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International Development Cooperation: The Case of the Municipal Savings Banks in Peru

HTW / MIDE Series: Germany's External Relations

Berlin, May 2, 2017

Germany's External Relations: International Development Cooperation - The Case of the Municipal Savings Banks in Peru

Do you hold the following statements for true or false? Please **read** them **aloud** and make your cross *immediately* and *spontaneously*! Afterwards, please compare *all your answers* with the ones of your neighbor!

	Correct	False	Statement
1.	<input type="radio"/>	<input type="radio"/>	The German Sparkassen are part of the municipal administration (Gemeinde, Stadt, (Land-)Kreis and governed by the corresponding elected parliaments/councils and mayors/burgomasters.
2.	<input type="radio"/>	<input type="radio"/>	German foreign aid agencies hire consultants for their technical assistance projects by competitive bidding. When problems arise (e.g. corruption), the consultant informs the agency's home office, and the next payments are held back until the case is settled.
3.	<input type="radio"/>	<input type="radio"/>	Like national development banks, municipal banks should be, in the first place, agents for the promotion of local business champions through cheap credit. In order to broaden their political support, a special microfinance program with soft loans should also be in place.
4.	<input type="radio"/>	<input type="radio"/>	Foreign aid should aim at "additionality" – both for the project effects in the receiving country and for the exports of the donor nation in order to ensure "ownership" on both sides.
5.	<input type="radio"/>	<input type="radio"/>	Microfinance does not need any "assistance". Only those special institutional arrangements are justified which try to overcome credit rationing by cost-covering, but not profit-maximizing banking, such as well-managed public banks, engagé private banks, municipal savings banks, credit unions /cooperatives and NGO-driven revolving or guarantee funds.
6.	<input type="radio"/>	<input type="radio"/>	The governance structure of the Peruvian Cajas Municipales de Ahorro y Crédito (CMAC) were modeled along the lines of the German Sparkassen, namely arm's-length distance to elected bodies, but firmly rooted locally, supervisory board with business leaders (but – different from Germany! – no labor representatives) and other locals, strong national federation, and supervision by banking authority.
7.	<input type="radio"/>	<input type="radio"/>	International development cooperation is always dependent on the "ownership" by the local partners. Consultants often overlook local customs and try to establish unnecessary German standards.
8.	<input type="radio"/>	<input type="radio"/>	Bilateral cooperation experience tends to spread globally – when successful. But it is considered "treason" by the initial local partner.

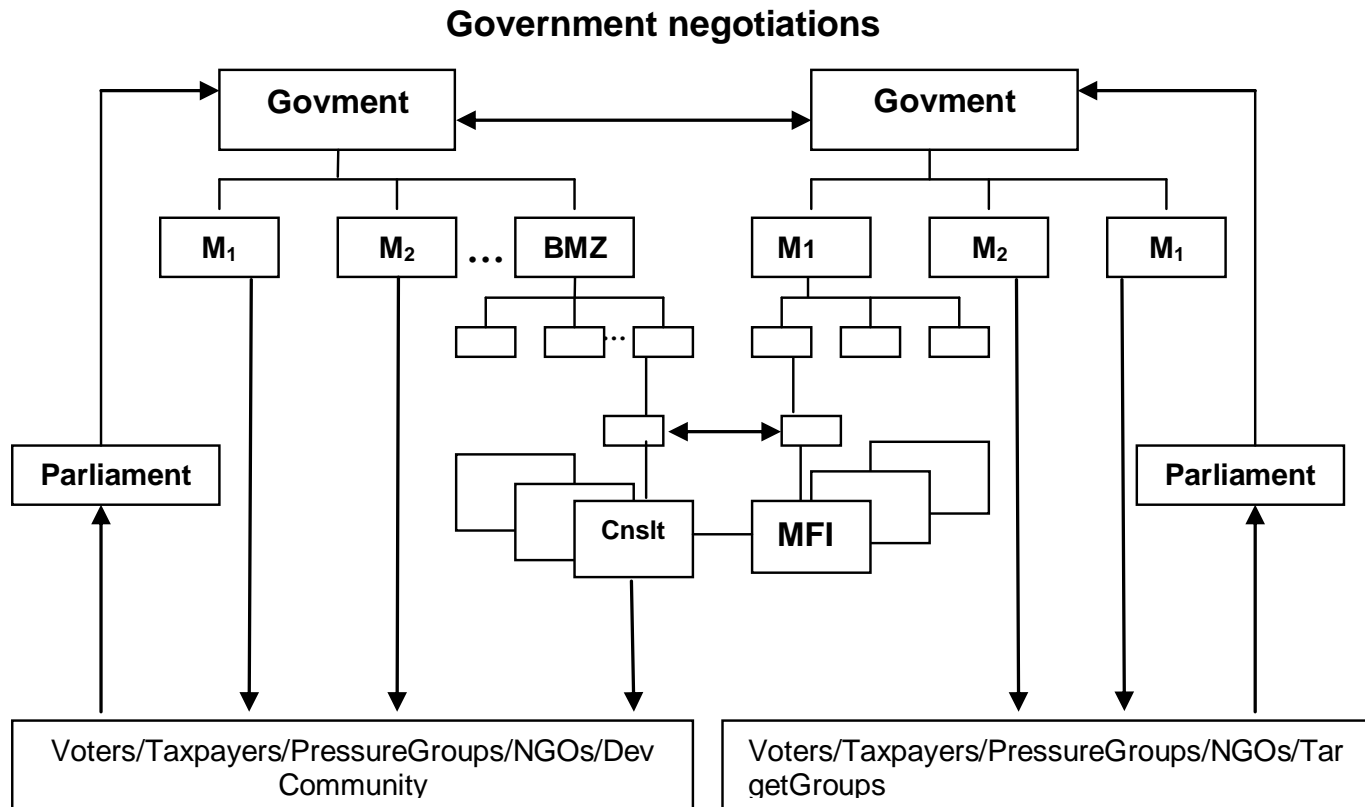
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- Right False Statement

- 1. Sparkassen are institutions of the municipal administration.
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- 4. Foreign aid aims at “**additionality**” for the receiving and the donor nation in order to ensure “**ownership**” on both sides.
- 5. Microfinance needs cost-covering banks.
- 6. Sparkassen are banks at arm's-length distance from politics
- 7. Consultants often impose unnecessary German standards questioning local “**ownership**”.
- 8. Bilateral cooperation experience spreads globally in spite of resistance from local partners.

4 – 7: “Ownership” – “Additionality”

Structure of International Development Cooperation



“Ownership“: Principal-Agent approach to institutions

- The **Principal as the master** of resources and command
 - Traditionally: rich and powerful
 - **Old** Institutional Economics: agent speaks for collectivity/class/ministry/firm/GTZ/Consultancy firm
 - Compliance through ideology, money and dismissal
- The **Agent as the master** of information and as the subject with his/her own open or hidden agenda
 - **New** Institutional Economics / Game theory; declared vs. true objectives and strategies
 - Accountability, reporting and transparency upwards and downwards

“Ownership“ via Institutionalism: Old and New

- **Old** (Marx, Veblen, Marxists, Welfare economists)
 - Collectivities matter
 - Class analysis
 - Individuals speak for countries, firms, ministries, trade unions, pressure groups, etc.
- **New** (Monetarists, Neoliberals, Mainstream economists)
 - Methodological individualism: Only individuals take decisions.
 - There is no common good, no national interest, welfare function, or public / municipal interest, nor an objective function of a bank
 - Individuals follow only and always their personal agenda, as top managers, professors, policepersons, judges, politicians, workers, spouses, workers, bureaucrats, journalists - or robbers

Papaya

- “!*No dar papaya y no perder papaya!*“
 - Don't let yourself be used / exploited by others!
 - Don't let out a chance to use / exploit others!
- Realistic image of *homo oeconomicus* ? !
- International Cooperation: Grant element
 - Duck-feeding – easy for children, *papaya* banking with the *amigos* of the politicians
 - Salt-licking – challenge for social engineers

“Additionality”

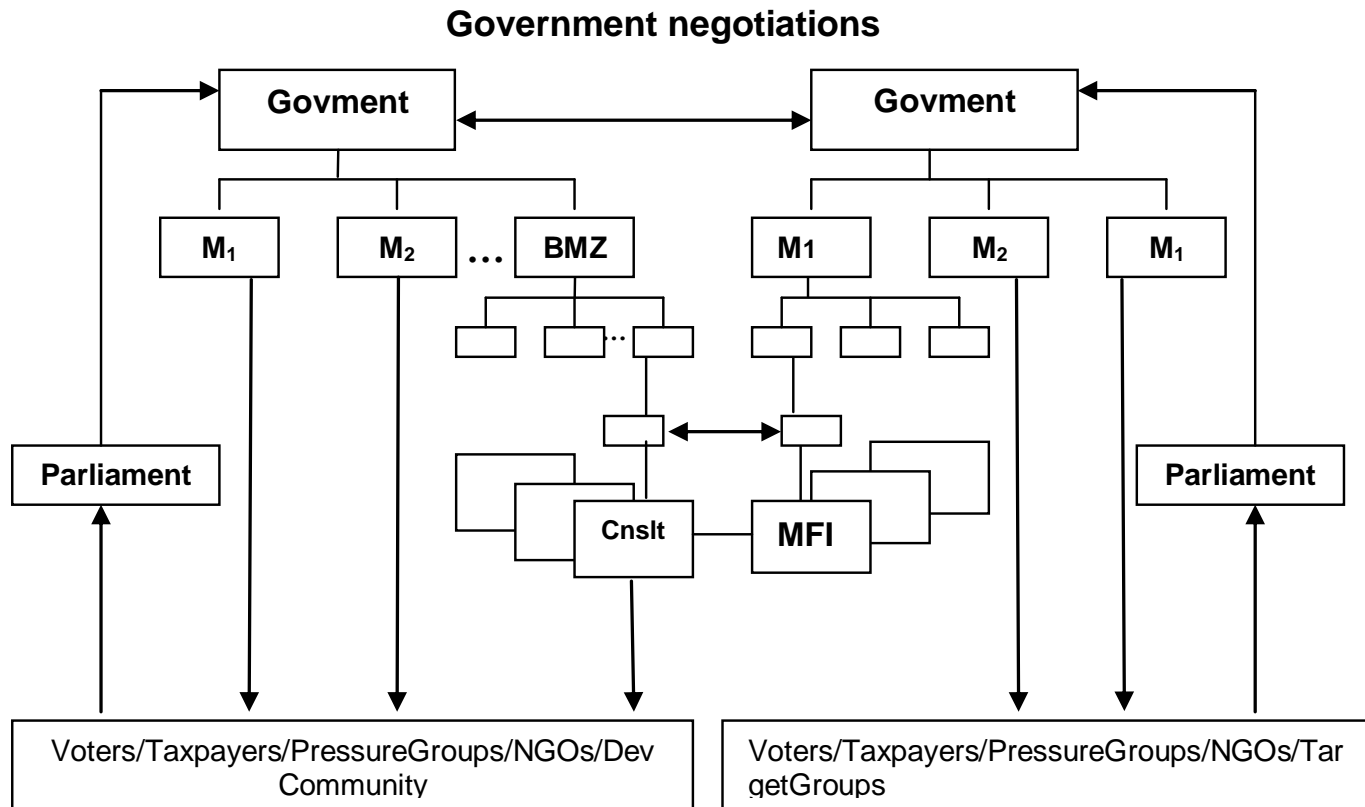
- **Donor nation: Exports**
 - ExImBank (USA) – explicit objective of export-financing and guaranteeing agencies
 - Berne Convention: No national supply “<Lieferbindung>” condition in Foreign Aid (ODA) projects; since many decades: **Dirty word**
 - New institutional economics: No rational agent cares anyhow.
- **Receiving nation**
 - Ambivalent concept: With and without additionality!
 - Parliaments don’t give the money, foreigners do; democracy?
 - Parliaments give priority to airports, military equipment or metro lines; foreign donors and World Bank/IADB etc. take over and substitute local resources, liberating them for <even more dubious> deals and *amigos*.
 - Our case: New minister had to do something additional for Piura, and there was no serious alternative, - looks like additionality.

Relation: “Ownership“ vs. “Additionality“

- Ownership **over** Additionality
 - **Duckfeeding**; airports, military equipment and budget aid
- Additionality **over** Ownership
 - Reserves for indigenous peoples (KfW: bank secrets)
 - National parks and similar ecological projects
- **Neither** Ownership **nor** Additionality
 - Development bank loans for established small customers
 - Disaster relief by foreigners, where local efforts would have sufficed to relieve the damage
- Both Ownership **and** Additionality
 - **Salt stones** – like cost-covering (= expensive) banks for poor people with support from local authorities
 - No costs for local vested interests

4 – 7: “Ownership” – “Additionality”

Structure of International Development Cooperation



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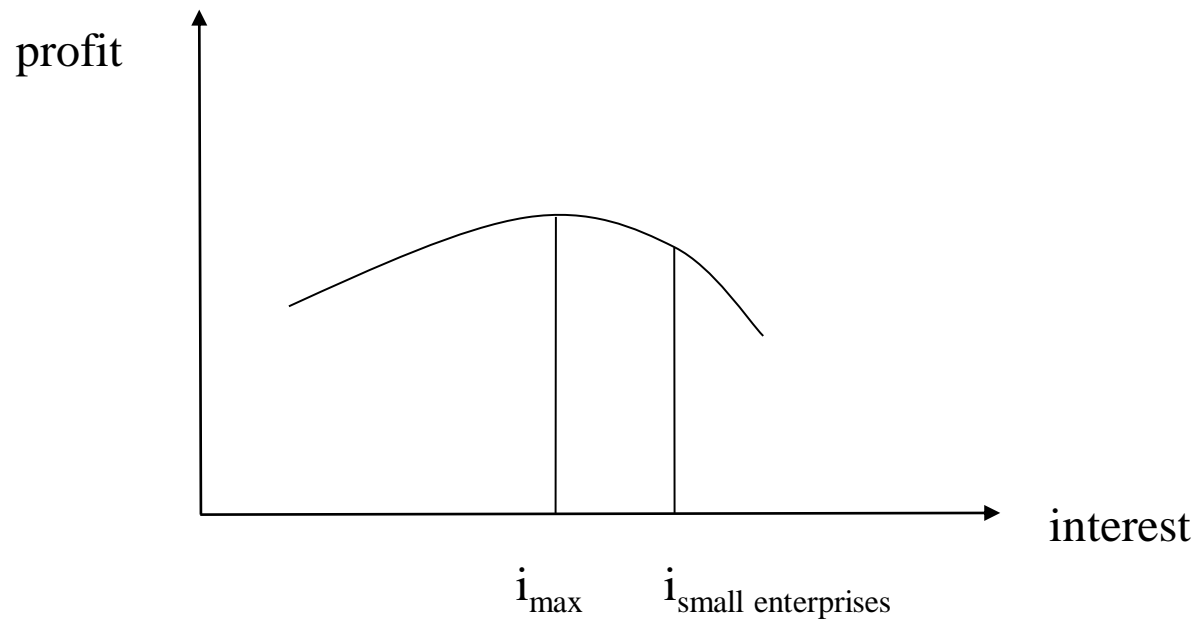
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1 – 6: Sparkassen

- *Sparkassen* – since the 19th century
 - **Savings first** – municipalities have to take care of the poor
 - The German *Sparkassen* System: Local banks, association, second-tier banks of the *Länder* (*Landesbanken*)
 - National system: Auditing and training; under banking supervision; access to Bundesbank / European Central Bank
 - International relations and cooperation: Foundation
- *Sparkassen* are full-fledged banks with local politicians and representatives from business on their supervisory councils; one half: labor representatives (!) because of Germany's "co-determination" – economic democracy
- National reach, European and global networks
- Theoretic justification: credit rationing

Credit Rationing by purely commercial banks



- Adverse selection through asymmetrical information

- Authors: Stiglitz/Weiss, AER 1981

Cajas Municipales in Peru

- Initial project proposal from the city of Piura
- My first visit: Modest municipal pawnshop with jewelry, motorcycles, household goods, TV, clothing, etc.
- Next year: Weather disaster *El Niño* – basement flooded; better: only gold jewelry - local tradition; **women's bank / pawnshop**
- Other *Cajas Municipales*:
 - Cash-box of the municipal treasury (planned in Arequipa)
 - Very special public service in Lima: Counter the trade unions of public workers through 50 non-working *Caja* employees “negotiating” salary increases
 - Close to close-down because the city treasurer did no longer cover the budget (Callao)
- Unspecific legislation, no association and lax supervision
- Difference between budget (flow) and asset (stock) management

The Project

- Upgrade the *Caja de Piura*
- Study and establish similar *Cajas* in other cities and provinces
- Leave out Lima and Callao
- Form an association with strong auditing, training and consultancy functions
- Train the personnel
- Bring together: *Sparkassen* and *Cajas*

Contribution of the *Sparkassen*

- Main influence: We compete with banks and have a considerable market share
- Internships for Peruvian staff members
- Counterweight to consulting firm and university professors: “*Praxis*”
- Mutual visits of politicians and bankers
- Backing of the project in Parliament, Ministry, GTZ and locally
- Technical advice

Sparkassenstiftung für internationale Kooperation

- Since 1992 (before – the Association)
- Professionalization of banking services, including cooperatives, village banks and other non-municipal financial institutions
- Professional education and training institutes
- Studies
- Projects for development agencies around the world
- Very little participation in equity

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| . | | | |

2-7-8: The Role of Consultants

- My own experience as professor and consultant
 - Hired by the Ministry for evaluating development banks
 - Later together with CP Zeitinger, IPC
 - Member of the Supervisory Board of IMI (1998)
 - Later renamed ProCredit – I am no longer involved.
- The role of IPC in the CMAC project
 - Subcontractor of GTZ, together with *Sparkassen*-Foundation
 - The *cholo* to do the work, but dismissed when bothering
 - Corruption difficult to sanction; compliance control ?
 - Quasi-project “The consultant is the project” – own agenda
- IPC – IMI – ProCredit: We can do it ourselves!

International Cooperation

- CMAC experience with local partners
 - Piura – successful, but not happy with activities beyond Piura
 - National Association of CMACs – too weak
 - Banking Supervision Authority – powerful and successful
- IPC in other projects – Eastern Europe
 - Consultants make a fortune, but banks go broke afterwards
 - Bail-in commitment of consultants by equity investment
- Foundation of IMI (Internationale Micro Invest AG)
 - Holding for minority stock in MFIs (micro finance institutions)
 - Later ProCredit: Also main investor / owner / majority share
- Partners: KfW (Kreditanstalt für Wiederaufbau) with participation and loans; other European Development Banks; NGO banks;
- IFC (Intern. Fin. Corporation) – World Bank branch for equity

International Development Institutions

- United Nations with its various agencies
- IMF
- World Bank
 - IBRD – International Bank for Reconstruction and Development
 - IDA – International Development Association
 - ICSD – Intern. Centre for the Settlement of Investment Disputes
 - IFC – International Finance Corporation
 - Shares / equity and loans
 - CGAP – Consultative Group to Assist the Poor (with IBRD and others)
- Other intergovernmental organizations
- Others (business, NGOs, churches, foundations, etc.)
- .

ProCredit Holding / banks

- Consulting firm owner and employees frustrated as consultants insisting on “unnecessary German standards“ (No. 7)
- Become board members and even owners – first IMI, then ProCredit
- Mission statement: Transparency; no consumer lending; no financialization; market orientation; profit-making, but not profit maximization
- Since 2011 also in Germany

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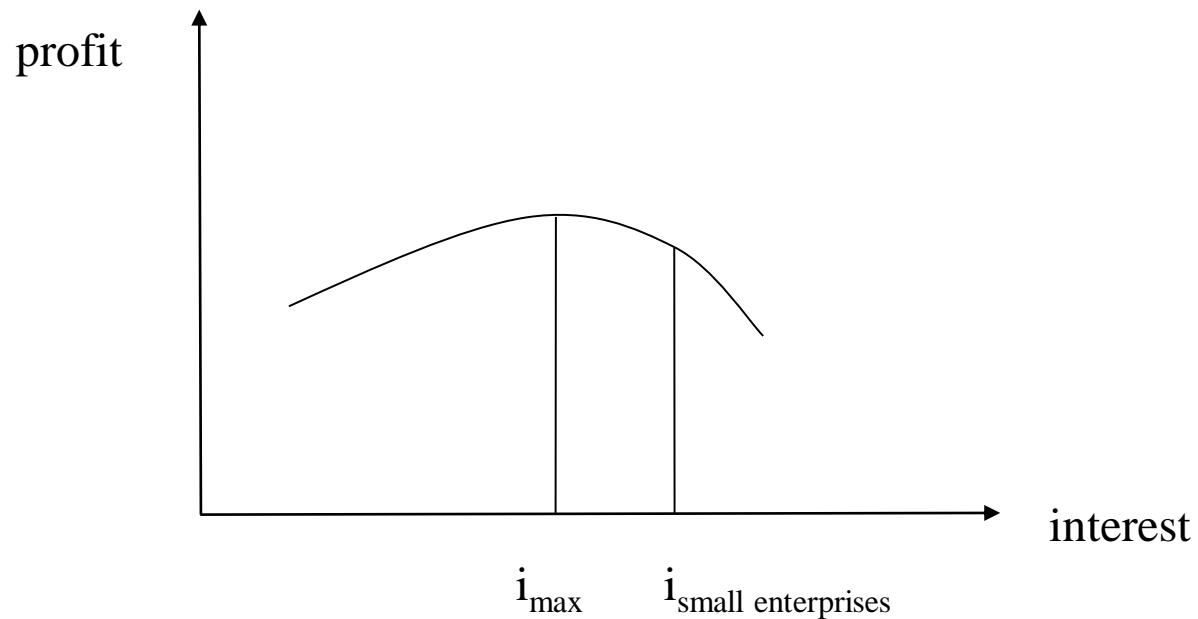
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3 – 5: Finance and development

- Cheap credit as *papaya* vs. “New Development Finance”
- Bankarization of the poor, the micro-enterprises and the SMEs (small and medium enterprises)
 - CGAP
- Theoretical justification for profit-seeking, but not profit-maximizing banks for micros and SMEs
 - “Credit rationing“: Banks cannot charge the necessarily high SME fees and interest payments, because they would lose their other clients.
 - Special institutional arrangements are warranted, which cover costs, including return on investment.
- .

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Microfinance hype

- 1990s and beyond: Microcredit boom
- Yunus' Nobel Prize
- UN Year of Microfinance
- First IPOs (initial public offering)
- First securitization – investment; financialization
- Impact studies: No impact to be detected
- Suicides in India
- Criticism and sober evaluation
 - Technology makes possible bank account for everybody
 - No panacea for fighting poverty, but a small step

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- 1. *Sparkassen*: prone to *papaya* treatment; auditing; **ownership**
- 2. Consultant: **agent** with own agenda; frustrated by lax **principal**
- 3. Cheap credit: *papaya*; economics of **institutions – old and new**
- 4. Project aim: **additionality** and **ownership** in receiving country
- 5. Microfinance: **credit rationing**; profit-making, not maximizing
- 6. *Sparkassen*: banks manage **stocks**, politicians manage **flows**
- 7. Consultants: **from agents to principals/owners** of banks
- 8. **Banking with/for the poor: global mission**, mindset, technology

Thank you

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