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A Public-Private Sector Initiative

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DRAFT REPORT OF THE WORKSHOP ON PROMOTING A FAVORABLE POLICY ENVIRONMENT FOR SUSTAINABLE MICROFINANCE (*WITH EXECUTIVE SUMMARY*)

Office of the Advisory Group Chair



COMMERCIALLY SUSTAINABLE MICROFINANCE A STRATEGY FOR PROMOTING FINANCIAL INCLUSION IN APEC

REPORT OF A WORKSHOP JOINTLY ORGANIZED BY
**THE ADVISORY GROUP ON APEC FINANCIAL SYSTEM CAPACITY BUILDING AND
THE APEC BUSINESS ADVISORY COUNCIL**

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Indonesia

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**COMMERCIALLY SUSTAINABLE MICROFINANCE
A STRATEGY FOR PROMOTING FINANCIAL INCLUSION IN
APEC**

Report of A Workshop Jointly Organized by
The Advisory Group on APEC Financial System Capacity-Building and
The APEC Business Advisory Council (ABAC)

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FOREWORD

By Jeffrey L.S. Koo

Chair, Advisory Group on APEC Financial System Capacity-Building

Microfinance is a new industry that is expected to play an important role in the economic empowerment of financially underprivileged households and their integration into the market economy. As such, it helps provide a broad and firm base for more dynamic, sustainable and equitable economic growth, which is important for the attainment of the APEC vision.

In 2002, APEC undertook a major initiative on microfinance. The APEC Business Advisory Council (ABAC) submitted a number of recommendations to APEC Leaders and APEC Finance Ministers. Among them were the following. First, ABAC recommended that APEC promote a legal and regulatory environment that is conducive to the development of micro-enterprises and microfinance institutions (MFIs). Second, ABAC proposed that policy reforms be accompanied by capacity-building measures, supported by multilateral financial institutions and a rating system to reflect the creditworthiness and competence of MFIs. Third, ABAC called on commercial institutions to support lending to worthy microfinance programs, either as part of commercial lending (in which case lending should be on commercial principles) or as charitable activities. Fourth, ABAC called on regulators to separately measure the size of banks' lending to MFIs and consider these loans as a particular category of lending with an appropriate capital-weighting ratio applying to them.

Since that time, a number of important developments have changed the landscape of microfinance. Many traditional non-governmental organizations (NGOs) have been transformed into licensed financial intermediaries, thus gaining access to funds and deposits. There has been growing recognition by established commercial banks that microfinance offers significant opportunities to enhance their own product mix and profitability. Global financial institutions are also entering the market and new financial products have emerged to link microfinance to global capital markets.

With these new developments, the time has come for ABAC to revisit the subject and to develop new recommendations, with the goal of promoting commercially sustainable microfinance. In 2007, the ABAC Finance and Economics Working Group (FEWG) initiated discussions on how APEC may develop effective policy frameworks governing microfinance. This year, the Advisory Group on APEC Financial System Capacity-Building – a public-private sector initiative launched jointly in 2003 by ABAC and the Pacific Economic Cooperation Council (PECC) – began to consider what effective capacity-building measures APEC can undertake to promote the growth of microfinance.

For this purpose, the Advisory Group and ABAC co-organized a workshop on January 23, 2008 in Jakarta, Indonesia. This workshop aimed to help participants understand the forces reshaping the microfinance industry and its direction. It examined the policy environment in the region's developing economies and how it may be improved. It also touched on what APEC can do to help promote commercially sustainable microfinance. This report is the record of discussions during that workshop, and is intended to assist in identifying measures that APEC Finance Ministers and APEC Economic Leaders may undertake to promote the continued development of microfinance as a tool for increasing financial inclusion levels in the region.

On behalf of the Advisory Group and my ABAC colleagues, I take this opportunity to thank a number of institutions and individuals who have contributed valuable intellectual resources to the discussions at the workshop and the drafting of this report. For very substantial contributions to specific parts of the report, I particularly

acknowledge Dr. John Conroy of the Foundation for Development Cooperation (FDC), for his contributions to the introductory section and the section on financial inclusion as an issue for APEC Finance Ministers; Dr. Brigit Helms of the International Finance Corporation (IFC) for the overview section on microfinance as a tool for financial inclusion; Mr. Hiroshi Toyoda of the Inter-American Development Bank for the section on the Latin American experience of the path to commercially sustainable microfinance; Ms. Leny I. Silvestre of the Philippine Central Bank (Bangko Sentral ng Pilipinas or BSP) for the section on the Philippine experience in developing a policy and regulatory environment for microfinance; and Dr. Alfred Hannig of the German Technical Cooperation (Deutsche Gesellschaft für technische Zusammenarbeit or GTZ) for the section on creating an enabling policy and regulatory environment for financial inclusion.

A number of other participants have also helped shape the contents of this report through their thoughtful comments and interventions at the workshop. I wish to specifically acknowledge the contributions of Ms. Beris Gwynne of the Collaborative for Global Development and Mr. Palgunadi Setyawan of PT Asialab Indonesia, as well as my ABAC colleagues (in order of their respective interventions during the workshop) Mr. Michael Phillips of Russell Investment Group, who is also the Chair of the ABAC Finance and Economics Working Group; Mr. Mark Johnson of the Australian Gas Light Company, who is this year's ABAC Co-Chair; Mr. Rudjito of the Indonesia Deposit Insurance Corporation; Mr. Jeff Dowle of HSBC Bank Canada; and Mr. Yoshihiro Watanabe of Mitsubishi UFJ Financial Group, who is my Co-Chair in the Advisory Group.

I thank the Session Chairs for their able management of the workshop discussions (in order of their respective sessions): Dr. Julius Caesar Parreñas of Chinatrust Financial Holding Co; Mr. Kenneth Waller of ABAC Australia; and Dr. Twatchai Yongkittikul of the Thai Bankers' Association. I express my appreciation to the PECC Secretariat, represented at the workshop by PECC Secretary General Mr. Eduardo Pedrosa, for providing very helpful introductions to key microfinance experts within the PECC network. Finally, I wish to thank ABAC Indonesia for hosting the workshop and the excellent arrangements provided by the ABAC Indonesia Secretariat that have contributed to its success.

This report is, above all, a testament to the promise that public-private sector regional collaboration holds for the effective development of initiatives and identifying solutions to major issues in APEC. Being central to achieving shared prosperity and ensuring broad support for APEC's goals of trade and investment liberalization and facilitation and regional integration, financial inclusion is one of these major issues. I encourage all relevant policy makers in the region to study this report and to seriously consider its recommendations.

COMMERCIALLY SUSTAINABLE MICROFINANCE A STRATEGY FOR PROMOTING FINANCIAL INCLUSION IN APEC

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Executive Summary

Financial inclusion is an important issue that needs to be addressed. In developing economies, typically more than half – in some cases even as high as 80% – of the adult population, mainly belonging to low-income households, remain without access to banking services. In the 1980s, microfinance institutions (MFIs) emerged to serve this sector, offering small loans to individuals, solidarity groups and microenterprises. Since then, microfinance¹ has undergone remarkable growth, offering opportunities for increasing financial inclusion levels, distributional equity and financial deepening. This growth has accelerated particularly during the previous half-decade, as savings facilities extended to more low-income households have increasingly become linked to banking systems and capital markets. Among the most notable trends are the following:

- The range of microfinance services has rapidly expanded and now includes housing and consumer loans, utility bill payments, savings, fixed-term and deposit accounts, life and health insurance and domestic and international money transfers and payments.
- Access points are multiplying as microfinance service providers have taken advantage of innovation and new technology, such as better information systems connectivity, automated teller machines (ATMs), point-of-sale technology, mobile phones, smart cards and biometric information to reach a wider clientele.
- Financial institutions are increasingly seeing microfinance as a commercial opportunity rather than a charitable activity. It is attracting commercial banks and investors due to the high quality of loan portfolios and the potential to develop a large market that still remains unserved or underserved by traditional financial institutions. In most regions, the growing number of regulated MFIs, which are benefiting from lower funding costs through deposit-taking activities and credit ratings, are outperforming commercial banks and have demonstrated superior ability to withstand financial crises and stricter policies for bad debt provisions.
- Commercial banks are increasingly engaged in microfinance along a wide range of options from offering back or front office functions, wholesale lending and outsourcing of operations to MFIs and investing equity in these institutions, to

¹ This report does not cover “micro-equity” with reference to start-up equity finance mainly available in advanced and mezzanine markets and typically involving larger sums and equity-based angel investing.

establishing their own loan service companies and specializing in microfinance as a main business line.

- Funding through capital markets is growing, as an increasing number of institutional and individual investors are attracted to new microfinance investment vehicles (MIVs) offering geographic diversification with low volatility, low correlation and high asset quality. However, development has been uneven across regions, with Latin America and Eastern Europe attracting the greater portion of MIV activities due to the presence there of more commercially-oriented and regulated MFIs. This points to the importance of an enabling environment for such institutions throughout the region to accelerate the linkage of microfinance to capital markets.

Notwithstanding these positive trends, there is still a long way to go in actualizing the full potential of microfinance as a tool to promote financial inclusion. There is an enormous need for capacity-building to enable large numbers of MFIs to upgrade their governance structures, management, internal controls, credit policies and methodologies, and to take advantage of opportunities arising from innovation and new technology. Given the large demand for funding that banks and capital markets could provide, a key issue is how to attract and facilitate increased private sector participation and investment in microfinance.

Government has an important role to play in the process of promoting financial inclusion. This is to provide an enabling environment that addresses legal, policy and regulatory barriers in order to facilitate the development of microfinance and increase its access to commercial funds. This reflects the shift from the previous paradigm of directed credit and government lending that have proven unsuccessful, wasted public resources and produced distortions in credit markets to the new paradigm focused on facilitating market-driven private sector lending. Experiences, such as that of the Philippines detailed in this report, underscore the importance of emphasizing incentives over requirements in developing successful strategies to promote financial inclusion.

Governments can accelerate progress toward financial inclusion by identifying the most critical policy solutions. A study that examined alternative policy measures to promote financial inclusion identified six sets of access policy solutions that governments in the region could consider. These refer to policies and regulations governing correspondent banking agents, mobile phone banking, entry barriers to the financial sector, the governance and management of publicly-owned financial institutions, financial identity regulations and financial consumer protection.

In undertaking reforms, it is important to keep in mind a number of lessons from past experiences of governments in developing regulatory frameworks to promote financial inclusion. Among these lessons are the following:

- (a) Regulatory reform is more successful where there has been prior substantial improvement in the financial sector environment.
- (b) New regulations only make sense if there is a perceived opportunity to profit from an additional supply of financial services.
- (c) Regulation is useful if the benefits of access to cheap domestic savings outweigh the additional costs to supervisory and supervised entities.
- (d) Relaxing branching regulations is a powerful and economical alternative to introducing microfinance regulations.
- (e) The use of ICT, which helps reduce costs and expand coverage of financial services, can have a substantial contribution to financial inclusion.
- (f) Well-governed and commercially-oriented public sector banks can play an important complementary role in promoting financial inclusion.

- (g) Access to finance can rapidly expand in the absence of formal regulation up to a certain point, beyond which policy makers and regulators will need to step in to keep risk under control.

Considering its importance for spreading more widely the benefits of free and open trade, the issue of financial inclusion, with microfinance as an instrument of choice, should have a place in the APEC agenda. However, it should be treated not as a social welfare measure, but as part of APEC's suite of policy tools to advance economic and financial reforms. On account of financial inclusion being a central task of financial sector development, its significance to the development of banking systems and capital markets and the role that financial regulation and financial institutions would have to play in this process, its appropriate place should be within the APEC Finance Ministers' Process.

An APEC financial inclusion initiative could focus on providing an enabling legal, policy and regulatory environment through improvements in measuring levels of financial inclusion in member economies, policy dialogue and sharing of experiences and capacity-building activities. Strong private sector collaboration is important for the successful design and implementation of critical measures, both at the regional and domestic level. Thus, a meaningful involvement of ABAC and the Advisory Group on APEC Financial System Capacity-Building in a financial inclusion initiative undertaken by the APEC Finance Ministers would be very desirable.

With these considerations in mind, it is recommended:

- ***That financial inclusion as a policy goal, with microfinance as an instrument of choice, be adopted by the APEC Finance Ministers as part of their agenda, and endorsed by the APEC Economic Leaders.***
- ***That the APEC Finance Ministers undertake activities to promote an enabling policy and regulatory environment, including measurement of levels of financial inclusion in developing member economies, initiation of capacity-building activities and holding of policy dialogues, drawing from the conclusions of this report and with special attention to the following key areas that are relevant to the development of microfinance: (1) agent banking; (2) mobile phone banking; (3) increasing the diversity of microfinance service providers; (4) improving governance and management of public banks; (5) financial identity regulations; and (6) protection of consumer and creditor rights.***
- ***That the APEC Finance Ministers work closely with ABAC and the Advisory Group on APEC Financial System Capacity-Building in developing their financial inclusion agenda.***

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I. INTRODUCTION

The importance of microfinance² for the economic empowerment of financially underprivileged households, their integration into the market economy, and the development of a broad and firm base for more dynamic, sustainable and equitable economic growth is widely acknowledged. From its early days in the late 1980s, when the emergence of Grameen Bank in Bangladesh attracted attention to the role of microcredit as a source of finance for microenterprises, microfinance has evolved from an industry largely driven by non-governmental organizations' commitment to social objectives into an industry that is increasingly responsive to the demands of both private capital and its customers.

The evolution of microfinance is reflected in the transformation of traditional NGOs dedicated to the sector into licensed banks and non-bank financial intermediaries to gain access to funds and deposits, the growing recognition by established commercial banks and finance companies entering the market of its potential to enhance their own product mix and profitability, and more recently, the entry of global commercial and investment banks and the development of financial instruments and vehicles to facilitate the flow of funds to the industry via the mainstream capital markets.

This evolution is also reflected in the changing concepts and terminology used in professional circles. Over the past decade, the early notion of *microcredit* as a solution to poverty has lost ground to a more holistic concept of *microfinance*, which now encompasses a wide range of financial services being offered to the lowest-income segments of the economy (See Box 1). More recently, the term *financial inclusion* has emerged, focusing attention on the need to bring under the coverage of financial institutions those people – comprising very significant portions of the population in many emerging markets – who have as yet no access to banking services.

A number of factors account for this lack of access. These include geographic isolation, low population densities and gender. The delivery of financial services faces difficult challenges in certain sectors, such as smallholder and subsistence agriculture. Traditional lenders' requirements for formal physical collateral pose obstacles to financial access of many lower-income households in less developed economies that are often unable to meet these requirements, as a consequence, for instance, of land tenure and titling deficiencies that prevent collateralisation of land.

Increasing levels of financial inclusion will have very significant effects on the region's developing economies, particularly in terms of improved economic efficiency and

² This report does not cover "micro-equity" with reference to start-up equity finance mainly available in advanced and mezzanine markets and typically involving larger sums and equity-based angel investing.

equity. It will contribute to financial deepening, as low-income households in emerging markets – which usually demonstrate a higher propensity to save – gain access to safe and liquid deposit facilities providing positive real interest rates. It stands to enhance international competitiveness, wherever household-based microenterprises are linked through supply chains to export industries. By expanding the capacity of microenterprises to supply low-cost wage-goods and services to the industrial workforce, and by providing access to a wide array of financial services to industrial workers, microfinance also contributes to reducing wage pressures in the export sector.

BOX 1: FINANCIAL INCLUSION, MICROFINANCE AND POVERTY

The financial service needs of the poor are simple, but their satisfaction can be life-enhancing. A broad conception of microfinance embraces deposits, remittances, payments, micro-insurance and pensions, aside from credit. The poor need access to convenient, liquid and safe deposit services which are protected against inflation by positive real rates of interest. With savings in reserve, the poor are able to smooth their consumption expenditures in the face of uncertain income streams. Savings give households a shield against catastrophic events, whether affecting individuals or entire communities. Misfortunes such as illness or bereavement, or destruction due to natural disasters, might otherwise force the vulnerable to divest productive assets, tipping them over the divide between meagre sufficiency and poverty.

Access to deposit services also assists the recipients of 'lumpy' income flows, such as remittances or periodic crop receipts, to manage these more efficiently and prudently. This applies to domestic remittances in countries where internal migration is significant, but also in those countries with significant numbers of absentees working overseas. In either case, access to efficient and reasonably-priced remittance services can provide considerable welfare benefits.

Households in remote locations can benefit from payments services that greatly reduce the transaction costs, in time and money, of meeting a range of financial obligations. Microfinance institutions (MFIs) are often able to reach into areas too remote for formal financial institutions and government agencies. However in partnership with such agencies they are able to arrange payments for utility fees, government charges and other obligations for such households. There is also scope for households to receive payments from agencies of government, such as pensions, lease rentals and crop receipts, where applicable.

Micro-insurance is another financial product with potentially profound welfare benefits for poor households. Micro-insurers are learning how to pool risks among clients to provide simple forms of cover against contingencies such as death and illness. MFIs may offer cover to clients as an element in loan contracts, or arrange various forms of protection for savings depositors upon payment of an additional fee. While still rudimentary, micro-insurance is a growing element in the broader micro-financial services industry. Another development is a variety of long-term savings schemes that offer quasi-pensions to clients.

Poor households benefit from access to credit, which can increase the productivity of their labour in micro-enterprise activities. Access to credit from alternative sources can also free poor households from exploitative financial relationships with moneylenders. Further welfare benefits may occur if micro-credit is not restricted to financing narrowly-defined 'productive' activities. Recognizing the fungibility of money, which makes it difficult for lenders to know exactly how borrowers use the funds they receive, many microfinance service providers are prepared to lend for a wider range of welfare-enhancing purposes. These may include family needs, including school fees, and the purchase of consumer durables.

To say that micro-credit has been 'eclipsed' is not to say that the poor cannot benefit from credit, but only that credit should be provided in the context of a full portfolio of microfinance services. And of all potential micro-financial services, access to deposits is probably the most useful to most people, for most of their lives.

*Excerpt from John D. Conroy, **Financial Inclusion: A New Microfinance Initiative for APEC (Paper Presented at the Workshop).***

Financial inclusion facilitates the increased participation of low-income households in the market and enables them to benefit from economic growth, thus contributing to distributional equity. Households headed by women, which represent a large portion of low-income households in many economies, stand to reap a large proportion of gains from these new opportunities. Finally, increased financial inclusion enhances the capacity of low-income households and microenterprises to adjust to the impact of market-opening measures and take advantage of emerging opportunities.

The challenges to promoting greater financial inclusion are considerable. There is a large demand for funding, and greater involvement of the financial industry and capital markets would be required for these needs to be met. While a number of microfinance institutions (MFIs) have succeeded in terms of developing high-quality portfolios, these make up only a very small portion of the total number of MFIs worldwide.

Facilitating the development of a commercially sustainable microfinance industry in the region would require improving the environment for the effective and efficient operation of MFIs, increased flow of funds through banks and capital markets, and appropriate provision of public support. Workshop participants discussed this issue in considerable depth and reflected on proposals for policy reforms and capacity-building measures that can be undertaken by governments, public institutions and regional organizations, particularly APEC, in collaboration with the private sector. This report describes the content of these discussions and presents the conclusions and recommendations arising from them.

II. MICROFINANCE AS A TOOL FOR FINANCIAL INCLUSION: ITS EVOLUTION AND CURRENT SITUATION

A. BROAD OVERVIEW

Over the past few years, microfinance has undergone a rapid transformation, as its links to the formal financial system have expanded. Microfinance has gone far beyond the simple lending of small amounts to finance microenterprises and help the poor. Today, mainstream institutions are delivering a wide range of financial services. Delivery channels include non-governmental organizations (NGOs), commercial and state banks, and credit unions, providing access to a wide range of services to low-income clients, including deposit services, weather insurance, domestic money transfers and loans. Microfinance now involves the use of smart cards and biometric information.

The integration of microfinance is also taking place with respect to the supporting institutions of the financial sector. Credit rating agencies are now rating microfinance institutions (MFIs), and credit bureaus are enabling these MFIs to reduce risk and cut costs. In line with these developments, many governments have integrated microfinance into policy and regulatory frameworks governing the financial sector.

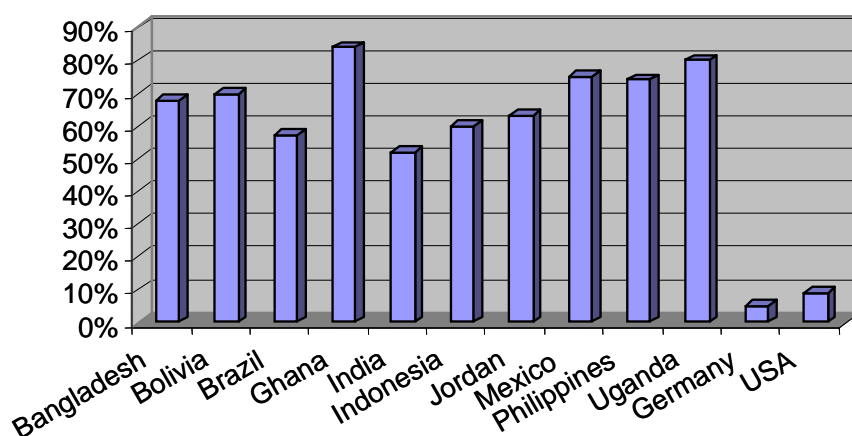
Access points for low-income clients are multiplying, as microfinance institutions (MFIs) and state and commercial banks leverage existing and new infrastructure. Today, low-income clients can access financing through self-help groups, loan service agents, lottery agents, traders and processors, point-of-sale networks, ATMs and mobile phones.

There is a large potential market, with about 83% of the global market yet to be tapped. These include the estimated 2.5 billion people worldwide at the bottom of the economic pyramid who do not possess bank accounts. In a number of economies, the percentage of the adult population that has no access to bank accounts range

from 50% to as high as 80%. (See Chart 1.) This has significant implications for the banking sector. In developed economies, where banking penetration rates are high, retail and small business clients have proven to be major sources of profits.³ Another study estimates that an increase in the number of microfinance borrowers from the current level of about 100 million to 1 billion borrowers worldwide would result in a funding gap of about US\$250 billion.⁴

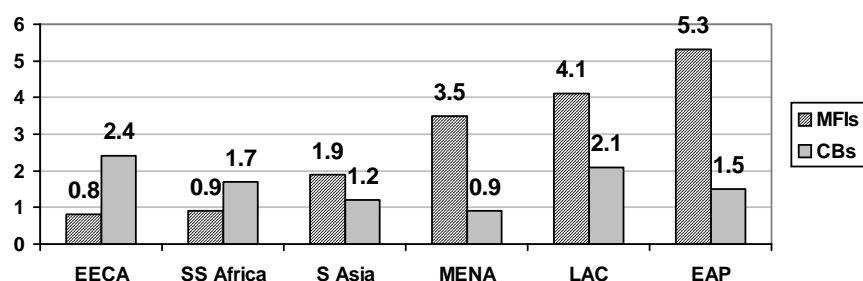
Microfinance is a profitable business. In four out of six developing regions (and especially in East Asia and Latin America), licensed MFIs are outperforming commercial banks. (See Chart 2). The profitability of the sector has also continued to grow. The percentage of MFIs becoming profitable within two years of inception has increased from 3% for those starting operations in 1995-96 to 29% for those starting in 1999-2000. Table 1, which provides key figures for several leading institutions in Asia, Latin America and Africa, illustrates the generally high quality of MFI loan portfolios (measured by portfolio at risk for more than 30 days ratio).

CHART 1: PERCENT OF ADULT POPULATION WITHOUT BANK ACCOUNT, 2006



Based on various household surveys.
Source: Honohan, 2007 (chart taken from presentation by Dr. Alfred Hannig, GTZ)

CHART 2: RETURN ON ASSETS (%), MFIS VS. COMMERCIAL BANKS (MEAN), 2005



Source: Microfinance Information eXchange Inc (MIX), December 2006 (chart taken from presentation by Dr. Brigit Helms, IFC)
376 MFIs with 2005 adjusted data and 1804 CBs from BankScope in MFIs' economies. Average weighted by assets. Only NGOs and licensed MFIs.

³ Examples include the case of Wells Fargo, whose business model based on mass retail has made it the 4th largest bank in the US; Citibank in North America, which derived more than 50% of its profits from consumer and small and medium enterprise loans in 2003; and Société Générale, whose retail operations have helped it attain 600% growth in total shareholder returns since 1990.

⁴ Deutsche Bank Research (2007), *Microfinance: An Emerging Investment Opportunity*.

TABLE 1: KEY DATA FOR LEADING INSTITUTIONS, END-2004

Institution	PaR 30 (%)*	Gross Loan Portfolio (USD mil)	Number of Borrowers
SHARE (India)	0.19	40.2	368,996
Compartamos (Mexico)	0.56	101.1	309,637
Banco Solidario (Ecuador)	1.54	177.1	72,787
ASA (Bangladesh)	1.68	201.1	2,772,719
PADME (Benin)	1.81	44.1	37,661
NovoBanco (Mozambique)	3.38	6.9	11,350
Centenary Bank (Uganda)	4.21	44.6	52,682
CMS (Senegal)	4.21	40.7	33,598

Source: Microfinance Information eXchange Inc (MIX) (table taken from presentation by Dr. Brigit Helms, IFC)

*Portfolio at risk for more than 30 days, estimated by adding the past due loan portfolio and loans in legal recovery and calculating them as a percentage of the total portfolio.

High administrative costs pose a challenge to MFIs. Measured as a percentage of MFIs' gross loan portfolio, they make up the main cost component across developing regions, ranging from an average low of 22%-25% in South Asia, Eastern Europe and Central Asia (EECA) and Middle East and North Africa (MENA) to an average high of 43% in Sub-Saharan Africa. The East Asia and Pacific (EAP) and Latin America and Caribbean (LAC) regions are somewhere in the middle with an average 30%-31%.

This is the case even for operationally sustainable MFIs with positive returns on assets. Although much lower than the average for all MFIs by region, they still involve considerable amounts in relation to gross loan portfolio, averaging 13% in South Asia, 18% for EECA, 21% for EAP, 23% for MENA and for Latin America/Caribbean (LAC), and 33% for Sub-Saharan Africa.⁵ These administrative costs are driven mainly by labor costs, loan size, and productivity.

Innovation and new technology present significant opportunities for expanding access of low-income clients to financial services by reducing costs and increasing transparency. Better information systems connectivity and wider use of credit scoring and personal digital assistants (PDAs) are reducing operating costs for financial institutions, as do the expanding use by banks of automated teller machines (ATMs) and point of sale (POS) technology. Growing use of mobile phones, smart cards and biometric information are also facilitating low-income clients' access to finance.

The impact of technology on operating costs can be illustrated by a comparison of transaction costs through different delivery channels, with a typical ATM transaction costing as much as five times less than a transaction done through a bank teller. Mobile phone banking especially presents enormous opportunities, with payments through mobile phone worldwide estimated to reach US\$37 billion in 2008.

While the use of technology in microfinance will face various challenges ranging from consumer and staff literacy, infrastructure, policy environment and capacity of financial service providers to availability of suitable information systems, there has already been a number of success stories that point a way forward. In Brazil, for example, banks have opened millions of new accounts by installing POS technology

⁵ These figures are based on adjusted and unadjusted data for 2004 and 2005 provided by Microfinance Information eXchange (MIX) in January 2007.

in supermarkets, retailers, postal, and lottery outlets with technology to deliver financial services.⁶

Funding sources are expanding. Commercial banks have become increasingly engaged in microfinance. Some are directly providing services through internal units, specialized financial institutions or service companies. Others work through existing providers through outsourcing, extending commercial loans to MFIs or providing systems and infrastructure.

Levels of engagement vary among commercial banks. At the low end, banks provide back or front office functions such as by renting out office space in their premises or sharing their branch networks with MFIs. At the middle level, banks engage in wholesale lending to MFIs, contracts out microfinance operations to MFIs and self-help groups, or invest equity in MFIs. At the high end of the spectrum, banks create loan service companies or specialize in microfinance as a main business line.

While banks possess certain advantages such as their broad range of services, branch infrastructure, points of sale, and ownership of capital and resources to invest in technology and innovation, they face significant challenges in serving this market. These include the difficulties of reaching remote low-income clients and tailoring products that meet their needs. In addition, while bank accounts provide better security than holding cash, the fees, minimum balances, and limited accessibility and service quality involved still make them seem less attractive to these clients.

Capital markets provide an increasingly important source of funding for microfinance. By April 2007, there were already 76 Microfinance Investment Vehicles (MIVs) with over US\$2 billion in total funds under management combined. Most (86%) of these have less than US\$20 million under management with average loans to MFIs amounting to US\$1 million and yields ranging from 2% to 8% for commercial investors. Over four fifths of these MIVs' investments are in LAC and EECA. Almost half (47%) of MIVs' funds come from individual investors and foundations; 36% are provided by international financial institutions and 17% by institutional investors, including pension funds. The ten largest account for 67% of the total MIV market.

Following are three examples illustrating how MFIs' funding sources have expanded in the past few years through growing linkages with the mainstream financial sector, as financial institutions take advantage of opportunities in microfinance.

Example 1: BlueOrchard Loans for Development S.A. (BOLD)

Being the first ever rated microfinance collateralised debt obligation (CDO) for private placement, it had by 2007 grown into a US\$108 million fund offering fixed-rate 5-year funding to 21 MFIs in 13 economies. Approximately 20% of the portfolio is in local currency, with local rates fixed for a period of 5 years, and foreign exchange risks completely hedged for investors through local currency swaps.⁷ BOLD is the largest single commercial investment transaction yet in the history of microfinance.

Morgan Stanley was involved in structuring the investment product. The Dutch development bank FMO underwrote the entire subordinated note class. Two classes of senior notes (US\$42 million in AA-rated Class A Notes and US\$16 million in BBB-

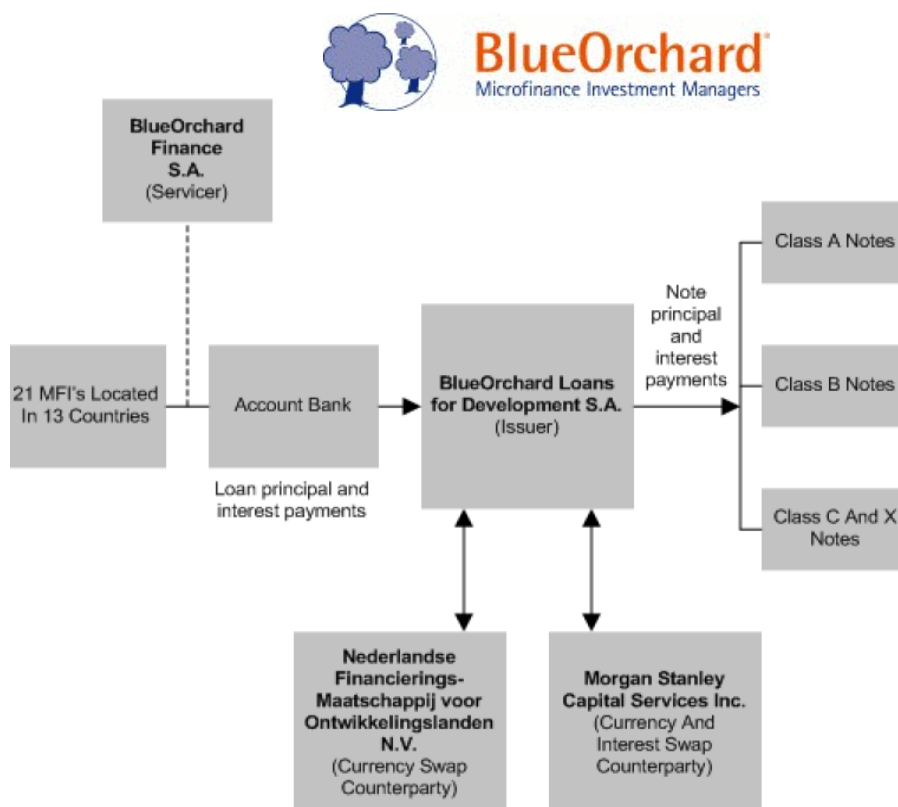
⁶ Branchless banking is bringing with it significant benefits along the value chain. For banks, it changes the economics of serving low-income clients, enables agent infrastructure to be leveraged to reduce capital expenditures while expanding services, and enables a rapid expansion of clientele. For agents, it increases walk-in business, reduces cash-on-hand and provides fee revenue from the bank. For clients, it provides greater comfort in dealing with familiar merchants and cost and time savings by offering proximity of service point.

⁷ Local currencies involved include Mexican peso, Colombian peso and Russian ruble. Non-local currency loans are in US dollars and euros.

rated Class B Notes denominated in US dollars, euro and British pound sterling protected by 61% and 46% of the total fund, respectively) were offered in fixed and floating rate tranches to mainstream institutional investors. The Class A Notes are listed in the Dublin Stock Exchange. (See Figure 1.)⁸

BOLD sets an example of development banks' role in capital market deals for microfinance. By taking the first loss position of the structure, FMO played an important role in attracting private investors to the deal. This CDO also set a milestone in broadening the microfinance investor base – traditionally made up of individual investors and foundations – by attracting mainstream investors, including large commercial banks that have not previously been involved in microfinance.

FIGURE 1: PROFILE OF BOLD TRANSACTION



Source: BlueOrchard (figure taken from presentation by Dr. Brigit Helms, IFC)

Example 2: The International Finance Corporation's Global Microfinance Facility Ltd (GMF)

The Global Microfinance Facility (GMF) was created in 2004 by the IFC together with the Kreditanstalt für Wiederaufbau (Germany) and Cyrano Management (an investment management firm based in Lima, Peru). It was established to help MFIs gain access to medium-term local currency funding from banks by providing credit enhancement products, such as standby facilities (letters of credit, letters of guarantee and direct funded loans or deposit products) at commercial terms through local commercial banks.

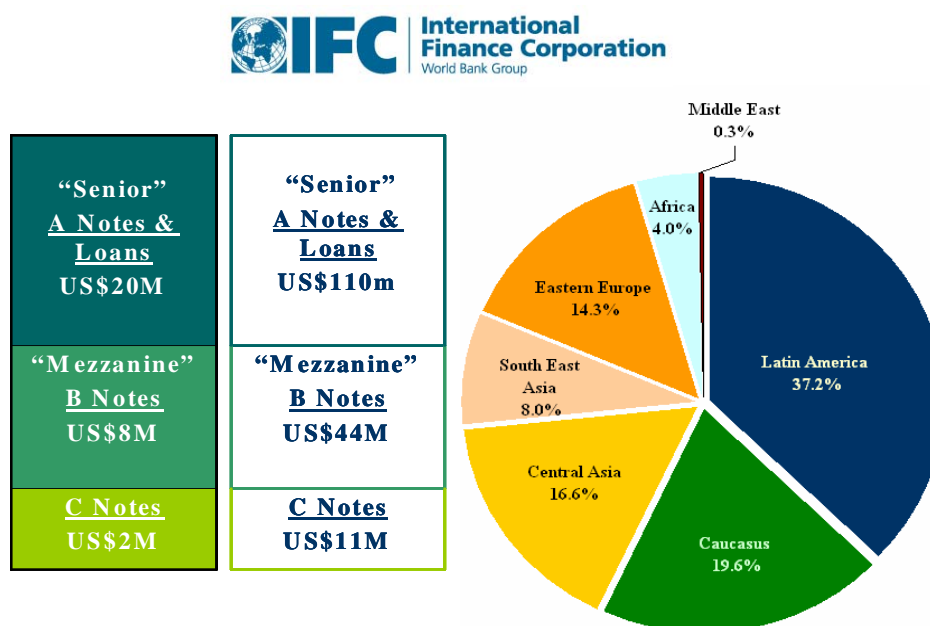
The Netherlands IFC Partnership Program provided a US\$2 million grant for GMF's first loss tranche, together with US\$100,000 from Cyrano, which manages the facility. A mezzanine B tranche funded by IFC and KfW totalling US\$8 million and a Senior A

⁸ See also information provided by Microfinance Information eXchange (MIX) in its website.

tranche partly funded by BIO (Belgium) and Credit Cooperatif (France), with the rest funded as part of a second closing, totalling US\$20 million, complete the US\$30-million Facility's structure. By 2007, GMF was providing funds for 17 MFIs in 10 economies with an average loan size of US\$1.8 million, generating some of the highest returns in microfinance.

The second phase of GMF involved additional investment to reach an asset base of US\$165 million, with the funding structure composed of US\$110 million in senior notes and loans, US\$44 million in mezzanine notes and US\$11 million in equity. The IFC's investment includes direct investment in equity, mezzanine notes and a stand-by liquidity facility for the senior debt to be issued by a partner private bank, which will act as arranger for private placement in the US. The portfolio targets 38 MFIs in 17 economies and an average loan size of US\$4 million. GMF II will be the second ever rated collateralized debt obligation (CDO) in the microfinance industry. The EECA (with 50%) and Latin America (with 37%) receive most of the funding provided by GMF. (See Figure 2.)

FIGURE 2: PROFILE OF THE IFC'S GLOBAL MICROFINANCE FACILITY



Source: IFC (figure taken from presentation by Dr. Brigit Helms, IFC)

GMF combined grants and commercial resources to alleviate MFIs' foreign exchange risk, a major problem for many MFIs that have been depending on hard currency loans to fund the growth of their local currency loan portfolios. Through partnership with a major private bank to enable distribution of investment paper issued by the Fund to a wider circle of investors, GMF II provides an example of how private banks can enter the market and promote microfinance globally as a profitable asset class. It also provides a model for commercial funding to help scale up MFIs and attracting other private and commercial investors to invest in the microfinance sector.

Example 3: Banco Compartamos, S.A., Institución de Banca Múltiple

Founded in Mexico in 1990 as an NGO with capital of US\$50,000 to offer credit for microenterprises, Compartamos has grown to become an MFI with a net worth of US\$126 million serving 616,000 borrowers by the end of 2006.

Compartamos became the first MFI to issue debt on the stock market with its own collateral and become a bridge between large investors and low-income borrowers. In 2004, through an IFC credit-enhanced bond program, it launched the first

microfinance rated bond targeting institutional investors. A first tranche issue amounting to MXP190 million in 2004 was followed by a second in 2005 amounting to MXP310 million.

In 2006, Compartamos was authorized to operate as a bank. In 2007, it became the first Latin American MFI to raise equity capital through an initial public offering on the Mexican stock exchange raising \$407 million. IFC sold 11,302,644 shares (25% of IFC's original holding) at MXP40 per share, earning \$38.9 million in proceeds.

B. THE PATH TO COMMERCIALLY SUSTAINABLE MICROFINANCE: THE LATIN AMERICAN EXPERIENCE

Latin America currently leads other developing regions in the development of commercially sustainable microfinance. MFIs in Latin America tend to have larger average loan size (US\$1,148 compared to US\$371 in Asia and US\$516 in Africa) and larger gross loan portfolio (US\$42.4 million compared to US\$35.9 million in Asia and US\$11.5 million in Africa), as of 2006. They are also the most well-capitalized, with a capital to asset ratio of 34.4% compared to 21.8% for Asian MFIs and 32.9% for African MFIs, and a commercial funding to liabilities ratio of 64.8%, compared to 74% and 74.1% for Asian and African MFIs, respectively, as of 2006.

Penetration rates vary greatly within the region, with Bolivia (37%), Peru (24%) and Guatemala (23%) at the high end, Honduras (14%), Mexico (12%) and the Dominican Republic (10%) at the middle, and Brazil (2%), Argentina (1%) and Venezuela (1%) at the low end.⁹ The importance of microfinance within the overall financial system also varies widely, as measured by the ratio of MFI loans to total financial system loans, which reaches 21% in both Bolivia and Nicaragua, 14% in Peru, 7% in Ecuador, 4% in Colombia, 2% in Guatemala and 1% in Mexico.¹⁰

Real active interest rates fell in many cases within the 25%-35% range (data for 2005), although going as low as 21.6% (in the case of Bolivia) and as high as 77% (in the case of Mexico). Operating expenses as a ratio of the gross loan portfolio hovered mostly within the 16%-19% range during the same period, although going down to as low as 15.4% (in the case of Bolivia) rising to as high as 26% (in the case of Mexico).

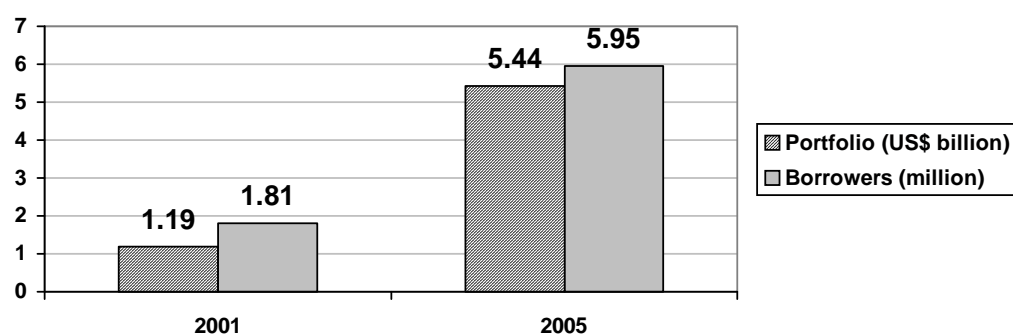
Microfinance in Latin America is currently the fastest growing and the least risky among the world's developing regions. As an industry within the financial sector, microfinance has generally outperformed the banking industry in developing regions, with Latin America's MFIs returning an average of 4.1% on assets. (Refer to Chart 2 above.)

Microfinance in Latin America and the Caribbean has grown considerably in the last few years, with portfolios growing 46% and the number of borrowers 35% annually on average between 2001 and 2005. By the end of this period, total portfolio has reached close to US\$5.5 billion and the number of borrowers almost 6 million. (See Chart 3) The bulk of this growth has come from regulated MFIs, which have benefited significantly from lower funding costs as a result of initiating deposit-taking activities and being rated, and now account for most the business (81% of total MFI portfolio and 64% of all MFI clients in the region by 2005).

⁹ S. Navaja and L. Telerina, *Microfinance in LAC: Connecting Supply and Demand* (Washington, IDB 2006), as described in the presentation of Mr. Hiroshi Toyoda.

¹⁰ Citigroup Investment Research (2007) and data from Microfinance Information eXchange (MIX), as described in the presentation of Mr. Hiroshi Toyoda.

CHART 3: LAC: GROWTH OF PORTFOLIO AND NUMBER OF BORROWERS



Source: S. Navaja and L. Tejerina, *Microfinance in LAC: Connecting Supply and Demand* (IDB, 2006), (chart taken from presentation by Mr. Hiroshi Toyoda, IDB)

The high loan portfolio quality of Latin American MFIs is illustrated in Table 2, which compares the performance of upgraded MFIs (nongovernmental microfinance organizations that have been transformed into formal financial institutions supervised by banking authorities) and the financial sector average, using data as of September 2005. Using PaR30 (outstanding value of loans with payments past due as percentage of the total portfolio) as an indicator of financial strength, MFIs performed better than the banking sector as a whole in their respective markets, with an average of 2.72% compared to the financial sector average of 4.34%.

TABLE 2: PERFORMANCE OF UPGRADED MFIS COMPARED TO RESPECTIVE DOMESTIC FINANCIAL SECTOR AVERAGES (%)*

Economy	Institution	PaR 30**	ROA	ROE	Op expense/ Avg portfolio
Bolivia	Banco Los Andes ProCredit, Bolivia	1.95	0.60	8.00	12.50
	BancoSol	5.40	1.30	11.00	12.60
	Financial sector average, Bolivia	13.68	0.42	4.21	6.85
Colombia	FinAmerica	4.20	1.90	11.30	16.30
	Financial sector average, Colombia	3.15	2.66	24.50	9.35
El Salvador	Banco ProCredit, El Salvador	2.07	1.30	10.00	12.50
	Financial sector average, El Salvador	2.16	1.05	9.64	4.62
Mexico	Compartamos	0.60	20.00	54.00	35.60
	Financial sector average, Mexico	1.99	1.91	15.69	5.08
Nicaragua	Banco ProCredit, Nicaragua	1.89	4.00	25.10	15.90
	Financial sector average, Nicaragua	2.38	2.17	26.80	9.55
Peru	MiBanco	2.99	5.80	33.90	18.80
	Financial sector average, Peru	2.68	1.53	21.28	6.81
Average	MFIs	2.72	4.99	21.90	17.70
	Financial sector average	4.34	1.62	17.02	7.04

Source: Mexico: CNBV (2005); Nicaragua: FELABAN (2005, October); other economies: FELABAN (2005, September); as presented in Marguerite Berger, Lara Goldmark and Tomas Miller-Sanabria, *An Inside View of Latin American Microfinance* (Washington DC, IDB 2006).

*Data is as of September 2005.

**Portfolio at risk for more than 30 days, estimated by adding the past due loan portfolio and loans in legal recovery and calculating them as a percentage of the total portfolio.

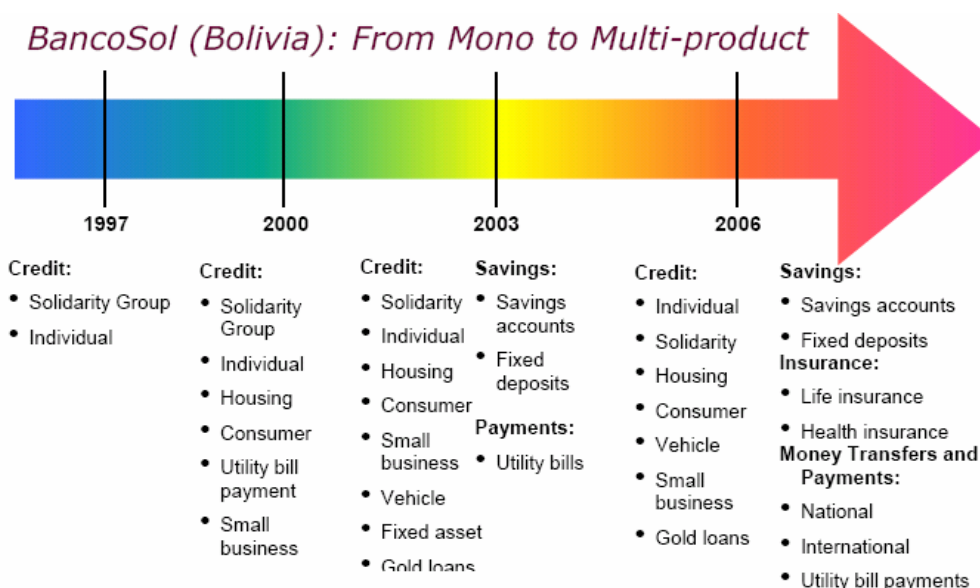
A number of factors accounted for upgraded MFIs' better performance compared to commercial banks in their economies, especially in terms of weathering and recovering from economic crises. First, the microfinance market is not as seriously affected as traditional banks by financial crises due to the general resilience of microenterprises that concentrate on domestic markets. Second, policies for bad debt provisions in upgraded MFIs are generally stricter than those established by supervisory authorities, as a result of changes in management, credit policies and methodologies introduced during the process of upgrading to formal financial institutions.

These MFIs also registered higher returns on assets and returns on equity compared to their respective domestic financial sector averages, although there is wide variation in the level of profitability of institutions across economies. Factors that account for these variations include government policy (e.g., government-imposed interest rate ceilings in Colombia) and varying degrees of exposure to political instability, financial crises and natural disasters. However, the experience of Latin America (particularly in Bolivia during a period of significant political and economic instability) demonstrates that upgraded MFIs are better able to withstand economic shocks than most financial institutions.

Surveys undertaken by the IDB and the Latin American Federation of Banking Associations indicate that microfinance industry is undergoing a transformation from specialized institutions to specialized products that a variety of financial institutions can offer. It is attracting increasing interest among commercial banks in the region. In a recent (2007) survey by Encuesta Online, 62.5% of a total of 320 respondents indicated that they consider microfinance to become the next major banking product in Latin America.¹¹

This transformation and growing interest of mainstream financial institutions in microfinance is being driven by increasing competition, which is exerting downward pressure on interest rates and transaction costs, encouraging wider area coverage and spurring innovations, including new products and services and cross-selling as well as the use of new technology and delivery mechanisms. The rapid evolution of Bolivia's BancoSol from a mono- to a multi-product institution within a period of ten years reflects this trend. (See Figure 3.)

FIGURE 3: THE EVOLUTION OF BOLIVIA'S BANCO SOL, 1997-2006



Source: E. Rhyne and M. Otero (2006), *Microfinance through the Next Decade: Visioning the Who, What, When, Where and How*.

Starting out in 1997 as an institution providing loans to solidarity groups and individuals, BancoSol first expanded the coverage of its business in 2000 to include housing, consumer and small business loans and utility bill payments. In 2003, it added vehicle, fixed-asset and gold loans, and introduced savings and fixed-term deposit accounts. In 2006, BancoSol expanded to life and health insurance and domestic and international money transfers and payments.

¹¹ América Economía, 29 October 2007

Remittances have recently attracted growing interest in Latin America. Remittance flows to the region has rapidly increased from US\$38 billion in 2003 to US\$62.5 billion by 2006, 75% of which originates from the US. These flows are equivalent to almost 9% of the region's total exports and exceed the amount of incoming foreign direct investment and official development assistance put together.

The continued growth of remittances to Latin America has significant implications for MFIs. There is substantial evidence that this process will be able to help large numbers of families in the region to access a variety of financial services. Receivers of remittances are also potential clients for microfinance services. Surveys indicate that a growing number of remittance senders intend to invest in the region, especially in health and life insurance, and home construction, mortgage, business and university loans.

Specialized investment funds play an increasingly important role in the establishment and upgrading of MFIs and in expanding the portfolios of traditional financial institutions offering microfinance products. Profund, the first microfinance-oriented investment fund with a financial return objective was established to invest in Latin American MFIs, leading the way for the over 40 microfinance investment funds worldwide that are now providing much of the capital for leading private MFIs. While international financial institutions such as the IFC and the IDB's Microfinance Investment Fund (MIF) and public investment funds or banks still play key roles, private sector participation is clearly growing.

C. ADDITIONAL CONSIDERATIONS

In addition to the above, other participants put forward the following issues during the discussions:

Importance of understanding the market. Developing the full potential of microfinance requires a realistic understanding of the market at the bottom of the pyramid. The low-income borrower, who is usually perceived as a victim, is in fact often pragmatic, resourceful and enterprising, and in many ways adept in confronting difficulties – a reality that underscores the tremendous potential of the market. This market is not homogeneous and has to be segmented both vertically (across stages of market and institutional development) and horizontally (taking into consideration the existence of low-income sectors within wealthy economies).

The growing involvement of the private sector is helping to transform and further develop the industry, especially at the level of mature MFIs. However, keeping in mind the characteristics (particularly the recognition of microfinance's social objective and partnership aspects) that have contributed to success at the early stages of market and institutional development and taking appropriate care in approaching this sector are important for the sustainable expansion of the market, especially as institutions continue to reach out to communities that are yet unserved. This would involve being able to offer a wide array of options of products and services across the various segments of the market corresponding to varying levels of development and risks and identifying policies, regulations, standards and protocols to effectively protect the interests of creditors and borrowers in this sector.

Effectively harnessing new technology. The growing role of new technology in microfinance underscores the importance and urgency of addressing issues related to these new technologies, such as those involving digital identities, security and the use of open architecture. It also requires greater efforts at capacity-building and education to promote more effective use of new technologies in emerging markets.

Defining microfinance and its scope. It is important to keep in mind the correct definition of microfinance in order to identify effective measures to promote its

growth. First, even as the borders between it and mainstream finance is blurring, microfinance is still essentially different from SME financing, and requires a different set of policy and development approaches. Second, there is yet no single internationally accepted definition of microfinance, given the wide variety of markets worldwide where it exists. Third, microfinance has gone beyond merely financing micro-enterprises, but now encompasses a wide range of business lines including consumer finance, insurance, savings, money transfers and others, reflecting the variety of opportunities at the bottom of the pyramid.

Promoting access to capital markets. Microfinance is increasingly being seen as an attractive asset class by investors. Securities backed by loans to MFIs, which have generally good financial and loan performance, offer geographic diversification with low volatility and low correlation as well as an absence of default, so far, from the experience of microfinance investment vehicles (MIVs).

MIVs that play important roles in linking MFIs to capital markets have been more active generally in Latin America and Eastern Europe than in Asia. The main factor has been the presence of more commercially-oriented and regulated MFIs in these regions. This points to the importance of an enabling environment for the emergence and development of such institutions throughout the region to expand the sector's linkage to capital markets.

III. THE POLICY AND REGULATORY ENVIRONMENT FOR FINANCIAL INCLUSION IN ASIA-PACIFIC EMERGING MARKETS

A. THE POLICY AND REGULATORY ENVIRONMENT FOR MICROFINANCE: LESSONS FROM THE PHILIPPINE EXPERIENCE

From directed credit programs to the National Strategy for Microfinance. A consideration of the Philippines' experience provides insights on how governments deal with various policy and regulatory issues in promoting the development of microfinance and the lessons learned in the process. The Philippines has had a long experience in dealing with these issues, starting in the 1960s when various directed credit programs were initiated to address the problem of unequal access to credit and the exclusion of particular segments of society, especially in the agriculture sector, from the credit market. The proliferation of these programs through the next three decades, however, failed to provide sustainable and effective solutions, and instead resulted in large losses to the government arising from subsidies and administrative costs, as well as in distortions in the credit markets.

Calls for a more consistent enabling credit policy environment led to the formulation by the National Credit Council of the National Strategy for Microfinance in 1997. This strategy veered away from active participation of government line agencies in the implementation of credit and guarantee programs. Instead, it focused on the provision of an enabling policy environment and capacity-building, the adoption of market-oriented financial and credit policies (including the use of market-oriented interest rates), and enhancing the role of private MFIs in the provision of financial services to low-income groups.

In support of this strategy, the government enacted laws and issued various executive orders and agency circulars. These provided for the rationalization of government-directed credit programs; capacity-building assistance to MFIs that did not involve seed funding, equity infusion or partnership funds from the government; a purely wholesale role for government financial institutions; the promotion of sustainable, community-based private MFIs, an emphasis on savings mobilization; and a recognition of the peculiar characteristics of microfinance.

The current environment for microfinance. There are presently three major types of providers of retail microfinance services in the Philippines: (a) microfinance cooperatives (numbering about 50 significant ones); (b) NGOs with microfinance operations (numbering about 500, with 30 conducting sizeable programs); and (c) rural and thrift banks (numbering over 200). Cooperatives typically provide savings, credit and remittance services to group members, NGOs provide credit, insurance and remittance services, while banks provide mainly savings and credit to the general public. Banks can engage in microfinance by establishing a microfinance-oriented bank, a microfinance-oriented branch, or by offering microfinance as one of its products.

MFIs currently reach around 3 million clients in the Philippines, estimated to comprise two-thirds of the potential market. The landscape of microfinance in the economy is rapidly undergoing major changes, with an expanding range of financial services, a shift away from directed credit and donor dependence toward more market-oriented approaches and financially self-sufficient institutions, a change in emphasis from evolving programs to evolving institutions, and growing commercialization with the entry of new players.

The regulatory framework. The Philippines' regulatory framework for microfinance covers all types of MFIs, whether bank or non-bank. Deposit-taking institutions, including microfinance NGOs that collect savings beyond the compensating balance, are subject to prudential regulation and supervision, which focus on portfolio quality, outreach, operational efficiency and sustainability, and information transparency.

A number of institutions comprise the regulatory structure. The Cooperative Development Authority is the regulatory authority for credit cooperatives. The central bank (Bangko Sentral ng Pilipinas) regulates and supervises all banks including those with microfinance operations. The Framework also envisions the Microfinance Council of the Philippines, a network of microfinance institutions, to serve as the repository of information for microfinance NGOs. NGOs are not supervised but need to register with the Securities and Exchange Commission.

Performance standards. A uniform set of standards was developed for all MFIs that is applicable to the peculiarities of each institution. These were designed for use by regulators, investors, donors, creditors, policy makers and as internal tools for MFIs themselves, and could be used for a rating system that may eventually be developed for the microfinance industry. These standards, with the acronym PESO, consist of portfolio quality, efficiency, sustainability and outreach. Portfolio-at-risk (PaR) is used as a measure of portfolio quality, while the other three components use other applicable ratios. PaR is the outstanding principal amount of all loans that have at least one instalment past due.

Central bank regulation and supervision. The General Banking Law of 2000 mandates the central bank to set the rules and regulations for microfinance within the banking sector. The law also specifically mandates the recognition of peculiar characteristics of microfinance, which include unsecured and cash flow-based lending, frequent amortization and market-based interest rates.

The central bank's policy approach is governed by the objectives of allowing banks to have a wider scope for sustainable microfinance operations and protecting the interests of depositors and microfinance clients and the financial system as a whole. The central bank follows a three-pronged approach, which focuses on the development of a microfinance-friendly policy and regulatory environment, capacity-building through microfinance training within the central bank and the banking sector, and promotion and advocacy.

The central bank has issued to date 14 circulars providing incentives and setting rules and regulations. These cover a wide variety of topics, including the definition of microfinance loans, allowing the establishment of microfinance-oriented banks and branches, opening of the rediscounting facility, adoption of best practices, involvement of large banks in microfinance and liberalized branching to expand outreach to those yet unserved by the banking sector. They also include measures to promote innovation and flexibility in the delivery of microfinance services, such as the approval of the use of microfinance technology to provide other financial products, including micro-agriculture finance, and the use of ICT.

Within the central bank, a high level Microfinance Committee is responsible for all its policies and programs concerning the industry. An Inclusive Finance Advisory Staff under the Office of the Deputy Governor implements and coordinates various programs and initiatives that promote increased financial inclusion. The central bank also has a Microfinance/SME Finance Specialist Group which is in charge of the supervision and examination of the microfinance operations of banks.

Capacity-building and training programs are being implemented to develop the industry. An active promotion and advocacy program involves information campaigns to improve knowledge and skills in the industry, the creation of networks and linkages to support cooperation and partnerships among stakeholders, as well as other initiatives to promote business development and financial literacy.

The introduction of the new strategy, regulatory framework, performance standards and supervisory approaches has led to the steady development of microfinance in the Philippines. There are now 227 rural, cooperative, thrift and microfinance-oriented banks operating in the Philippines with over 860,000 borrowers and a combined loan portfolio amounting to PHP6billion and collecting over PHP 2 billion in savings from microfinance clients. Commercial banks are increasingly entering the market generally by providing wholesale loans to retail microfinance institutions.

The openness of the Bangko Sentral to innovation has proven very beneficial for the industry. At present, new microfinance products such as Micro-Agri Products and Housing Microfinance Products have been approved by the BSP in response to the specific needs of microfinance clients. Banks are also increasingly using ICT in their operations, which now include mobile phone micro-payments, deposits and withdrawals, among others.

Lessons from the Philippine experience. In pursuing the development of microfinance, policy makers and government officials faced and were able to overcome three sets of challenges. The first was related to the paradigm shift from directed credit and government lending to market-driven private sector lending. The second was related to misconceptions about microfinance, such as mistaken beliefs that low-income borrowers are unable to pay, costs are too high or microfinance operations are not viable, among others. The third was related to the existence of legal and regulatory barriers.

The Philippine experience provides a number of useful lessons for policy makers. The first is that strong private sector collaboration from the beginning is needed to succeed in pushing for critical reforms. Such reforms would then encourage greater private sector participation in microfinance, ensuring a more competitive and sustainable environment. The second is that success can be achieved through less government intervention and a greater emphasis on creating an enabling environment that address legal and regulatory barriers. The third is that capacity-building assistance is more important for MFIs than subsidized credit funds. The fourth is that setting performance standards is very useful for the development of microfinance.

Future challenges. With the creation of an enabling environment and the establishment of a firm foundation for growth, Philippine policy makers are focusing their attention on a number of future challenges that will need to be addressed. The first is the threat of policy reversals, including a politically-motivated return to the use of subsidized credit programs. The second is insufficient access of microfinance clients to support services such as training, business development and financial literacy. The third is inadequate capacity of MFIs with respect to internal controls, governance structures, ability to access commercial funds, lending methodology and technology and support networks. The fourth is the lack of sharing of credit-related information through a comprehensive credit bureau.

MFIs will continue to face the challenges of continuously adapting to new technology and developments in the market as well as adopting innovations in products and services. There is also still a long way to go in reaching population segments that are yet unserved by the financial sector, especially in the Philippines' many remote rural areas.

B. CREATING AN ENABLING POLICY AND REGULATORY ENVIRONMENT FOR FINANCIAL INCLUSION

Microfinance is fundamentally being transformed by an increasing flow of capital (as it evolves from a donor-driven NGO-dominated sector to one characterized by growing linkages to capital markets) and by the introduction of technological innovations. These trends have also generated an increasing recognition of the role of policy, in response not only to their regulatory implications but also to the opportunities they bring in helping promote financial inclusion.

Policies are understood in this sense as the measures that government can undertake to influence financial markets. They can take the forms of legislation, regulation, enforcement, expenditures (such as with respect to financing public goods), or direct participation in the market through state-owned enterprises. An enabling policy environment should address key issues in three important areas: (a) types of financial services; (b) information and communication technologies; and (c) the number of market players and delivery channels.

A study undertaken by GTZ in cooperation with the Bill and Melinda Gates Foundation examined various alternative policy measures to promote financial inclusion in a number of economies. The following are among the key findings of the study:

- Regulatory reform efforts that have met with success benefited from prior substantial improvements in the financial sector environment.
- New regulations only make sense if there is a perceived opportunity to profit from an additional supply of financial services.
- Regulation is a useful policy solution whenever the benefits of access to cheap domestic savings outweigh the additional costs for supervisory and supervised entities.
- Relaxing branching regulations can be a powerful and economical alternative to the introduction of specific microfinance regulations.
- The use of information and communication technologies can have a substantial impact on access for clients who have been previously excluded from the financial sector.
- Well-governed and commercially oriented public banks can play an important complementary role in promoting financial inclusion.

- Access to finance can rapidly expand in the absence of formal regulation up to a certain point, but policy makers and regulators will eventually catch up and undertake regulatory initiatives in order to keep risk under control.

Among 35 policy tools for promoting financial inclusion that have been considered in the study, **six effective sets of access policy solutions** have been identified as the most critical for accelerating reforms toward financial inclusion:

1. **Agent banking:** The first set refers to policies and regulations governing correspondent banking agents, or agents from the non-bank sector such as retail commercial outlets including lottery kiosks, pharmacies, post offices and the like, which establish partnerships with banks to provide distribution outlets for financial services. The important role that agent banking can play in accelerating the process of financial inclusion is illustrated in the case of Brazil.

In 2000, there were over 1,600 municipalities – more than a quarter of Brazil's municipalities – without access to banking services through bank branches or agents. By 2003, banking services had become available in all municipalities throughout the economy through an increase in the number of non-bank agents. By the end of 2004, 57 banks and 17 financial companies have established over 38,000 formally recognized correspondent outlets, which grew further to 90,000 formal and informal correspondents within another year.

2. **Mobile phone banking:** The second set of policy solutions involves policies that lower transaction cost and increase access to financial services through mobile technologies and services. Mobile phone banking now involves a host of features, including cash deposits and withdrawals, third-party deposits into a user account, retail purchases, over-the-air prepaid top-ups using cash in the user's account, transfer of cash or airtime credits between user accounts and bill payments.

Japan and Korea account for most current users of mobile phone banking. In the Philippines, there are presently over 4 million users of mobile financial services such as G-Cash and Smart Money. There is huge business potential, given the dramatic growth rates of mobile phone subscribers in many emerging markets. In India, mobile phone subscribers grew from less than 10 million to almost 180 million within a five-year period from 2002 to 2007. In the Philippines, the number increased from 6.5 million in 2000 to 46.5 million by 2007.

Mobile phone banking presents challenges to regulatory capacity, as it cuts across various regulatory domains including banking, telecommunications, payments systems and anti-money laundering.

3. **Diversifying providers:** The third set of policy solutions deals with policies that lower the regulatory barriers for start-ups and for offering savings and insurance products for low-income clients. In Indonesia, entry barriers to the financial sector were lowered through the establishment of rural banks, which are second-tier banks that now number 2,100 units holding 5.7 million deposit accounts and 2.5 million outstanding credit accounts.

In the Philippines, the Insurance Commission introduced a specialized regulatory and supervisory framework for microinsurance mutuals, which are income tax-exempt and require less from the guarantee fund. A total of 2 million households have gained access to formal insurance through this model.

4. **Reforming public banks:** A fourth relates to policies that improve the governance and management of state banks to help them provide more effective financial services, including commercially sustainable financial services. Bank Rakyat Indonesia (BRI) and its Village Units provide the best known example of a

large state bank that has succeeded in becoming a successful microfinance industry player. Today, BRI has over 4,000 outlets providing microcredit to 3.3 million clients with a total portfolio of US\$3 billion and serving over 30 million savings account holders.

5. **Financial identity regulations:** A fifth refers to policies that endow clients with a financial identity, oftentimes by transforming their transaction history into a financial asset, which they can use to leverage access to credit and other banking services. Regulatory frameworks would need to adopt a flexible approach to supporting the generation of financial identity, facilitating information sharing in the initial stages of development and introducing protective measures during the later stages that involve large-scale information processing.
6. **Consumer protection:** The final set of policy solutions cover policies that address technical and delivery security, reducing predatory lending or increasing disclosure of information, efficient dispute settlement, data protection and enhancing comparability of offers.

Moving forward on these fronts to provide an improved environment for financial access will require international cooperation. There is an important role that regional organizations like APEC can play in promoting the implementation of these policy solutions. Key measures that can be undertaken as part of regional cooperation are as follows:

- Advocating access policy initiatives to member economies.
- Providing regional platforms for mutual learning among market players and regulators, which is crucial in order to address traditional and valid concerns while creating space for regulatory innovation.
- Making more use of innovations already available in emerging financial markets through South-South cooperation in sharing experiences and knowledge.
- Promoting multiple channels for information dissemination, user discussion and user-initiated access among policy makers.
- Engaging international standard setters in an analysis of their impact on access.

IV: THE ROLE OF APEC IN PROMOTING FINANCIAL INCLUSION USING MICROFINANCE

A. GIVING MICROFINANCE A FRESH START IN APEC: FINANCIAL INCLUSION AS AN ISSUE FOR APEC FINANCE MINISTERS

Microfinance is not a new issue for APEC. During its chairmanship of APEC in 2002, Mexico initiated discussions on micro-banking and micro-enterprise development within the APEC Economic Committee (EC) and the SME Ministers' process. These discussions led to the endorsement by the SME Ministerial Statement of the role of microfinance in micro-enterprise development, as well as the endorsement by APEC Ministers of a comprehensive statement of principles on micro-banking development, regulation and supervision.

In the following years, however, microfinance took a back seat to other issues in the EC, while struggling unsuccessfully to fit into the agenda of the APEC SME Working Group. During this period, discussions focused on issues related to poverty, and microfinance came to be seen principally as a social welfare measure rather than a policy tool that could address the systemic problem of financial exclusion. This situation was reflected in the choice of participants and area expertise that were

brought to the table. Consequently, these discussions failed to win for microfinance an important place in APEC's economic and financial reform agenda.

However, it is appropriate to undertake a renewed approach to microfinance within APEC as an instrument for achieving the goal of financial inclusion. From the standpoint of objectives, increasing financial inclusion levels will contribute not just to distributional equity, but also to financial deepening, as savings facilities are extended to cover millions of low-income households and as these are linked more closely to banking systems and capital markets. From the standpoint of who should deal with this issue, success hinges on measures under the direct purview of finance officials and regulators, as well as the active involvement of the financial industry.

As microfinance continues to rapidly evolve, it is becoming an increasingly diverse enterprise extending far beyond the traditional NGO model. Microfinance services are now being provided by regulated financial institutions, both banks and non-banks, in addition to those offered by a host of others, including private for-profit entities, public-private partnerships, voluntary sector agencies and informal entities. Investment in MFIs by financial institutions and MIVs are growing. Microfinance products include not just credit, but now embrace deposits, remittances, payments, micro-insurance and pensions. The blurring of borders between microfinance and the formal financial sector requires policy and regulatory responses from financial officials and regulators.

Current initiatives under the Finance Ministers' process include activities to promote financial sector reforms and capacity-building. These reflect such concerns as the need to strengthen domestic financial systems and to reduce barriers to the flow of capital across borders. Less developed APEC economies benefit from efforts to help diversify financial systems, including the development of bond markets. However, the low levels of financial inclusion in many of these economies have so far not yet been addressed.

The incorporation of microfinance into the APEC Finance Ministers' agenda is justified by the need to address these low levels of inclusion as one of the central tasks of financial sector development, and by the significance of its potential impact on the development of banking systems and capital markets. Following are relevant thoughts on how the incorporation of microfinance into the Finance Ministers' agenda might be undertaken.

- The focus of such a new APEC initiative should be on **financial inclusion** as a policy goal, with **microfinance as an instrument** of choice to achieve that goal. While it is undoubtedly a powerful tool that can help address poverty and gender-related issues, it is important within the context of this APEC initiative to look at microfinance not as a social welfare measure, but primarily as part of APEC's suite of policy tools to advance its economic and financial reform agenda.
- APEC can best support microfinance and promote financial inclusion by promoting the capacity of member economies to provide **an enabling policy and regulatory environment** that facilitates appropriate pricing of products and services in accordance with risk and market conditions and development of ICT and financial products to reduce costs and expand coverage of microfinance. While governments may also extend direct judicious support measures, experience (including the Philippine experience discussed in the previous section) suggests that some well-intended measures do more harm than good. Examples of measures that should be avoided include direct government lending or providing resources for lending and packaging micro-credit schemes into projects in other sectors without regard for their validity as financial sector initiatives.

- There are many paths to increased financial inclusion, and the diversity of APEC provides an opportunity for member economies to learn from the experience of others. ***Policy dialogue and sharing of experiences*** are activities where APEC has a particular comparative advantage. In addition, considering the wealth of expertise and resources available outside APEC member economies and in various international financial and development institutions, an initiative on financial inclusion should allow for appropriate participation of such international organizations, institutions from relevant non-member economies, the private sector and non-governmental microfinance networks to support the work of APEC in this field.
- Such a new initiative could undertake work to improve the ***measurement of levels of financial inclusion*** in member economies. Much needs to be done with respect to improving the availability and quality of data on financial access in member economies. The World Bank's Finance and Private Sector Research program has published estimates of financial access for a number of economies, including 17 APEC member economies. Nevertheless, there is still much that APEC could do to ensure the collection of comparable data for member economies that are also suitable for policy analysis. Activities under this initiative could include (a) developing consensus on criteria for measuring financial inclusion; (b) regular publication of financial inclusion data; (c) comparative surveys of domestic policy frameworks addressing financial exclusion; and (d) documentation of initiatives in member economies, including those undertaken by government, private for-profit, voluntary, public-private and donor-sponsored institutions to increase the level of financial inclusion.
- ***Capacity-building to promote financial inclusion*** has an important role to play in an initiative within APEC, complementing ongoing work being done by international agencies active in the region. Capacity-building activities could focus on defining and disseminating best practice in policy and regulatory frameworks and institution-building, and on assisting member economies in their efforts to attain these standards, allowing them to demonstrate measurable progress toward agreed goals. Capacity-building activities could target both officials and financial professionals. An inclusion initiative may in the beginning be primarily of concern to developing economies; in time, however, it is expected to be useful and relevant for all.

B. PROMOTING FINANCIAL INCLUSION IN APEC: THE ROLE OF ABAC AND THE ADVISORY GROUP

ABAC and the Advisory Group on APEC Financial System Capacity-Building could play very important roles in promoting this initiative. It was suggested that ABAC seriously explore the issue of financial inclusion in APEC member economies, consider reporting on this subject to APEC Finance Ministers, and recommend that Ministers launch an initiative, which should clearly identify financial inclusion as its rationale, with microfinance as the policy tool of choice. ABAC was urged to also consider whether it may be appropriate to recommend to Finance Ministers that the dimension of inclusiveness be incorporated in all their policy initiatives, so that the concept of inclusion may be internalised within the process.

The Advisory Group could be an appropriate forum for ABAC to examine financial inclusion drawing on outside expertise and in collaboration with like-minded institutions, including international financial and development institutions and regional private sector organizations that participate in its work. The outcomes and recommendations arising from this work could be reviewed by ABAC and eventually communicated to Finance Ministers. Individual ABAC members could assist in

building a constituency in their respective economies in order to promote adequate sponsorship and strong support for the initiative.

Financial inclusion is a big idea that should appeal to APEC Finance Ministers and APEC Economic Leaders. It fits in very well with APEC's finance agenda, as well as its structural reform agenda. It also fits in very well with the 2008 ABAC theme under Peruvian chairmanship (minding the gap and making globalization an opportunity for all), and Peru's own achievements and wealth of experience in microfinance. In promoting an APEC financial inclusion agenda, ABAC should agree to have one or several members volunteer to champion this idea within APEC over an extended period, in the same way that the work of ABAC on bond markets was developed over the years.

Continuous involvement of the private sector, especially through ABAC, is also important for the proper design and development of the initiative. Private sector perspectives are valuable in dealing with a number of key issues that are important for microfinance to succeed. These issues include transparency, minimizing financial and political risk as well as financial market distortions, providing the right incentives for borrowers, and adjusting to local conditions, which would include, for example, the use of the Islamic banking framework. Private sector experience with the use of information and communications technology in microfinance could also be helpful in the development of a financial inclusion initiative.

V: CONCLUSION AND RECOMMENDATIONS

There was extensive agreement among participants on a broad range of issues that were discussed in the workshop. There was substantial agreement on the central importance of addressing the issue of financial inclusion, and on the general trends in the development of microfinance, its rapid transformation and expanding links to the formal financial system, and the increasing number of access points for clients. There was also much agreement on the growing roles of ICT and financial innovation, particularly in expanding the industry's reach and funding sources as well as in reducing administrative expenses, which account for the most significant portion of total costs.

The presentations and subsequent discussions highlighted the transformation of microfinance from specialized institutions to specialized products that a variety of financial institutions can offer. Latin America, which leads the developing world in terms of MFIs' growth and asset quality, provides examples of MFIs that are rapidly expanding their businesses from providing loans to individuals and microenterprises to a broad range of financial services. These services now include housing and consumer loans, utility bill payments, savings, fixed-term and deposit accounts, life and health insurance and domestic and international money transfers and payments.

There was a widely shared view that microfinance is attracting a growing number of financial institutions and investors due to a number of factors. Among these are the increasing profitability of upgraded MFIs, the high quality of their loan portfolios and their potential to develop a large market that still remains unserved or underserved by traditional financial institutions. In most regions and economies, these MFIs have performed above their respective domestic financial sector averages, especially as a consequence of their superior ability to withstand financial crises and stricter policies for bad debt provisions. For investors, securities backed by loans to MFIs offer geographic diversification with low volatility and low correlation, as well as high quality.

With these positive developments, participants agreed that microfinance has tremendous potential in addressing the issue of financial inclusion. In many developing economies, including within APEC, large portions of the population at the bottom of the economic pyramid have as yet no access to financial services. Harnessing microfinance to increase financial inclusion levels will promote not just distributional equity but also financial deepening, as savings facilities being progressively extended to more low-income households are increasingly linked more closely to banking systems and capital markets.

However, there was also broad agreement that there is still a long way to go in actualizing the full potential of microfinance as a tool to promote financial inclusion. There is an enormous need for capacity-building to enable large numbers of MFIs to upgrade their governance structures, management, internal controls, credit policies and methodologies, and to take advantage of opportunities arising from innovation and new technology. There is also a large demand for funding that international and domestic financial institutions, banks and capital markets could provide.

Participants shared the view that government has an important role to play in this process, which is to provide an enabling environment that addresses legal, policy and regulatory barriers in order to facilitate the development of microfinance and increase its access to commercial funds. This view reflects the shift from the previous paradigm of directed credit and government lending that have proven unsuccessful, wasted public resources and produced distortions in credit markets to the new paradigm of facilitating market-driven private sector lending.

To accelerate progress toward financial inclusion, it would be useful for governments to identify the most critical policy solutions. Participants endorsed the results of the study undertaken by the German Technical Cooperation that examined alternative policy measures to promote financial inclusion, and its identification of six sets of access policy solutions that governments in the region could consider. These refer to policies and regulations governing correspondent banking agents, mobile phone banking, entry barriers to the financial sector, the governance and management of publicly-owned financial institutions, financial identity regulations and financial consumer protection.

Participants also endorsed a number of important considerations for policy makers to take into account in ensuring the success of regulatory reforms, based on lessons from past experiences. Among these lessons are that: (a) regulatory reform is more successful where there has been prior substantial improvement in the financial sector environment; (b) new regulations only make sense if there is a perceived opportunity to profit from an additional supply of financial services; (c) regulation is useful if the benefits of access to cheap domestic savings outweigh the additional costs to supervisory and supervised entities; (d) relaxing branching regulations is a powerful and economical alternative to introducing microfinance regulations; (e) the use of ICT can have a substantial contribution to financial inclusion; (f) well-governed and commercially-oriented public sector banks can play an important complementary role in promoting financial inclusion; and (g) access to finance can rapidly expand in the absence of formal regulation up to a certain point, beyond which policy makers and regulators will need to step in to keep risk under control.

Finally, participants agreed that, considering its importance for spreading more widely the benefits of free and open trade and promoting broader support for trade and investment liberalization and facilitation, the issue of financial inclusion, with microfinance as an instrument of choice, should have a place in the APEC agenda, not as a social welfare measure, but as part of APEC's suite of policy tools to advance economic and financial reforms. On account of financial inclusion being a central task of financial sector development, its significance to the development of

banking systems and capital markets and the role that financial regulation and financial institutions would have to play in this process, its appropriate place should be within the APEC Finance Ministers' Process.

There was very broad support among participants for a financial inclusion initiative that would focus on providing an enabling legal, policy and regulatory environment through improvements in measuring levels of financial inclusion in member economies, policy dialogue and sharing of experiences and capacity-building activities. Participants were in agreement that strong private sector collaboration from the beginning is necessary for the successful design and implementation of critical measures, both at the regional and domestic level, and that a meaningful involvement of ABAC and the Advisory Group on APEC Financial System Capacity-Building in a financial inclusion initiative undertaken by the APEC Finance Ministers would be very desirable.

With these considerations in mind, participants agreed to make the following recommendations:

- ***That financial inclusion as a policy goal, with microfinance as an instrument of choice, be adopted by the APEC Finance Ministers as part of their agenda, and endorsed by the APEC Economic Leaders.***
- ***That the APEC Finance Ministers undertake activities to promote an enabling policy and regulatory environment, including measurement of levels of financial inclusion in developing member economies, initiation of capacity-building activities and holding of policy dialogues, drawing from the conclusions of this report and with special attention to the following key areas that are relevant to the development of microfinance: (1) agent banking; (2) mobile phone banking; (3) increasing the diversity of microfinance service providers; (4) improving governance and management of public banks; (5) financial identity regulations; and (6) protection of consumer and creditor rights.***
- ***That the APEC Finance Ministers work closely with ABAC and the Advisory Group on APEC Financial System Capacity-Building in developing their financial inclusion agenda.***

APPENDIX A: WORKSHOP PROGRAMME

PROMOTING A FAVORABLE POLICY ENVIRONMENT FOR COMMERCIALY SUSTAINABLE MICROFINANCE

January 23, 2008

Krakatau Room, The Grand Hyatt Jakarta
Jakarta, Indonesia

- 8:30 am **Opening Remarks**
Jeffrey L.S. Koo, Chair, Advisory Group on APEC Financial System Capacity-Building and Chairman, Chinatrust Financial Holding Co Ltd
- 8:35 **Introductory Remarks**
Michael Phillips, Chair, ABAC Finance and Economics Working Group and Chairman, Russell Investment Group
- 8:40 **Session One: The Evolution and Current Situation of Microfinance**
Session Chair: Julius Caesar Parreñas, Coordinator, Advisory Group on APEC Financial System Capacity-Building

Overview presentation
Brigit Helms, Sector Leader, Access to Finance, East Asia and the Pacific Department, IFC

Microfinance: The Latin American Experience
Hiroshi Toyoda, Special Advisor for Asia, Inter-American Development Bank

Beris Gwynne, Collaborative for Global Development
Palgunadi Setyawan, Chairman, PT Asialab Indonesia
- 9:50 Coffee break
- 10:10 **Session Two: The Policy and Regulatory Environment**
Session Chair: Kenneth Waller, Senior Adviser, ABAC Australia

Overview presentation
Alfred Hannig, Director of Sustainable Economic Development Programs in Indonesia, German Technical Cooperation (GTZ)

Ms. Leny I. Silvestre, Managing Director, Supervision and Examination I and Microfinance Committee Member, Philippine Central Bank (BSP)
- 11:20 **Session Three: The Role of APEC in Promoting Microfinance**
Session Chair: Twatchai Yongkittikul, Member, ABAC Thailand and Secretary General, Thai Bankers' Association

John Conroy, Special Consultant, The Foundation for Development Cooperation

Mark Johnson, Chairman, Australian Gas Light Company

Rudjito, Chairman of the Board of Commissioners, Indonesia Deposit Insurance Corporation (IDIC)

Jeff Dowle, Executive Vice President, HSBC Bank Canada

12:20

Closing Remarks

Yoshihiro Watanabe, Co-Chair, Advisory Group on APEC Financial System Capacity-Building and Chief Risk Officer, Mitsubishi UFJ Financial Group

APPENDIX B: LIST OF ABBREVIATIONS

ABAC	APEC Business Advisory Council
APEC	Asia-Pacific Economic Cooperation
ATM	Automated teller machine
BOLD	BlueOrchard Loans for Development
BRI	Bank Rakyat Indonesia
BSP	Bangko Sentral ng Pilipinas (Central Bank of the Philippines)
CB	Central bank
CDO	Collateralized debt obligation
CNBV	Comisión Nacional Bancaria y de Valores (National Banking and Exchange Commission)
EAP	East Asia and Pacific
EC	Economic Committee
EECA	Eastern Europe and Central Asia
FDC	Foundation for Development Cooperation
FELABAN	Federación Latinoamericana de Bancos (Latin American Federation of Banks)
FEWG	Finance and Economics Working Group
FMO	Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden (Netherlands Development Finance Company)
GMF	Global Microfinance Facility
GTZ	Gesellschaft für technische Zusammenarbeit (German Technical Cooperation)
ICT	Information and communications technology
IDB	Inter-American Development Bank
IDIC	Indonesia Deposit Insurance Corporation
IFC	International Finance Corporation
KfW	Kreditanstalt für Wiederaufbau (Reconstruction Credit Institute)
LAC	Latin America and Caribbean
MENA	Middle East and North Africa
MFI	Microfinance institution
MIF	Microfinance Investment Fund
MIV	Microfinance investment vehicle
MIX	Microfinance Information eXchange
NGO	Non-governmental organization
PaR	Portfolio at Risk

PDA	Personal digital assistant
PESO	Portfolio quality, Efficiency, Sustainability and Outreach
POS	Point-of-sale
ROA	Return on assets
ROE	Return on equity
SME	Small and medium enterprise
SSA	Sub-Saharan Africa