

Is the Price Right?

An exploration of microlender pricing

October 13, 2011



FIELD

at the Aspen Institute

Advancing microenterprise through knowledge and innovation

Microenterprise Funders Group



- Founded in 2005 -- a forum to explore funder interest in microenterprise development in the U. S.
- As of October 1, 2011 – merged into Asset Funders Network.

For more information:

<http://www.assetfunders.org/>

A brief note on technology



Tech Support

- Email: jackieo@aspeninst.org

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Goal of today's webinar



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Exploration of microlender pricing:

- Where's the US field on pricing
- Issues raised/emerging dynamics
- Implications for funders



Invited Guests



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Brett Simmons,
Director of Programs
and Policy



Paul Leonard,
California Director

The U.S. context



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State usury laws

Differing views on use of subsidy

Highly subsidized rates

Positioning--alternative to high-priced
Predatory lenders

Emerging Tensions



Emergence of for-profit microlenders =
some consumers value access and speed



Concern that higher rates negatively impact
disadvantaged entrepreneurs

Emerging Tensions



Limited earned revenue =
sustainability ↓



For-profits moving aggressively towards
self-sufficiency/earned revenue

Pricing Picture



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nonprofit

subprime cards

for-profit

Annual Percentage Rate (APR)

3 - 18%

23.95%

18-60%

(n=137)

Effective Interest Rate?

Fees

Flat fees

2-7%

\$18 to \$150

Flat fees

5% - ?

Impact on Bottom Line



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	<u>\$1000/6 mos.</u>	<u>\$2500/1 yr.</u>	<u>\$25,000/3 yr.</u>	<u>\$25,000/5 yr.</u>
Interest Rate				
50%	\$191.80	\$268.96	\$1,352.85	\$1,140.12
8%	\$170.58	\$217.47	\$783.41	\$506.91
Difference: 50% vs. 8%	\$21.22	\$51.49	\$569.44	\$633.21

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Take-away



- Understand the pricing process
- Examine expectations regarding scale/sustainability
- Support market research around pricing sensitivity
- Promote transparency v. pricing restrictions



Download at:
<http://fieldus.org/Publications/FunderGuide17.pdf>

FIELD Funder Guide



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Is the Price Right? The Role of Pricing in Microenterprise Lending

The past several years have seen a great deal of controversy regarding the interest rates and prices charged by some microfinance institutions (MFIs) in developing countries.¹ The debate has emerged in part because of the entrance and success of for-profit microfinance institutions that have, in some cases, reaped significant returns for their investors. Further, the ongoing discussion about interest rates and pricing is linked to an emerging concern about the extent to which MFIs are providing a route out of poverty.

The interest rates and prices charged by U.S. microenterprise lenders have, to date, not been significant issues of debate or discussion among practitioners, donors or in the general media. This is partly because interest rates in the U.S. are, for a variety of reasons, lower than those charged in developing countries. In fact, most, if not all, nonprofit microlenders in the U.S. are charging prices that are subsidized (in other words, are well below their costs). Most U.S. microlenders are, therefore, seen as “affordable” sources of financing that are a clear alternative to payday or predatory lenders.

Two emerging dynamics may lead to greater focus on interest rates and pricing in the United States. The first is the entry into some markets of several for-profit microlenders and microfinance institutions that have shown strong rates of growth over a short period of time but in some cases are charging substantially higher rates than nonprofit lenders.² The second is the growing recognition that the fact that the rates currently charged by nonprofit microlenders are well below their costs may be one factor hindering their growth and sustainability. This guide explores the issues relating to the pricing of microenterprise loans that funders may want to consider as they engage with lenders.

The pricing picture

There is no available industry-wide data on the prices charged by nonprofit microlenders.³ However, FIELD has collected pricing information from a set of five lenders participating in its Scale Academy for Microenterprise Development. The interest rates charged by these lenders range between 5 and 18 percent (with most falling below 13 percent). Closing fees also vary, with some of the five lenders charging flat fees that range from \$35 to \$250 and others charging a percentage of the loan ranging from two percent to seven percent. Both interest rates and fees vary across the different loan products offered by these lenders, based on a variety of factors, including the source of the loan capital, and the size and purpose of the loan.⁴

In comparison, according to creditcards.com, the national average credit card interest rate was 14.67 percent as of April 27, 2011; the national average for business credit cards was 12.91 percent and for individuals with subprime

¹ Eva Pereira, “Re-Examining the Microfinance Mission: Should Interest Rates be Capped?” *Forbes*, September 30, 2010, <http://blogs.forbes.com/evapereira/2010/09/30/re-examining-the-microfinance-mission-should-interest-rates-be-capped/>, (accessed June 20, 2011).

Also, Anel Karmani, “Microfinance Needs Regulation,” *Stanford Social Innovation Review*, Winter 2011, http://www.ssireview.org/articles/entry/microfinance_needs_regulation/, (accessed June 20, 2011).

² Luz Gomez and Elaine L. Edgcomb, *A Newly Crowded Marketplace: How For-Profit Lenders are Serving Microentrepreneurs* (Washington, D.C.: The Aspen Institute, 2011), <http://fieldus.org/Publications/ForProfitLenders.pdf>.

³ Although, there may be data available soon. The U.S. Microenterprise Census, conducted by FIELD at the Aspen Institute, includes a question on interest rates. Three hundred and sixty-nine microenterprise organizations provided detailed responses to survey questions in the last census, which collected data on 2008 performance. The current Census is collecting 2010 data, and the analysis is projected to be available in fall 2011.

⁴ Elaine L. Edgcomb, Joyce A. Klein and Luz Gomez, *Dollars for Dreams: Scaling Microlending in the United States* (Washington, D.C.: The Aspen Institute, 2010), pp. 17-20.

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