APRACA FinPower Program

No. 3

COMPLETION REPORT:

FinPower Microfinance Development Forum – Dialogue in Lao PDR:

National Rural Finance Policy

Facilitator:
Benedicto S. Bayaua

Documentor and Expert:
Eduardo C. Jimenez

An APRACA FinPower Publication with the Special Sponsorship of
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This book is published during the incumbency of Mr. Abdurakhmat Boymuratov, APRACA Chairman, and Mr. Won-Sik Noh, APRACA Secretary General.

MESSAGE

APRACA has successfully established among its members a machinery for systematic interchange of information on sustainable rural and agricultural financial services, encouraged inter-country studies and provided training, consultancy, research and publication services on matters of common interest in the field of rural finance and microfinance.

The holding of the Microfinance Development Forum in Lao PDR in Vientiane, Lao PDR is part of APRACA's mandate of ensuring that enabling and client-friendly microfinance policy environment and regulatory framework are created in each APRACA represented-country.

The International Fund for Agricultural Development is APRACA's key strategic partner under the FinPower Program. I wish therefore to acknowledge the IFAD support to APRACA.

In particular, I wish to thank Dr. Thomas Elhaut, IFAD Asia and the Pacific Division Director, and Dr. Ganesh B. Thapa, IFAD Regional Economist, for the trust and confidence they have continuously bestowed on APRACA and for their commitment to help alleviate poverty and accelerate rural growth and development among countries in Asia and the Pacific.

I also wish to extend our deepest gratitude to the Bank of Lao PDR and to the Agricultural Promotion Bank of Lao PDR for hosting the forum-dialogue.

I hope that this completion report will likewise be APRACA's modest contribution to the growing wealth of knowledge in the field of rural finance and microfinance.

Abdurakhmat Boymuratov
APRACA Chairman

Acronyms and Abbreviations

AMCFP	Agro-Industry Modernizattion Credit and Financing Program
APRACA	Asia-Pacific Rural and Agricultural Credit Association
ACPC	Agricultural Credit and Policy Council
BDS	Business Development Service
BOL	Bank of Lao PDR
BSP	Bangko Sentral ng Pilipinas (Central Bank)
CBOs	Community-Based Organizations
CDA	Cooperative Development Authority
CIC	Credit Information Corporation (Philippines)
CISA	Credit Information System Act
DBP	Development Bank of the Philippines
DCPs	Directed Credit Programs
EIU	Economist Intelligence Unit
IGA	Income Generating Activity
KTB	Krung Thai Bank, Thailand
LBP	Land Bank of the Philippines
MCPI	Microfinance Council of the Philippines, Inc
MFI	Microfinance Institution
NCC	National Credit Council
NGO	Non-Governmental Organization
OFWs	Overseas Filipino Workers
PCFC	People's Credit and Finance Corporation
PFIs	Private Financial Institutions
RBAP	Rural Bankers' Association of the Philippines
SEC	Securities and Exchange Commission
SME	Small and Medium Enterprise

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Foreword and Acknowledgments

The goal of the International Fund for Agricultural Development (IFAD) is to reduce rural poverty through sustainable improvements in household food security and incomes. In order to contribute to this goal, one of IFAD's strategic objectives is to provide improved financial and related non-financial services in rural areas. In fact, two-thirds of the Fund's current projects have a rural finance component and approximately one-fifth of the Fund's resources are dedicated to rural finance. Hence, IFAD aims at providing sustainable access of the rural poor to financial services, to be enhanced by institutional diversity and a supportive rural financial infrastructure. IFAD's rural finance policies focus on four focus areas:

- Building sustainable rural finance institutions with outreach to the rural poor;
- Fostering stakeholder participation, including the poor, in the development of rural finance;
- Building a diversified rural financial infrastructure; and
- Promoting a conducive policy and regulatory environment.

Since 1977, APRACA has aspired to work for rural growth and development, with priority emphasis on the uplift of rural poor. It has pursued the promotion of efficient and effective rural financial systems and broadened access to rural financial services. It established among its members, a machinery for systematic interchange of information on sustainable rural and agricultural financial services, encouraged inter-country studies, provided forums to discuss matters of common interest in the field of rural finance, and provided training, consultancy, research and publications services.

APRACA, with its wide network of member rural financial institutions and central banks, is a viable and strong partner for IFAD to engage with senior policy makers and central banks on key policy issues. IFAD had collaborated with APRACA between 1996 and 2001 under the APRACA MicroServ program, implemented with IFAD's funding support, wherein replicable rural finance models were disseminated to member institutions and to a wider audience. The program showed that the replicability of innovative models was further enhanced when conducted through an organization with an existing, wide geographic network such as APRACA, thereby yielding more cost-effective results, broader geographic reach, and assured project continuity.

In 2007, the International Fund for Agricultural Development (IFAD) provided APRACA with a five-year Technical Assistance Grant to implement the Regional Program of Accelerating the Financial Empowerment of Poor Rural Communities in Asia and the Pacific through Rural Finance Innovations, dubbed as the APRACA FinPower Program.

The goal of the five-year FinPower program is to promote the financial empowerment of the rural poor in Asia-Pacific countries through policy dialogue, innovative pilot programme, and knowledge-sharing among actors in the rural finance sector. The activities undertaken by the programmes are expected to further consolidate rural finance knowledge and replicate successful approaches among beneficiaries in the Asia-Pacific region.

The three program objectives, which correspond to the three central components of the FinPower Program, are:

Component 1: Participatory Dialogue and Policy Forums: Foster an enabling, pro-poor and client-friendly policy environment and regulatory framework for sustainable rural financial systems;

Component 2: Pilot Programmes, Exposure Visits and Documentation: Encourage innovative approaches to rural finance through the adoption of reforms and improvement of rural finance mechanisms that empower the rural poor; and

Component 3: Training, Regional Study and Sharing of Innovative Practices: Extract lessons from the wealth of rural finance innovations promoted by IFAD-supported projects and APRACA initiatives to promote information sharing and replicate successful approaches in the region.

In line with the sharing of rural experiences in creating conducive rural and microfinance policy environment and regulatory framework, APRACA FinPower conducted the Microfinance Development Forum in Vientiane, Lao PDR on February 2, 2010.

The forum was intended to share the experiences of the Bangko Sentral ng Pilipinas in the creation of conducive and client-friendly rural and microfinance policy environment and regulatory framework, to highlight the status of Lao PDR's development in this regard and to assist the key Lao PDR stakeholders in their formulation of a plan of action towards the development of strong rural financial markets, including sound policies and regulatory framework. A total of 36 participants from Lao PDR joined the forum.

This completion report consists of an introduction to the Lao PDR Rural Financial Landscape, Sharing on the Microfinance Environment and Regulatory Framework of Lao PDR by Ms. Keasorn Manivong, Chief of Microfinance Institution Division, Bank of Lao PDR, Sharing on the Experiences of Krung Thai Bank by Ms. Nisanard Yothasmut, Krung Thai Bank Vice President, Sharing on the Philippine Microfinance Policy Environment and Regulatory Framework by Mr. Eduardo C. Jimenez, Consultant of the Bangko Sentral ng Pilipinas, and a Summary of Findings and Recommendations. The full text of Mr. Jimenez' paper is attached as an annex to the report.

APRACA FinPower wishes to thank Ms. Keasorn Manivong, Chief of Microfinance Institution Division, Bank of Lao PDR, for sharing the experiences of Lao PDR, Mr. Eduardo C. Jimenez, microfinance consultant of the Bangko Sentral ng Pilipinas, who shared the central bank's experiences in formulating and implementing rural and microfinance policies and regulations and Ms. Nisanard Yothasmut, Krung Thai Bank Vice President, who presented her institution's experiences in formulating savings mobilization policies and implementing schemes.

Readers' comments are invited.

Won-Sik Noh
APRACA Secretary General

1. Lao PDR Rural Financial Landscape

1.1 Introduction

The People's Democratic Republic of Laos (Lao PDR) is located in the Indochina Peninsula. The tropical country has an approximate total land area of 236,800 square kilometres, of which about 75 percent are mountainous. The remaining area covers three (3) major plateaus, considered as the granaries of the country.

Based on the official report of the National Statistics Centre of Lao PDR[1] , the population of Lao PDR reached 5.62 million in March 2005, of which 2.82 million were females and 2.80 million were males. The population has grown by 1,047,000 persons or by 2.1 percent per year with the last census taken in March 1995 as the basis. In the latest report of World Food Program (WFP)[2] , the estimated Lao PDR population is reported at 6.9 million with two thirds of the population residing in rural areas which still remain underdeveloped.

With an estimated per capita income of USD460 in 2005, the country is one of the poorest countries in East Asia and it is classified by the UN as a Least Developed Country (LDC).[3] According to the World Bank, 71 percent of Lao PDR's population in 2004 lived on less than US$2.00 a day and another 23 percent lived on less than US$1.00 a day. Per World Bank's report, although the social indicators have been improving in the last decade, Lao PDR remains one of the worst in the region and the quality of life remains low.

Following the reforms initiated in 1986, Lao PDR started to move away from a centrally-controlled economy towards a market-oriented economy. The shift has resulted in steady and significant growth in the last decades.

1.2 Overview of the Financial System

As in other countries, the Lao PDR's financial system is composed of formal, semi-formal and informal sectors. The formal sector, still under-developed, is composed primarily of three state banks, three joint-venture banks and eight foreign banks. It was estimated that the three state banks account for about 70 percent of the total outreach of the country. The three banks, Agricultural Promotion Bank (APB), the Banque pour le Commerce du Lao (BCEL) and the Laos Development Bank are also undergoing reforms within their respective organizations to cut down the incidence of non-performing loans in their respective portfolios.

Except for the Agricultural Promotion Bank, the main State bank focused in assisting the rural poor, the operations and outreach of practically all banks are concentrated in the capital region of Vientiane. APB has an extensive network of branches in all three regions and provinces in the country. It has an extensive exposure in agricultural credit, including microfinance loans to the rural populace.

The private banks as well as the foreign-owned banks share a small market partly because of the existing barriers to entry and expansion within the regulated market.

[1] http://www.nsc.gov.la/Products/Populationcensus2005/PopulationCensus2005_chapter1.htm
[2] http://www.wfp.org/countries/laos
[3] Lao PDR Economic Monitor, The World Bank Office, Vientiane, November 2006.

The semi-formal market is characterized by the presence of credit unions and cooperatives, international NGOs and locally registered organizations. Various Government agencies are also implementing development projects with the support of bilateral and multilateral donors and they are also part of this sector. They work closely with the Lao Women's Union as their conduits. A number of cooperatives also exist and the Bank of Lao PDR has also issued guidelines to support their work.

The informal sector, on the other hand, is mostly composed of private unregistered lenders and the thousand of autonomous savings and credit associations (SCAs). The Lao Women's Union has a strong partnership with most of these autonomous SCAs. As reported by Badiola[4] the other main forms of informal finance are banks that provide credit in-kind (e.g. rice and buffalo), RoSCAS (or Houay), loans from friends and family and credit from suppliers.

Lao PDR is still in its embryonic phase of development when it comes to rural finance and microfinance unlike some of its neighbouring countries. In a study[5] done by the Banking with the Poor Network of the Foundation for Development Cooperation, it is estimated that 75 percent of the population do not have access to formal or semi-formal financial services. The potential microfinance market is 268,000 borrowers and 560,000 depositors. The same report shows that only 25 percent of this market are currently served by microfinance providers (APB and moneylenders being the main financiers).

The Bank of Lao PDR, the nation's Central Bank, and the APB are steadily shepherding the growth of sustainable rural finance and microfinance in the country. The BOL had issued several circulars and pronouncement aimed, among others, at clarifying the terms and definitions and which institutions are allowed to provide microfinance in Lao PDR. A set of standards and a uniform set of Chart of Accounts were also issued by the BOL and to be used by cooperatives and banks.

[4] Creating a Conducive Rural Finance and Microfinance Policy Environment in Lao PDR by Jocelyn Alma R. Badiola
[5] http://www.bwtp.org/arcm/laos/I_Country_Profile/laos_country_profile.htm

2. The Lao PDR Microfinance Environment and Regulatory Framework

2.1 The Beginnings of Microfinance in the Country

In her paper, Ms. Keasorn Manivong, Chief of Microfinance Institution Division, Bank of Lao PDR, reported that the need to have a very clear legal and regulatory environment of microfinance in Lao PDR can be traced back to projects that started in 1997 when the UNDP/UNCDF started rural and microfinance projects in three provinces. The Asian Development Bank (ADB) on the other hand, started its Technical Assistance programs to Lao in 2004 through its TA 3413 (First Initiative Project) when it piloted the Savings and Credit Model in three provinces. Subsequently, ADB TA 4827 was implemented focusing on providing technical support to the Bank of Lao PDR. Another technical assistance was made through ADB/JFPR 9095 focused on providing support to microfinance institutions and other savings and credit unions.

2.2 Factors Affecting the Growth of Rural Microfinance

The Bank of Lao PDR, in crafting the country's microfinance regulatory framework, has taken note of the following four essential factors affecting the growth of rural microfinance:

- **Expansion**

  The best macroenvironment policy support is needed. The providers of microfinance services should aim for "best" practices in running their operations. The macroeconomic fundamentals should be closely monitored, which means inflation should be kept at suitable levels, Gross Domestic Product (GDP) should be increasing and a stable political environment as well as social security should be sustained. The Government believes that promotion of microfinance should be enhanced. Studies reveal that the existing number of MFIs in Lao PDR are not significantly reaching out the poor; hence, there is a need to experiment on appropriate methods as well as encourage the growth of microfinance providers like those of the credit unions or cooperatives, microfinance NGOs and private institutions to provide the needed financial services of the poor.

- **Diversity**

  The commitment to diversity emanates from the establishment of good and working regulatory environment for microfinance as well as clearly laid out policies and action plans adapted to the Lao PDR context.

  A close coordination among policy makers, bilateral and multilateral organizations should be in place. Coordination between and among local and provincial authorities with the microfinance practitioners should likewise be enhanced. Due to the limited resources of the public institutions in the country, the initiatives of the private sector, with some degree of independence in their operations, should be supported.

- **Sustainability**

  To ensure sustainability of microfinance operations, microfinance providers should be supported to provide the best services to their clients. Simple loan processes and loan approval as well as transparency in providing services should be integrated in the operations of the providers of microfinance services.

MFIs should be managed professionally with full time staff. The MFI Board of Directors and its management should strictly follow the “best” and sound governance practices, procedures and philosophies.

Microfinance providers should set interest rates that are able to cover all expenses related to the running of the microfinance operations. The MFIs should also promote the habit of savings and not just the provision of loans.

- **Security**

  Microfinance institutions should comply with existing and approved microfinance laws and regulations. The MFIs should follow “best” practices in implementing financial ratios like Portfolio-at-risk (PAR), operational self-sufficiency (OSS), financial self-sufficiency (FSS), and loan loss reserves. As MFIs take capital build up and/or savings from their member-clients, prudential standards to ensure safety and security of deposits should be followed by MFIs.

  The MFIs should allow both on-site and off-site inspections of their operations as well as be committed to have their books audited by reputable external auditors as well as by the proper Government regulatory agency.

  Institutionalization of capacity and technical building of staff members of microfinance institutions should be taken into consideration.

2.3 Types of Microfinance Institutions

In the Lao PDR context, the microfinance model consists of three institutions, i.e., deposit-taking microfinance institutions, savings and credit unions and non-deposit taking microfinance institutions. The requirements for the establishment of these institutions are as follows:

Type of MFI	Capitalization	Structure	Membership
Deposit-taking	Minimum 1 billion Kip	Microfinance By-laws with organizational structure Board, Managing Director and full time staff	
Saving and Credit Unions (SCU)	Minimum 100 million Kip	SCU By-laws and organizational structure Board, Managing Director and full time staff	At least 100 people
Non-Deposit Taking	No limitation of capital	By-laws and Board structure	At least 10 people

The general category of microfinance in Lao can be considered as formal, semi-formal and informal microfinance. Formal institutions need to take formal license and registration from the Bank of Lao PDR while the semi-formal institutions offering microfinance programs are those established by the Lao Government. Some of these semi-formal institutions/programs are the Lao Women Union, Lao Youth and Village Development Fund.

The informal providers are the unregistered individuals providing loans and they are generally categorized as money lenders or the black market.

2.4 MF Regulations Issued

As of reporting period, three regulations have been issued covering the regulated microfinance institution while one order was issued covering the savings and credit unions. A uniform and standard chart of accounts was also issued to be used by microfinance institutions.

The BOL also issued two guidelines covering the conduct of on-site inspection and off-site analysis.

The Bank of Lao PDR uses the CAMEL, which stands for **C**apital adequacy, **A**ssets, **M**anagement, **E**quity and **L**iquidity, as its framework in conducting on-site as well as off-site analysis of the operations of microfinance institutions.

3. Sharing on the Experiences of Krung Thai Bank

Ms. Nisanard Yothasmut, Senior Vice-President and Manager of Krung Thai Bank PLC (KTB), the second largest commercial bank in Thailand, presented the savings mobilization scheme of her institution. While KTB core business activity focuses on bigger commercial loans, the bank also undertakes microfinancing. KTB generates fund from commercial and other institutional sources, which are in turn loaned out to commercial borrowers in the urban setting. In the course of the KTB doing business in the rural community, the Bank assists the entrepreneurial poor with loans, which were treated as commercial loans. Savings generated from rural and community-based savers are used to provide loans to rural borrowers, thus the move to promote savings products focused on the rural and community-based clients.

The microfinance model of KTB provides an avenue for community-based organizations that are "collecting" savings from the rural poor to properly link up those savings being collected with a formal regulated institution like KTB. As savings from the rural poor are channelled to KTB, the Bank in turn make those funds available to the entrepreneurial members of the communities for productive activities. The KTB believes that the poorest of the poor in Thailand should be given support under a distinct and separate poverty alleviation programs; however, the economically active poor should be provided commercial microfinance loans.

There was synergy with the "Sufficiency Economy" theory being espoused by His Royal Highness, the King of Thailand. The said theory looks into three stages of sufficiency in Thailand: The first stage is more focused at assisting the very poor and those lacking skills. Thailand takes a lead role in addressing the needs of those poor people at this stage. The second stage of Sufficiency Economy looks into strengthening the skills and businesses of the entrepreneurial poor. This is where the KTB and their partner community financial organizations (NGOs, cooperatives, other community-based organizations or associations) cooperate.

There are three business models and approaches that KTB employs as it provides microfinance services. In Model 1, the Bank provides wholesale funds to partner community organizations that in turn provide the needed retail funds of their respective members. KTB also provides training on relevant business and technical skills, both by the partner organizations and their members. KTB also assists the partner community organizations to develop and provide savings products and services to their members; hence, savings generated are then plowed back to the KTB. In the aftermath of the destructive tsunami that hit Thailand back in December 2008, KTB partnered with Ban Nam Khem Community Bank by providing the needed capital to help restore the businesses of the clients of the community bank. KTB provided wholesale funds to the community bank as well as other psycho-social interventions to the affected members of the community bank.

KTB's Model 2 mandates KTB to provide loans to groups of entrepreneurs. These entrepreneurs' groups may or may not be legally registered but they have functioning sets of officers. KTB deals only with the sets of officers of the groups who in turn monitor the use of the funds. KTB also provides other technical assistance like marketing, management and product development as well as linking the produce of the concerned groups to the greater market.

KTB's Model 3 is the provision of direct loan requirements of individual borrowers. The branches of the KTB are used to release the loans as well as to receive payments and savings of the clients. The KTB also makes available to the individual borrowers the necessary skills needed, if requested.

Krung Thai Bank, in partnership with major institutions with large network or outlets, allows the retails units of said institutions to do cash deposits, withdrawals, payments and mobile top-up for cell phones. These units are called Convenience Counters. A total of 86,579 units composed of credit unions, village funds, Thai Posts and credit card companies partner with KTB for the delivery of financial services needed by the Bank's clients.

4. Sharing on the Microfinance Policy Environment and Regulatory Framework of the Philippines

4.1 Socio-Economic Profile

The Philippines, is an archipelagic nation of about 7,100 islands, with three (3) major island concentrations, i.e, Luzon, Visayas and Mindanao. In its 2007 census, the Philippines reported a total population of 88.7 million. The Philippines is politically and administratively divided into 16 regions with Metro Manila as the center of business and commerce as well as political activities. Metro Manila reports a current population of about 11 million.

Even with the adverse economic, environmental and political events that affected most of the countries of the world in the last eight years or so, the Philippines continued to exhibit resiliency and sustained growth. As of the second quarter of 2009, the Philippines, posted a very modest growth as GDP grew by 1.5 percent compared to the 4.2 percent posted during the same period of the previous year. This growth was brought about by the push from government spending as well as from the construction, mining and quarrying sectors, while the manufacturing sector posted negative growth in the last two quarters of 2009. The Government's economic resiliency plan boosted Government consumption to grow by 9.1 percent from its zero growth in 2008. Meanwhile, the agriculture, fishery and forestry sector also recorded minimal growth of 1.0 percent, mainly brought about by fishery, banana, poultry, livestock and palay[6] . The reported growth in the 2nd quarter, effectively avoided the recession that had threatened the Philippines when GDP declined in the previous reporting quarters.

The continuous US dollar inflows sent by the Overseas Filipino Workers (OFWs), estimated to reach at over USD16.0 billion by yearend, also helped stabilize the Philippine economy. The inflows stemmed the negative impact as total exports dived to negative 16.7 percent, the lowest since the 4th quarter of 1998.

Secretary General Romulo A. Virola of the National Statistical and Coordination Board (NSCB) in the same report, pointed out that as population reached an estimated 92.0 million as of June 2009, per capita GDP declined by 0.5 percent from 2.1 percent in the previous year while per capita GNP decelerated to 2.4 percent from 3.2 percent. He also reported that at current prices, the per capita GNP now stands at PhP44,828.00 or US$937.00 for the first semester.

On the immediate short-term, the big challenge for the Philippine economic managers for the remaining months of the year is to see to it that growth would continue, however modest, and not fall into recession. The Philippines in the last few years have made inroads in battling poverty through pro-poor and middle class programs, including access to financial resources, which are generally hard to access by the poor from the regulated financial sector.

About half of the population of the Philippines live in rural areas where poverty is most severe and widespread. Dependence on agriculture, mostly subsistence farming and fishing are generally the only source of income for the poor rural people. The root causes of poverty in the rural areas differ from island to island but generally, the causes of rural poverty can be traced to the decline in the productivity of farm activities, unsustainable practices that led to environmental degradation as well as absence of economies of scale due to smaller farm sizes.

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[6] Government Stimulus Resuscitates Economy to 1.5 percent GDP Growth: Second Quarter 2009 Report by NSCB

As we look into poverty in the Philippines, the NSCB official poverty statistics for 2000, 2003 and 2006 show that ironically, farmers and fishermen, the producers of our basic food commodities, rice and fish, are two of the poorest sectors because of insufficient income. Indeed, responding to the needs of our fishermen and farmers should be a major issue that must be addressed by any poverty reduction program. We need to increase the production/supply of rice and fish to ensure affordable prices but at the same time, we need to increase the income of our farmers and fishermen.[7]

The unabated population growth continues to exert pressure not only for the policy makers and government in general, but practically on the whole country as limited resources are strained to the maximum. As can be gleaned in Table 1, the average annual population increase stood at 2.04 percent, which is much lower compared to the last 6 censuses made; a lower growth rate is very much desired. On the average, the population growth in the last 4 decades is 2.52 percent.

Table 1. Population of the Philippines, Census Years 1903 to 2007

Year	Population	Ave. Annual rate of increase (%)	Source of data
1903	7,635,426		Census
1918	10,314,310	2.03	Census
1939	16,000,303	2.11	Census
1948	19,234,182	2.07	Census
1960	27,087,685	2.89	Census
1970	36,684,486	3.08	Census
1975	42,070,660	2.78	Census
1980	48,098,460	2.71	Census
1990	60,703,206	2.35	Census
1995	68,616,536	2.32	Census
2000	76,504,077	2.36	Census
2007	88,574,614	2.04	Census

4.2 Rural Finance and Microfinance Policy Development

The Philippine financial system is made up of formal, semi-formal and informal financial institutions and providers. The formal financial system, which is dominated by banks and non-banks institutions with quasi-banking activities, is supervised, monitored and regulated by the Bangko Sentral ng Pilipinas (BSP) otherwise known as the Central Bank of the Philippines. Insurance companies, on the other hand, which are part of the formal regulated financial system, are under the ambit of the Insurance Commission.

Table 2 shows that as of 30 June 2009, the Philippine banking system is composed of 804 institutions, composed of universal and commercial banks, thrift banks, rural and cooperative banks. The 38 universal and commercial banks is the largest single group in terms of assets and other resources. These banks offer the widest choices of banking services in the banking sector. Aside from the regular commercial services that they can offer, these banks are also allowed to engage in underwriting and related investment functions. They can also invest in equities of non-allied undertakings.

The thrift banking sector is made up of 74 savings and mortgage banks, private development banks, and stock savings and loan associations. This sector is focused on providing varied developmental type of lending, especially to small and medium enterprises (SMEs). These banks generally provide short-term working capital and medium- and long-term financing to economic activities engaged in agriculture, services, industry and housing, and other allied and financial interests.

[7] Statistically Speaking: www.nscb.gov.ph/headlines/StatsSpeak/2009/091409_rav_bbb_food.asp

Table 2. Financial Institutions Under BSP Supervision/Regulation

TYPE OF FINANCIAL INSTITUTIONS (FIs)	End-March 2009			End-September 2009		
	TOTAL	HEAD OFFICE	OTHER OFFICES	TOTAL	HEAD OFFICE	OTHER OFFICES
BSP SUPERVISED/REGULATED FIs	*22,654*	*7,259*	*15,395*	*22,884*	*7,245*	*15,639*
I. BANKS	*7,876*	*811*	*7,065*	*7,914*	*797*	*7,117*
A. Universal and Commercial Banks	*4,422*	*38*	*4,384*	*4,444*	*38*	*4,406*
Universal Banks	3,928	18	3,910	3,940	18	3,922
Private Domestic Banks	3,497	11	3,486	3,510	11	3,499
Government Banks	415	3	412	414	3	411
Branches of Foreign Banks	16	4	12	16	4	12
Commercial Banks	*494*	*20*	*474*	*504*	*20*	*84*
Private Domestic Banks	410	7	403	420	7	413
Subsidiaries of Foreign Banks	69	3	66	69	3	66
Branches of Foreign Banks	15	10	5	15	10	5
B. Thrift Banks[1]	*1,297*	*76*	*1,221*	*1,298*	*73*	*1,225*
C. Rural and Cooperative Banks	*2,157*	*697*	*1,460*	*2,172*	*686*	*1,486*
Rural Banks[1]	2,025	653	1,372	2,030	642	1,388
Cooperative Banks	132	44	88	142	44	98
II. NON-BANK FINANCIAL INSTITUTIONS	*14,771*	*6,441*	*8,330*	*14,965*	*6,443*	*8,522*
A. With Quasi-Banking Functions	36	13	23	37	14	23
B. Without Quasi-Banking Functions	*14,735*	*6,428*	*8,307*	*14,928*	*6,429*	*8,499*
NSSLAs[2]	151	76	75	149	74	75
Pawnshops	14,500	6,285	8,215	14,703	6,294	8,409
Others	84	67	17	76	61	15
III. OFFSHORE BANKING UNITS	7	7		5	5	0

Source: Supervisory Data Center, Supervision and Examination Sector

[1] Including Microfinance-Oriented Banks

[2] Refers to non-stock savings and loan associations

The rural and cooperative banks, on the other hand, totalling 692 are the more popular and closest to the rural communities. These banks are primarily established to promote and expand the rural economy, which are normally run by the local entrepreneurs. Rural banks as well as cooperative banks help farmers by providing the needed financial services so that production, marketing, distribution of agricultural produce can be done efficiently. Generally, rural banks are organized by private individuals and families while cooperative banks are set up and managed primarily by cooperatives or federations of cooperatives.

A total of 7,898 units composed of head offices, branches and other banking offices support the banking requirements of the Filipinos. Most of these units however are located in highly urbanized and developed centers, thus the big need to address the requirements of those in the rural and other areas outside of the urban centers.

The Bangko Sentral ng Pilipinas also regulates and monitors 6,451 non-bank financial institutions. The total number of non-bank financial institutions with quasi-banking functions is very small, totalling only 14 institutions plus 6 offshore banking units. The big bulk of the non-bank financial institutions (without quasi-banking authority) sector, is mostly composed of pawnshops numbering about 6,296. Pawnshops typically provide credit accommodations to the general public on a collateralized basis and with a higher interest rates compared to the regulated banks.

Aside from the rural and thrift banks that have strong physical presence in the rural areas, non-governmental organizations (NGOs), cooperatives, lending investors, private moneylenders, traders/millers and other government line agencies also provide financial services to the general public which include farmers, fishermen and other agrarian based workers.

In an interview with Mr. Edgardo Garcia, Executive Director of Microfinance Council of the Philippines, Inc (MCPI), as to the current update of microfinance providers in the informal sector, he stated that around 500 non-governmental organizations (NGOs), out of the more than 30,000 registered with the Securities and Exchange Commission (SEC) are involved in some form of providing microfinance services. He also said that around 300 cooperatives, from the over 66,000 registered with the Cooperative Development Authority (CDA) are doing some form of microfinance operations but only about 100 are doing serious microfinance operations with acceptable operational self-sufficiency ratios.

4.3 The Philippine National Strategy for Microfinance

One of the government's strategies in poverty alleviation is to provide households engaged in micro-enterprise and income generating activities access to production and consumption smoothing credit. A number of directed credit and guarantee programs, especially focused on agriculture, were started in the 1970s up to middle of 1980s. These credit and guarantee programs were either funded by the national government through budgetary allocation or foreign borrowings and implemented by national line agencies and through the rediscounting windows of the then Central Bank of the Philippines. Most of these credit and guarantee programs were provided at highly concessional rates to the end users. These programs, with all good intentions to help the poor, through the provision of credit and related services, did not fare well, that is, outreach were low, financial sustainability was poor and the fiscal cost to the government was enormous. Furthermore, its replicability could not be sustained and the desired positive impact to the intended users of funds was low. Several studies and evaluations made pointed out these negative findings.

Presently, the approved National Strategy is envisioned to (1) have a viable and sustainable private microfinancial market and (2) provide poor households and micro-entrepreneurs greater access to microfinancial services.

The National Strategy has the following four core principles:

- Greater role of private microfinance institutions (MFIs) in the provision of financial services;
- Provision of an enabling policy environment that will facilitate the increased participation of the private sector in microfinance;
- Adoption of market-oriented financial and credit policies, e.g., market oriented interest rates on loans and deposits; and
- Non-participation of government line agencies in the direct implementation of credit and guarantee programs.

Upon approval of the national strategy, several laws and issuances were subsequently enacted to support the operationalization of the strategy. These laws and issuances, with their features were:

- Social Reform and Poverty Alleviation Act or RA 8425
  - Rationalization of Government-directed credit and guarantee programs
  - Emphasis on savings mobilization
  - Capacity-building assistance to MFIs but excluding any and all forms of capital seed funding, equity infusion and partnership funds from Government to MFIs

- Agriculture and Fisheries Modernization Act or RA 8435
  - Consolidation of Government-directed programs in the agriculture sector in the AMCFP
  - Adoption of market-based credit and financial policies
  - Government financial institutions as wholesalers
  - Private sector MFIs as conduits and retailers
- General Banking Act of 8791
  - Recognition of the peculiar characteristics of microfinance (e.g., non-collateralized loans, short-term, frequency of payments, etc.)
  - Use of household's cash flow as a basis in the design of microfinance product
- Executive Order No. 138
  - Transfer of directed-credit programs of Government line agencies to Government financial institutions
  - Discontinuance of interest rate subsidies
  - Government financial institutions to act as wholesaler of funds to avoid competition with MFIs
  - Use of sustainable community-based private MFIs in the actual delivery of microfinance services
- Barangay (Village) Micro Business Enterprises Act or RA 9178
  - Government financial institutions to set up wholesale credit windows for accredited MFIs
  - Private sector MFIs will be tapped to provide credit support to micro-enterprises
  - Small Business Guarantee Corporation (SBGC) and Quedan Corporation to provide the necessary credit guarantee cover to barangay micro businesses
  - Loans under the BMBE window shall be computed at twice the amount of its face value in complying with the Agri-Agra Law and the Magna Carta for Small and Medium Enterprises

4.4 The Regulatory Framework for MFIs

The need for a very clear regulatory framework for the practice of microfinance in the Philippines came out as a response to clarifying the roles, responsibilities and accountabilities of institutions providing various microfinance services in light of the increasing commercialization of microfinance in the country. The regulatory framework is also in answer to the increasing competition among the microfinance players as well as to uphold certain performance standards in governance and operations. As in other countries, microfinance services are given by the following three major providers of retail microfinance services: cooperatives, banks and NGOs.

The regulatory framework encompasses all types of microfinance institutions, whether bank or non-bank. The emphasis of the framework is on: portfolio quality, outreach, efficient and sustainable operations and transparent information.

Insofar as the regulatory structure is concerned, the framework affirms that the CDA is the regulatory authority of the credit cooperatives while the BSP will continue to regulate and supervise banks doing microfinance operations. The NGOs on the other hand, which are not regulated, will have the MCPI as their repository of information.

A uniform set of standards that cuts across all types of MFIs, applicable to the peculiarities of each institution was crafted and approved. The performance standard is known by its acronym PESO: Portfolio Quality, Efficiency, Sustainability and Outreach. The regulatory framework has also incorporated the principle of "compensating balance" for those NGOs that are not allowed to mobilize savings but would take capital build-up from their clients. The compensating balance basically means that at any point of time during the partnership between the NGO and its clients, the NGO would always be a net lender to the clients; hence, the risk is much bigger as compared to the clients of the NGO.

4.5 The Key Rural Finance and Microfinance Players

The growth of rural and microfinance financing in the Philippines can be traced, to a large extent, to the approval, acceptance and functioning of a very clear national strategy as well as the setting up enabling laws and regulations, before and after the national strategy was approved. The national strategy as well as the regulatory framework, especially for microfinance will be discussed later in this paper. The three major players are the policy makers and regulators, wholesalers and retailers.

- **Policy Makers and Regulators:**

  National Credit Council (NCC)/Department of Finance (DOF) – The National Credit Council was created by an Administrative Order No. 86 signed by then President Fidel V. Ramos on October 8, 1993. It is tasked mainly to rationalize and optimize government credit and guarantee programs. It aims at institutionalize consultations and policy dialogues so that a higher level of private sector participation in the delivery of credit in the countryside. The Secretary of the Department of Finance concurrently chair the Council with the Land Bank of the Philippines as co-Chairman. It is composed of government regulators, government financial institutions and other government line agencies as well as representatives from the private sector. Under the leadership of the NCC, several policy dialogues and consultations were made that resulted in the crafting of the National Strategy for Microfinance. The NCC was also instrumental, together with Agricultural Credit Policy Council (ACPC) in crafting and supporting changes in laws, regulations and policy framework that supported growth of credit in the rural areas.

  Agricultural Credit and Policy Council (ACPC) – The ACPC is an attached agency of the Department of Agriculture (DOA). It is the agency tasked to oversee the country's rural financial system, by adopting a holistic approach towards an efficient, effective and sustainable delivery of rural financial services in the countryside[8] Executive Order No. 113, signed by President Aquino in 1986, mandated ACPC to provide policy directions on agricultural credit towards a healthy and sustainable rural financial system. The ACPC, in support of its mandate, assists in credit facilitation so that credit can flow to the countryside. The ACPC is also the lead agency that developed a system whereby Government credit resources were used when all directed credit programs were terminated and subsequently replaced by virtue of the Agro-Fishery Modernization Credit and Financing Program (AFMCFP) under the AFMA Law of 1997.

  Bangko Sentral ng Pilipinas (BSP) – The Bangko Sentral ng Pilipinas or Central Bank of the Philippines is the regulator, supervisor and examiner of all banks in the Philippines. The BSP also regulates a number of non-bank institutions, either with quasi-banking functions or not. The BSP employs a three-pronged approach to microfinance in the banking sector, i.e., (a) development of a "microfinance-friendly" policy and regulatory environment, (b) capacity building through microfinance training within the BSP and the banking sector and (c) promotion and advocacy.

  Cooperative Development Authority (CDA) – The CDA is the Government agency tasked to register, monitor, develop and supervise all cooperatives in the Philippines. The Congress of

[8] Creating a Conducive Rural Finance Policy Environment and Regulatory Framework in the Philippines: A Paper by Jocelyn Alma R. Badiola

the Philippines recently amended the Cooperative Code of the Philippines, thus, empowering the CDA to do more supervision and regulatory functions over the cooperatives.

Securities and Exchange Commission (SEC) – The SEC is the government registering agency for all non-governmental organizations (NGOs). The SEC only registers and gives legal personality to an NGO but monitoring and supervision activities over NGOs are not done. However, the SEC has required all NGOs providing microfinance loans to categorically state in their respective charters and by-laws that microfinance is part of the services that the NGOs are providing.

Insurance Commission (IC) – The Insurance Commission, which is administratively under the Department of Finance (DOF), supervises all insurance activities in the Philippines, including the provision of microinsurance products. The IC is currently reviewing its policies and regulations insofar as the practice of microinsurance is concerned, especially by Mutual Benefit Associations or MBAs. Hopefully, a very clear framework would evolve in the future.

Microfinance Council of the Philippines, Inc (MCPI) – The MCPI, is not a Government agency but a duly registered NGO with the Securities and Exchange Commission. In the approved microfinance regulatory framework in the Philippines, the MCPI is viewed as the repository of data of microfinance practitioners. It is envisioned that, over time, the MCPI will act as a self-regulatory organization (SRO), especially for the NGOs doing microfinance programs in the Philippines.

- **Wholesalers of Funds to Retailers**

  In the Philippine setting, as enunciated in the national strategy and the regulatory framework, the wholesalers of microfinance funds are the Government financial institutions. Private commercial banks are strongly encouraged to act as wholesalers but there is no prohibition for them to do direct retail. So far, commercial banks have established their own subsidiaries like rural and/or thrift banks that provide retail microfinance services. A couple of commercial banks have asked the BSP for licenses to set up microfinance-oriented branches to service the requirements of their clients. The People's Credit and Finance Corporation (PCFC) is the microfinance apex institution in the Philippines. It is a Government-owned and-controlled corporation and is an attached Agency of the Land Bank of the Philippines (LBP). The LBP, Development Bank of the Philippines and the Small Business Corporation are the three major government financial institutions doing wholesale lending to conduits and retails.

- **Direct Retailers to End Users**

  Cooperatives, rural and cooperative banks as well as microfinance NGOs are actively servicing the requirements of both urban and rural clients. Some of the best performing microfinance banks and NGOs are members of the MCPI and the Alliance for Philippine Partners in Enterprise Development (APPEND), Inc., the oldest network of microfinance NGOs in the Philippines.

  The MCPI, as a network organization, has some of the largest and oldest microfinance institutions in the Philippines. It reported that as of 31 December 2008, the total number of active borrowers of its member organizations (Table 3) registered 1,554,336 with a total outstanding volume of PhP8.707 billion.

Table 3. MFI Ranking Based on the Number of Active Borrowers and Gross Loan Portfolio (as of December 31, 2008)

MFI		2008 Clients	2008 Portfolio	Ranking
1	CARD NGO	364,483	1,738,951,972	1
2	CARD Bank	205,097	956,177,546	4
3	TSPI	199,087	1,096,667,445	3
4	TSKI	172,857	1,234,006,153	2
5	KMBI	123,913	386,395,980	8
6	NWTF	84,958	444,874,313	6
7	CCT	70,023	478,858,003	5
8	ASKI	41,303	414,995,711	7
9	PB CARAGA	36,349	298,199,604	9
10	ABS-CBN	29,895	246,722,259	10
11	KCCDFI	23,493	114,598,572	15
12	KAZAMA	21,757	119,856,867	13
13	PALFSI	20,887	165,038,573	11
14	MILAMDEC	20,080	85,671,709	17
15	FCBFI	19,919	83,970,376	18
16	KASAGANA-KA	15,083	60,957,114	21
17	ASHI	14,932	155,060,761	12
18	ARDCI	13,317	116,820,296	14
19	MALLIG	12,854	76,411,130	19
20	OMB	12,628	69,530,658	20
21	SERVIAMUS	9,439	39,241,853	26
22	BK	8,135	86,574,161	16
23	PMDF	7,539	39,452,908	25
24	CANTILAN	7,463	49,771,197	24
25	CMEDFI	7,219	54,079,816	23
26	TALISAYAN	5,457	24,752,348	27
27	ECLOF	4,392	59,392,766	22
28	MEDF	1,777	10,150,351	28
	TOTAL	**1,554,336**	**8,707,180,443**	

4.6 Current Rural Finance and Microfinance Update

In the formal financial sector, microfinance services are given directly by the rural, cooperative and thrift banks. Wholesale lending by commercial banks, universal banks as well as by government specialized banks are given to microfinance institutions (cooperatives, non-governmental organizations and to other rural finance institutions, including rural banks) who in turn do the retailing of microfinance loans. As can be seen in Table 4, total microfinance loans by 213 rural and thrift banks registered at PhP6.346 billion and assisted a total of 902,104 households. Similarly, a total of PhP1.550 billion as savings was generated from the same number of microentrepreneurs and small farmers.

Table 4. Microfinance Exposures of Rural/Cooperative/Thrift/Microfinance Oriented Banks as of 30 June 2009 (Preliminary, in Million PhP)*

	Number of Banks	Number of Borrowers	Loan Amount (In Million)	Savings Component
Microfinance-Oriented Rural Banks	5	161,886	903.48	58.70
Microfinance-Oriented Thrift Banks	3	56,285	221.96	119.80
Sub-total	8	218,171	1,125.44	178.58
Microfinance-Engaged Rural Banks	161	581,511	3,857.52	1,083.10
Microfinance-Engaged Cooperative Banks	25	85,528	907.49	151.00
Microfinance-Engaged Thrift Banks	19	16,894	456.29	137.30
Sub-total	205	683,933	5,221.30	1,371.53
Grand Total	213	902,104	6,346.74	1,550.10

* Preliminary report of BSP MSFG on the operations of banks with microfinance

The performance of these banks would have not been possible if the Bangko Sentral ng Pilipinas did not seriously undertake the pursuit of sustainability but with prudential standards in microfinance operations. The BSP was mandated by the General Banking Act of 2000 through sections 40, 43 and 44 to recognize microfinance as a legitimate banking activity. Since then, 19 circulars have been issued by the BSP to support the practice of microfinance in the banking sector. The BSP has also taken proactive and significant initiatives and activities to promote the development of sustainable microfinance programs in the Philippines. Prior to 2001 when the first BSP circular on microfinance was issued, only a handful of banks were reporting microfinance loans.

The growth of microfinance in the formal regulated sector was enhanced with the issuance of 19 circulars to date. These circulars cover a wide range of prudential as well as regulatory practices that made possible such growth of microfinance in the banking sector. These circulars with their respective subjects are:

- Circular 272 (January 2001) provided the operating guidelines of the General Banking Law Provisions. Specifically it recognized cash-flow-based lending as a peculiar feature of microfinance, defined microfinance loans and provided for the exemption of microfinance loans from rules and regulations issued with regard to unsecured loans;
- Circular 273 (27 February 2001) partially lifted the moratorium on the establishment of new banks as long as the new banks are microfinance-oriented;
- Circular 282 (19 April 2001) opened a rediscounting facility for rural banks/cooperative rural banks engaged in microfinance;
- Circular 324 (2 March 2002) opened a rediscounting facility for thrift banks engaged in microfinance;
- Circular Letter 2002 – required the reporting of banks with microfinance operations;
- Circular 340 (30 July 2002) provided the rules and regulations concerning the establishment of branches or loan collection and disbursement points (LCDPs);
- Circular 365 (16 January 2003) liberalized select provisions of Circular 340;
- Circular 364 (19 January 2003) provided for the reduction to 75 percent of the risk weight applicable to small and medium enterprises (SMEs) and microfinance loan portfolios that meet prudential standards;
- Circular 369 (17 February 2003) liberalized select provisions of Circular 340;
- Circular 374 (11 March 2003) provided guidelines for the implementation of the Barangay Micro-Business Enterprise Law;

- Circular 409 (14 October 2003) provided the rules and regulations for the portfolio-at-risk (PAR) and the corresponding allowance for probable losses which depend on the number of days of missed payment;
- Circular 505 (22 December 2005) revised branching guidelines by allowing qualified microfinance-oriented banks and microfinance-oriented branches of regular banks to establish branches anywhere in the Philippines;
- Circular 549 (09 October 2006) exempted microfinance from the required submission of additional documents for the granting of loans;
- Circular 570 (24 May 2007) allowed wholesale loans of universal, commercial and branches of foreign-owned banks to non-bank microfinance institutions as compliance to the 6 percent mandatory credit allocation to small enterprises;
- Circular 607 (30 April 2008) provided the Reportorial Requirements for Microfinance Loans;
- Circular 624 (13 October 2008) stipulated amendments to branching regulations with incentives for microfinance-oriented banks or microfinance-oriented branches;
- Circular 625 (14 October 2008) provided the implementation of Mandatory Allocation to MSMEs as per Republic Act 9501;
- Circular 649 (March 2009) covered the regulations on the issuance of electronic money; and
- Circular 669 (22 October 2009) amended the existing rules on loan collection and disbursement points of microfinance-oriented banks and microfinance-oriented branches by allowing the servicing of deposits and withdrawals only of microfinance clients.

What is microfinance? For a clearer of appreciation of microfinance in the Philippines, we need to look at how the multilateral and other bilateral organizations have defined it. The Philippines defines it as the provision of a broad range of services which include savings, credit, remittance, transfers and insurance to poor and low-income households.

Related to the provision of microfinance loans and savings, some of the Philippine microfinance institutions are also providing microinsurance products, to their clients. MFIs either partnered with insurance companies to provide insurance products or directly provided limited types of microinsurance products to their clients. A handful of MFIs, on the other hand, facilitated the establishment of mutual benefit associations or MBAs that are owned by the clients of MFIs. Some of the microinsurance products being offered to the clients are either life or non-life in nature, agricultural insurance linked with weather based data/index, or plain insurance of loans. The government is currently reviewing the legal, regulatory framework of these activities, and hopefully, in the next year or so, a very clear, sound and prudentially focused framework would evolve to help the poor, whether in the rural or urban setting.

The practice of microfinance in the Philippines has been cited as one of the most advanced in the world, from a list of 55 countries. In a pilot index and study done by the Economist Intelligence Unit (EIU)[9] as commissioned by the International Finance Corporation (IFC), Inter-American Development Bank (IADB) and by the Corporacion Andina de Fomento (CAF), the Philippines ranked number 3, largely due to a very clear and supportive regulatory framework. The study focused on three broad categories: regulatory framework, investment climate and institutional development. The Philippines landed number 1 in regulatory framework. The Philippines got an index score of 68.4, after the South American countries, Peru and Bolivia, with index ratings of 73.8 and 71.7, respectively.

The selection of the Philippines as number 3 (and number 1 in Asia), after Peru and Bolivia, of the world leaders in sound microfinance regulatory environment is a testament to the commitment of the key Philippine stakeholders to see a vibrant, dynamic and sustainable microfinance environment at work in the Philippines.

[9] Global Microscope on the Microfinance Business Environment: A Pilot Index and Study by the Economist Intelligence Unit of the Economist.

According to the report, the countries at the top of the index share several characteristics:

1. Their governments seek to foster market development through policies that address microfinance activities directly.
2. In cases, where the "sector" is not specifically addressed by laws and regulations, the more general framework that govern microfinance still allows it to grow.
3. Governments in these countries also refrain from implementing large scale and distorting subsidy programs.
4. In cases where subsidies exist, they have not crowded out microfinance provision by specialized microfinance institutions like NGOs and cooperatives.
5. In some cases, central banks in these countries have created specialized microfinance units in their organizations.

One may surmise that, with this recognition, the Philippine microfinance outreach would be in the millions, approximating the reported outreach of Bangladesh, India and other Latin American countries. The Philippine outreach and volume, however, are not in the same league due to contextual reasons. For one, the total population in the Philippines is much lower than that of the countries reporting outreach by the millions. The physical terrain in the Philippines and the little infrastructure to physically reach with financial services those in the hard-to-reach areas are to other factor to consider. The microfinance practice in the Philippines is making inroads and is now substantially reaching a greater number of poor clients as against the total population.

4.7 Lessons Learned/Future Directions and Issues

- **Lessons Learned**

  The world of rural finance and microfinance is a very dynamic and a very challenging one. The commitment to serve the poor, whether in the urban or rural setting in a viable, replicable and sustainable manner, brings tensions, pressures and challenges to the players involved. The tensions and pressures to produce profit at the end of the day coupled with the social dimension of bringing down poverty and creating more incomes and resources for the poor will always be in the mind of the providers of credit and other financial resources. Regulators and policy-makers have a common objective, i.e., protect the soundness of the system and to craft policies and regulations that will not exclude people, especially the poor, but would rather move towards financial inclusion for all.

  The lessons learned can be summarized in the following acronym:

  – **C: COMMITMENT** to Financial Inclusion
  – **B: BOLDNESS** and to think outside of the box
  – **A: ADAPTIVE**
  – **N: NATIONALISTIC**
  – **K: KNOWLEDGE FOCUSED**
  – **E: "EARTHY" MIND**
  – **R: RESPONSIVE**

- **Challenges and Issues**

  With these points in mind, we can then look at the challenges ahead with greater resolve and certainty that we would be able to hurdle them. Looking into the Philippine setting, a number of evolving challenges and issues ahead are listed below:

– **Credit pollution**

As microfinance institutions expand their respective microfinance programs and services, the tendency to be lax in client selection and in preparing their clients, whether individuals or groups, has become an issue. In a number of anecdotal reports as well as some official reports of MFIs, the quality of portfolio was reported to be going down. As MFIs tend to "poach and capture" good clients of competing MFIs, preparing the clients in the old fashioned way of credit discipline and savings habit has been forgotten. Community organizing and community development preparation have been shortened too, thus increasing the risk of bad portfolio over time.

A solution to this problem is the use of a credit bureau. Although there are at least three (3) functioning private credit bureaus in the Philippines, their operations are not covering microfinance loans. On top of these, these credit bureaus do not share information among themselves and they only focus on the negative list, i.e., clients who have bad credit history.

The Philippine Congress recently passed the Credit Information Systems Act (CISA) which aimed at establishing a comprehensive data system and structure that would help systematize relevant data of borrowers. It is envisioned that all borrowers of banks and cooperatives, and later even that of the NGOs would be subjected to the credit information processes that will be handled by Credit Information Corporation, a Government-owned corporation established by the Act. With the approval of the CISA, access to credit by micro, small and medium as well as agri-based workers would be enhanced as well as the risks issue involved in multiple borrowings of clients addressed.

– **Financial literacy and consumer protection of clients**

As clients get exposed to financial transactions offered by various providers of funds, regulators and providers of funds need to think of ways so that clients can be empowered to become financially literate. Clients need to be aware of their rights and responsibilities in the use of credit as well as savings. Budgeting, planning and investing skills are needed by the clients and there is a need to build capacities of the clients in these skills. Finally, consumer protection of clients must be an on-going concern by all.

– **Need for business development services (BDS)**

As clients' businesses expand, the most common need that is expressed by them is how to help them improve their products and services. Clients need help in product design, marketing, branding, and compliance with standards. The response of the MFIs is either to link these clients to existing organizations who are focusing on these needs. The MFIs need not directly address these particular needs of their clients but by linking them up to appropriate organizations, the services needed by the clients can be met.

– **Branchless banking/phone banking**

The Philippines is known as the "texting capital of the world", with over 650 million texts that go around everyday. More than 55 percent of the population own each at least one cell phone. Along this line, the BSP and in partnership with the Rural Bankers' Association of the Philippines has allowed the use of cell phones for loan payments, deposits and withdrawals of savings by microfinance clients. Allowing the use of this technology has brought down the cost of such transaction and increased convenience for both the institution and the client. This facility has enabled the clients who are unable to travel to the physical branch office of the bank to transact with the bank.

5. Summary of Findings and Recommendations

In the light of the sharing of the three experts from Bank of Lao PDR, Krung Thai Bank and the Bangko Sentral ng Pilipinas, and the ensuing discussions during the forum on what is best way forward for Lao PDR, several key findings and recommendations had emerged:

5.1 Delivery of Appropriate Products and Services

The APB recognizes the need to deliver appropriate and relevant savings products, which maybe in tandem or not with the provision of credit services, to the present microfinance/agricultural clients and to prospective clients.

The APB leadership might want to undertake research on market-led financial products, specifically savings product to cater to the needs of its clientele. As shown by the KTB model, the entrepreneurial poor are indeed trustworthy and reliable when given the opportunity to get involved in the program of the KTB. The particular savings product need to consider the peculiarity, life and work cycle of the users, i.e., the rural poor farmers. The rural poor definitely have needs for credit but several literature and studies also point out that the poor need other financial instruments and services so that the poor's longing to save can be met by the banking players.

One of the constraints why the poor do not save is the set of various requirements needed to prove the poor's financial identity before a savings account can be opened. Generally, a minimum amount of money and maintaining a specific amount of average daily savings balance are also imposed by banks to open a savings account.

The APB as well as other banks supporting the growth of rural and microfinance might want to consider offering a "no-frill savings account" which basically allows the entrepreneurial poor to open a savings account with a lower minimum requirement, say US$2.00 or no maintaining average balance. Since the policy on the requirements for opening savings bank account is within the business decision of the concerned banks, allowing such changes would definitely result in more financial inclusion as well as getting the poor to save in the banking institutions.

5.2 Strengthening the Legal and Regulatory Environment

The Bank of Lao PDR should continue its efforts to strengthen the enabling legal and regulatory environment for rural credit and microfinance and to strengthen its regulatory and supervisory approaches in dealing with banks doing microfinance and rural credit programs.

The BOL should strictly monitor and enforce that banks make the necessary loan-loss provisions as well as require banks to have duly approved writing off policies.

The BOL may want to consider to link up with regional and international network of regulators and policy-makers and to participate in meetings, fora and training sessions thus increasing the Bank's knowledge, attitude and skills towards sound regulatory and policy practices.

5.3 Capacity Building of Clients

The Government, in partnership with donors and rural financial institutions, should work towards building the capacity of clients through financial education and literacy.

The major Lao PDR stakeholders in rural credit and microfinance (BOL, APB, donors, etc.) should work towards establishing a very clear operational framework to empower the clients as well as the providers of financial services in areas of financial literacy and education, addressing such issues as roles and responsibility of borrowers, budgeting and planning, consumer protection and transparency, savings and investments and microinsurance.

After crafting a very clear national strategy on financial education and literacy, the BOL and other stakeholders may continue to collaborate with each other in the conduct of culturally relevant training and capacity building sessions focused on the providers of financial services, microfinance and rural clients, other Government and private agencies thus empowering clients, providers and regulators on financial education and literacy.

Annexes

Annex 1

FinPower National Microfinance Development Forum
Vientiane, Lao PDR February 2, 2010

Schedule of Activities

08:30-08:45	Opening Remarks: Mr Bounvong Doangdokket, Managing Director, APB
08:45-09:00	Introduction to the Forum: Mr. Benedicto S. Bayaua, Secretary General, APRACA
09:00-09:40	Presentation on the Lao PDR MicroFinance Policy Environment and Regulatory Framework by Ms. Keasorn Manivong, Chief of Microfinance Institution Division, Bank of Lao PDR
09:40-10:00	Break
10:00-11:30	Presentation on BSP MicroFinance Policy Framework and Regulatory Framework by Mr. Eduardo C. Jimenez, Consultant, Bangko Sentral ng Pilipinas
11:30-12:00	Open Forum
12:00-13:30	Lunch
13:30-15:00	Presentation on KTB Savings Mobilization by Ms. Nisanard Yothasmut, Vice President, Krung Thai Bank, Thailand
15:00-15:30	Open Forum
15:30-16:00	Integration and Closing Session

Annex 2

List of Forum Participants

1. Mr. Bouangeunh PHONGSAVATH, APB Deputy Director
2. Mrs. Phetsamay SIDACHANH, APB HR Division
3. Mr. Bounsy THANOUSING, APB Plan & IR Division
4. Mr. Bounyou MEUANGMAHAVONG, APB C&M Division
5. Mr. Souvanh PHOMMALONGSINE, APB Nakhonhluang
6. Mr.Thongdam THEPPHAVONG, APB Pongsaly
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