

The Character Based Lending Approach

An innovative credit appraisal

1. AIRDIE, a micro credit provider in the south of France

AIRDIE is a state-aided provider of micro credits in Montpellier, in Languedoc-Roussillon in the south of France. By providing micro credits for the start-up of small scale enterprises, AIRDIE enables persons who are excluded from the labour market to become self-employed entrepreneurs.

The target group consists of (1) Persons who, excluded from the labour market and depending on state aid, can enable themselves to become self-employed and get a new means of existence by starting a (new) own business; (2) Groups committed to the creation of new jobs or apprenticeship, training positions for socially deprived persons, excluded from the labour market.

AIRDIE, is a solidarity-oriented institution that has no commercial intentions. Therefore, interest rates for credits are below market level and the financial resources on which AIRDIE depends are to be understood in terms of the objective of an overall social development: Social efficiency has the priority over cost efficiency, hence the work of AIRDIE and its credit technology is based on the idea of solidarity. AIRDIE cooperates with a number of partner banks, which provide the credit, once the applicant's project has been approved by AIRDIE. In cases where banks refuse the financing of a project, AIRDIE might hand out credits from its own resources.

2. Selection criteria for micro credits

AIRDIE offers up to 11 different credit and financing schemes up to a maximum amount of 23.000 EUR which are adjusted to the demand of AIRDIE's clients.

Since clients are usually persons who have no access to regular bank services, AIRDIE uses special adjusted methodologies for the assessment of the creditworthiness of a person. This allows the institutions to offer tailor-made financing schemes to their clients.

Main principles of the character based lending approach

The method of character based lending was developed in the framework of the worldwide Microfinance movement. Character based lending means that the assessment of the creditworthiness is not based on documents (amongst others balance sheets, income statements) but on the careful observation of the personality of the entrepreneur in terms of relevant expert knowledge, entrepreneurship, good knowledge of the relevant market, the ability to handle crisis and the social context of the entrepreneur. Therefore character based lending requires full confidence between the applicant and lending institution. As an innovative instrument to assess the creditworthiness of small scale entrepreneurs, character based lending has been successfully implemented in developing and transition countries worldwide during the last 20 years.

Method for granting of loans

From the first contact between the applicant and the credit institution to the granting of a loan AIRDIE uses a four step approach:

Step 1: Telephone interview

The first contact to the applicants includes a pre-selection of the candidates on the basis of a standardised questionnaire on the phone.

- Duration 15-30 minutes
- result: completed questionnaire
- 50% denials



Step 2: Personal interview with the applicant

During one or two intensive personal interviews the credit agent assesses the marketability of the business idea and the creditworthiness of the applicant. Furthermore the business idea is concretised and the financial needs of the project are clarified on the basis of the financial situation of the applicant. During the interviews the agent attempts to get an all embracing impression of the applicant to assess whether the business idea is in line with the situation and personal abilities of the applicant.

- duration: 4-16 h
- result: completed evaluation sheet
- about 25 % denials

Step 3: Decision of credit committee

If the credit agent holds the applicant to be successful with his business idea the evaluation sheet is submitted to a credit committee, containing of former entrepreneurs, employees of correspondent banks, representatives of social associations, volunteers of private sector and the chairman of AIRDIE. The decision is made collectively by the credit committee after an investigation of the evaluation sheet. By that means the final decision is submitted from the agent to the committee

- committee duration biweekly 2-5 h
- credit decision per case up to 30 minutes
- denials 50-60 %

Step 4: credit agreement

The application presented to the committee already contains a proposed financial instrument. The last step after the acceptance is hence a credit agreement with a bank or AIRDIE.

3. Criteria relevant for the decision

The decision of the credit agent is based on a tripartite confidence and guided by the overall objective of social integration and occupational rehabilitation of persons excluded from the labour market. The three levels of confidence consist of the confidence in the client, in the project and in the repayment.

Alternative Collateral - Moral guarantors

During the second step the applicant is obliged to nominate at least one "moral guarantor" out of his

personal environment, who testifies his confidence in the skills of the applicant and his business idea and could provide moral or if needed financial support.

Guiding principle: social approach

AIRDIE believes that a denial of an application at an early stage is better than advancement at any cost in order to avoid the suffering of a further set-back an additional debts for the applicant. AIRDIE seeks for "social effectiveness", believing that demand orientated and sustainable supply of microcredit is not compatible to a mere commercial orientation. The promotion of socially excluded persons requires additional subsidies due to high costs and low yields.

4. Transferability to Brandenburg

In the framework of the EU co-financed ChaBaLEU-project a proposal of action was developed for a microfinance provider located in Brandenburg. In contrast to AIRDIE, the concept for the provider is based on a commercial approach. A high number of clients and a fee, which has to be paid to the provider, should guarantee for cost efficiency in the long run. In Brandenburg, a higher interest rate and service charge - comparable with effective interest rates prevailing at the market - is intended.

Nevertheless, the character based lending method applied by AIRDIE is to be seen as a role model. The success of AIRDIE in the reintegration of deprived and long term unemployed and the transfer of successful clients to "regular" banks is worthy for imitation. The entrepreneurs, who have been promoted by AIRDIE, indeed constitute a potential market or business opportunity for banks. The volume of this market has to be further analysed as it constitutes a potential source of income for microfinance service providers: successful and creditworthy entrepreneurs could be "transferred" to banks for a premium.

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