aspects of the financial intermediary. Then, the Foundation evaluates the financial feasibility of the operation and the repayment capacity of the institution.

The conditions required by FUNDA-PRO are principally that the financial intermediary be legally

established, either as a bank or non-bank entity, with a proven credit technology and experience in attending the segment of the market targeted by FUNDA-PRO.

The interest rate charged to its loans, is based on the average weighted rate for fixed-term dollar deposits, for over 360 days, as published by the SBEF. Additional percentage points established by FUNDA-PRO are added to this baseline, according to the type of institution (regulated or non-regulated), the guarantees presented and the perceived risk of the operation.

The average term is approximately three years. The guarantees accepted vary and include mortgages, personal guarantees and the loan portfolio of the institution.

B. Bolivian National Finance Corporation

General Aspects

The Bolivian National Finance Corporation (NAFIBO) S.A.M. is a second-tier financial entity whose objective is the intermediation of medium and long-term funds to private financial institutions legally established in the country, which then channel these resources to the private and productive sectors of the economy.

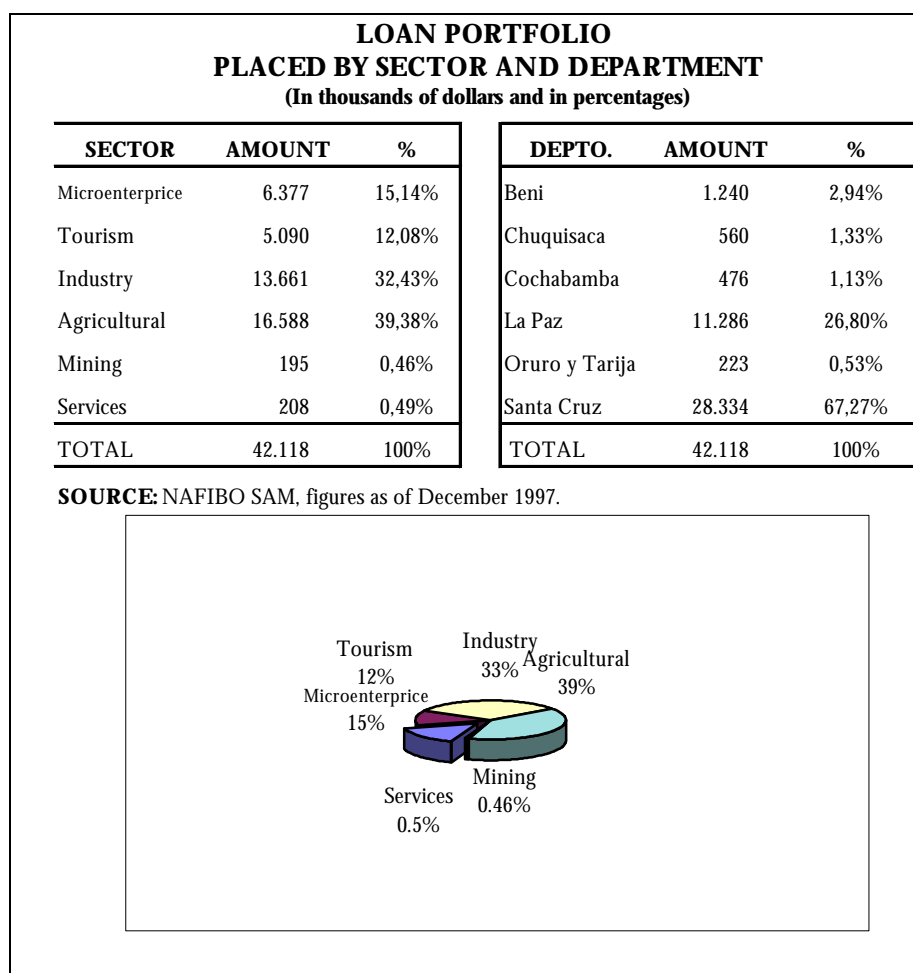
An Agreement signed between the Bolivian government and the Andean Development Corporation (CAF) in 1994, decided the closing of the Development Division of the Central Bank of Bolivia and, instead, the creation of NAFIBO.

In October 1995, the National Congress approved the Law of the Central Bank of Bolivia N°1670, which ratified the aforementioned Agreement and also authorized the creation of second-level financial entities. In September 1996, NAFIBO received its operating license from the SBEF to initiate operations. Its first credit operation was with Los Andes, a financial fund dedicated exclusively to microcredit activities.

Services Offered

NAFIBO, as a second-tier bank, operates with only those financial entities which are legally established and authorized by the SBEF. Amongst the services it offers are included loans for investment capital, working capital and others directed to the small and micro enterprise. It also administers funds as trustee for third parties.

Through its credit window for the small and microenterprise, this institution places medium-term funds for financing the activities of those entrepreneurs whose total indebtedness in the national financial system is less than or equal to US\$ 20,000.



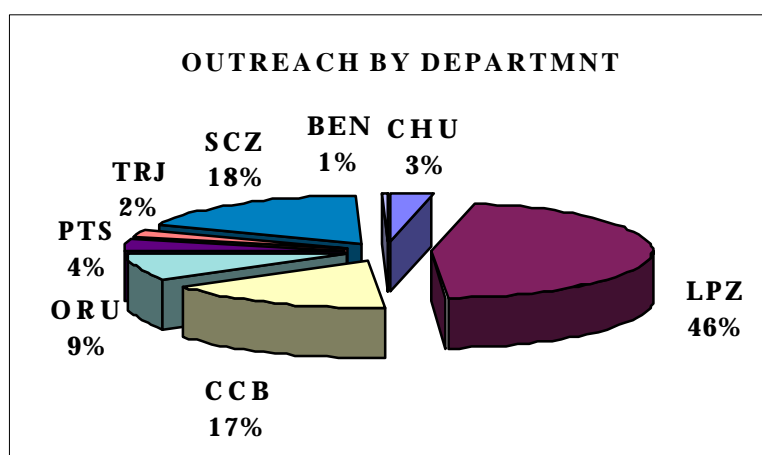
Method of Operation

NAFIBO approves microcredit lines to financial institutions with proven experience in microcredit operations. The financial entities can also intermediate these funds at their own risk, to other specialized microcredit institutions.

The financial conditions under which NAFIBO places these resources are : terms of up to five years, with semi-annual capital payments and quarterly interest payments, and the institution is required to contribute a minimum of 20% of the total financing cost of the project. The interest rates applied are the average weighted of the costs of raising the funds in the market. In 1997, the average annual rate applied was 9.94%.

IV. Outreach

One of the important advances made in the microfinance market in Bolivia is the high degree of outreach achieved by the institutions specialized in the field. As of December 1997¹² the total loan portfolio was US\$ 146 million, of which 74% was placed in urban areas and 26% in rural areas. Regarding the number of clients, of a total of 238,192 for the same year, 65% were located in urban centers and 35% in rural areas.



¹² Data corresponds to institutions associated with CIPAME and FINRURAL, La Paz, 1997.

The activities of the microcredit institutions have achieved nationwide scope, including the department of Pando, where PRODEM began operations in 1997.

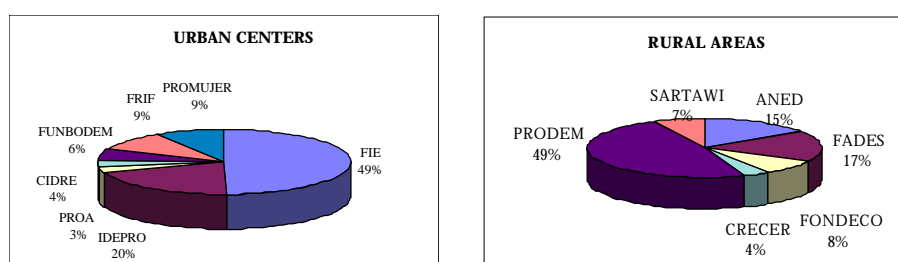
The regions which have most benefited from these activities are La Paz, Santa Cruz and Cochabamba, both in the placement of loans and in the number of clients.

V. Institutional Development

A. Non-Governmental Organizations

Non-governmental organizations¹³, also called private development institutions (IPDs), are civil non-profit associations which, under the Civil Code¹⁴, can perform financing and granting activities with government and external funds. The IPDs are the principal source of funds for the low-income population, both in the urban and rural areas. However, while institutions are not currently regulated by the SBEF, the monetary authorities have recognized their importance in channeling resources to regions where conventional banks do not find profitable, and the plan of the current government contemplates their regulation as financial intermediaries.

GROSS LOAN PORTFOLIO BY INSTITUTION AS OF DECEMBER 1997 (In percentages)



The principal IPDs in urban centers are associated with the Corporation of Private Institutions to Assist the Microenterprise (CIPAME), and those in the rural areas are affiliated with the Association of Financial Institutions for Rural Development (FINRURAL), whose constitution and primary objectives are discussed further in this document. The large part of the IPDs were formed in the 1980's. As of December 1997, the loan portfolio of the IPDs in urban centers totaled US\$ 23 million attending to 37,000 final borrowers. The loan portfolio of the IPDs in rural areas registered US\$ 48 million with 120.000 clients.

¹³ According to the National Directory of NGOs in Bolivia, in 1996 approximately 500 non-governmental institutions had registered with the Finance Ministry, of which around 20 specialized in credit.

¹⁴ Supreme Decree No. 22409 of March 11, 1992.

B. Private Financial Funds

From the point of view of regulated entities, the microcredit market was considered unattractive and was perceived as being high-risk with low return. This may be due to the fact that these institutions did not apply appropriate credit technologies to attend to this market segment. From the point of view of the financial NGOs, the greatest restrictions were : the dependence on financing from donor organizations and the inability to raise funds from the public.

In consequence, it was deemed necessary to create a new type of financial intermediary to attend to this market segment largely ignored by commercial banks, under a legal framework called a private financial funds (FFPs). The FFPs were created to finance the activities of the medium, small and micro enterprises in the productive, commercial and individual consumption sectors. The principal norms applied to these type of institutions are summarized in section VI.C1.

PRIVATE FINANCIAL FUNDS IMPORTANCE IN THE FINANCIAL SYSTEM (In thousands of US dollars and percentages) Figures as of December 1997				
INSTITUTIONS		%	LOANS	
Banks	3.025.482	83,55%	3.455.003	77,45%
Savings & Loans	342.382	9,45%	285.098	6,39%
FFP's	93.688	2,59%	125.953	2,82%
Cooperatives	159.731	4,41%	175.642	3,94%
Other*			419.284	9,40%
TOTAL	3.621.283	100,00%	4.460.980	100,00%
Source: SBFE				
*State Funds and Mixed Financiers				

LOS ANDES

The Caja de Ahorro y Préstamo Los Andes S.A. FFP is the first result of the legislation approved in 1995 which authorizes the creation of private financial funds. However, its history is closely related to PRO-CREDITO, the principal shareholder of the FFP, established in 1991 as a financial NGO. In addition to PRO-CREDITO, Los Andes also has international organizations and individuals as shareholders.

The prime objective of Los Andes is to promote the integration of social and economically disadvantaged sectors in the financial system, applying the individual credit technology. Notwithstanding its short period of existence, has achieved self sustainability and a healthy loan portfolio, which has registered an annual average growth of 70% since its establishment as an FFP in 1995.

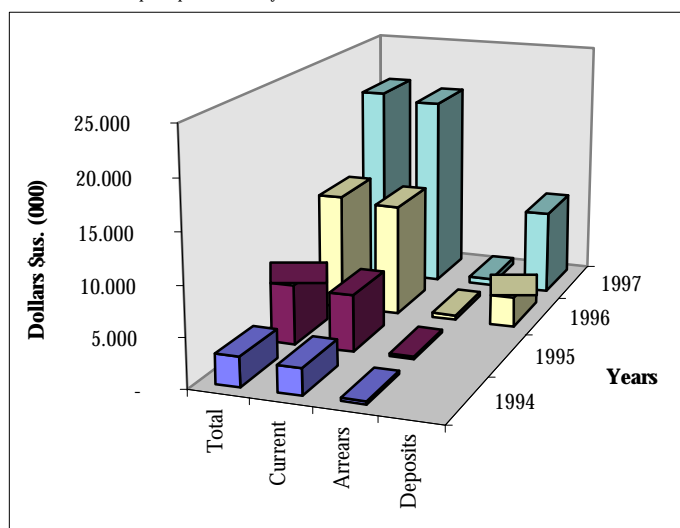
During 1997 Los Andes grew to a total of 11 urban branches. Approximately 60% of its loan portfolio is placed in the commercial sector with an average loan amount of US\$ 700. Annual interest rates fluctuate between 18% and 30% for loans denominated in dollars and between 36% and 42% for loans in bolivianos. The maximum loan term is 5 years with the majority of its loans placed between 9 and 18 months.

LOAN PORTFOLIO AND DEPOSITS (In thousands of US dollars)

Year	Total	Current	Arrears	% Arrears	No. Borrowers	Deposits
1994	2.974	2.675	317	10,66%	9.432	
1995	6.049	5.754	295	4,88%	15.954	
1996	11.881	11.409	472	3,97%	22.257	3.074
1997	20.430	19.742	688	3,37%	27.876	8.640

Source: LOS ANDES

Note: Los Andes started to accept deposits in May 1996.



By 1997, four FFPs were legally recognized in the financial system. One of these is exclusively dedicated to providing consumer credit, another two attend to the needs of the micro and small enterprise, and a fourth attends to both.¹⁵ In less than two years, these institutions have achieved an important market share, both measured in terms of loan portfolio (2.82%) and of deposits

¹⁵ This fourth FFP is "FA\$\$IL".

(2.59%).

Before the creation of the FFPs, the demand for microcredit was principally supplied by financial NGOs. However, the rapid growth in the microenterprise sector has been accompanied by the need for expansion in the supply of microfinance services. Although the institutions involved in this field have made great efforts to attend to this expanding demand, indications remain that restrictions exist in expanding the supply which can be offered.¹⁶

C. Cooperatives

Cooperatives have operated in Bolivia since the 1950's, and since their establishment have provided microcredit services. Regarding financial performance, the savings and loan cooperatives have had very unequal development. Cooperatives have experienced some very strong crisis periods, especially in the 1970's, and as a result many of them present weaknesses regarding the quality of their loan portfolio and in their administration.¹⁷ In order to assist in their strengthening, the World Council of Credit Unions (WOCCU) and the Confederation of German Cooperatives (DGRV) are working on different programs.

According to a survey of savings and loan cooperatives in 1993, performed by WOCCU, the number of cooperatives in the country is 278, of which only 3 are licensed for operations. In general, the cooperatives attend to the financing needs of merchants, professionals and individuals, and to a lesser degree to the productive sector.

COOPERATIVE JESÚS NAZARENO LTDA.

The microcredit program of the cooperative Jesús Nazareno Ltda. of Santa Cruz, initiated in 1992, grew naturally out of the growing demand of its members whose credit history was already known by the institution. The portfolio of

¹⁶ CAMACHO Efrain. Private Financial Funds - Alternatives for the Financing of the Small and Micro Enterprise. IBEE, La Paz, July 1995.

¹⁷ CENTRAL BANK OF BOLIVIA. Informative Bulletin No. 48. Year 4, March 1997.

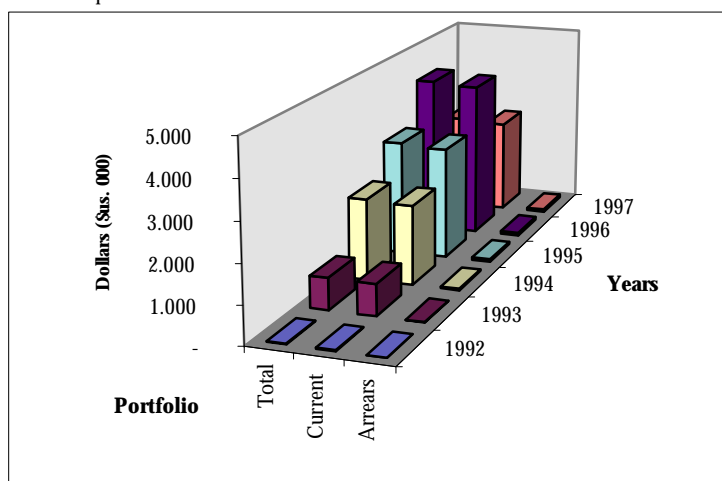
microcredit is placed in the urban sector, principally in commercial activities. This demand is met by 6 branches located close to different markets in the city of Santa Cruz.

The first years of the program showed the greatest growth. The microcredit loan portfolio has two programs, Solidarity Credit and Individual Credit. The average loan amount is approximately US\$ 520. Annual interest rates fluctuate between 18% and 36% for loans in dollars, with an average term of six months.

MICROCREDIT PROGRAM
(In thousands of US dollars)

Year	Total	Current	Arrears	% Arrears	No. Clients
1992	20	20	N.D.	N.D.	N.D.
1993	831	824	7	0,84%	4084
1994	2.141	2.098	43	2,01%	6587
1995	3.013	2.948	65	2,16%	6748
1996	4.186	4.108	78	1,86%	5506
1997	2.574	2.507	67	2,60%	3294

SOURCE: Cooperative Jesús Nazareno. Santa Cruz 1997.



D. Associations

Corporation of Private Institutions to Assist the Microenterprise

The Corporation of Private Institutions to Assist the Microenterprise (CIPAME) was founded on May 10, 1993 and was granted legal status in 1994. To date it has eight affiliate institutions, six

of which provide financial services and the remainder other types of services, all in urban centers. These institutions are : the Center for the Promotion of Economic Initiatives (FIE), the Institute for the Development of the Small Productive Unit (IDEPRO), the Center for Research and Regional Development (CIDRE), the Banco Solidario S.A. (BancoSol), the Center for Integrated Services for Urban Development (PROA), the Center for Research of Labor and Agrarian Development (CEDLA), the Bolivian Foundation for Women's Development (FUNBODEM) and Catholic Relief Services - USCC (CRS).

The objectives of CIPAME are to provide services to its members and coordinate and represent their interests.

Services. CIPAME offers its members a range of services, whose cost is included in their member fee and is supplemented by funds from international organizations and by those who pay for its services.

Principal Goals Achieved. According to its executives, CIPAME has achieved the following goals : *Institutional recognition* of various organizations which participate in microenterprise-related activities. *Consensus* with the government, multilateral cooperation organizations and entities in the microenterprise sector. *Coordination link* with the government, assisting on topics relevant to the development of the microenterprise sector.

Association of Financial Institutions for Rural Development

The Association of Financial Institutions for Rural Development (FINRURAL) was created on September 28, 1993. Its members are : the National Ecumenical Association for Development (FADES), the Foundation for Alternative Development (FADES), the Fund for Communal Development (FONDECO), the Foundation for the Promotion and Development of the Microenterprise (PRODEM), the Foundation SARTAWI and Freedom from Hunger.

FINRURAL has the following principal objectives : strengthen its member institutions, provide efficient and quality services and develop initiatives to support the work of rural financial entities.

Services. FINRURAL provides a range of services for its members. A minimal portion of the cost incurred is covered by the fee paid by its members, and the majority is financed by international donors.

Principal Goals Achieved. FINRURAL has been able to provide a forum for the rural financial NGOs in the microcredit market. In this sense, according to its executives, FINRURAL has become the representative of the interests of the rural microcredit sector to governmental organisms, namely concerning the legal recognition of financial NGOs.

On the other hand, FINRURAL is implementing a rural savings program in conjunction with the assistance of other institutions involved in financial activities in the rural areas.

VI. Legal Framework

A. Law of Banks and Financial Entities

The Law of Banks and Financial Entities of April 14, 1993 was the culmination of a process of financial reform started in Bolivia in 1987¹⁸ whose objective was the strengthening of the banking system and the expansion of its role of assigning resources to different sectors of the economy. In order to achieve these goals, the Law focuses on assuring monetary stability and establishes the requirements for an adequate development of financial entities.

Regarding microcredit, the Law of Banks and Financial Entities made an important advance in allowing other types of financial entities (FFPs) to intermediate resources on a sustainable basis

for small and micro-enterprises. All of the norms and requirements are defined in the Law in order that the financial intermediaries remain solvent and operate prudently. However, financial NGOs which work in the rural areas continue to believe that additional norms should be legislated to facilitate their entry into the regulated financial market.

B. Law of the Central Bank

The Law of the Central Bank, approved on October 31, 1995, establishes that this entity is the sole monetary and exchange rate authority of the country, with the primary objective of maintaining the purchasing power of the local currency.

According to its Article 31, the Central Bank of Bolivia is also the only institution responsible in issuing norms regarding the financial system. In addition, in its role as the governing body of the financial system, the Central Bank is charged with executing the monetary policy, regulating the quantity of money in the economy and the volume of its credit in accordance with the monetary program.

Regarding second-tier banks, Article 31 clause i) of the Law refers to these entities, and Articles 84 and 85 of the same explicitly approve the creation of NAFIBO as a mixed autonomous corporation.

C. Special Regulations

C1. Private Financial Funds

The creation of private financial funds (FFPs) was authorized by Supreme Decree No. 24000 of May 12, 1995. Their constitution and functioning is authorized by the SBEF.

Their principal objective is the channeling of resources to finance small and micro-enterprises, while at the same time providing consumer loans to individuals. FFPs facilitate access to credit to

¹⁸ Supreme Decree 21660 of 1987.

those individuals unable to obtain financing through conventional forms of financing by accepting non-traditional forms of guarantees. FFPs are only allowed to accept savings and fixed-term deposits from the public. Notwithstanding this limitation, they retain a wide range of other instruments for their clients, which include financial leasing, guarantee certificates, transfers, etc., and in addition are authorized to intermediate loans from second-tier financial entities.

In order to assure credit access at levels much lower than those provided by other financial institutions, and at the same time maintain an acceptable level of credit risk, FFPs cannot provide loans for amounts greater than 3% of their equity to any one individual or borrower group.

Regarding guarantees, these institutions are authorized to accept non traditional guarantees, including furniture, jewelry, etc.. Loans with personal guarantees to an individual or borrower group cannot exceed 1% of the equity of the FFP.

An FFP must have a minimum capital of 630.00 DEGs¹⁹ to obtain a license from the SBEF. FFPs are prohibited from lending or maintaining credit relations with any financial institution for no more than 20% of their equity. Finally, the sum of the non-guaranteed loans cannot be superior than twice the equity of the FFP.

C2. Opened and Closed Cooperatives

In 1958 the General Law of Cooperative Societies was approved, establishing that the government should support and provide an adequate regulatory framework to these entities. However, it was not until 1990 when supervision was initiated for the largest saving and loan cooperatives. In consequence, until 1993 only three cooperatives had obtained their operating license from the SBEF. It was not possible for more of these institutions to obtain the operating licence as the legal framework established in the Law of Banks and Financial Entities of 1993 did not revoke the articles of the law of 1958 which presented obstacles to this process.

¹⁹ A DEG is the average of a basket of currencies which vary periodically. As of December 31, 1997, one DEG was equivalent to \$us 1.35.

(which provides services to members only) which are then subject to the supervision of the National Institute of Cooperatives (INALCO).

Around seventy cooperatives presented their intention to operate as SBEF. These institutions are required to present their financial projections and business plan as a first step in obtaining their operating license. This process began on September 30, 1997 and as of May 1998, the SBEF has not yet given operating licenses to any of these institutions.

VII. The Role of the Government

In recent years the government has played a far more prominent role given the increasing importance of microenterprises and the growing demand for resources from diverse institutions that attend to the financial and non-financial needs of this sector.

The new government installed in August 1997 has presented a plan of action designed to promote the development of the microenterprise. Generally this plan aims at improving the quality of life of the poorest sectors of the Bolivian population through permanent self-employment, for which it supports the creation and expansion of microenterprises into small industry enterprises.

At the regulatory level, the government has proposed modifications to the Law of Banks and Financial Entities in order to enable more regulated financial intermediaries in the microfinance market. In addition, it will support the strengthening of the Intendency of Non-banking Financial Institutions of the SBEF and the establishment of a risk information center of the microenterprise sector.

The government is planning to provide integral support to microfinance institutions, which have shown the potential to convert into solvent, profitable and adequately administered intermediaries and are in the process of transforming into FFPs. At the same time, it supports training and technical assistance programs by subsidizing non-financial services.

The above-mentioned plan also states that NAFIBO will channel government funds to institutions which are in the process of being regulated.

A. Development Fund for the Financial System and Support for Production

The Development Fund for the Financial System and Support for Production (FONDESIF) was created in 1995 to capitalize and strengthen the commercial banks, given the problems that they were then experiencing.

Regarding microcredit institutions, in 1996 the Supreme Decree 24436 incorporated the Assistance Program for the Microenterprise (PAM) into FONDESIF as the principal mechanism for the development of these entities. This program had the principal objective of striving for the "sustainability" of non-banking financial entities through their institutional strengthening and the passage of new regulation.

Under the new government in 1997, PAM was replaced by a Microcredit Fund, created to support the strategy of the fight against poverty, under the management of FONDESIF.

The Fund targets the development of the microfinance market in four ways: first, through the diversification of financial services to rural areas. Second, through the expansion of the frontier of

credit services with the opening of new branches and agencies by non-banking financial institutions. Third, by linking microcredit with the provision of non-financial services and investment in basic infrastructure. Finally, it supports the regulation of microcredit institutions.

The financial resources needed to implement these programs will come from projects already underway, donations and external sources received by the government. The Microcredit Fund will work with private financial funds, opened cooperatives and civil associations or foundations.

Regarding institutional strengthening and the opening of new branches, non-banking financial institutions will be selected based on the following criteria: attention to the target population, potential growth, proven experience, operating capacity and the equity and financial standing of the institution.

To date the Microcredit Fund continues in the process of institutional organization.

B. Central Bank of Bolivia

As the governing body of the financial system, the Central Bank is responsible for approving the norms that regulate the functioning of the financial intermediaries, including of those working in the microfinance market.

The Central Bank has recently issued a regulation for second-tier institutions that channel resources for diverse financial intermediaries, amongst which are those dedicated to microcredit activity. It is also working on additional norms for FFPs.

C. Superintendency of Banks and Financial Entities

The Superintendency of Banks and Financial Entities (SBEF) began a more active role in the microcredit sector in 1995, when the creation of FFPs was authorized. The norms applied to these funds are similar to those used for banking institutions, while modified to consider the characteristics and volume of operations of the FFPs.

The controls placed by the SBEF are designed to avoid introducing distortions in the market, thus assuring fair and transparent competition and access to information to both, banks and non-banking institutions. In the opinion of the SBEF, the norms applied to microcredit institutions must be strict, above all those used to evaluate the loan portfolio, the quantification of arrears (which is closely related to loan use) and guarantees.

For this purpose, the SBEF created the Intendency of Non-Banking Institutions at the end of 1997, which seeks to introduce an appropriate regulatory framework for the activities of these institutions and thus achieve a fair, competitive and transparent system.

VIII. The Role of Foreign Donors

One of the determinant factors for the development of microcredit in Bolivia was the aid provided by international organizations, mainly through the supply of financial resources during the second half of the 1980s when new credit technologies were being introduced to the market.

Amongst the principal international organizations which supported this activity is the United States Agency for International Development (USAID), which made possible the creation of PRODEM, with initial financing coming from the PL-480 program. The creation of BancoSol was also possible with initial assistance from USAID of \$us 2 million.

During the period 1978 to 1996 the Interamerican Development Bank (IDB) approved approximately \$us 17 million in loans under its Small Projects Program. This program has two principal components : *Credit Lines* for portfolio, investment and marketing, and *Technical Cooperation* given in conjunction with these loans as donations for institutional strengthening.

The German Technical Cooperation (GTZ) has supplied technical assistance to projects through governmental agencies. This organization is one of the principal supporters of the individual credit technology and provided an important economic assistance to PRO CREDITO which ultimately

decided to create an FFP, Los Andes.

In the opinion of almost all of the international organizations consulted, microcredit is amongst their highest priorities. Generally more than 10% of the annual resources available to these programs are used to target the microcredit sector.

Given the evolution in the microcredit market, a qualitative change has come about regarding the type of assistance provided by international organizations. Beyond the supply of credit resources these organizations are now more interested in providing funding for technical assistance, institutional and administrative strengthening, research studies and other related services.

In addition, external cooperation is focusing its efforts on institutions which are becoming financially sustainable, mainly those NGOs in the process of transforming into FFPs.

IX. Future Challenges

A. Savings Mobilization

A large part of microcredit services has been developed from the supply-side, generally as the preconception has been that providing services to the poorest segments of the population is not profitable or that they have to be subsidized.

Therefore, the development of other financial services has been very limited, specially in the area of savings mobilization. Attracting savings is a source of funding, as external financing becomes ever more scarce. This presents a challenge to microcredit institutions.

Just as the research and diffusion of results was important in the development of microcredit, it is equally necessary to support this kind of work in relation to savings. Improving the knowledge regarding the mobilization of savings is key to adequately design and implement strategies for attracting savings.

B. Access to Financial Services in the Rural Areas

Rural areas in Bolivia are inhabited by the poorest segments of the population. The limited presence of financial services in many regions even non-existent in some areas, inhibits the development of economic activities of their population.

The majority of the resources channeled to rural areas come from NGOs or IPDs, which are generally not sustainable and in addition confront a scarcity of resources. Currently only one FFP is timidly offering financial services in rural areas.

In addition to these restrictions there are diverse structural limitations in the rural economy, including legal and regulatory problems regarding land ownership, guarantee problems and a deficient physical infrastructure, aspects which discourage formal financial institutions such as banks and make the work of IPDs more difficult, increasing the costs of their operations.

It is necessary to promote financial intermediation in the rural areas to permit the rural populations to gain access to financial services.

C. Regulation of Financial NGOs

All of the financial entities involved in the microcredit sector should be subject to the same rules and regulations to assure transparency and avoid unfair competition with those institutions which have achieved a greater degree of development and are in the process of converting into FFPs. Even though many of these institutions, above all NGOs, are located in regions with difficult access, this is not a sufficient rationale for the total lack of regulation.

Also many of these institutions do not have a long-term vision for their operations, and as a result it is possible that many will not survive in the market for long. Establishing clear rules permits a degree of "consumer protection," the true principal protagonist in the microenterprise sector. The lack of these rules works against credit education in that these institutions can attract clients but are not forced to take on the corresponding responsibility.

On the other hand, there are those who point to the success of certain microcredit institutions in light of the lack of a regulatory framework as evidence that governmental regulation is unnecessary. Although this conclusion is strictly correct, it is important to take into account that current market conditions are very different, as are the possibilities for access to future financing sources.

It is recommendable that regulation be put into place for financial NGOs, with adequate norms which permit the expansion of their operations, especially regarding regions traditionally without financial services. Evidently this is a long process and certain flexibility is needed under these circumstances.

Finally, it is important not to underestimate the capacity of financial NGOs to take advantage of the benefits resulting from regulation. It is healthy for institutions to operate in accordance with the regulations of the SBEF, and given that currently these institutions cannot attract public deposits, it is possible that they will be allowed to in the future. In addition the legalization of these entities brings a degree of international acceptance for the country.

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