

## **Crisis in Bolivian Microfinance**

Elisabeth Rhyne

Senior Vice President, Research, Development & Policy, ACCION International

for *Monday Developments*

On July 2, 2001, associations of poor fruit vendors, cobblers and farmers took Bolivia's Superintendency of Banks hostage. Laden with dynamite, they demanded forgiveness or reduction of the debt they've incurred through microlenders and consumer lenders. The situation was resolved, but over-indebted microfinance clients and the sour taste of revolt remain. How did the flourishing, socially-motivated Bolivian microfinance industry of the late 1990s attract such public anger?

Since the early 1990s, Bolivia has boasted successful microfinance institutions (MFIs) that have transformed from NGOs into regulated commercial institutions, including BancoSol, the first transformed microlender. Bolivia's commercial microfinance experience took on a new dimension in the late 1990s, as transformed MFIs grew and consumer lenders began overlapping with microfinance markets. This increase in competition converged with a major recession in Bolivia. These events led to a crisis in which borrowers became overindebted and institutions suffered falling profits and dangerously high delinquency rates.

### **The Rise of Consumer Credit**

Consumer credit, a lending methodology imported into Bolivia from Chile, has had momentous impact on microfinance in Bolivia. Consumer lenders offer loans about the same size as microenterprise loans, quickly and flexibly, to salaried workers. While in theory the market for consumer lending is distinct from the microcredit market – salaried employees versus informal enterprises – in practice, consumer lenders competed directly with microlenders.

Consumer lenders assumed that many clients would pay late, and built these expectations into their pricing. They charged fines for late payment that increased their revenues, making a few days or a week of delinquency welcome, not just tolerated. Conversely, Bolivian microlenders swore by immediate (one day), personal follow up of missed payments. In lending to the self-employed, microlenders are sensitive to lax attitudes towards repayment that can sweep through an institution's clientele.

The consumer lenders also increased risk through aggressive marketing techniques that lured good clients from microlenders by offering them larger, faster and cheaper loans, or offering loans to already indebted clients. Default shot up among consumer lenders during 1999 and 2000, creating the crisis of *sobreendeudamiento* (overindebtedness).

Most of the consumer lenders did not survive in Bolivia. And among microlenders, defaults rose to unprecedented heights, although still well below those of consumer lenders.

### **The Crisis of 1999-2000**

Clients capitalized on the increased competition, often maintaining two or more loans at a time, borrowing more than they could handle. Some let repayments slip, or worse, they began bicycling loans – using the proceeds of one loan to pay off another.

In 1999, after fifteen years of progress, Bolivia suffered its first serious economic setback just as overlending was heating up. The timing of the economic slide propelled the overindebtedness problem to crisis proportions. Bolivia began to experience heightened social unrest, with mass protests about things like water and electricity prices. Microfinance, too, felt the anger of the powerless. Interactions with clients started to sour, as loan officers spent more time wheedling collections from customers faced with too much debt and shrunken demand. These conditions set off a backlash against microcredit.

### **The Debtors' Revolt**

A handful of “professional” union organizers began gathering borrowers into debtors’ associations to protest against consumer and microfinance lenders. The associations staged protests, mainly at the offices of Acceso, CrediAgil, and other consumer lenders, but at MFIs as well, including Caja los Andes and BancoSol. They demanded full debt forgiveness.

The affected institutions, working through their newly created association, Asofin, sought aid from the courts to stop the demonstrations. But hunger strikes and the tearful testimony of a few market vendors captured media attention and public sympathy. Eventually, the debtor associations forced a dialogue with the Superintendency of Banks and Asofin, in which the microlenders agreed to consider debt relief on a case-by-case basis. Only a few cases were resolved, however.

Shortly thereafter, the debtors’ associations threw their own leaders in jail. One association was a true pyramid scheme where leaders illegally collected debt service payments due to the microlenders and used them to make new loans. Another association’s leaders mishandled membership dues, a less spectacular crime, but enough to bring them down.

After a few months’ hiatus, the associations surfaced with new leaders. In addition to debt forgiveness, their demands included prohibitions against certain collection practices, extended grace periods, longer loan terms, and annual interest rates of two percent. Tactics escalated. In the most extreme example, in July 2001, demonstrators carrying dynamite took over the Superintendency of Banks, holding employees hostage and threatening to blow up the building. Although negotiations with government and financial institutions have been achieved, the concessions granted have been minor. The major

importance of the debt protestors has been to politicize microfinance, changing attitudes about credit and damaging Bolivia's repayment culture.

### **Consumer Lenders and the Public Identity of Microfinance**

Microfinance lenders operating side-by-side consumer lenders must face an extremely awkward fact: from the client's perspective, their product looks very similar to the product of lenders often considered unscrupulous. Microlenders and consumer lenders offer loans with similar terms with a similar quick turnaround and with similar rhetoric about the benefits to the client. The borrowers' revolt in Bolivia illustrates the thin line between socially-motivated microfinance and purely profit-motivated consumer lending. The debt protestors do not greatly distinguish between them.

In response, MFIs and donors alike must rethink the public image of microfinance and the values it represents. What distinguishes "good" lending from destructive lending? If the private sector contains unscrupulous elements, how should the microfinance industry position itself? The Bolivian experience suggests that the principal public image issues for microfinance are high interest rates and the consequences of default – age-old concerns about moneylending.

\* \* \*

This article is based on Elisabeth Rhyne's book, *Mainstreaming Microfinance: How Lending to the Poor Began, Grew, and Came of Age in Bolivia* (Kumarian Press, 2001). For information on her book, please visit [www.accion.org/pubs/main.asp](http://www.accion.org/pubs/main.asp). Ms. Rhyne is the senior vice president for Research, Development & Policy at ACCION International.