

## EXECUTIVE SUMMARY

*Would a regulatory adjustment boost the microcredit market in Colombia?*

The incredible dynamism of the microcredit sector in Colombia and its ever increasing outreach brought since few years the regulatory issue on the table. Colombian MFIs seem to be under the “rush to regulate”. Summits, conferences and work groups have been organized around this issue; however any concrete answers have been given with regards to the regulatory barriers and a potential better regulatory model. It looks as if nobody would dare to say its opinion. The recent creation of a microfinance providers union aims primarily at solving this issue but its first reports will not be available until 2010.

As a consequence, we believed interesting to provide some insights on the following research question: would a regulatory adjustment propel the Colombian microcredit market into an integration phase? Taking into account the length of this paper and the technicality of this complex question, we “only” wish to lay the foundation for an objective analysis and give some elements to answer.

We first analyzed the Colombian microcredit market, looking at its maturity stage. The market is characterized by a strong presence of very professional, experimented and mature NGOs that are increasingly ceding some market shares to commercial banks, resulting today in a 50% market shares for each institutional type. This tough competition is obviously leading to an increasing default rate within the market for both actors. The very good achievement and outreach of the microcredit market is mainly due to an internal dynamism driven by MFIs themselves, in order to make progress the industry. The growth does not lie in a supportive and enabling regulation.

Indeed, we observed that the regulatory environment of microcredit in Colombia and the government role are typical from a semi liberalized financial system. Main regulatory limitations to microcredit development are due to an inappropriate regulation and to a lack of specific regulation. Inadequate regulatory elements are: the definition of a microcredit operation, its usury limit and the policy of state intervention within the market.

These regulatory gaps coupled with market evolution are causing some market imperfections: over indebtedness, limited efficiencies of MFIs and difficulties of reaching remote and poor micro entrepreneurs at a national level.

However it should be taken into account that the political instability is another important factor that might limit the sector of evolving in the right way. From one side, it discourages MFIs to reach the poorest of the poor usually located in conflictive areas and from the other side, it discourages foreign investors.

Our conclusion underlines that there is a real mismatch between industry's achievements and desire to progress towards integration within financial system, versus, the regulatory framework and government vision imposed to local actors.

We thus believe that a regulatory reform would definitely be appropriate, but we did not have sufficient elements to be in a favor of a special regulatory window for microfinance or any type of regulation scheme. This would be a topic for further research. We think that the market is at a real turning point and it could be the appropriate moment to think about a reform.