

# [Banco compartamos case study](https://assignbuster.com/banco-compartamos-case-study/)

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Social innovation and enterprise is one way of eradicatingpovertyand illiteracy in society. The model that an enterprise takes determines their social impact in the long run. While some organizations maintain their social values over time, others abandon or diminish those values and venture into more financially profitable activities (Yunus 205). The paper addresses how the micro-financebusiness model used by Compartamos Bank compares with the village bank model of Grameen Bank. Microfinance in this sense refers to the supply of small loans, insurance, savings, and basic financial services to poor people, who are often unable to access such in conventional banking institutions.

It looks at the shift of Compartamos Bank to a commercial bank, impacts of the shift to its initial mandate, and the effectiveness of both models in poverty alleviation. When the need for profit making and scaling competes with the need to alleviate poverty, the social motive often diminishes. Sustainability of any social enterprise lies in maintaining its initial social values. Commercialization drives capitalism, which is often incompatible with social good. Making profound and lasting impacts on poverty alleviation requires consistency in social orientation.

Comparison of Microfinance Models

Compartamos Bank is a commercial microfinance while Grameen Bank is a village bank. The main difference between the two models is their funding methods. As a village bank, Grameen is primarily funded through local funds from community saving deposits, while Compartamos is funded as traditional commercial banks, engaging in IPO as one way of fundraising. Both models aim at reducing poverty, reaching scale, and financial sustainability though by applying different approaches. In place of collateral required by traditional banks, Grameen Bank uses voluntary formed small groups of five people for mutual and morally binding guarantees (Volkmann, Kim and Kati 253).

The banking system is based onaccountability, participation, mutual trust and creativity, a complete reverse from requirements of conventional banking. Village banking offers women equal access to financial aid, as they have been recognized as very enterprising. Operations of Grameen Bank are executed by bicycle bankers in various community branch units (Fotabong).

Group members meet weekly for collection of the repayments and are accountable for each other. Compartamos Bank as a commercial bank offers loans, insurance and savings to its clientele. It operates as a conventional bank targeting the poor. It is for-profit organization that charges higher rates and opened up to public and private investors in a bid to scale up its profitability and financial sustainability. Compartamos started as a not-for profit organization and its shift to a commercial enterprise has been received with mixed reactions. The major concern of the shift is not in the high interest rates charged but on the importance placed on profitability more than social good. With all the profits and scaling the people who benefit most from such a set up are the already rich investors at the expense of poor borrowers.

Evolution of Compartamos

Founded in 1990 as a non-government organization, Compartamos aimed to eradicate poverty by giving credit to small businesses, especially poor women. It was initially supported by international donors and philanthropists to serve indigenous people in the poorest parts of Mexico. The company turned into a for-profit organization in 2000 in order to increase their funding (Carrick-Cagna and Santos 4). The company began accessing capital markets in 2002 raising millions of bonds over the next years. It slowly involved private investors and further obtained a commercial banking license in 2006 to enable them offer more services to its clients such as savings and insurance.

The need to scale made the company raise hundreds of millions from a successful initial public offering (IPO), earning huge returns from private and public sectors without using any additional capital according to Carrick-Cagna and Santos. The profits allowed Compartamos to achieve financial self-sufficiency, no longer relying on donor aid. Thirty percent of the company was given to private investors and in essence the founders, with their visionary socialgoalshave no complete control over the organization. The commercialization of Compartamos may seem to emphasize profit making over social good. Currently it offers microcredit services such as loans, insurance, and savings to low income earners and is among the largest and most profitable microfinance institutions in Latin America (MFI Solutions, LLC, USA and La Colmena Milenaria, A. C., México 13).

Investors in the bank make enormous profits, which is a good thing for any organization but for a microfinance dedicated to improving lives of the poor, it is seen as a problem. The extent to which Compartamos benefits the already-rich private investors far outweigh the benefits accrued to poor borrowers. It charges up to 100 percent interest rates per year to borrowers. In the perspective of fundamental values of microfinance, the actions of Compartamos are not pro-poor.

Social Values

In the social enterprising context, the stand of Compartamos Bank is controversial. While to others it is a pro-poor initiative, others see a shift in its operation no different from conventional banks which are often anti-poor, anti-illiterate and anti-women according toYunus. Inequalities between the rich and the poor are a question of access to financial credit. Compartamos allegedly charges very high interest rates to its borrowers, who struggle to the rate while investors highly profit. Most of the poor people are also illiterate and few understand the idea of interest rates. What most borrowers focus on is how much they have to repay weekly but calculated in real sense, the interest rates are much higher than those of common commercial banks. The result is confining the poor in a never-ending cycle of poverty where they borrow more to service their credits.

Implications for Increased Commercialization

Compartamos IPO was a huge success in financial markets but majority of the shares went to hedge fund managers and commercial investors rather than the socially-responsible investment entity. According to MFI Solutions and La Colmena Milenaria, the lending capacity of the Bank increased after the IPO, though the interest rates charged went higher and higher with time. The bank has more than doubled its reach to clients in need of financial services in Mexico. In order to cater for the expansion and operating costs, the bank charges interests above the normal commercialMexicanrate.

It has however continued to expand and retain many of its clients. It is a major concern to microfinance, on the appropriate balance between the goal of providing access to financial services to the poor and profitability and sustainability of microfinance institutions. The shift of microfinance from social investors to commercial investors is a threat to social enterprises aimed at alleviating poverty. The IPO has sent a message that social service and profitability go together.

It is a message that will definitely attract more private investors into microfinance. Compartamos IPO does not exclusively have implications on the company but to the entire microfinance entity. As a non-profit organization started off by grants, the implication is that society may have a different view of social enterprises. Some would question ethical, moral, and social values of such establishments.

The Future of Microfinance

Players in the sector are uncertain about the future of microfinance, especially with the move of Compartamos to commercialize its operations. Commercialization of microfinance is seen as an opportunity to expand access of the poor to financial services. The high profit margins will attract more investment into microfinance, thereby availing moremoneyto extend to people to help them out of poverty. Additionally, it is felt that if other microfinance players shift to commercialization, the profit maximizing behavior will further take advantage of the poor. This would worsen the existing gap between the rich and the poor, profiting the rich and sending the poor into more poverty.

Initiatives of the past two decades to make businesses socially responsible will also have been a waste. Communities and socially-responsible investors may shy away from initiatives aimed at addressing serious social issues. Microfinance faces a danger of turning into how well investors are doing of how profitable microfinance institutions are instead of actively focusing on ending poverty. In conclusion, those who founded formal microfinance intended it for the social good, but when more people got involved, the objectives and intentions of social enterprises shifted. The best model that is well adapted to create wealth for the poor is Grameen’s village model. With commercialization it becomes difficult to determine where microcredit ends and loan sharking ends.

Involvement of private investors, whose main aim is often profit making would make social enterprises in microfinance serve more the interests of investors at a disadvantage of poor clients. It would turn microfinance from an area where non-profits and donors effect beneficial social and economic change into a haven for profit-maximizing investors. We are living in a capitalist society where the need to satisfy personal interest overrides social good. In view of microfinance and addressing poverty, it is better to operate on the traditional approach of such initiatives other than commercializing it.