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## Global Partnerships to lend in local currency

By Robert Celaschi, Contributing Writer

Next year Global Partnerships, a Seattle nonprofit that makes small loans to South American business owners, will start making the loans in local currency instead of dollars. It's a major shift in the way the nonprofit does business, and was a couple of years in the making.

Microfinance involves lending very small amounts, as little as \$100, to people with little income or collateral who want to start or expand a business.

Global Partnerships estimates that 140 million people in Latin America today live on less than \$2 a day, and even a small loan can be the boost they need to make better lives for themselves. Global Partnerships works in Bolivia, El Salvador, Guatemala, Honduras, Nicaragua and Peru, providing capital to partner microfinance institutions so that they can make the loans.

The whole field of microfinance has gained stature among lenders in recent years, especially after Bangladeshi economist Muhammad Yunus and his Grameen Bank won the 2006 Nobel Peace Prize for their use of microloans to spur development among the poor.

"What's happened since the Nobel Peace Prize is the flow of capital in microfinance has been increasing rapidly. The breakthrough was the shift from a philanthropic model to using investment dollars," said Global Partnerships CEO Rick Beckett.

Until now, Global has been providing money to microfinance institutions in dollars. That put a lot of risk on the ultimate borrowers, as the local currency might be much less stable than U.S. currency. With a big swing in the exchange rate, the borrower must scrape together a lot more to match the dollar amounts that the lender owes to Global and other organizations like it.

"Two years ago we set out to solve that," said Beckett.

Global and similar organizations created MFX Solutions in Washington, D.C., a for-profit organization that will let Global and other funders assume the credit risk instead of borrowers, and hedge that risk. First-stage investors include the Grameen Foundation, of Washington, D.C.; BlueOrchard Finance S.A., of Switzerland; Gray Ghost Fund, of New York; Appui au Développement Autonome in Luxembourg; Incofin, of Belgium; Developing World Markets, of Connecticut; Unitus, of Seattle; AfriCap, of Mauritius; FINCA International, of Washington, D.C.; and the Ford Foundation, of New York.

Hedging instruments haven't been available before now because the microfinance institutions have been too fragmented.

"No one is big enough to get the attention of the industry," Beckett said.

MFX Solutions won't do any lending itself, but will allow the lenders funded by Global and others to cut the risk of using local denominations through a device called a currency swap.

"A currency swap is a commonly used tool in finance. It's actually not one of the sophisticated, fancy derivatives that have proved so problematic of late," said Brian Cox, executive director of MFX Solutions.

Normally a bank acts as a middleman, finding people who want to swap dollars for, say, Honduran lempira, and matching them with others who have lempira but want dollars. The bank adds a margin for itself, and the deal is struck.

But banks are used to doing deals 10 times the size of what a microlender can bring in, said Cox, and banks often want collateral.

"The other problem is that in a lot of markets where microfinance operates, these products aren't available," he said. That is, there's nobody for the other side of the swap.

MFX got around that problem by working with The Currency Exchange Fund, a new \$600 million-plus fund backed by the Dutch government.

"Instead of running a match, they basically take the risk from all these developing markets—Honduras, Egypt,

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Uganda, and others—and by virtue of holding a diversified basket of all these risks, they get the risk down,” Cox said. “The volatility gets worked out.”

Calvert Foundation, in Washington, D.C., another nonprofit that helped set up MFX, has been lending in local currency for a couple of years, but the methods have been relatively crude, said Eliza Erikson, who manages Calvert’s international microfinance portfolio. Basically, Calvert had been providing guarantees to local banks by tying up money in deposits.

“We are an investor in MFX Solutions because we think they are going to go much farther providing credit solutions in countries that the banks won’t touch right now,” Erikson said. “It will be an interesting dance of supply and demand. As long as we are able to provide a service to meet that demand, we could start proving ourselves in six to eight months.”

Global expects to close in November on a new \$20 million fund that will be part of the test. Its first two microfinance funds were launched in 2005 and 2006.

Global’s direct participation is only 6 percent of the fund, and that investment acts as a loan-loss reserve. Two percent of the total comes from foundations, 27 percent from development banks, and the rest from endowments and other wealthy investors.

“We turn \$1.5 million of philanthropy into \$20 million in growth capital,” Beckett said.