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FACT

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**MILLIONS FOR MILLIONS**

by CONNIE BRUCK

This year's Nobel Peace Prize winner and some high-tech entrepreneurs are competing to provide credit to the world's poor.

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Over the Labor Day weekend of 1995, a ponytailed, bearded young software engineer named Pierre Omidyar wrote a code that enabled people to buy and sell items on the Internet. In the first few weeks after the program was introduced, items ranging from a Maxx comic book to a 1952 Rolls-Royce Silver Dawn changed hands. That program eventually became eBay. Not long after the company went public, in 1998, Omidyar's share of the stock offering was roughly ten billion dollars, and he became the richest thirty-two-year-old in the world. He found the experience slightly unsettling—he told friends that he had never planned to get rich—and he continued driving his Volkswagen Golf. With his wife, Pam, he started a foundation to give away large sums of money, but he was frustrated by the constraints and inefficiencies of the nonprofit world. Omidyar was searching for a way to change things on a grand scale, and, like many other highly successful young West Coast entrepreneurs, he became interested in a field called microfinance, or microcredit. In November, 2004, he and Sergey Brin and Larry Page, the co-founders of Google, and other leaders of the high-tech community gathered at the San Francisco home of the venture capitalist John Doerr for a weekend session with Muhammad Yunus, who is considered the godfather of microcredit.

Yunus, a silver-haired man of sixty-six with a round, luminous countenance, is a highly gifted interlocutor between the extremely poor in the developing world and the West, and for years he had been seen as a candidate for the Nobel Peace Prize. (This December, he will go to Oslo to receive it.) During the famine of 1974 in Bangladesh, when the dying lined the doorsteps of the better-off in Dhaka, Yunus, an economics professor at Chittagong University, found the theories he was teaching maddeningly irrelevant; so he went into a neighboring village and began talking to the poor. He experimented with ways of helping them—initially, he lent twenty-seven dollars to a group of forty-two villagers—and before long he became convinced that he had a remedy for their condition: providing very small individual loans to the impoverished to start activities ranging from making bamboo stools to buying a dairy cow. In 1976, after local banks refused his entreaties to make the loans, he resolved to do it himself, and he founded the Grameen Bank.

Yunus is a mesmerizing salesman. In the eighties and early nineties, the Grameen Bank received close to a hundred and fifty million dollars in soft loans and grants; today, funded by savings deposits from borrowers and others, it essentially supports itself. It has disbursed more than \$5.3 billion to nearly seven million borrowers who have no collateral; ninety-six per cent of them are groups of women, who meet once a week and, through incentives, help to insure their individual loan repayments. (Traditionally, Third World banks lend only to men. Yunus says that he developed the policy of lending mainly to women not only because

they were more responsible about re-paying the loans but because families benefitted more when the women controlled the money.) To cover the high cost of servicing these small loans, borrowers pay interest rates of up to twenty per cent, and Grameen claims that it recovers ninety-eight per cent of the loans. Some of Grameen's numbers have been challenged, but no one disputes Yunus's assertion that, contrary to traditional banking doctrine, the poor can be reliable borrowers, even at high rates of interest. These days, Yunus raises money for the Grameen Foundation, a global nonprofit group that supports microcredit institutions around the world. Many are related to the Grameen Bank, but only loosely; Yunus believes in locally designed, run, and controlled institutions.

As microcredit has changed in the past thirty years, achieving broad recognition and even some early commercial success, Yunus has modified his methods, but he has never wavered from his goal. He insists that microcredit can lead to a world in which poverty has been extinguished and that eventually, as he puts it, there will be "poverty museums." He told his audience at Doerr's home that more than fifty per cent of the Grameen Bank's borrowers who have been in the program for more than five years have risen out of poverty, according to a simple measurement system that he himself had devised. (To have graduated from poverty, a family must have, among other things, a house with a tin roof; clean drinking water; a sanitary latrine; warm clothes for winter and mosquito netting for summer; about seventy-five dollars in a savings account; and schooling for the children.)

At lunch, Janet McKinley, a Grameen Foundation donor who used to run a major mutual fund and retired at the age of forty-nine to concentrate on microfinance, told the group that in 1995 she had visited a small program run by the Vietnam Women's Union, and saw how a loan of twenty dollars could change a woman's life. Her companion, George Miller (now her husband), gave the union a five-year grant of a million dollars, enabling it to expand from five hundred women to ten thousand, so that the more successful participants could get bigger loans and hire other women. McKinley and Miller returned each year. "There was a woman who started out with a mud hut," McKinley recalled. "When we came back, she had a three-room house with a cement floor, and the pigs were in the hut she had stayed in before." When the women first came for loans, "they sat hunched, looking down into their laps. They would take the money and fold it into a hairpin behind their ears, looking so frightened—because, they said, they were afraid they couldn't pay it back. Two or three years later, these same women were running businesses, and were often involved in politics in their village." She continued, "Does everyone succeed? No. But it is the same in the investment business. You don't want to take a lot of risk? Buy some ducks. But the more risk-taking borrowers will pool their loans and buy a baby water buffalo and rent it to men for farming. And then there are those who blow right past livestock and build a brick factory."

That afternoon, the participants broke into discussion groups, and were given forty-five minutes to devise a solution to end world poverty. The entrepreneurs weren't humbled by the challenge. "The inner graduate student in all these people came out," Alex Counts, the Grameen Foundation's president, said later. "They were all rushing up, taking turns at the whiteboard. And they took it so seriously!"

None, perhaps, more than Pierre Omidyar. Born in Paris to Iranian parents, Omidyar came to this country as a child in the nineteen-seventies, and viewed himself as a truly transformative capitalist. His purpose in creating the program for what became eBay was to

create a perfect market, something realized only in economics textbooks, where buyers and sellers would all have equal access to information and opportunity. And microfinance, after all, was about equal access to capital.

Counts recalled that Omidyar, who is given to phrases like “Wow!” and “That’s neat!” kept refining the numbers throughout the day. Omidyar was struck by Yunus’s statement that the poor are natural entrepreneurs, essentially because their business activities are a matter of survival. “By giving them the tools, you unleash the entrepreneurial instinct,” Omidyar told me. Janet McKinley said, “All these wealthy entrepreneurs loved it, because they say, ‘This woman is an entrepreneur—just smaller scale.’”

The event at Doerr’s home had been billed as a learning session, not a fund-raiser, but several participants insisted that they be given a chance to contribute. Alex Counts introduced an idea that had been discussed at the Grameen Foundation for some time: a guarantee fund. If the guests would each guarantee a certain amount of money, the combined pledged funds would constitute a letter of credit, which Grameen could present to banks in various countries to induce them to loan to local microfinance institutions—in larger amounts and at a lower rate than they otherwise would. The donors’ money could continue to work in their portfolios and would be called upon only if an institution defaulted on its loan. According to Counts, John Doerr declared that everyone should commit no less than 0.1 per cent of his net worth. “It was kind of awkward,” Counts recalled, “but finally some raised their hands and said they would do it.” Ultimately, nine people committed a total of thirty-one million dollars to the guarantee fund, which aims to reach fifty million dollars.

Omidyar, however, wasn’t among them. As much as he admired Yunus’s belief that anyone, provided the means, can become self-sufficient—even successful—he has a different idea about the future of microfinance. Yunus is now seen by Omidyar and many others as the archetypal founder, too wedded to his original vision. In recent years, younger and nimbler players have been taking microfinance—their preferred term—toward the idea of building a fully commercial, profit-making sector. This conflict, between pure do-gooders and profit-minded do-gooders, has come to define the current debate in the microfinance world.

During that weekend at Doerr’s, Omidyar told me later, he was most impressed by the notion of “sustainability,” and by the idea that microfinance could help millions of poor people. “I was asking questions—‘How much does it cost to reach a new borrower? How much does it cost to open a new branch?’ What I was hearing back from Professor Yunus was very encouraging. So if you do the math, say it’s two hundred dollars per client—and that includes initial loan capital and the cost of the loan officer and the branch. This is cocktail-napkin math, right? But multiply the two hundred dollars by the three hundred million poorest people.” He estimated that three hundred million heads of household represented the world’s 1.2 billion poorest people. It would cost sixty billion dollars. “And then you’re done! It’s not an annual number. Once it’s scaled”—that is, once it has expanded to its full potential—“it’s a self-sustaining, profitable model, which opens the door to reaching large numbers of people who need to be reached by this tool of access to capital.” Microfinance institutions would eventually be able to raise money in the capital markets, and no longer have to rely perpetually on donor funding. “Rather than saying it’s going to cost forty-five billion dollars a year, this year, next year, and forever, you can think of it as an initial investment—but there’s a cap to how much you’re ever going to put in.

That's the difference between microfinance and the typical sort of government aid or charity, which is an ongoing thing."

Yunus, too, believes in sustainability, and he certainly wants to reach all the world's poor, but he is convinced that the traditional goal of business—maximization of profit—is inappropriate when dealing with the poor. "I had a long debate with Pierre," Yunus told me, referring to Omidyar. "He says people should make money. I said, Let them make money—but why do you want to make money off the poor people? You make money somewhere else. Here, you come to help them. When they have enough flesh and blood in their bodies, go and suck them, no problem. But, until then, don't do that. Whatever money you are taking away, keep it with them instead, so they can come out more quickly from poverty."

The discussions at the Doerr event, Omidyar told me, led him to "a little epiphany." He and his wife are alumni of Tufts University, to which they had already made substantial contributions; but a capital campaign was starting soon, and the president of Tufts, Lawrence Bacow, "was sort of circling," Omidyar said. "I was hearing, 'You're a pretty successful alumnus—you may have to step up.' " Typically, when a donor makes a gift to a university endowment, the principal goes into an investment pool, and the annual return on that capital is what the donor can direct to a specific use. "I said, Wait a minute! Instead of making a gift to an endowment and having it go into this pool, why not use that capital to further the mission of microfinance? Kill two birds with one stone—support the alma mater and support the mission. That's pretty neat!" Several months later, Omidyar gave a hundred million dollars to Tufts—the largest gift in its history. But he stipulated that the principal be dedicated to a fund to invest in microfinance—specifically, in investments that would promote microfinance's commercialization.

The idea of reaching billions of the poor by achieving "scale"—a word invoked ceaselessly in the microfinance community—has enticed foundations, rich individuals, even investors into channelling millions into microfinance. The \$1.2-billion Michael and Susan Dell Foundation—established by the founder of one of the world's largest computer manufacturers—has begun making grants to microfinance institutions in India, a country of 1.1 billion people, most of whom have no access to financial services. In October, 2005, Google established a philanthropic entity called Google.org, with seed money of about a billion dollars, to fight disease, global warming, and poverty; microfinance is expected to be a key component of its poverty portfolio. And last April the Bill and Melinda Gates Foundation announced that it would devote an undisclosed amount of money to expanding financial services for the poor in developing countries. Dr. Rajiv Shah, who oversees the new Gates program, said of microfinance, "This can reach hundreds of millions of people, and do so in a way that helps them move out of poverty and that sustains over time."

In 1990, Carmen Velasco, a Bolivian psychologist, and Lynne Patterson, an American then living in Bolivia, founded an organization called Pro Mujer. It is, in many ways, a classic microcredit N.G.O., inspired by the Yunus model, and its clients are predominantly very poor women. It provides credit for income-producing activities, but, unlike a bank, it also offers its clients training in health care, family planning, child development, and self-esteem. Velasco, who still runs the organization, says, "If you give them a loan and don't see that their other needs are met, perhaps they are worse off. They have a debt to repay, but still they have no sanitation, no health care, no education." Unlike many N.G.O.s, however, Pro

Mujer largely supports itself. “We don’t fudge on our numbers, we have the best auditing firms, we have received awards and high ratings for our business practices,” Velasco said. “And as soon as we become more efficient we lower the interest rates our clients have to pay. If we weren’t financially viable, we wouldn’t have the right to argue for our way.” By “our way,” Velasco meant the traditional emphasis on social justice—even though, as she put it, “the fashion today is all about making it into a business.”

Last spring, I accompanied some Pro Mujer officials to the rural town of Tizayuca, about a two-hour drive from Mexico City. Twenty Pro Mujer clients—all women—were sitting under the canopy of a large tree outside a simple stucco house. “*Presente*,” one after another responded as their names were called. They were attending their weekly meeting. The women ranged in age from their twenties to their fifties; many had small children with them, who played nearby or sat solemnly on their mothers’ laps. This day’s session—after the women had made their payments to the treasurer—was devoted to self-esteem. The instructor, a relentlessly energetic woman, was encouraging members of the group to stand and describe how they viewed themselves. One by one, they rose, took a few steps into the center of the circle, and began to speak.

Like all Pro Mujer clients, the women had begun by forming a group and then taking a week of training to learn about the process and develop a business plan. By the week’s end, they had elected their board and chosen a name for themselves—Mujeres del Futuro. They had started by each borrowing two thousand pesos, or about two hundred dollars, in a three-month loan; then they had graduated to three thousand pesos, then four thousand, and now they were borrowing five thousand pesos, in a six-month program. They had advanced to the higher loan level after repaying the smaller loans. Weekly savings were mandatory, as were the installments on repaying the loan. Each woman was engaged in what might be called a microbusiness. Some sold quesadillas or tortillas at a market stand; others sold women’s underwear, Tupperware, or blankets, mainly door to door.

The Pro Mujer officials began asking questions. What do your husbands do? Several were carpenters and construction workers. Should men join the group? That sparked a great deal of laughter and rolling of eyes. “No, but let them have a different group,” a woman suggested. “They would be thinking differently. They wouldn’t be on the same wavelength,” another said. A young, soft-spoken woman said, “There is a little machismo here. It is a great help to go out. Some husbands don’t really agree that we should be here. Even when there is not enough income, it is difficult for husbands to acknowledge that. So there are double challenges. We have to do everything at home so that when we are here they don’t have any problems in our house.” Do their husbands know about their savings? “No!” they responded at once. “If they knew we managed to save,” one said, “they would give us no money for the house.” Not one of them had ever had a bank account, although they were all familiar with moneylenders, who generally charge about twelve to fifteen per cent a month, and in some instances as much as fifty per cent a week.

We drove to another small town, San Francisco Zacacalco, and waited on a narrow, dusty street. After a time, a stocky figure appeared, walking beside a bicycle that had been modified into a three-wheeler. It was a portable oven: balanced over the front wheel was a bright-red propane tank, which was attached by a pipe to a large aluminum can, carried in a makeshift cart between the two rear wheels. Its inventor and owner, Ilze Concepción Rodríguez Chávez, invited us into her workplace, a two-room concrete structure, painted

blue, about eight feet high. A huge Rottweiler was on the roof, barking ferociously. “Close your eyes,” Chávez said, grinning with mock dismay as we entered the small room, where cans, pots, and tamale ingredients were strewn over the counters.

A warm, self-possessed woman of fifty-four, Chávez was wearing a navy baseball cap and a blue work shirt over a pink-and-blue plaid apron. She has eight children and twenty-five grandchildren. Eight years ago, she said, she and her husband were extremely poor, and they saw no way to improve their situation. But then a friend who had become a Pro Mujer client invited her to attend a meeting. Chávez said that she was worried about the one-week training program (“I learned how to read and write making tortillas—I don’t know much”), but she decided to join.

With the help of instructors, Chávez developed a business plan. She realized that the hot-tamale vender outside a nearby school came only in the afternoons; she could be there in the mornings. She started with a four-month loan amounting to about two hundred dollars. Each week, she met with the other members of her group—about twenty women—to make her payments, and take part in sessions dedicated to financial decision-making, health topics, domestic violence. With the initial loan, she was able to rent her workroom. With her second loan, of about three hundred and fifty dollars, she bought the bicycle and rebuilt it. She now has a loan of five hundred and fifty dollars, and next time she will ask for six hundred and fifty. She has added empanadas to her repertoire. On a good week, she makes as much as two hundred dollars. Her workroom contained a microwave, a television, and a DVD player. She explained that she had bought these on an installment plan, and that she organizes her week according to her debt obligations—generally, three days to pay the interest on her consumer loans, two days to pay Pro Mujer. Pro Mujer Mexico is a relatively new, small organization; its size, extra services, and the high cost of operating in Mexico result in an annual interest rate (including taxes and other fees) of about eighty-four per cent.

But Chávez didn’t find it exorbitant; the poor are accustomed to expensive credit. Chavez said that she never writes any of these figures down, but she was very precise in detailing the various amounts. She said that she had decided she needed a small car, even if it was old. She paused, and then gestured theatrically toward a beat-up white sedan parked outside. She had already bought it! She added that she now wanted a professional oven, with three levels, which the car could transport. She told us that her husband became jealous when she joined Pro Mujer, and wanted her to quit. But her daughter and son-in-law defended her. “My husband said, ‘How is it possible that there is a group that allows a woman to feel so independent? What is this group doing?’ ” She laughed. “It’s the machismo—they want a woman here,” she said, pointing to her knee.

She smiled even more broadly, looking around the room at her admiring guests. “I wish my husband could be here, to see me being interviewed,” she said.

The broader shift toward the profit model began in the nineties, when Acción International, a network of Latin-American institutions, concluded that commercialization was the only way microfinance could serve large numbers of people, because commercial enterprises could tap the capital markets for the funds they needed to grow. In 1992, Bolivia’s BancoSol, an Acción affiliate, transformed itself from a nonprofit into the first private

commercial bank in the world dedicated exclusively to microfinance—and dozens of other institutions have followed.

“Acción created the commercial model, and the commercial model is the one that works,” the organization’s president, Maria Otero, declared. She and Pro Mujer’s Carmen Velasco were schoolgirls together in Bolivia, and their fathers were best friends. Now they are on opposite sides of this small, fractious community. “Pro Mujer is performing well, and it could become a commercial bank,” Otero told me. “But Carmen believes becoming commercial will dirty you with the ‘P’ word of profit. She thinks it will compromise the program.” Otero thinks that nonprofits don’t have much of a future in microfinance.

The debate is about much more than purity of motives. The Yunus faction worries about “mission drift,” saying that, as the drive for profitability increases, only the so-called “less poor” (as opposed to the very poor) will qualify for loans. “On the one side, there are the people saying, essentially, We want to be Citigroup for poor people,” said Jonathan Lewis, the C.E.O. of MicroCredit Enterprises, which provides loan guarantees from wealthy donors to institutions that serve mainly the poorest women. “But, on the other side, we’re saying, We didn’t start this to become a bank. We started this to end poverty. So we’re going to experiment with all the different ways, profitable or not, that we can work with our constituencies—who are our customers, not our shareholders. If your core mission is to provide a channel out of desperate poverty, it creates a different set of questions than if your mission is to create a global market in microfinance futures.”

Hyperbole distorts the debate on both sides. Muhammad Yunus speaks eloquently about eradicating poverty, but some advocates of commercialization argue that microcredit burdens the very poor with debt, and that the less poor are the only appropriate customers. Since relatively few rigorous studies on the impact of microfinance have been completed, ideology tends to dominate. Jonathan Morduch, a professor of public policy and economics at New York University’s Wagner Graduate School of Public Service, who has studied the field for more than a decade, said that there is clear evidence that microfinance can help the very poor, but he added that “credit alone is not a panacea.” He emphasized the success of groups that combine lending with other initiatives, such as education and health care. And although the lives of individuals have improved, loans to the poor have not yet had a demonstrable effect on aggregate poverty levels. “The boldest claim for microfinance—that it can single-handedly eliminate a large share of world poverty—outpaces, by a long distance, the evidence accumulated to date,” Morduch told me.

After the announcement of Yunus’s Nobel Prize, some in the microfinance community worried that exaggerated claims about microfinance would lead eventually—when unrealistic expectations were not met—to the discrediting of the field. Outside critics have argued that microfinance is merely a palliative measure, which does nothing to bring about the large societal reforms necessary to reduce poverty—and even serves to preserve the status quo, by making the lives of the poor more tolerable. “That is a valid critique, to a point,” Morduch said. “But get real. How long are you willing to wait for the revolution? I can’t see any moral foundation for not trying to address the current deprivations of the world’s poorest billions. If microfinance can help provide options in cost-effective ways, we should celebrate it.”

The United Nations designated 2005 the International Year of Microcredit, and this was primarily intended to encourage policymakers to support favorable regulatory environments. But even the title provoked bitter fighting. Shouldn't it be the Year of Microfinance? Acción and other profit-minded groups demanded that the name be changed. So did a World Bank affiliate, the Consultative Group to Assist the Poor (CGAP), a consortium of government and private development organizations working to expand microfinance. When CGAP was created, in 1995, the "P" stood for "poorest"—something for which Yunus had lobbied hard. In 2003, "poorest" was replaced with "poor." ("Their explanation was that the poorest can't handle credit, so we should be looking only at the upper part of the poor," Yunus said. "That was absolutely against the intention of the creation of CGAP.") In the end, at the insistence of developing countries—Bangladesh in particular—"microcredit" retained its place in the name, but Secretary-General Kofi Annan used the word "microfinance" in his opening statement.

A few years ago, Pierre Omidyar left Silicon Valley and moved his family to Henderson, Nevada, just outside Las Vegas. A slight, unprepossessing figure with hints of gray in his wavy black hair, he tends to think aloud, following desultory paths, looking for theoretical solutions to problems. If anything, his approach has become more abstract over the years. As a young software engineer, he solved problems as they arose, but now he likes to reflect on the nature of the eBay phenomenon and how it supports his philosophy. He often cites Adam Smith's doctrine that unrestrained market forces and self-interest drive the most efficient—and socially beneficial—use of resources. Omidyar sees Smith's principles at work in eBay; he believes that eBay's commercial success was linked to a profound social good. "I did an early investors' road show in the fall of 1997, and I went to New York and talked to some Wall Street folks, and I said, O.K., this is strangers from all over the country, sometimes internationally, and they're doing business together over the Internet. And people were shaking their heads. 'That'll never work! It's impossible! You can't trust anybody—you're going to get ripped off!'" Now, he says, eBay has taught "more than two hundred million people that they can trust a complete stranger." Omidyar told me that he believes the trust that was inculcated on eBay has carried over to other online sites and, perhaps, to real-life interactions as well. "People have learned that, in general, people are basically good. And we've demonstrated that."

Omidyar believes that eBay had another powerful social impact. "I remember in early focus groups, when I started meeting some of our customers, there was a housewife who had sort of accidentally begun to sell things on eBay. She went to flea markets, bought things for a quarter, put them online, and sold them for twenty-five dollars, and she said, 'Wow!' She said, 'Now I finally feel like I'm contributing to the household.' So that's an incredibly empowering thing, when an individual discovers his or her own ability to generate economic value." He added, "There are three-quarters of a million people or more who make their living selling on eBay."

His frustration with the traditional philanthropic world eventually resulted in what one of his colleagues described as an "Aha!" moment. eBay would be his template for the future. In 2004, he founded Omidyar Network, which makes for-profit investments as well as philanthropic donations, and as he began to search for vehicles with eBay-like properties he decided that microfinance was an amazing fit. Both eBay and microfinance allow people to

discover that they can be entrepreneurs. Both are based on trust. Both can be viewed as demonstrations of free-market principles. Both can be seen as businesses whose profitability is linked to their social impact. Omidyar stopped talking about microfinance as a way to end world poverty, and instead described its mission in a way congruent with the eBay experience.

Indeed, when Omidyar was invited to participate, with Yunus, on a panel on poverty alleviation at the Clinton Global Initiative conference in September, 2005, he and his colleagues at Omidyar Network debated for some time about whether he should accept. Would it send the wrong message? Ultimately, he did go, but one of his first statements was “For us, it’s not just about alleviating poverty; it’s about economic self-empowerment.” Omidyar told me that in the two years or so since he became involved in microfinance he had not visited a microfinance institution or met a borrower. Just the opposite of Yunus’s entry into microfinance: Yunus left theory behind to listen to the poor, and Omidyar seems to rely largely on theory. Omidyar sees himself as an agent of global change—in this case, the commercialization of the microfinance sector. Hence his insistence that his hundred-million-dollar gift to Tufts be invested in ways that will promote that commercialization.

“Pierre takes his role in the world quite seriously,” Lawrence Bacow, the president of Tufts, told me in his office recently. He pointed to the hundred-million-dollar eBay stock-transfer certificate, framed and hanging on the wall in his office. “He changed the world once, with eBay. And he wants to change the world again.”

In 2005, Citigroup, the largest banking network in the world, launched a microfinance business division. At the time, Robert Annibale, who is now the division’s global director, said that two and a half billion people had never used a bank: “Forty per cent of the world is beyond the world we know.”

Stanley Fischer, a former World Bank official who was then the president of Citigroup International and now heads the Bank of Israel, told Citigroup senior management that the microfinance division would try to earn a reasonable rate of return. But he also said that “although there were very high rates of return being earned in this industry—we’d heard that companies were making forty and fifty per cent—a company like Citigroup could not, from a public-relations viewpoint, go out there and maximize return on capital, nor would we want to.” (Clearly, engaging in microfinance might help Citigroup with regulators, too—but not if it looked as if it were profiteering from the poor.) Fischer argued that many of these microfinance clients would develop economically and become a whole new client base for Citigroup.

Annibale insists that the challenge of reaching the “un-banked” is so vast that there is room for every approach: profitable, sustainable, and subsidized. But he is a commercial banker, and he talks not about reducing poverty but about “financial inclusion.” By this he means retail banking for the poor, which includes not only loans and savings accounts but also insurance and remittances. “Hopefully, one day, ‘microfinance’ will kind of go away, and we’ll talk about who’s providing financial services to whom,” Annibale said. “Is it people living on three dollars a day that the banks should serve, and those on two dollars a day that the nonprofit microfinance institutions should serve? I don’t really have a clear view, but I do think that what we’re really talking about is just expanding access to financial services.”

(Technology should speed that advance. In India, Citi has begun to install A.T.M.s in microfinance institutions, and clients will be able to open Citi savings accounts, with no minimum balance; the machines, which can identify clients by their fingerprints, will speak to them in any of six dialects.) For his part, Annibale said, “I want to treat somebody as a client, not like a beneficiary of a donation. Because when we have someone that we psychologically think of now as a client we say, ‘How are we going to satisfy them?’ If you’re just going to give money, it’s very different.”

In the past several years, Citigroup and its subsidiary Banamex raised seventy million dollars in the capital markets for the Acción affiliate Compartamos, the largest microfinance institution in Latin America, with more than five hundred thousand clients. This June, Compartamos became a fully regulated bank. “The only way to have massive impact is to do it profitably,” Compartamos’s co-C.E.O. Carlos Labarthe declared. “As an N.G.O., getting donations, we were not able to grow. But when you are able to go to the market, then the sky’s the limit.” Labarthe said that Compartamos now has access to two hundred million dollars in the market. In five years, he predicted, eighty to ninety per cent of all microfinance institutions will be for-profit institutions.

I interviewed Labarthe and his partner, Carlos Danel, in their offices at the Compartamos headquarters, in a tall glass building in Mexico City. The “two Carloses,” as they are known, started Compartamos in 1990, operating mainly in the poor southeastern states of Oaxaca and Chiapas. Both came from prosperous Mexican families, and graduated from conservative universities; in the early years, much of their funding came from members of Gente Nueva, a network of nonprofit organizations. Labarthe, a genial, expansive man who was wearing a white shirt, unbuttoned at the chest, and a large silver cross, told me that he attributes much of Compartamos’s success to the partners’ corporate sense of purpose. In 1993, when they had only three hundred clients, they took a close look at the Grameen Bank. “We had then the vision that this can really explode and be huge,” he said.

It was the size of Grameen—not Yunus’s philosophy—that excited them. “Muhammad Yunus always has said that credit is a human right,” Labarthe said, his voice tinged with sarcasm. “Well, I don’t believe that. Opportunity is a human right, education—but credit is for the one that has an opportunity to make something productive with that. This is in a way creating wealth, more than wiping out poverty. Not bringing up the destitute.” I asked what he thought of the Grameen Bank’s program of loans to beggars, which enables them to sell small items door to door. Yunus charges them no interest, cross-subsidizing their loans with interest paid by other borrowers. Labarthe waved a hand dismissively. “There’s no interest and no payment schedule—it’s a local grant.” Compartamos’s target population, on the other hand, is, he said, “what some call the working poor—people who are well nourished, a level of well-being that allows them to engage in economic activity. We believe that that is where microfinance is effective.”

Compartamos’s loan model is simple credit; it does not provide sessions on family planning or domestic violence or women’s empowerment. Even though the company lends predominantly to women, Labarthe emphasized that “it is not a philosophical thing; it is very practical.” He pointed to the Grameen Bank’s “Sixteen Decisions”—a collection of resolutions made by borrowers, which include planning for smaller families and forswearing the dowry system, in which daughters, particularly in very poor families, are viewed as burdens. “They clearly have a cultural agenda,” Labarthe said. At Compartamos, they lent to

women at the start not only because they knew women were more reliable borrowers but also because in many villages most of the men had emigrated to the United States, and the women were the heads of household. In the past five years, as they expanded to urban areas, they have been lending to men as well.

More than seventy per cent of Mexico's population lacks access to banks, and there were no other major providers of microfinance. Compartamos "became a virtual McDonald's of village banking," wrote Jonathan Schlefer, in a 2004 case study for the Kennedy School of Government. "A near monopoly offering one product in one market."

That lack of competition has helped enable Compartamos to charge interest rates that are breathtakingly high, even in the world of microfinance. For most loans, Labarthe explained, Compartamos borrowers pay an annual rate of a hundred and five per cent in interest and taxes. Some rates, when adjusted to reflect their real costs, are higher than a hundred and twenty per cent. (Labarthe predicts these numbers will go down.) Recently, the Mexican central bank issued regulations that forced credit providers to clearly state the actual amount that a borrower will pay in interest, commissions, and fees, and Compartamos is making a better effort to explain hidden costs to clients.

CGAP has stated that some microfinance institutions are more profitable than commercial banks, and Compartamos belongs to that category, in part because of its extraordinarily high rates. Danel and Labarthe expect to double their client base by 2008, to a million. And when Fidel Castro dies they plan to take Compartamos to Cuba. At the time I met with them, they had just returned from Washington, D.C., where they had presented their proposal to an official at the Inter-American Development Bank, which, according to one of their bankers, was "very enthusiastic." But, given U.S.-Cuba relations, the banker added, it was agreed that the United States would remain in the background of this enterprise.

"Now that we can tap into the markets, many banks, finance companies, and private investors are looking at Compartamos, and they're seeing this is good business," Labarthe said. "Before, the poor were always thought of as the problem of the private sector. But now they can be an opportunity."

Last year, when Lawrence Bacow first explained to the Tufts trustees that Omidyar had insisted that the university create a separate fund for his gift which would invest only in microfinance, some of the trustees said, "We're going to do what?" They were worried about the extreme "immaturity" of the sector—data on returns are poorly documented, information about different investment vehicles is not easily accessible, currency risk in investments is endemic, and ways of exiting the market (that is, finding a buyer when one wants to sell) are limited, at best. In the end, though, Omidyar's hundred-million-dollar proposition had proved irresistible.

The Omidyar-Tufts Microfinance Fund's goal—in line with the rest of the Tufts endowment—was a return of at least nine per cent. But there are not many places to obtain that reward in the microfinance world.

"We've discovered that a hundred million dollars might be difficult to place," Omidyar told me. The problem was with the microfinance institutions themselves, many of which weren't yet sufficiently evolved or profitable. "The rhetoric is ahead of the reality," Omidyar said. "When people are saying, 'We are commercially viable'—well, they're not really

commercially viable.” He now hopes that the fund will serve as a “carrot,” so that institutions hungry for capital will get rigorous in the hope of becoming eligible. The return, if achieved, will draw other investors into the market. Omidyar views the fund as a way of testing his theories about commercializing the sector. “It’s really the demonstration impact I’m looking for, primarily,” he said. Currently, much of the fund is sitting in short-term investments, waiting to be disbursed.

There are good reasons to wait. The stars of the commercial microfinance world—financially and operationally strong institutions like Compartamos—make up only a small percentage of all microfinance institutions. The best performers are the most popular, favored not only by investors but by donors, too. (According to CGAP, eighty per cent of all funding goes to the same twenty institutions.) Omidyar and his colleagues say that the biggest obstacle to commercialization of the sector is philanthropic capital. They say that it distorts the market—not only by filling channels that might otherwise draw commercial investors but also by keeping unsustainable programs alive. “One of the things we need and we will get is a cycle of creative destruction,” said Tryfan Evans, the director of investments at the Omidyar-Tufts fund, who previously worked at U.S.A.I.D. “If you’re inefficient, you will get overtaken by competitors.” Evans said that he is confident about achieving the fund’s goal of nine per cent—and more. (His bonus depends on that.) The fund plans to be fully invested within three years.

“I would love investors and donors to really think about this,” Omidyar said, earnestly. “There is a difference between undemanding capital”—contributed by donors, who expect nothing in return—“and demanding capital,” which requires transparency of financial reporting and an appropriate reward for risk. His goal, he says, is “to shrink the undemanding source of capital and grow the other.” That mission, however, might be complicated by the recent entry of some of his colleagues in the technology community, including Bill Gates, Michael Dell, Sergey Brin, and Larry Page. Omidyar believes that there is a role for philanthropic capital in carefully delineated areas like funding research and building infrastructure. But if these foundations commit large sums to other kinds of enterprises—as the Gates Foundation did in its grant to Pro Mujer, a microfinance organization that Omidyar told me he would not support—then his effort could become more difficult. The “cycle of creative destruction” might be slowed. Regarding his colleagues’ grants, Omidyar said, somewhat stiffly, “I would hope that businesspeople would see the value of a business-oriented approach.”

“The Omidyar fund represents a faith-based belief in the market,” Jonathan Lewis, of MicroCredit Enterprises, said. And, in all the excitement about what the market can offer, hard questions have been obscured. Individual borrower repayment rates are excellent, he added, but there are few statistics available for default rates of microfinance institutions; if an institution defaults, how will investors get their equity out without hurting the institution’s clients? “Someday, people will have to cross a Rubicon, because there will be events like foreclosures,” Lewis said. “Will the president of Tufts and Pierre Omidyar, when they are waiting for a liquidity event, say to thirty-seven thousand women, ‘Sorry, we’re closing down and you’re going to lose your loans—so go back to feeding your kids twice a day’?”

For that matter, will *any* interest rates paid by very poor women to rich investors be deemed too high? The issue of interest rates arose last March in the state of Andhra Pradesh, known

as India's capital of microfinance, where a number of women borrowers committed suicide. The link between the suicides and the lenders (one was SHARE, a Grameen Foundation partner) has not been definitively established, and the question of whether abuses occurred has become highly controversial. Microfinance has been growing at a furious rate in the past couple of years in Andhra Pradesh, with intense competition between private institutions and a state-sponsored program. The government and its supporters accused microfinance groups in the province of charging exorbitant rates and of bullying clients who were overextended and unable to repay their loans. Microfinance groups claim that the suicides were largely incidental to their activities, and that the deaths were exploited by the government to dampen private competition. The rates among the microfinance groups varied; some were about thirty per cent, but, because of the way they were structured, and because of various hidden costs, they had appeared to be much less. Today, the private microfinance institutions in Andhra Pradesh have lowered their rates—a few are as low as eleven per cent—and have adopted codes of conduct. Opposing sides in the commercialization debate drew different lessons from the episode. For Yunus's allies, it demonstrates how the emphasis on profit can blind lenders to social values; the other side worries that rates lowered for political rather than economic reasons probably aren't sustainable. What nearly everyone can agree on, though, is that it is a reminder of the dangers facing this immature and rapidly growing field.

The Omidyar-Tufts fund has invested in a Frankfurt-based banking network called ProCredit Holding, which is managed by a former German radical of the generation of 1968 named C. P. Zeitinger. His goal today, he says, is to found banks for what he calls "ordinary people." With grants from international financial institutions and from the U.S. government (totalling about fifty million dollars in the past eight years), he has built a network of nineteen banks in Eastern Europe, Latin America, and Africa; he plans to expand the network into Colombia, Honduras, Sierra Leone, Armenia, Kyrgyzstan, and Mexico (where he looks forward to competing with Compartamos). After a few years, the banks are expected to start operating on their own. Of the nineteen existing banks, Zeitinger says, eighteen are profitable. Zeitinger's forte is high-risk areas where he is freer to impose order. He pointed to the recently opened ProCredit bank in Congo. "Someone wanted to make a ten-thousand-dollar deposit, and he tried to give a fifty-dollar bribe—to make a deposit! It is part of their cultural heritage, you might say. We try to build up a different culture—Protestant ethics."

Chain-smoking, irascible, erupting every so often in short bursts of indignation, Zeitinger is impatient with questions about microfinance's serving the poor. "In a way, I don't want to belong to that world. It is a field occupied by 'visionaries' who are actually politicians. 'Credit is a human right'! Can we please remember that credit means you owe something and you can get overly indebted?"

He went on, "It is an altogether different thing than what we do. We say, These are banks for ordinary people. That means everybody who does not have access to the financial system. I want to stabilize the middle class in these countries as well. I want to be a different type of banker. But I only want to be a banker, not a microfinance banker. Yunus is against banks. He is for social revolution.

“Museum of poverty!” he muttered. “It’s ridiculous! To claim that microfinance is going to solve poverty is a myth. From ancient Greece to today, poverty has been with us and it will occupy us forever.”

Zealous as he is about his commercial approach, Zeitinger thinks that the role of philanthropic capital has been too widely denigrated. For one thing, notwithstanding his banks’ profitability, he is still trying to obtain more grant money, for expanding into new, harder-to-serve rural regions. He also said, “We don’t want to be the only M.F.I.s in the world. There need to be others. But if you look at the level behind us, there aren’t enough scale players. What’s going to make the difference there? Strategic investment of grant money, linked to investors who don’t have fixed demands on returns.”

Zeitinger believes that Omidyar’s resistance to the use of grant money in microfinance is naïve. “He will not learn unless he is engaged, seduced rationally, to change his thinking.”

One of the proposals under consideration by the Gates Foundation is Zeitinger’s request for a major grant to enable him to expand into rural Africa. Omidyar’s fund of a hundred million dollars generated great excitement initially, but it has since been somewhat overshadowed both by the expected size of the Gates Foundation’s commitment—thought to be as much as several hundred million dollars annually—and the breadth of the Gates approach. “It’s not so much a debate between a Compartamos or a Pro Mujer model,” Rajiv Shah, at Gates, said. “You need a range of different business models. Some are going to be very commercial.” Some, he noted, will be commercial eventually but not right away. And others will need some degree of continued support, in order to reach the destitute and specific communities in certain parts of the world. Shah said that Gates is giving grants and loans, and even making investments, to reach its goal of moving hundreds of millions out of poverty. “But the goal is always that—it’s not to get a return. That distinction is important, because Omidyar has taken a different approach.”

The Gates Foundation’s approach is notable for its catholicism—not only within the field of microfinance but in its over-all program, aimed at reducing inequities around the world, which includes global health, education, and agricultural production as well as financial services for the poor. The Gates staff conducted an intensive study of microfinance for about a year before Bill Gates formally made the initiative part of his foundation’s portfolio. What stirred him was a visit last December to BRAC, Bangladesh’s largest microlender and the largest national nonprofit in the world. In its offerings to its clients, BRAC provides not only financial services but also schools, legal training, and help with marketing. Its subsidiaries offer dairy products, textiles, and crafts—all produced by borrowers. BRAC makes the Grameen Bank look spare.

In early May, representatives from eight microfinance institutions around the world were invited to a three-day event at the Gates Foundation’s headquarters, in Seattle; among them were Carmen Velasco, of Pro Mujer; Maria Otero, of Acción; and Ingrid Munro, the founder and executive director of an organization called Jamii Bora, which serves the very poor in the slums of Nairobi. “We wanted to hear from people who have had a lot of firsthand experience, and we wanted to bring people from different geographies together,” Rajiv Shah said, noting that the visitors came from Latin America, Africa, and Asia. “When you do that, you realize there are very different approaches to this, and certainly there are few right

answers in terms of one approach versus another when you look broadly across a big part of the globe.” For instance, in the case of Ingrid Munro and Jamii Bora, he said, “Is Citigroup ever going to securitize her loan portfolio? Probably not. Is she going to be wildly profitable, to the point where she’s spitting off the kinds of dividends Compartamos spits off? I doubt it. But she can sustainably provide important services that are helping to move people out of poverty in the heart of a very poor community. So shouldn’t she also have the ability to innovate and reach scale?”

At one point, the group met with Melinda and Bill Gates, and with Warren Buffett, too. It was several weeks before Buffett would announce that he was giving roughly thirty-one billion dollars to the Gates Foundation; the guests assumed that he just happened to be visiting Bill and was curious about microfinance. Buffett asked incisive questions about interest and repayment rates—and dazzled several of those present with the speed with which he ran the numbers in his head.

Acción and Pro Mujer were both already Gates grantees, but Jamii Bora was a newcomer. Munro started it in 1999, and today it is the fastest-growing microfinance institution in Kenya. Munro is from Sweden and her husband from Canada, but they have lived in Kenya for the past twenty-one years. In 1988, they adopted a boy from the streets. “It was a small seven-year-old boy who more or less adopted us,” she said, chuckling. “And then we later found his two brothers and adopted them. With a situation like that, like in all great love stories, in literature and in real life, you are a helpless victim, you know?” Through her sons, she got to know other street children, and their mothers, who were beggars. She was the head of the African Housing Fund, which works with the homeless. “When I retired from the African Housing Fund, the beggars kept coming to my house and banging on the door, and they said, ‘You can’t abandon us now, Mum, you are our mother.’ So they really challenged me, and I said, ‘O.K., if you want me to do something for you, now you have to do something for yourself.’ I challenged them to save a little bit of money. ‘For every shilling you save, I promise, I will find somebody who will give two shillings, and then you can borrow twice as much as you’ve saved.’ ”

“The unique thing is, then, that it started with trust,” she said—sounding like Pierre Omidyar, her doctrinal opposite. “Also, I thought it was just a small club, a group of women I thought were very special. But, really, it grew like a bushfire! After a few months, we had to formalize it. We decided to call it Jamii Bora—*jamii bora* means ‘good families’ in Swahili. And that’s what we say—you can be very poor but you’re still a good family, and you still have the talent to get out of poverty.”

Munro started with a group of fifty beggars from the slums of Nairobi, and over the past seven years Jamii Bora has expanded to sixty-one branches, serving about a hundred and thirty thousand members; Munro aims to reach at least five hundred thousand by 2009. She says that she has stuck to the original idea, “that you can borrow twice as much as you’ve saved—which means we have a very strong foundation, because we have a lot of savings, and our members take very small risks.” Jamii Bora has received some grants, but it largely pays for itself. About a third of its borrowers are men. And nearly all of its staff members are former borrowers or their relatives.

This is important, Munro said. Some microfinance organizations in Kenya will not open an office in the worst slums. “My staff is not afraid, because they were born in the very same

slum, and the thugs and thieves were their classmates in primary school. I don't agree at all with those who say you can't reach the very desperate with microfinance. But you have to be involved—*really* involved, you know? You can't just sit there in the bank and wait for them to come in."

Munro emphasized that she continues to work with the poorest of the poor. "Very few in microfinance do that, because it costs just as much to administer a loan of twenty dollars as two hundred dollars, or two thousand—but, of course, the income from a twenty-dollar loan is very small. Our average loan is ninety-five dollars."

Munro added housing loans, health insurance, and life insurance to her services. About a year after she started Jamii Bora, she realized that when clients defaulted on their loan repayments it was usually because a family member had been hospitalized. No insurance company would offer an affordable policy to her borrowers, so Munro decided to do it herself. "We charge about twelve dollars a year for an adult member, with a maximum number of four kids. After that, it's an extra few dollars for each kid. There is no upper limit on cost, and we don't exclude people with H.I.V. and AIDS. And we're covering our costs and have never used donor money on our health insurance."

Munro's latest project is to build a town on a two-hundred-and-ninety-three-acre parcel of land near Nairobi. It will include housing, a town center with shops, a school, a hospital, and a small industrial area, and some two thousand Jamii Bora families will live and work there. About two years ago, local groups seeking to block the project obtained a ruling from an environmental-management authority to the effect that the development would have a negative impact on wildlife; that ruling has since been overturned, but now it has been appealed to the high court. "It's the classic thing that rich people don't want to have poor people around," Munro said. "But you can never finally get out of poverty if you can't get out of those slums." She hopes for a decision before the end of the year.

Although most of Jamii Bora's loans are very small, loans as large as nine or ten thousand dollars are available to exemplary long-term clients. "Among the very poorest of the poor, you have some absolutely outstanding, brilliant people, who would have been top executives anywhere if they'd had the chance to go to school," Munro says. She likes to cite a woman named Claris Adhiambo, one of Munro's original group of fifty beggars, whose husband drove her out of their home after she gave birth to her fifth child. Adhiambo saved sixteen dollars and borrowed thirty-two dollars to open a food stall, selling fish. Three years later, she became a wholesaler and opened a restaurant. She bought land and built a small rooming house and small stores. She has repaid eleven loans, and her current loan is for thirty-two hundred dollars. "If you were to see her today, she looks like a member of parliament—you can't believe she was a beggar!"

Munro said that Melinda Gates would be impressed if she came to Kenya and saw Jamii Bora in action. "Because that is the time you really understand. You know, when people visit the worst kinds of slums—even worse than anyone can imagine—and they walk around and meet people in their little businesses and little homes, almost always, their first comment is 'Why are they so happy?' They are smiling, proud, with dignity, showing what they have achieved. And I say, 'It's because they have something today which they didn't have a month ago, and they have a plan and dream of something they're going to have in a month's time that they don't have today.'" ♦