

# Ethical Standards in Microfinance Practice – Perspective of KfW

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**Matthias Adler, KfW**

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EUROPEAN  
**MICROFINANCE**  
PLATFORM

NETWORKING WITH THE SOUTH

## Why is this topic so important?

- growing attention in the last years
    - „irresponsible finance“ in partner countries
    - increase of ethical investors demanding ethical standards
    - financial crisis may affect some MFIs
    - biggest „banana skins“ have a lot to do with responsible finance!
- **need for action for both financial institutions and investors**



# Dimensions of Responsible Finance from a Development Finance perspective



## Donors and Investors

- long term involvement
- strengthening of local financial markets
- supporting transformation processes
- Focus on MFI ownership

## Supporting financial institutions

- transparent credit selection process
- adequate assessment of clients repayment capabilities
- sound client protection standards
- measuring social performance

## Supporting Regulatory Bodies

- ...have a role to play
- banning irresponsible collection practices
- proactive client protection, but not with interest rate caps!

## Support at Client level

- strengthening financial education
- raising overall confidence in the financial sector
- promoting savings collection

# What Does Responsible Finance Mean: For KfW Entwicklungsbank?



**commitment to promote responsible finance cannot be separated  
from commitment to build inclusive financial systems**

- Active dialogue with partner institutions to promote ethical standards (accompany processes)
- Long term involvement („buy and hold“)
- Try to „crowd in“ ethical investors
- Support transformation processes
- Help build local capital markets



## Examples of Mainstreaming Responsible Finance in Development Finance (I)

- integrating responsible finance standards in due diligences
- discussing ethical standards in board /IC meetings of investee MFIs/funds
- strong first loss pieces help to keep confidence in times of crisis
- no support for pure consumer finance institutions
- social competency and ethical orientation as part of the recruitment profile of partner MFIs

# Responsible Finance and Consumer Finance – Issues for discussion



## 1. Preliminary question: What is / how consumptive is a „consumer loan“?

### 2. Some facts

- MF-lending to non-MSME is a fact, demand for such loans exists
- consumer loans can go hand in hand with client over-indebtedness. intransparent lending and aggressive marketing
- indicators for „irresponsible finance: combination of high RoE, high interest rates, bad quality, low loan loss reserves

### 3. Preliminary answers/issues for discussion

- sound credit selection process is key
- to help build client assets
- to avoid over-indebtedness
- „reasonable“ product mix



## Examples of Mainstreaming Responsible Finance in Development Finance (II)



### → helping to raise international and local awareness

- organizing events involving central banks in relevant countries (e.g. Serbia, October '07)
- co-organisation of an international responsible finance conference (February 2008)
- Publication of a position paper on Responsible finance
- Endorsing CGAP Client Protection Principles

**Thank you for your attention**



**Contact:**

**Matthias Adler**

**Principal Financial Sector Economist**

**KfW Competency Centre, Financial Systems**

**Development**

**Tel.: 069/7431-2941**

**Fax: 069/7431-2547**

**[matthias.adler@kfw.de](mailto:matthias.adler@kfw.de)**

