

PHILIPPINES

MICROFINANCE INDUSTRY REPORT



Citi Foundation



Microfinance Industry Report
Philippines
2010

Published by the Microfinance Council of the Philippines, Inc.
In collaboration with the SEEP Network

Funded by the Citi Foundation as an activity of the Citi Network Strengthening Program



Citi Foundation



Acknowledgements

The 2010 Philippine Microfinance Industry Report was written by Dr. Ma. Piedad Geron under the direction of the Microfinance Council of the Philippines, Inc. (MCPI). The report was also a result of an unpublished industry assessment report written by Mr. Joel Umali in 2008.

MCPI would like to thank all those who participated in the production of the 2008 and 2010 reports, including representatives of the Bangko Sentral ng Pilipinas (BSP), the Rural Bankers Association of the Philippines (RBAP), the Microenterprise Access to Banking Services (MABS) Program, and the Cooperative Development Authority (CDA). Special thanks to Dr. Gilbert Llanto and Ms. Kelly Hattel for reviewing the report.

- List of Acronyms • 3**
- Executive Summary • 4**
- Background and Purpose • 6**
- The Philippines: General Overview • 6**
 - Geographical location • 6**
 - Demographics • 6**
 - Economic Growth • 7**
 - Labor and Employment • 7**
 - Poverty Situation • 7**
- The Philippine Financial Sector • 8**
 - The Formal Financial System • 8**
 - Overview • 8
 - Performance • 8
 - Informal Finance • 10**
- The Philippine Microfinance Sector • 11**
 - The Development of the Microfinance Sector • 11**
 - The Beginning • 11
 - Changes Adopted: Microfinance Policy Initiatives • 11
 - The Providers of Microfinance Services • 12
 - The Regulatory Environment for Microfinance Institutions • 13**
 - The Regulatory Framework for Microfinance • 13
 - The Performance Standards for Microfinance Operations • 15
 - Microfinance Sector Performance • 15**
 - Retail Microfinance Institutions • 15
 - Wholesale Microfinance Institutions • 16
 - Meso-level Support to the Microfinance Sector • 17**
 - Establishment of a Credit Bureau • 17
 - Microfinance Associations and Councils • 17
 - Microfinance Technical Assistance and Support Service Providers • 19
 - Recent Developments and Innovations • 20**
 - Mobile Banking • 20
 - Most Recent Microfinance Products • 20
 - Social Performance Management • 20
 - Business Development Services (BDS) • 22
 - Partnership between Microfinance Institutions and PhilHealth (KASAPI) • 22
 - Responding to the Challenge of Risk Protection: Microinsurance • 22**
 - The National Strategy and the Regulatory Framework for Microinsurance • 22
 - Recent and On-going Developments for Microinsurance Development • 23
 - Donor Support to the Microfinance Sector • 23**
- Remaining Challenges for the Microfinance Sector • 25**
 - Addressing Multiple Borrowing • 25**
 - Looking for the Right Design for Financing the Poor in Agriculture • 25**
 - Protecting Microfinance Clients • 25**
 - Graduating Microfinance Clients: The Missing Middle • 26**
 - Regulating and Supervising Cooperatives Engaged in Savings and Credit Operations • 26**
 - Managing Mission Drift • 27**
- References • 28**
- Annex A. Policy Reform Measures Adopted • 29**
- Annex B. Minimum Capitalization Requirements • 30**
- Annex C. List of BSP Circulars Related to Microfinance • 31**
- Annex D. Performance Standards for Microfinance • 32**

ACPC Agricultural Credit Policy Council	MOB Microfinance Oriented Banks
ADB Asian Development Bank	MORR Manual of Rules and Regulations
AIM Asian Institute of Management	MSME Micro, Small and Medium Enterprises
ASKI Alalay sa Kaunlaran Inc.	MSP Microfinance Support Project
BDS Business Development Services	NAPC National Anti-Poverty Commission
BEMO Banks Engaged in Microfinance Operations	NATCCO National Confederation of Cooperatives
BMC Bicol Microfinance Council, Inc.	NBFIs Non-Bank Financial Institutions
BSP Bangko Sentral ng Pilipinas	NCC National Credit Council
CALF Comprehensive Agricultural Loan Fund	NGOs Non-Government Organization
CARE Cooperative for Assistance and Relief Everywhere	NSCB National Statistical Coordination Board
CARD Center for Agriculture and Rural Development	NSP Citi Network Strengthening Program
CCT Center for Community Transformation	NSSLAS Non-Stock Savings and Loan Associations
CDA Cooperative Development Authority	ODA Official Development Assistance
CISA Credit Information Systems Act	PCFC People's Credit and Finance Corporation
CLAM Central Luzon Association of Microfinance Institutions	PDAP Philippine Development Assistance Program
CLF Central Loan Fund	PFCCO Philippine Federation of Credit Cooperatives
CMDI CARD MRI Development Institutions	PhilHealth Philippine Health Insurance Corporation
CPP Client Protection Principles	PWRF Philippine Water Revolving Fund
CUES Credit Union Enhancement and Strengthening Program	RBAP Rural Bankers Association of the Philippines
CUMI Credit Union Microfinance Innovations Program	ROSCAS Rotating Savings and Credit Association
DBP Development Bank of the Philippines	RuMEPP Rural Micro-Enterprise Promotion Program
DCP Directed Credit Program	SBC Small Business Corporation
DOF Department of Finance	SCA Standard Chart of Accounts
EU European Union	SCWE Savings and Credit with Education
FPSDC Federation of People's Sustainable Development Cooperative	SEAD Sustainable Economic Activity Development, Inc.
GF Grameen Foundation	SEC Securities and Exchange Commission
GFIs Government Financial Institutions	SEEP Small Enterprise Education and Promotion Network
GFSME Guarantee Fund for Small and Medium Enterprises	SPM Social Performance Management
GIS General Information Sheet	TSKI Taytay sa Kauswagan, Inc.
IC Insurance Commission	UNDP United Nations Development Programme
ICCO Interchurch Organisation for Development Cooperation	USAID United States Agency for International Development
IFAD International Fund for Agricultural Development	VAMI Visayas Association of Microfinance Institutions
KASAPI Kalusugang Sigurado at Abot-Kaya sa PhilHealth Insurance	
LBP Land Bank of the Philippines	
MABS Microenterprise Access to Banking Services	
MCN Model Cooperative Network	
MCPI Microfinance Council of the Philippines, Inc.	
MDG Millennium Development Goals	
MFI Microfinance Institution	
MICOOP Microfinance Innovations in Cooperatives Project	
MIS Management Information System	
MIX Microfinance Information eXchange	
MMC Mindanao Microfinance Council	
MOA Memorandum of Agreement	

The development of the microfinance sector in the Philippines started to pick up when the government deliberately envisioned the provision of viable and sustainable financial services to the poor. This was clearly articulated in the National Strategy for Microfinance that was launched in 1997 and issued by the National Credit Council under the Department of Finance. The National Strategy is anchored on the following key policy principles:

- i) greater role of the private sector in the provision of financial services to the poor;
- ii) establishment of an enabling environment that will facilitate increased participation of the private sector in the provision of financial services to the poor;
- iii) adoption of market-oriented financial and credit policies; and
- iv) non-participation of government non-financial agencies in the implementation of credit and guarantee programs.

The adoption of the National Strategy led to the issuance and implementation of various policy measures that called for the non-participation of government in the delivery and implementation of subsidized credit programs and adoption of market-based credit and financial policies.

As the government veered away from directly intervening in the credit market, several private financial institutions started to provide financial services to the poor. These are the rural banks and thrift banks, cooperatives engaged in savings and credit services and microfinance NGOs. Most recently, a number of commercial banks (mostly engaged in wholesale microfinance operations) have also entered the market.

The regulatory framework for microfinance developed by the National Credit Council in 2004 recognizes the relevant regulatory authorities for each type of institution engaged in microfinance. Banks engaged in microfinance operations remain under the supervision of the *Bangko Sentral ng Pilipinas*, cooperatives fall under the regulatory ambit of the *Cooperative Development Authority* (CDA) while microfinance NGOs, as non-deposit taking institutions are not subject to any prudential regulation. Microfinance NGOs are required to register with and disclose to the *Securities and Exchange Commission* (SEC) that they are engaged in microfinance and related services.

Aside from ensuring that each type of MFI is under the supervision of a regulatory authority, the regulatory framework also called for the development of a set of performance standards that focuses on the following areas: **P**ortfolio quality, **E**fficiency, **S**ustainability and **O**utreach (i.e., the P.E.S.O. Standards).

The favorable policy and regulatory environment for MFIs facilitated the growth and development of the Philippine microfinance sector. From only a handful of MFIs catering to a few thousands of clients in the early 90's, the sector has grown to several thousands of MFIs serving millions of clients.

Estimates of the performance of the microfinance sector show that as of 30 June 2010, there are 14,934 MFIs in the country catering to more than 4.9 million active borrowers. This estimate assumes that about 50 percent of the members of cooperatives engaged in savings and credit operations have microfinance loans since cooperatives cater mostly to those that belong to the relatively lower income sector. The estimate may, however, be overestimated due to cases of multiple borrowings among clients. It is possible that one client may be borrowing from any two or all the three types of MFIs.

The estimates also show that microfinance NGOs tend to provide smaller sized loans compared to microfinance banks. Average loan outstanding of borrowers from microfinance NGOs was only about PhP6,000 while that from microfinance banks was higher at PhP7,600 indicating that the microfinance NGOs cater to the relatively lower end of the low-income market compared to the banks.

Considering that there are a number of borrowers that may have borrowed from several sources at the same time, the implementation of the Credit Information Systems Act (CISA) is imperative. The implementation of the CISA is expected to increase access to credit by micro, small and medium enterprises as well as address problems of multiple borrowings that could lead to delinquencies. The implementing rules and regulations of the CISA have already been approved and some members of the Board have already been appointed. To date, the implementation and operations of the Credit Registry are, however, hampered by the lack of budgetary appropriations from the National Government for the initial capitalization requirement of the Bureau.

MFIs formed both regional and national associations to provide technical support to member MFIs. These associations provide the venue for member MFIs to share knowledge, experience and information on the latest technology and developments in making MF operations more efficient and more responsive to MF client needs. These associations also provide the necessary critical mass in advocating for relevant reforms to further develop the microfinance sector. Aside from the associations, several technical assistance and support service providers, some of which are funded internationally, also provide technical and, in some cases, financial support to MFIs. Most of these institutions cater to the MFI demand for training and capacity building

services that would help them move towards greater outreach and efficiency.

With the growth of the MF sector comes innovations and developments. Recent advancement in technology as well as the popularity for mobile phones in the country led to the recognition of the huge potential of mobile banking in the country. In partnership with Globe Telecoms, a number of MFIs, rural banks in particular, have started to provide mobile banking services to its clients. Other innovations in the sector include the development of additional products and services needed by microfinance clients. These are:

- i) microfinance housing to meet the housing improvement and repair needs of MF clients;
- ii) microfinance that will cater to the credit needs of clients in the rural areas;
- iii) loan products that will finance water connection in some low-income households allowing them to have access to safe water supply; and
- iv) partnership with PhilHealth in providing PhilHealth coverage to the MFI clients.

Aside from product innovation, some MFIs have also provided business development services to their clients to improve the capacity of microentrepreneurs as well as to increase the value added of their microenterprises. Also, a number of MFIs have deliberately focused on social performance management to ensure that their institutions do not drift away from their original mission of providing the poor access to financial services. The Microfinance Council of the Philippines, Inc. (MCPI), for its part, spearheads the promotion and adoption of SPM among its network members.

Most recently, MFIs realized that gains resulting from continued access to savings and credit services are usually eroded when contingent events arise. The poor are vulnerable to risks such as illness, physical injury, accident, or death; basic business risks; loss of property; loss of job; theft; and abrupt swings in the economy. MFIs realized the need to assist their clients with financial products that will help them manage these risks and/or provide financial relief when contingent events occur, hence the birth of microinsurance.

To facilitate the provision of microinsurance, the government through the Department of Finance (DOF)-National Credit Council (NCC) and Insurance Commission (IC) spearheaded the development of the National Strategy and the Regulatory Framework for Microinsurance. These documents provide the pillars for the development of the microinsurance market in the Philippines by calling on and enjoining the private insurance

providers to provide risk protection to the low-income sector. To date the IC has already issued several circulars that provide a regulatory space for the provision of microinsurance by the private sector.

Despite the growth and development of the microfinance sector, several issues and challenges still remain.

With an increased number of MFIs, borrowers are provided more sources of borrowings, sometimes resulting in clients borrowing from multiple sources. Overleveraged borrowers may result in higher defaults among MFIs. Also as more institutions provide financial services to the poor, the poor are exposed to higher risks resulting from non-transparency and full disclosure of MFIs. In view of this, it is always important to educate potential and existing clients of microfinance on the roles and responsibilities of both lenders and borrowers, including their rights and privileges.

Considering that most of the poor are in the rural areas, there is also a need to design and innovate for the right MF product design for clients engaged in agricultural activities.

Also as businesses of MF clients grow from micro to small enterprises, higher amount of working capital is needed, which oftentimes are beyond what MFIs can afford to lend. Hence, serving the increased capital requirement of MF clients is another challenge that must be addressed.

Cooperatives engaged in savings and credit operations comprise a sizable number of MFIs. As of June 2010, there are 1,444 credit cooperatives and more than 13,000 multi-purpose cooperatives, about 80 percent of which are engaged in savings and credit operations. These cooperatives are significant players in microfinance. However, at present, these cooperatives are not regulated and supervised as desired. CDA has focused mainly on its developmental functions rather than on its regulatory functions, in part because the CDA Charter is ambiguous and does not grant the CDA the necessary authority to regulate cooperatives. The thrusts of the CDA need to be refocused and its policy and regulatory functions need to be enhanced so that it can help strengthen cooperatives in the areas of governance, management and operations, among others.

To sustain the development and growth of the Philippine microfinance sector, it is imperative that these challenges are addressed and appropriate measures are adopted by the concerned stakeholder.

Box 1. Philippine Map



Background and Purpose

In 2008, the Microfinance Council of the Philippines, Inc. (MCPI) conducted a sector assessment of microfinance in the Philippines as part of the Citi Network Strengthening Program (NSP).¹ The sector assessment provided an overview of the Philippine microfinance sector, including developments and information on key players and stakeholders. This paper updates the 2008 sector assessment to include significant and latest developments.

This study was conducted to provide relevant information and updates on the Philippine Microfinance Sector to the various constituencies of MCPI. The document provides MCPI network members a broader perspective of the key developments in the microfinance sector. The study is also useful for external stakeholders (e.g. donors, government agencies and service providers) as source of information on the latest updates and developments in the sector. It also provides a guide to MCPI in determining strategic interventions that will benefit the sector in general and its network members in particular.

Section 2 provides a general overview of the country context. Section 3 describes and discusses the performance of the Philippine financial sector while Section 4 discusses the Philippine microfinance sector with specific focus on its evolution and how government policies and regulations have encouraged private sector participation and shaped up the sector to what it is today. The most recent performance of the microfinance sector is also discussed in this section including recent innovations and developments. The various organizations providing support to the sector are also mentioned in this section. Section 5 discusses recent developments and product innovations being implemented by the key players in the sector while the last section discusses remaining gaps and challenges faced by the Philippine microfinance sector.

THE PHILIPPINES: GENERAL OVERVIEW

GEOGRAPHICAL LOCATION

The Philippines is an archipelago in Southeast Asia bordered by the Bashi Channel on the north, Celebes Sea on the south, the Pacific Ocean on the east and South China Sea on the west. The country has an exclusive economic zone of 200 nautical miles (370 km.) from its shores and a total land area of approximately 300,000 km².

¹ The Citi Network Strengthening Program was implemented in coordination with SEEP Network and with funding support from Citi.

Topographically, the Philippines has one of the longest coastlines in the world. It is also situated in the coral triangle of the world and has three-fourths of the world's coral resources.

As an archipelago, it consists of 7,107 islands of which around 1,000 are populated. The country is divided into three major island groups: Luzon, Visayas, and Mindanao. The nation is grouped into 17 regions that are further divided into local government units (LGUs) with the 80 provinces as the primary unit. Provinces are further subdivided into cities and municipalities that are in turn composed of barangays, the smallest political unit.

DEMOGRAPHICS

The Philippine population grew at an annual average growth rate of 2.75 percent from 1950 to 2006. The 2007 Census of Population reported a total population of 88.57 million people compared to 76.5 million in 2000 and 68.62 million in 1995. Almost 40 percent of the population is below 19 years of age while another 32 percent are adults aged 20 to 44 years.

By the end of 2010, the country's population is expected to reach 94.1 million and by the year 2015, there will be approximately 111 million Filipinos.

Compared to other developing countries, the Philippines has relatively high literacy rate. The adult literacy rate (percentage of people over the age of 15 who can read and write) for both male and female for the period 2000-2004 stands at 93 percent.

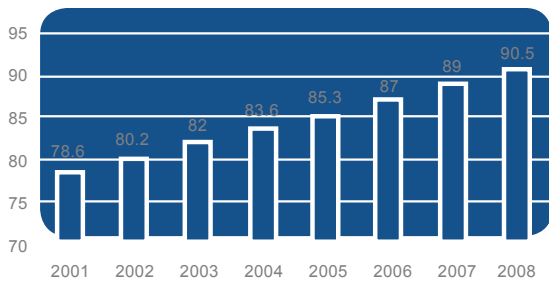


Figure 1. Population Projection
Source: National Statistics Office

Further, youth literacy rate (percent of people between 15 and 25 who are literate) is around 95 percent.² However, functional literacy rate or the ability of a person to not only read and write but to also do arithmetical skills only stands at 86 percent.³

ECONOMIC GROWTH

The Philippine economy grew by 7.9 percent for the first half of 2010, the highest semestral growth since peaking at 9.3 percent in the second semester of 1988. The National Statistical Coordination Board (NSCB) attributes this to “a synergistic confluence of factors, despite the El Niño phenomenon that scorched the Agriculture sector” during the period.⁴ According to the statistical agency, “the peaceful national elections, improved investors confidence especially among local investors, the global economic recovery, increased capital expenditure of government and a low base fueled the domestic economy to a scintillating 7.9 percent growth in the second quarter of 2010 from 1.2 percent last year.”

During the first semester, the growth of the Industry sector strongly supported by Services fueled much of the economy’s growth. In response to the improved domestic and external demand, the output of the manufacturing sector (representing 66 percent of the sector) rose by 16.2 percent. This mainly came from export-oriented electronics manufacturers. Improvement in the Trade, Government Services and Private Services, particularly recreational and business services, also contributed to the higher than usual growth during the second quarter. Meanwhile, the growth of the agriculture sector had declined by 0.2 percent during the semester as a result of the El Niño phenomenon that hit the country during the period.

Increased consumer and government spending during the first two quarters contributed to the growth from the demand side. Increased investments in Construction and Durable Equipment and the high growth in external trade also fueled the growth during the period.

During the first six months of 2010, remittances of Overseas Filipino Workers (OFWs) increased by 7.7 percent. The growth in remittances boosted Gross National Product (GNP), which grew by 8.2 percent during the semester.

As a result of improved economic growth during the first semester, bank lending to both consumers and businesses has

expanded in 2010, with growth in credit for production activities picking up to 12 percent year-on-year in July (the highest rate of growth since June 2009). Bank capital adequacy ratios are well above 10 percent while non-performing loan ratios remain in the low single digits.⁵

LABOR AND EMPLOYMENT

The economic growth during the first two quarters of 2010 translated to an increase in employment of almost two million. Unemployment rate slightly improved from 7.7 percent in January 2009 to only 7.3 percent in January 2010. Employment creation was seen more on the services sector followed by industry. In October 2008, labor and unskilled workers comprise almost half of the total number of employed persons. Under-employment rate, however, increased from 18.2 percent in January 2009 to 19.7 percent in January 2010.

POVERTY SITUATION

Latest available official poverty incidence statistics (2009) reveal that 20.9 percent of Filipino families or 27 out of 100 Filipinos are living below the poverty threshold.⁶ This translates to about 3.9 million families or a total of 23.1 million poor Filipinos. The NSCB reported that a Filipino needed PhP974 in 2009 to meet his/her monthly food needs and PhP1,403 to stay out of poverty. A family of five, therefore, needs PhP4,869 monthly income to meet food needs and PhP 7,017 to stay out of poverty. Hence, to stay out of poverty, a family of five should earn a daily income of at least PhP231.

The huge number of Filipinos and Filipino families living below the poverty threshold comprise the market for microfinance services. Aside from this, those living just above the poverty threshold, who do not yet have access to the formal financial system in the country, also comprise the potential market for microfinance products and services.

² Literacy data culled from the International Labor Organization website at www.ilo.org

³ National Statistics Office, 2003 Functional Literacy, Education and Mass Media Survey

⁴ www.nscb.gov.ph

⁵ www.asiandevbank.org/Documents/Books/ADO/2010/Update/ado2010-update-phi.pdf

⁶ This poverty statistics used the new refined methodology of the NSCB. See, www.nscb.gov.ph/poverty/2009/presentation_RAVirola.pdf

THE FORMAL FINANCIAL SYSTEM

Overview

The Philippine financial system is comprised of formal and informal sub-systems.⁷ The formal system consists of banks and non-bank financial institutions (NBFIs)⁸ while the informal sub-system is comprised of those that are not included in the published statistics of the *Bangko Sentral ng Pilipinas* (Central Bank of the Philippines).

Banks are financial institutions regulated and supervised by the *Bangko Sentral ng Pilipinas*. They are categorized into universal and commercial banks, thrift banks, and rural and cooperative banks and are classified according to the amount of capitalization required and the type of services allowed.⁹ Universal banks have the highest capital requirement. Together with commercial banks, they are authorized to provide a wide range of financial services such as underwriting of investment houses and investments in equities of non-allied undertakings. Universal banks usually operate in cities and major urban areas. Thrift banks, on the other hand, are mostly engaged in providing short-term working capital and long-term financing to businesses. Meanwhile, rural and cooperative banks have relatively lower capital requirements and are limited to only provide savings and credit services. They operate mostly in the rural and poor areas and provide the much needed financial services to rural communities such as farmers, fisher folks and micro and small microenterprises.

At present, thrift, rural and cooperative banks engage in the provision of microfinance services (savings, loans, payment and money transfer for the low income sector). The BSP classifies these banks into two categories: microfinance banks and microfinance-oriented banks. Microfinance banks are those whose total loan portfolios are 100 percent microfinance while

microfinance-oriented banks are those that have at least 50 percent of microfinance loans in their gross loan portfolio.

Non-bank financial institutions (NBFIs), on the other hand, are entities that are engaged in financial services but may or may not have quasi-banking functions.¹⁰ These include the investment houses, financing companies, investment companies, securities dealers/brokers, fund managers, lending investors, pension funds, pawnshops, credit card companies, venture capital corporations and non-stock savings and loan associations.

Aside from the banks, there are credit and multi-purpose cooperatives and microfinance NGOs that are not considered part of the statistics in the Philippine financial system.¹¹ Since these institutions perform functions that are similar to those performed by the other recognized financial institutions in the system, they are considered significant players under the Philippine financial system, especially in microfinance. For instance, the credit cooperatives, while not licensed as banks, are legally permitted to offer loans and take deposits from its members. Microfinance NGOs, on the other hand, provide credit services to their client members. They are, however, not allowed to take deposits from the public nor from its members.¹² While these institutions are not regulated and supervised by the *Bangko Sentral ng Pilipinas*, they are also subject to regulation. The credit cooperatives are registered and legally under the regulation and supervision of the Cooperative Development Authority (CDA) while the microfinance NGOs are registered with the Securities and Exchange Commission.

Performance

As of the first half of 2010, there were 24,072 offices of financial institutions in the country of which more than half (15,382) are offices of non-bank financial institutions. This number includes head offices, branches and extension offices of the banks and non-bank institutions (see Table 1).

⁷ Llanto and Alip, "Overview of the Emerging Microfinance Industry," in Regulatory Architecture for Microfinance in Asia, Asian Productivity Organization, 2006.

⁸ Banks and NBFIs differ in the type of instruments they issue. Only banks are allowed to use deposit instruments such as demand deposits/checking accounts, savings deposits (passbooks) and certificates of time deposits. NBFIs primarily use deposit-substitute instruments like promissory notes, repurchase agreements and certificates of participation/assignment. (Lirio, R. "Central Bank's Regulatory Role over Non-Bank Financial Institutions," 2002).

⁹ Universal and commercial banks represent the largest category in terms of bank resources. They offer the widest selection of financial services. They are authorized to engage in underwriting of investment houses and to invest in equities of non-allied undertakings. These banks usually operate in cities and major urban areas.

Thrift banks are composed of savings and mortgage banks, private development banks, stock savings and loan associations, and microfinance thrift banks. These banks usually engage in accumulating savings and using these for investments. They are mostly engaged in providing short-term working capital and long-term financing to businesses.

Rural and cooperative banks are banks that operate mostly in the rural and poor areas. They provide much needed financial services to rural communities such as farmers, fisher folks and micro and small microenterprises. Rural banks are privately owned and managed while cooperative banks are organized or owned by cooperatives.

¹⁰ NBFIs are generally classified into two major groups: (1) NBFIs with Quasi-Banking Function, and (2) NBFIs without Quasi-Banking Function. Quasi-banking is the issuance of deposit substitutes or borrowing instruments to twenty or more persons or entities. Borrowing from the said number of persons/entities is considered as borrowing from the public and would require the prior approval and authority from the *Bangko Sentral ng Pilipinas*. (Lirio, 2002). Regulation of non-bank financial institutions without quasi-banking functions has recently been transferred to the Securities and Exchange Commission (SEC) in accordance with Section 130 of the New Central Bank Act (RA 7653).

¹¹ Per BSP statistics, these institutions are not counted as part of the Philippine Financial System. However, it is believed that it should be part of the financial system inasmuch as they perform functions that the other recognized financial institutions in the system are doing.

¹² Under the regulatory framework for microfinance, microfinance NGOs are allowed to collect savings from their members up to the amount of the member's compensating balance. The collection of savings from the members of microfinance NGOs is currently one of the policy issues being discussed between the BSP, the NCC and the concerned stakeholders.

Table 1. No. of Financial Institutions in the Philippines

TYPE OF FINANCIAL INSTITUTIONS (FIs)	End-March 2010			End-June 2010		
	TOTAL	HEAD OFFICE	OTHER OFFICES	TOTAL	HEAD OFFICE	OTHER OFFICES
BSP SUPERVISED/REGULATED FIs	<u>23,897</u>	<u>7,249</u>	<u>16,648</u>	<u>24,072</u>	<u>7,249</u>	<u>16,823</u>
I. BANKS	<u>8,663</u>	<u>779</u>	<u>7,884</u>	<u>8,685</u>	<u>773</u>	<u>7,912</u>
A. Universal and Commercial Banks	<u>4,545</u>	<u>38</u>	<u>4,507</u>	<u>4,596</u>	<u>38</u>	<u>4,558</u>
Universal Banks	4,019	19	4,000	4,063	19	4,044
Private Domestic Banks	3,578	11	3,567	3,621	11	3,610
Government Banks	424	3	421	425	3	422
Branches of Foreign Banks	17	5	12	17	5	12
Commercial Banks	<u>526</u>	<u>19</u>	<u>507</u>	<u>533</u>	<u>19</u>	<u>514</u>
Private Domestic Banks	441	7	434	444	7	437
Subsidiaries of Foreign Banks	71	3	68	75	3	72
Branches of Foreign Banks	14	9	5	14	9	5
B. Thrift Banks 1/	<u>1,339</u>	<u>74</u>	<u>1,265</u>	<u>1,329</u>	<u>74</u>	<u>1,255</u>
C. Rural and Cooperative Banks	<u>2,779</u>	<u>667</u>	<u>2,112</u>	<u>2,760</u>	<u>661</u>	<u>2,099</u>
Rural Banks 1/	2,617	624	1,993	2,603	620	1,983
Cooperative Banks	162	43	119	157	41	116
II. NON-BANK FINANCIAL INSTITUTIONS	<u>15,229</u>	<u>6,465</u>	<u>8,764</u>	<u>15,382</u>	<u>6,471</u>	<u>8,911</u>
A. With Quasi-Banking Functions	37	14	23	37	14	23
B. Without Quasi-Banking Functions	<u>15,192</u>	<u>6,451</u>	<u>8,741</u>	<u>15,345</u>	<u>6,457</u>	<u>8,888</u>
NSSLAs 2/	164	70	94	166	70	96
Pawnshops	14,953	6,321	8,632	15,105	6,328	8,777
Others	75	60	15	74	59	15
III. OFFSHORE BANKING UNITS	<u>5</u>	<u>5</u>	<u>0</u>	<u>5</u>	<u>5</u>	<u>0</u>

1/ Including Microfinance-Oriented Banks

2/ Refers to non-stock savings and loan associations

Source : Supervisory Data Center, Supervision and Examination Sector, BSP, www.bsp.gov.ph

Of the total banking offices (8,685), 53 percent are offices of universal and commercial banks while about 32 percent are offices of rural and cooperative banks. Of the total non-bank offices, about 98 percent are pawnshops.

As of March 2010, the total resources of the banking sector amounted to Php6.1 trillion pesos. Of this amount, about 89 percent were from universal and commercial banks (75 percent and 13.2 percent, respectively). The rural banks and the cooperative banks put in a measly 2.8 percent of the total resources (see Table 2). Over a five-year period, the market share based on assets of each type of bank remained relatively the same.

The foregoing information shows that big commercial and universal banks largely dominate the formal financial system (in terms of number of offices and in terms of resources). This probably explains why for a long time, most of the BSP rules and regulations were biased against micro and small lending

(e.g., requirement of collateral in order for such loans not to be considered as sub-standard). It was only in 2001 when the BSP started to carve out a regulatory space for banks engaged in lending to micro and small enterprises.¹³

As indicated in the earlier section data coming from the financial transactions of cooperatives engaged in savings and credit operations and microfinance NGOs are not included in the BSP's data on the financial system. CDA data shows that as of 30 June 2010 there are 1,444 credit cooperatives and 13,267 multi-purpose cooperatives that in most cases are engaged in savings and credit operations.¹⁴ There are, however, about 25 microfinance NGOs as of December 2009 as indicated in the data of the Microfinance Council of the Philippines, Inc. (MCPI).

¹³ As discussed in the succeeding section, the General Banking Act of 2001 specifically directed the Monetary Board to consider the peculiar characteristics of microfinance lending in issuing relevant rules and regulations.

¹⁴ The National Confederation of Cooperatives (NATTCO) reported that about 80 percent of multi-purpose cooperatives are engaged in savings and credit operations.

Table 2. Market Share based on Assets, By type of Bank, March, 2010

Type of Bank	Total Assets (in billion pesos) March, 2010	%share	Total Assets (in billion pesos), December, 2005	%share
A. UNIVERSAL AND COMMERCIAL BANKS	<u>5,456.468</u>	88.5	<u>3,856.806</u>	89.3
1. Universal Banks	4,645.866 ¹	75.4	3,160.572	73.2
2. Commercial Banks	810.602	13.2	696.235	16.1
B. THRIFT BANKS	<u>533.236</u> ²	8.6	<u>346.027</u>	13.3
C. RURAL AND COOPERATIVE BANKS	<u>172.004</u>	2.8	<u>116.579</u>	2.7
1. Rural Banks	156.754	2.5	109.078	2.5
2. Cooperative Banks	15.250	0.2	7.501	0.2
ALL BANKS	<u>6,161.708</u> ³	100.0	<u>4319.412</u>	100.0

¹ Inclusive of foreign banks and government banks with universal banking license.

² As of March 2010, figures adjusted to net off the account "Due from Head Office" with "Due to Head Office" of branches of foreign banks.

³ Figures adjusted to net off the account "Due from Head Office" with "Due to Head Office" of branches of foreign banks.

Table 3. Borrowing Incidence, by Major Source of Loans, In Percent

	1981-2000	2000-2008
Formal institutions	30.6	50.1 ^a
Informal lenders	69.4	56.6 ^a
All Borrowers	100.0	100.0
% Borrowing	41.7	65.0
% Non-borrowing	58.3	35.0

^a There were 7 percent who reported borrowing from both formal and informal sources
Source: ACPC Small Farmers Credit Accessibility Survey, various years

INFORMAL FINANCE

The informal finance sub-system is comprised of moneylenders, trader lenders, input suppliers, and savings clubs such as the Rotating Savings and Credit Associations (ROSCA). These are entities providing credit services (or in the case of ROSCA, savings services) that are not registered with any authorized registering entity.

Informal finance still remains a significant source of funds among the low-income and marginalized sector. Among small farmers, for instance, about 56 percent still rely on informal credit sources such as traders, private moneylenders, and relatives/friends. The proportion of those borrowing from informal sources however has significantly dropped from 69 percent in the 1980s. The survey on small farmers' credit accessibility conducted by the Agricultural Credit Policy Council (ACPC) showed that the proportion of small farmer borrowers significantly increased from 41.7 percent during the period 1981-2000 to 65 percent during the period 2001-2008. Only half of those who borrowed received loans from formal sources such as cooperatives, rural banks, and non-governmental organizations (NGOs) including savings and loan associations or SLAs (see Table 3).

THE DEVELOPMENT OF THE MICROFINANCE SECTOR

The Beginning

The low-income sector is perceived as a sector that do not have access to financial resources they need. With very low income, private formal financial institutions were reluctant to lend to the sector due to the perceived costs and risks associated with lending to the poor.¹⁵ Hence, from the 60s up to the early 80s, the government has mostly been providing financial services (specifically credit) to the poor at subsidized interest rates.

Given this perspective, the government implemented several credit programs targeted towards specific clientele groups. These credit programs were funded out of government resources and were implemented by government non-financial agencies. For some credit programs, the government had enjoined the private financial institutions to provide credit to the poor using government funds at subsidized interest rates.¹⁶ Perceived as government dole-outs, most of the credit programs suffered from very low repayment rates. This weakened the financial performance of several private financial institutions (rural banks in particular), which were used as conduits of cheap government funds. As a result, the flow of funds from most of the subsidized credit programs implemented during the period declined over time due mostly to high levels of default, disqualification of many borrowers and rural banks from program participation (due to massive default problems), the termination of major foreign-supported on-lending projects, and rediscounting restraints.¹⁷

With the onset of financial reforms in the 80s,¹⁸ government terminated the implementation of subsidized credit programs in the agriculture sector.¹⁹ However, subsidized credit programs in the other sectors (e.g., industry, labor, science and technology) were continually implemented. In view of this, a strong lobby to

bring back the implementation of subsidized credit programs was mounted resulting in the issuance of Cabinet Resolution No. 20 in 1986, which allowed the implementation of livelihood programs in all sectors, including agriculture. By the end of 1992, subsidized credit programs have once again mushroomed, undermining the government's market-oriented credit and financial policy and the viability of the formal rural financial markets.

Despite the continued implementation of subsidized credit programs and the large amount of government and donor resources allotted for these programs, a large majority of the poor, especially those in the rural areas, still lack access to credit. With very high default rates and without achieving the objective of providing the poor access to credit, implementation of government directed credit programs resulted in huge fiscal losses for the government.

In view of this, the Social Pact on Credit was formed. This is an informal group comprised of representatives from various non-government organizations, people's organizations, academia, concerned government agencies and government financial institutions. This informal group initiated discussions on the inefficiency and ineffectiveness of subsidized government directed credit programs (DCPs) and the poor's continued lack of access to credit despite the proliferation of government DCPs. These discussions led to the creation of the National Credit Council (NCC) under the Department of Finance (DOF) on 8 October 1993, through Administrative Order No. 86.²⁰ The NCC was given the following mandates: i) rationalize and optimize government credit programs; ii) develop a credit delivery system that incorporates capability upgrading and institutional strengthening mechanisms; iii) encourage greater private sector participation in the delivery of credit; and iv) define and rationalize the role of guarantee programs and guarantee agencies.

Changes Adopted: Microfinance Policy Initiatives

With the creation of the NCC in 1993, several studies reviewing the implementation as well as the efficiency and effectiveness of subsidized directed credit programs were conducted.²¹ Results of these studies were presented in regional consultations, workshops and policy discussions with concerned policymakers and technical bureaucrats. These consultations and discussions led to the crafting of the National Strategy for Microfinance in

¹⁵ Large transaction costs and high risks associated with small scale lending prevented private financial institutions (i.e. banks in particular) from providing the needed financial services to the lower income segment of the population.

¹⁶ Loans were provided at highly subsidized interest rates to bring down the cost of borrowing of the targeted sectors. For instance, to direct credit resources into the agriculture sector, special time deposits and a subsidized rediscounting facility were made available by the Central Bank of the Philippines to both private and government financial institutions that were used as conduits of government funds for agriculture. These funds were provided to participating financial institutions at subsidized rates.

¹⁷ Due to limitations imposed by domestic credit ceilings, the tightening of the rediscount window in 1984 in response to economic and financial difficulties had seriously affected the provision of agricultural credit.

¹⁸ The following key policy reforms in the financial market were implemented: interest rates were deregulated; subsidized rediscounting facility of the Central Bank for agriculture was terminated; and development financing function of the Central Bank was transferred to Government Financial Institutions (LBP and DBP).

¹⁹ EO 113 was issued on December 24, 1986 abolishing twenty (20) directed credit programs and transferring these to the Comprehensive Agricultural Loan Fund (CALF). CALF is a fund that was used as a guarantee fund for agricultural loans extended by private financial institutions. Eighty five percent of the loan was guaranteed under CALF.

²⁰ The AO specifies the membership of the NCC to include representatives from concerned government agencies, government financial institutions, non-government organizations and people's organizations. The NCC served as a fora for policy discussions and provided specific policy recommendations on matters related to the provision of financial services to the informal and marginalized sectors of the economy.

²¹ The survey DCPs conducted in 1997 reported that there were 86 directed credit programs implemented by more than 20 government agencies.

1997, which paved the way for the development of the Philippine microfinance sector.

The National Strategy for Microfinance issued by the DOF-NCC in 1997 envisions the establishment of a viable and sustainable financial market that provides the poor access to a broad range of financial services (i.e., savings, credit, insurance, transfers, and remittances). Under the Strategy, the following key policy principles were adopted and used as guiding principles in providing the poor access to financial services: i) greater role of the private sector in the provision of financial services to the poor; ii) establishment of an enabling environment that will facilitate increased participation of the private sector in the provision of financial services to the poor; iii) adoption of market-oriented financial and credit policies; and iv) non-participation of government non-financial agencies in the implementation of credit and guarantee programs.

With the adoption of the National Strategy for Microfinance, several laws were enacted and policy measures were issued. These measures are enumerated in Annex A.

The Providers of Microfinance Services

As the government veered away from directly intervening in the credit market, several private financial institutions started to provide financial services to the poor. These are:

Non-Government Organizations (NGOs). Registered as non-stock, non-profit organizations, these are entities whose initial main objective is to provide developmental services to specific clientele in various geographical locations. As they provide developmental support services (e.g. health and sanitation, education, livelihood), a number of them realized and recognized that most of their target clientele are unable to engage in livelihood or entrepreneurial activities due to the lack of access to financial service (e.g. credit for working capital). As a result, a number of these NGOs started to pioneer the provision of financial services to the poor through the use of the Grameen technology.²² Learning from the lessons of failed directed credit programs and recognizing that credit is a responsibility that the poor are willing and able to take on, most of these NGOs adopted lending methodologies that are tailor-fitted to the needs and peculiarities of the poor (i.e., cash-flow based lending). To date, there are a number of microfinance NGOs engaged in providing financial services to the poor using varied lending methodologies that suits the needs and demands of their clientele. Majority of them provide small amounts of microenterprise loans to their clients through groups. More recently, some of the larger microfinance NGOs have diversified into other types of loans (e.g. housing repair loans, agricultural microfinance loans, emergency loans) to meet the increasing demand of their clients. The 2005 MIX Benchmarking report for the Philippines indicated that NGO MFIs have the deepest outreach indicating that they serve poorer clients. NGOs have a median average loan balance per borrower of USD \$75, or roughly 6.4 percent of per

²² Among the pioneer NGOs are the members of the APPEND Network and the PHILNET. These are the two biggest networks of NGOs prior to the establishment of the Microfinance Council of the Philippines.

capita Gross National Income (GNI). With lower average loan balance catering to the poorer segment of the economy, NGOs tend to charge higher interest rates to cover the high cost of dealing with the lower income sector.

Aside from loans, microfinance NGOs offer compulsory savings wherein a small proportion of the loan is retained as member savings. Since they are not licensed as banks, they are not legally allowed to mobilize savings from their members; hence most NGOs call this capital build-up.

More detailed discussion of the performance of the microfinance NGOs is provided for in Section 4.3.

Cooperatives. Aside from the microfinance NGOs, cooperatives engaged in the provision of savings and credit services are one of the low-income sector's earliest sources of credit resources. Community-based and open-type cooperatives are registered as institutions that can only provide services and transact with their members, who usually belong to the lower middle-income sector and those living below the poverty line. While considered to be lending to the poor, most of these cooperatives use the member's share capital as basis in determining the amount of the member's loan.²³ For most cooperatives, the member-borrower's capacity to pay and his/her cash-flow are not used in determining creditworthiness and repayment terms. Also, a number of these cooperatives were used as conduits of cheap government credit funds resulting in high default rates. Recognizing this problem and with the introduction of microfinance, a number of these cooperatives shifted towards cash-flow based lending. Some have extended cooperative membership to the lower income group.²⁴ To date, there is a growing number of cooperatives providing microfinance services. Microfinance services offered by cooperatives mostly include microenterprise loans and savings. Loans are provided either on an individual basis or in some cases, cooperatives use the group lending technique. Some cooperatives require compulsory savings through loan retention. These savings are then used to build member's capital to eventually be able to meet the required member share capital for regular members. Interest rates charged by cooperatives on their microfinance loans are usually higher than the regular loans offered to the regular members. This is to cover the cost of lending to this income segment.

More detailed discussion of the performance of cooperatives engaged in microfinance is provided for in a section below.

Banks. Prior to the issuance of the National Strategy for Microfinance, most of the banks were reluctant to lend to the poor due to the perceived risks and transactions costs associated with lending to this sector. Their experience with government subsidized directed credit programs in lending

²³ Cooperatives call this share-leveraging.

²⁴ Recognizing that the poor may not initially have the required initial amount of share capital for regular membership, some cooperatives initially register the low-income individual as associate member with relatively lower amount of share capital requirement. A capital-build up program is usually designed for these members.

to this sector have also contributed to this indifference. With the adoption of market-based credit policies and the termination of the participation of government non-financial agencies in the implementation of credit programs, an increasing number of private financial institutions (rural banks in particular) have ventured into microfinance. Increased participation of rural banks in microfinance is also attributed to the favorable regulatory environment. In 2001, the *Bangko Sentral ng Pilipinas* (BSP) issued several circulars recognizing non-collateralized cash-flow based lending. Non-collateralized microfinance loans were not considered sub-standard by regulation. Also, the moratorium on establishing bank branches was lifted for those banks that will engage in microfinance operations.²⁵ These regulatory policies, coupled with some technical assistance,²⁶ encouraged an increasing number of rural banks to engage in microfinance operations.

Rural banks engaged in microfinance provide both savings and credit facilities to their clients. The MIX MicroBanking Bulletin showed that rural bank data includes loan portfolios that combine a broad range of products including salary loans, agricultural loans, commercial loans, and housing loans. Compared to microfinance NGOs, rural banks cater to a broader range of clients with higher average loan balance. In view of this, most rural banks engaged in microfinance provide individual loans to their clients. Only a handful of rural banks provide group loans to their clients.

THE REGULATORY ENVIRONMENT FOR MICROFINANCE INSTITUTIONS

To date, three different types of institutions provide microfinance services in the country. These are the thrift and rural banks, the cooperatives with savings and credit services, and the non-government organizations with microfinance services. Different regulatory authorities regulate each of these institutions. The regulatory framework for microfinance and the specific regulatory environment in which a type of MFI operates are discussed below.

The Regulatory Framework for Microfinance

The need to ensure that the provision of microfinance services to the low-income sector is done in a safe and sound manner prompted the government, through the Department of Finance-National Credit Council (NCC), to develop and adopt the Regulatory Framework for Microfinance in 2002. The regulatory framework underscores the importance of developing sound, safe and sustainable microfinance institutions. Since the policy environment encourages the development of a diverse type of microfinance institutions and recognizes the strength of each type of institution, the regulatory framework for microfinance recognizes and builds on these institutional strengths.²⁷

Given this, the regulatory framework recognizes the relevant regulatory authorities for each type of institution engaged in microfinance. Banks engaged in microfinance operations remain under the supervision of the *Bangko Sentral ng Pilipinas*; cooperatives fall under the regulatory ambit of the *Cooperative Development Authority* (CDA); while microfinance NGOs, as non-deposit taking institutions, are not subject to any prudential regulation. Microfinance NGOs, nonetheless, are required to register with and disclose to the *Securities and Exchange Commission* (SEC) that they are engaged in microfinance and related services. The regulatory environments for each type of microfinance institutions are discussed below.

Aside from ensuring that each type of MFI is under the supervision of a regulatory authority, the regulatory framework also called for the development of a set of performance standards that focuses on the following areas: **Portfolio quality**, **Efficiency**, **Sustainability** and **Outreach**. The performance standards for microfinance were developed in 2004 and are discussed below.

The Regulatory Framework for Microfinance also recognizes the need for and the importance of an effective and functioning credit bureau that collects credit information of microfinance borrowers to address potential problems associated with multiple borrowings and/or credit pollution.

Thrift, Rural and Cooperative Banks

The *Bangko Sentral ng Pilipinas* (BSP) is the regulatory authority over all banking institutions in the Philippines including those engaged in the provision of microfinance. Banks are classified according to capitalization levels, geographical/market area coverage, and permitted financial services. The minimum capitalization requirements for each type of banks are shown in Annex B.

Rural, thrift and cooperative banks are the types of banks that are engaged in retail microfinance operations.²⁸ Banks with microfinance loans that are at least 50 percent of their gross loan portfolio are classified as “Microfinance-Oriented Banks (MOB)”. Meanwhile, banks whose microfinance portfolio is less than 50 percent of the total loan portfolio are classified as “Banks Engaged in Microfinance Operations (BEMO)”. Both MOB and BEMO are able to access the incentives provided to banks engaged in microfinance operations.

BSP adopts a risk-based approach in the supervision and examination of banks. This approach assesses the quality of the bank’s risk management systems and practices. Under this approach, banks are allowed to take risks for as long as they are able to manage and control their risk exposures. Risk-based supervision draws from a more comprehensive understanding of risks faced by a microfinance bank, unlike the traditional approach.²⁹ BSP looks into the various risks

²⁵ BSP Circular No. 273

²⁶ For instance, the USAID-funded Microenterprise Access to Banking Services (MABS) Project provided technical assistance to rural banks that wants to engage in providing microfinance services (savings and credit products).

²⁷ For instance, the community based-orientation of most rural banks, and credit cooperatives are considered ideal delivery vehicles for microfinance. Banks also have the distinct advantage of being able to mobilize savings from the public. Microfinance

NGOs, on the other hand, have the advantage of not being subjected to any branching limitations and prudential regulations and therefore are able to immediately respond to client demands through innovative products and services. Lastly, cooperatives, being member-based organizations ensure that profits earned are returned back to members.

²⁸ Cooperative banks are banks established by primary and secondary/tertiary cooperatives for the main purpose of providing financial and credit services to cooperatives.

²⁹ Under the traditional approach, BSP bank examiners check for compliance with banking

affecting a microfinance bank. These are: i) asset quality, portfolio at risk and adequate loan loss provisioning; ii) quality of management information system or MIS (for instance, ability to track loan performance on a daily basis); and iii) information disclosure through submission of periodic reports to facilitate offsite surveillance.

This supervision approach encourages banks to expand their microlending operations inasmuch as microfinance loans are typically given without collateral.

Aside from adopting a supervision approach that does not discriminate against microfinance operations, BSP has also issued several circulars that support and encourage banks to engage in sustainable microfinance operations. For instance, microfinance loans are exempted from rules and regulations issued with regard to unsecured loans. The moratorium on establishment of new banks is also partially lifted as long as the new banks are microfinance-oriented (i.e., with at least 50 percent of the bank's gross loan portfolio at all times shall consist of microfinance loans). (*Annex C provides a complete list of BSP Memorandum Circulars related to microfinance.*)

Credit and Multi-Purpose Cooperatives Engaged in Savings and Credit Operations

The Cooperative Development Authority (CDA) is the designated regulatory authority for cooperatives engaged in savings and credit operations. The law (Republic Act No. 6939) defining the functions and mandate of the CDA allows the agency to do both regulatory and development functions. Given conflicting mandates of regulation, development and promotion, the CDA, since its creation in 1991, has not effectively supervised and examined cooperatives, particularly those engaged in the provision of savings and credit services. It has, instead, focused its efforts on the following: conduct of training and seminars on the organization of cooperatives, provision of lending funds, and conduct of activities to promote the formation and registration of cooperatives. This resulted in almost 70,000 registered cooperatives by December 2005 with very limited information regarding the status of operations and financial performance of these cooperatives. Based on the submission of cooperative's annual report, CDA pointed out that only about 50 percent of the more than 70,000 registered cooperatives in 2005 are operating. About 80 percent of the reportedly operating cooperatives are engaged in savings and credit operations.

Realizing that cooperatives use members' money in their lending operations, the CDA and the cooperative sector recognized the need to ensure that cooperatives engaged in savings and credit operations are operating in a safe and sound manner.³⁰ To ensure this, CDA refocused its efforts

laws, rules and regulations. The soundness of the bank is established on the basis of procedures for loan approval, supervision and collection that would apply to traditional banks.

³⁰ The Credit Policy Improvement Project (CPIP), a USAID technical assistance to the National Credit Council, conducted a review of the regulatory environment for cooperatives engaged in savings and credit operations 1999. The study pointed out the inadequacy of an effective and appropriate regulation and supervision of cooperatives engaged in savings and credit operations. Particularly, the study pointed out the conflicting regulatory and development mandates of the CDA.

towards the establishment of an appropriate and effective regulatory environment for cooperatives, especially those engaged in savings and credit operations.

As an initial step, the CDA developed and formulated the Standard Chart of Accounts (SCA) for cooperatives engaged in savings and credit operations. The establishment of the SCA and its adoption by all credit cooperatives and other types of cooperatives with savings and credit services indicates CDA's firm commitment to effective regulation and supervision. Following the adoption of the SCA and its accompanying accounting manual, the CDA also adopted the COOP-PESOS (Portfolio Quality, Efficiency, Stability, Outreach and Structure of Assets) as the performance standards for cooperatives engaged in savings and credit services. The adoption of the SCA and the COOP-PESOS are important strides that provide the platform for the basic information infrastructure needed for effective regulation and supervision. Following these developments, the CDA also developed the Manual of Rules and Regulations (MORR)³¹ and the Risk-based Supervision and Examination Manual for cooperatives engaged in savings and credit operations.

In 2008, RA 9520 (The New Cooperative Code of 2008) amended RA 6938 (the Cooperative Code of 1991). Under the New Cooperative Code, a new category of cooperative—Financial Service Cooperatives—was defined. Financial Service Cooperatives are financial organizations owned and operated by its members and authorized to provide financial services other than savings and credit to its members. Once a cooperative decides to provide these “other financial services”, the Code provides that they shall seek appropriate authority/license from the BSP.³² The BSP shall also prescribe the appropriate rules and regulations for FSCs in coordination with the CDA. The CDA, on the other hand, is mandated to exercise lead regulatory powers and supervision over FSCs.

To date, however, the appropriate arrangements for the supervision and examination of FSCs and the specific rules and regulations are still being developed and are yet to be agreed on between BSP and CDA.

RA 9520, however, did not specifically provide for CDA to issue rules and regulations for credit cooperatives and multi-purpose cooperatives engaged in savings and credit operations. In view of this, CDA has yet to develop specific regulations for cooperatives engaged in microfinance. CDA also still needs to build its capacity for regulating and supervising cooperatives, particularly, cooperatives engaged in microfinance. While a number of training and mentoring activities have already been conducted to develop the capacity of CDA for supervision and examination, the capacity of its staff still needs further beefing up. Likewise, appropriate institutional structures are yet to

³¹ While the President has approved the implementation of the MORR in 2007, the cooperative sector has filed a complaint in court questioning the mandate of CDA to issue rules and regulations. Pending the resolution of the case, MORR implementation is held in abeyance. Meanwhile, some important provisions of the MORR were already included in the amendments to the Cooperative Code. Among other things, these include provisions on the qualifications as well as the training requirements for the members of the Board of Directors.

³² These “other financial services” are currently being discussed by both the CDA and the BSP.

be established. For instance, CDA is yet to implement the provision of the new Cooperative Code to establish regulatory units at the CDA central and extension offices.

Microfinance NGOs

All NGOs engaged in microfinance are required to register with the Securities and Exchange Commission (SEC) as non-stock, non-profit organizations. An NGO that intends to engage in microfinance activities are required, per SEC Memorandum Circular No. 2, Series of 2006, to state in its incorporation papers that it is conducting microfinance operations pursuant to Republic Act No. 8425 (otherwise known as the Social Reform and Poverty Alleviation Act).

More recently, to ensure proper disclosure of NGO activities, SEC required all NGOs to disclose their microfinance activity in the annual submission of the General Information Sheet (GIS) as per SEC Memorandum Circular No. 9, Series of 2006.

Although microfinance NGOs are required to make appropriate disclosures and file audited financial statements and general information sheets on an annual basis to the SEC, they are not subject to prudential regulation and supervision. There is also no single institution that has a complete set of relevant information on the financial performance of NGOs.

The Performance Standards for Microfinance Operations

As provided for in the Regulatory Framework and to ensure greater transparency in microfinance operations, the NCC in collaboration with concerned regulatory authorities and private sector representatives, developed the Performance Standards for Microfinance Operations in 2004. The Performance Standards focus on the following key areas of microfinance operations: Portfolio Quality (40 percent), Efficiency (30 percent), Sustainability (15 percent) and Outreach (15 percent), otherwise known as the PESO standards. Annex D provides the details of the Performance Standards for Microfinance.

Various stakeholders use the Performance Standards for varying purposes. For instance, in addition to the existing regulatory tools, the benchmarks are being used by the different regulators in assessing the financial institutions with microfinance operations that are under their supervision. Private or government wholesale financial institutions also use these standards, as complement to their existing guidelines, for evaluating the creditworthiness of a microfinance retail institution.

The managers of MFIs, on the other hand, use the indicators and standards to identify weak areas of operations that need specific or immediate management attention. Domestic and international private investors can use these standards as guideposts to decide whether to invest in a certain MFI. Donor agencies, for their part, may be guided by these standards to more appropriately identify the type or area of assistance that is needed by a specific MFI.

Key government financial institutions such as the People's Credit and Finance Corporation (PCFC), Land Bank of the Philippines (LBP) and the Development Bank of the Philippines (DBP) have adopted the various PESO indicators in evaluating and assessing

the performance of retail microfinance institutions. Some wholesale commercial banks (e.g., Bank of the Philippine Islands, United Coconut Planters Bank) have also adopted the PESO in assessing and evaluating MFIs that would like to access their wholesale funds.

MICROFINANCE SECTOR PERFORMANCE

Retail Microfinance Institutions

The policy and regulatory environment for MFIs facilitated the growth and development of the Philippine microfinance sector. From only a handful of MFIs catering to a few thousands of clients in the early '90s, the sector has grown to several thousands of MFIs serving millions of clients.

As mentioned earlier, there are three types of MFIs in the Philippines that directly provide retail financial services to the poor and low-income clients. Since each of these institutions is under a different regulatory authority, there is no single body that generates a systematic set of information on the performance of the sector. An attempt to consolidate information from different sources was done to get an estimate of the performance of the microfinance sector in terms of the number of borrowers and the total amount of microfinance loans outstanding.

Table 4 below shows an estimate of the microfinance sector data as of 30 June 2010. Based on the estimate, there are 14,934 MFIs in the country catering to more than 4.9 million active borrowers. Since cooperatives cater mostly to those that belong to the relatively lower income sector, the estimate assumes that about 50 percent of members of cooperatives engaged in savings and credit operations have microfinance loans.

The estimates show that microfinance NGOs tend to provide smaller sized loans compared to microfinance banks. Average loan outstanding of borrowers from microfinance NGOs was only about PhP6,000 while that from microfinance banks was higher at PhP7,600. This is probably explained by the fact that most NGOs use the group lending technology for their microfinance clients while microfinance banks are mostly engaged in individual microfinance lending. This may also indicate that the microfinance NGOs cater to the relatively lower end of the low-income market compared to the banks. No data on amount of loans outstanding was available from the cooperatives.

Table 4. Microfinance Sector Data * As of June, 2010

Type of MFI	No. Reporting	No. of Active Borrowers	Total Loans Outstanding (in million Pesos)	Average Loans Outstanding
Microfinance NGOs**	25	1,768,819	10,122.40	5,722.72
Microfinance Banks***	200	876,109	6,716.39	7,666.16
Cooperatives ****	14,711	2,459,692	n.a.	n.a.
Total	14,936	5,104,520		

*Data estimated from existing information from various sources

**NGO data from MCPI and MIX market data as of December, 2009 (excluding data from banks and cooperatives)

***Data from BSP, As of June 30, 2010

****Basic Data from CDA, As of June 30, 2010. The estimate assumes that 80 percent of the members of multi-purpose cooperatives have loans and savings, of which 50% have microfinance loans. It was also assumed that 50% of the members of credit cooperatives have microfinance loans.

The foregoing estimate shows that while microfinance NGOs and banks are most often considered major players in the microfinance sector, the cooperatives engaged in savings and credit operations apparently also play a significant role. It is, however, unfortunate that the data provided is only an estimate inasmuch as CDA, the regulatory body for cooperatives, has not yet segregated information on the microfinance activities of cooperatives under their jurisdiction. The assumptions used in estimating the number of microfinance clients is based on the fact that most of the community-based cooperatives engaged in savings and credit cater to the relatively low-income sector. Most of the loans extended by these cooperatives are used for microenterprises and are usually below PhP100,000.

It should be noted though that the consolidated data on the number of microfinance borrowers does not take into consideration cases of multiple borrowings hence, resulting estimate may be overestimated. With multiple borrowings, it is possible that one client may be borrowing from any two or all the three types of MFIs. Hence, some double counting may have occurred.

Wholesale Microfinance Institutions

Lending funds of private retail financial institutions are sourced either from deposits in the case of banks and cooperatives, or external borrowings and donor funds. With the development of the microfinance sector in the Philippines and an increasing need for donor funds in transition economies, MFIs in the Philippines resort to either deposit mobilization (in the case of banks and cooperatives) and external borrowings as source of loanable funds. Government financial institutions (GFIs), which include the People's Credit and Finance Corporation (PCFC), the Land Bank of the Philippines (LBP), the Development Bank of the Philippines (DBP), and the Small Business Corporation (SBC), are considered one of the important sources of external funds for MFIs. Credit policy reforms implemented by the government have limited the involvement of GFIs to the provision of wholesale funds for retail microfinance institutions.

Aside from GFIs that are allowed and mandated to provide wholesale lending funds at market rates,³³ an increasing number of commercial banks are now also engaged in providing wholesale lending funds to the microfinance sector (e.g., the Bank of the Philippine Islands, Allied Bank and the United Coco Planters Bank).

People's Credit and Finance Corporation

The People's Credit and Finance Corporation (PCFC) is a government-owned and controlled corporation (GOCC) registered with the Securities and Exchange Commission (SEC) authorized to operate as a financing company. It is tasked to provide microfinance services to poor households in the Philippines and to act as the lead government entity specifically tasked to mobilize financial resources from both local and international funding sources for microfinance

³³ GFIs such as the Land Bank of the Philippines, Development Bank of the Philippines, and Small Business Corporation are mandated by law to undertake microfinance operations. This mandate is spelled out in two laws: RA 8425 known as the Social Reform and Poverty Alleviation Act and RA 9178 known as the Barangay Microenterprise and Business Enterprises (BMBE) Act passed by Congress in 2002. Both laws mandate GFIs to set up a special credit window for microenterprises and to promote microfinance programs for the poor

services (RA 8425, Social Reform and Poverty Alleviation Act).

As wholesaler of microfinance funds, PCFC provides lending funds to its conduits comprised of cooperatives, rural and thrift banks, and non-government organizations – collectively called microfinance institutions (MFIs). PCFC provides MFIs any of the following:

- *Investment Credit Facility*– revolving wholesale credit to MFIs to support their relending activities to end-clients;
- *Institutional Credit Facility*- for strengthening the MFIs' capability to implement, manage and viably operate a microfinance project;
- *Capability Building* – conduct of training, dialogues, and conferences; assistance in setting up MIS and internal control systems.

As of 30 June 2010 PCFC has an outstanding loan portfolio of PhP3.1 billion. Table 5 below shows PCFC's cumulative accomplishments from the start of its program in 1996 to June 2010:

Land Bank of the Philippines

The Land Bank of the Philippines (LBP) is a government financial institution that was created under the Agrarian Reform Law in 1963. It was specifically created to provide financing support to agrarian reform beneficiaries. Today, it has evolved into a full-service commercial bank. However, it still continues to fulfill its social mandate of promoting countryside development while remaining financially viable.

As one of the GFIs mandated by law to provide support to

Table 5. PCFC Accomplishments As of June, 2010

Major Indicators	From start of program (1996) to June 2010
Number of borrowers served	5,374,703
Number of active clients	2,909,472
Amount of loans released	PhP 13.56 billion
Geographic coverage	130 of 131 cities; 82 of 82 provinces; and 1,260 of 1,497 towns nationwide

the microfinance sector, the LBP has provided guarantee to the loans obtained by PCFC from the ADB-IFAD Rural Microenterprise Finance Project (RMFP) and the World Bank for the funding needs of PCFC. As of 31 December 2010, LBP has lent out to 130 microfinance institutions with a total microfinance loans outstanding of PhP130 billion. These MFIs served about 316,000 borrowers.

Development Bank of the Philippines

The Development Bank of the Philippines (DBP) was established by an act of Congress in 1949 to provide banking services to SMEs. In support to the microfinance sector, DBP launched its Financing Program for Micro Enterprises (FPME) in July 2001. It allocated PhP500 million pesos from its Window III facility for wholesale lending to retail MFIs.

At the end of October 2010, DBP has extended a total omnibus line of PhP3.08 billion to 20 MFIs. Outstanding loans amount to PhP1.549 billion.

Small Business Corporation (SBC)

The SB Corporation is the result of a merger between the Small Business Guarantee and Finance Corporation (SBGFC) and the Guarantee Fund for SMEs (GFSME) under Executive Order No. 98 in November 2001.³⁴ The Corporation is mandated to offer a range of financial services for small and medium enterprises engaged in manufacturing, processing, agribusiness (except crop level production) and services (except trading). These financial services include among other things, guarantee, direct and indirect lending, financial leasing, secondary mortgage, venture capital operations and the issuance of debt instruments for compliance with the mandatory allocation provision.

The mandate of SB Corporation to undertake microfinance operations is included in the BMBE Act of 2002. The Micro Finance Facility of Small Business Corporation is a lending program to sustainable and viable microfinance institutions. SBC has the following MF programs:

a) *Microfinance wholesale lending program.* Wholesale loan funds are provided to partner rural banks, microfinance institutions, and cooperatives. These financial institutions then re-lend the funds to eligible “pre-enterprises” which include both the graduating and start-up microenterprises.³⁵

b) *Direct lending to registered micro, small and medium enterprises (MSMEs).* The program is intended to bridge the financing gap for the “pre-bankable but viable” MSMEs that are usually “unserved” by the banking system. Through the program, MSMEs are given financing for their business needs and training for them to gain credit track record and experience in order to access bank financing in the future.

SB Corporation’s microfinance loan portfolio as of end 2008 amounts to PhP36.8 million. At the end of 2008, SB Corporation had total resources of PhP4.74 billion, a loan portfolio of PhP478.2 million, and a net income for the year of PhP 104.4million (based on its 2008 Annual Report).

³⁴ SBGFC was created under Republic Act 6977 in 1991, which was amended in 1998 by the Magna Carta for SMEs (RA 8289). On the other hand, the GFSME was a guarantee fund operated independently by a Management Committee and professional staff under the Livelihood Corporation, a corporation attached to the Office of the President of the Philippines.

³⁵ Graduating micros refer to those unregistered yet existing enterprise that are willing to register as an enterprise, have a livelihood track record as well as credit track record with a micro-finance institution, and with tangible assets. Start up micros, on the other hand, are starting enterprises that do not meet these qualifications yet.

MESO-LEVEL SUPPORT TO THE MICROFINANCE SECTOR

Establishment of a Credit Bureau

The increasing number of microfinance players is expected to promote competition among the service providers resulting in more efficient operations and eventually lower cost of services. Recent developments, however, show that competition may lead to multiple borrowings or, at worse, credit pollution. Microfinance clients may borrow from multiple sources affecting their ability to pay loans, which could lead to delinquencies, hence affecting the quality of an MFI’s loan portfolio.

Realizing this and its effect on financial institutions engaged in microfinance, Congress, in 2008, passed the Credit Information Systems Act (CISA), which provides for the establishment of a central credit registry. All regulated entities are required to submit all credit information of borrowers to the Central Credit Registry. In turn, all entities submitting information to the Registry are allowed to access information from it.

The implementation of the CISA is expected to increase access to credit by micro, small and medium enterprises as well as address problems of multiple borrowings that could lead to delinquencies. On a larger scale, the sharing and dissemination of credit information will lead to a sound, healthy and vibrant credit market. To date, the implementing rules and regulations of the CISA have already been approved and some members of the Board have already been appointed. The implementation and operations of the Credit Registry are, however, hampered by the lack of budgetary appropriations from the national government for the initial capitalization requirement of the Bureau.³⁶

Microfinance Associations and Councils

National Associations

Microfinance Council of the Philippines, Inc. (MCPI).

MCPI started in 1996 as a tactical coalition of NGOs engaged in microfinance (then known as the Philippine Coalition for Microfinance Standards)—an offshoot of the USAID-funded Developing Standards for Microfinance Project.³⁷ The Coalition was initially comprised of 69 institutions and represented by the key stakeholders in microfinance in the Philippines. Aside from developing standards for microfinance, the Coalition also conducted advocacy to key policymakers and concerned government agencies for the establishment of an appropriate policy environment for the growth and development of the microfinance sector.

With the completion of the USAID project in 1998, the Coalition’s Policy Advisory Group agreed “to establish an institution that will continue the work of the Coalition beyond the life of the Standards Project”. The institution was named the Microfinance Council of the Philippines, Inc. (MCPI) and became a legally registered institution in 1999.

³⁶ The CISA provides that the Central Credit Information Corporation shall have an authorized capital of Php500,000. The National Government shall own and hold sixty percent (60%) of the common shares while the balance of 40% shall be owned by and held by qualified investors, which shall be limited to industry associations of banks, quasi-banks and other credit-related associations.

³⁷ The project was implemented to build the capacity of Philippine MFIs to provide microfinance on a sustainable basis. Specifically, the project aimed to develop performance standards to achieve increased outreach and sustainability among Philippine MFIs.

MCPI is considered one of the leading microfinance networks of 47 institutions with the vision of becoming the national network of microfinance institutions providing sustainable, innovative, and client-responsive solutions to poverty reduction. The 47 institutions include 39 practitioners and 8 service providers. While membership among the practitioners is currently dominated by non-government organizations, the roster of practitioners also includes rural banks, one thrift bank, and two credit cooperatives.

MCPI provides support to its member-MFIs by: promoting the adoption of poverty assessment tools and social performance management systems; promoting the adoption of and adherence to international performance standards; advocating for a policy environment that is conducive to the growth and development of a market-oriented microfinance sector; helping build members' capacity for innovation that enhances the development of a market oriented microfinance sector; promoting market-oriented microfinance products and services; initiating the conduct of international and national forums for best practices in microfinance; and mobilizing resources and networking with government, donors, funding agencies, investors, and financial markets in order to enhance the development of the microfinance sector.

MCPI also collaborates with government agencies, other microfinance support organizations, donors and international networks to pursue its objectives. For instance, it has partnered with the Microfinance Information eXchange (MIX) in coming up with the Benchmarking Report for the Philippines.

Recognizing the social value of providing microfinance services, MCPI is also an active member of various groups and initiatives, such as the Imp-Act Consortium, the Social Performance Task Force, the Smart Campaign and Microfinance Transparency. It also plays an active role in the various working group meetings conducted by the National Credit Council in developing and formulating relevant policy measures for the development of the MF sector in the Philippines.

Rural Bankers Association of the Philippines. The Rural Bankers Association of the Philippines (RBAP) is an organization comprised of rural bank owners and operating officers. The organization was formed to support and enable its members to offer quality banking services, comply with regulatory requirements, and promote the welfare of the communities in which they operate. In support of these objectives, RBAP provides various training programs on corporate governance, risk management, financial management, credit and fund management and other relevant areas that will help rural banks improve their operations.

In 1998, RBAP received a technical assistance from the USAID to implement the Microenterprise Access to Banking Services (MABS) Program. The program is an initiative to encourage the Philippine rural banking industry to provide microenterprises access to microfinance services. In this regard, the MABS Program provides technical assistance and training to rural banks in the area of microfinance operations.

Trained banks in turn offer microfinance loan and deposit services specially tailored to microenterprise clients.

Federations of Cooperatives. Under the Cooperative Code and based on international cooperative principles, primary cooperatives are enjoined to form or join cooperative federations. Cooperative federations are organized to provide assistance to its member cooperatives in the areas of education, business and advocacy. At present, there are a number of cooperative federations formed and organized in various parts of the country. The following are the big cooperative federations whose primary cooperative members are mostly engaged in microfinance operations.

National Confederation of Cooperatives. The National Confederation of Cooperatives (NATCCO) is a national federation of cooperatives that provides continuous capacity building services to its members in the following areas: good governance, financial management, accounting and bookkeeping, human resource management, and management information system. It also provides ancillary services such as the federation's liquidity fund.³⁸ NATCCO is also engaged in advocacy work related to the establishment of an appropriate regulatory environment for cooperatives. The federation also participates in various legislative hearings on proposed bills involving cooperatives.

In 2006, NATCCO launched the Microfinance Innovations in Cooperatives (MICOOP) Project. The MICOOP Project seeks to help cooperatives in providing microfinance services to individuals who are engaged or wish to engage in microenterprises but have no access to financial services. The MICOOP Project provides capacity building assistance in the following areas: i) financial intermediation (savings and credit) operations and ii) microfinance operations. The MICOOP Project also provides assistance in improving the total savings and credit operations of the participating cooperative. NATCCO implements various models and schemes in helping its member-cooperatives become sustainable and viable microfinance providers.

As of June 2008, the MICOOP has established 59 branches strategically located all over the country and has garnered a total outreach of 79,550. Thirty-two of the branches operate according to the Build, Operate, Adopt, Transfer (BOAT) partnership arrangement while six branches have opted for the 50/50 investment partnership.

Philippine Federation of Credit Cooperatives. The Philippine Federation of Credit Cooperatives (PFCCO) is the first cooperative federation in the Philippines and in Asia. As a federation, PFCCO is mainly involved in providing capacity building and ancillary services to its member primary cooperatives (e.g., conduct of training on governance, financial management and accounting). It is also active in various fora advocating for a more cooperative friendly policy environment.

³⁸ Members are given the option to deposit their excess liquidity with NATCCO, which then manages and invests these funds in safe and high yielding investments in behalf of the member.

One of the banner programs of PFCCO is their Credit Union Microfinance Innovations Program (CUMI). CUMI is a specially designed product that provides sustainable and affordable access to both savings and credit to entrepreneurial poor that do not have access to formal financial institutions. Under the CUMI, partner cooperatives joining the program provide microfinance loans to the poor in the community where the cooperative operates. The client is initially considered an associate member until he/she is able to build up his/her enough savings for her share capital contribution. Microfinance loan funds come from the cooperative's resources.

Realizing the importance of good clients in maintaining a sound microfinance program, PFCCO is now starting to come up with assistance in providing market linkage services to its members. Having several primary cooperatives whose membership varies in terms of products and entrepreneurial activities, PFCCO has started to pilot test the establishment of business development centers, which facilitate the exchange of information regarding markets for the various products of the cooperative member.

Regional Microfinance Associations

During the past few years, regional microfinance associations were established. The People's Credit and Finance Corporation (PCFC) initially facilitated the formation of these regional networks for its partner MFIs in various regions in the country. The regional councils serve as network of MFIs in the region where best practices in the provision of microfinance services are shared. The regional councils organize forum on microfinance to facilitate exchange of knowledge and networking among member-MFIs. At present, there are six regional microfinance associations: 1) Mindanao Microfinance Council, Inc. (MMC); 2) Bicol Microfinance Council, Inc. (BMCI); 3) Central Luzon Association of Microfinance Institutions (CLAM); 4) Northeast Luzon Council; 5) Region 1 and CAR Council; and 6) Visayas Association of Microfinance Institutions (VAMI). These regional councils provide a venue for MFIs to share best practices in microfinance. There are also discussions on how to exchange credit information of borrowers among members of the regional councils to address credit pollution in areas where MFIs operate.

Microfinance Technical Assistance and Support Service Providers

As MFIs expand their operations and as new institutions enter the microfinance market, demand for training and capacity building on microfinance increase. A number of institutions were recently established to provide these services.

PinoyME Foundation

PinoyMe Foundation is a private sector, multi-stakeholder, social consortium and movement whose main objective is to bring multiple sectors together to widen access of the poor to financial services. It aims to contribute to reducing poverty by providing five million poor people with financial and non-financial services and mobilizing PhP5 billion in new capital for microfinance in five years. It aims to achieve its goal through capacity building, resource mobilization, business development services, and knowledge management. The

PinoyMe consortium consists of different institutions from the academe, MFIs, corporations, foundations, and NGOs.

MICRA Philippines

MICRA Philippines is a consulting and advisory firm that provides technical inputs and support to various stakeholders in the microfinance sector. As an independent resource center, MICRA is committed to promoting innovations, transparency, improved outreach to the poor and ever-improving performance in the microfinance sector through the following services: i) training and technical assistance; and ii) research and innovations. MICRA provides these services on a fee-for-service basis.

Oikocredit

Oikocredit is an international organization that continues to provide support to the microfinance sector in the Philippines. It is a cooperative financial institution that finances and invests in microfinance institutions, cooperatives and small and medium-sized enterprises in developing countries, aimed at social impact.

Oikocredit started to support projects in the Philippines in 1983 and has since approved loans amounting to PhP3.07 billion (€52.65 million). It has 44 active partners in the Philippines at present—17 in Luzon, 13 in the Visayas, and 14 in Mindanao—benefiting over 2.9 million economically active poor Filipinos, the majority of whom are women. At present, Oikocredit Southeast Asia offers the following types of products to its partner MFIs: loans, credit line, equity investment, and technical assistance.

Oikocredit is also one of the pioneers that launched the first Social Performance Management (SPM) Peer Learning Community in collaboration with MCPI and Grameen Foundation.

Grameen Foundation

Grameen Foundation (GF) is a global foundation that helps the world's poorest, especially women, improve their lives through access to microfinance and technology. In the Philippines, GF has provided support to some of the largest and most progressive MFIs since 2003. These MFIs are now considered the leaders in the Philippine MF sector. Realizing that smaller MFIs, are mostly found in the areas where most of the poor resides, GF started in 2009 to work with more MFIs and other stakeholders to bring the benefits of microfinance and technology to the rural areas where most of the three million poor and still unserved families reside. At present, GF provides assistance to the MFIs through a combination of catalytic capital, systems, automation, and social performance metrics. Grameen Foundation also works with other microfinance intermediaries to build a better infrastructure for collective action and encourage greater accountability, efficiency and transparency across the sector. Aside from providing access to capital (either through advisory services to assist MFIs in accessing commercial capital or direct lending capital) and help MFIs to automate and manage business information, GF also works with MCPI

and Oikocredit in creating a peer learning community where local MFIs can develop a robust SPM strategy, implement a concrete SPM initiative, and share the critical lessons of implementation with each other.

Federation of People's Sustainable Development Cooperative (FPSDC)

FPSDC is an organization comprised of non-government organizations, cooperatives and people's organizations. FPSDC started from the Central Loan Fund (CLF) under the Philippine Development Assistance Program (PDAP) and has metamorphosed into a network of PDAP's affiliate organizations that provide both financial and non-financial assistance to its member-organizations. At present, FPSDC has a credit facility and a social investment facility for its members. The former provides credit funds to its member organizations while the latter is designed to provide alternative investment opportunities to organizations to earn better returns for their money and at the same time support development initiatives of the disadvantaged communities. Aside from these, FPSDC also provides institutional support to beef up the capability of its members and partners to deliver financial and non-financial products and services, and to implement community enterprises to their respective clientele.

SEEDFINANCE Corporation

Founded in 2002, SEEDFINANCE Corporation is a non-governmental organization that provides savings and loans products, as well as technical and implementation assistance, to poor and low-income individuals and small businesses in the Philippines. On 30 April 2007, SEEDFINANCE Corporation was registered as a financing company that will continue the work of CARE-USA (Cooperative for Assistance and Relief Everywhere-USA) and SEAD, Inc. (Sustainable Economic Activity Development, Inc.–Philippines). Both institutions were initially involved in providing microfinance services to the poor and low-income households through a network of partner organizations. As of April 2010, SEEDFINANCE and its 70 partner organizations work with approximately 1.2 million clients across the Philippines.

Other service providers. Other service providers in the Philippines are the following: Asian Institute of Management (AIM)–Center for Development Management, Punla sa Tao Foundation, and the CARD Mutually Reinforcing Institutions Development Institute (CMDI). All of these institutions have various training modules on the different aspects of microfinance operations. CMDI, for its part, provides training in the following areas: microfinance management, social performance management, micro-insurance, basic financial management training, internal auditing and financial controls, training of trainers on micro-enterprise management, various lending methodologies, leadership and governance.³⁹

³⁹ CARD MRI Development Institute was primarily established to serve its CARD MRI staff members. Over time and based on demand from other MFIs, the institute offered training courses and sponsored study tours and exchange visits for the staff members of other MFIs. The experiences of CARD as one of the leading microfinance institution in the country has been one of the reason why most MFIs avail of the training courses under the institute.

At present, there are also various universities that are offering management courses, e.g., the Ateneo de Manila University and De la Salle University. In Ateneo, for instance, they are offering some courses that are focused on management of microfinance operations.

Aside from the foregoing there are other international development organization such as PlaNet Finance that has recently set-up local offices in the country. Likewise, international microfinance rating agencies such as Planet Rating and MicroFinanza Rating have also set up offices in the country indicating support and recognition of the robust and vibrant microfinance sector in the Philippines.

RECENT DEVELOPMENTS AND INNOVATIONS

Mobile Banking

With the advancement in technology and with the popularity of mobile phones, mobile banking is recognized to have a huge potential to provide access to the unbanked. The Consultative Group to Assist the Poorest (CGAP) reported in December 2009 that based on a survey conducted by GSMA and McKinsey, "...one billion people do not have a bank account but do have a mobile phone."⁴⁰

Findings from the Philippines show that one-half of the active mobile money users are unbanked. Of these, 26 percent are poor, living on less than US\$5 per day (the poverty line in the Philippines) and that 1 in 10 unbanked users saves an average of US\$31 (one-quarter of their family savings) in a mobile wallet.

Even before the results of the study, the Microenterprise Access to Banking Services (MABS) Project,⁴¹ already saw mobile phone banking as a technology solution to extend low-cost banking services to existing clients and un-banked individuals especially in rural areas. MABSs partnered with Globe Telecom, a leading mobile phone operator in the Philippines that developed the G-Cash platform in 2004.⁴² In partnership with Globe, MABS developed various products and services using the G-Cash platform. Among which are: using SMS to deposit, to pay bills, to remit and transfer funds, to pay loans, and to withdraw. They have also developed a product wherein the salaries of rural banks employees are received through text or SMS. As of June 2007, there are 37 accredited rural banks and 87 accredited bank branches with cumulative G-Cash transactions of 110,000, totalling PhP380 million or US\$7.6 million.

Most Recent Microfinance Products

Microfinance Housing

Aside from enterprise loans, some MFIs have started to offer microfinance housing loans, which are small, incremental loans at market interest rates and amortized over shorter terms. Microfinance housing loans cater to the low-income

⁴⁰ In early 2009, CGAP teamed up with the GSM Association (GSMA) (a global trade association for the mobile communications industry) and McKinsey (a global management consulting firm) to measure the global market for financial services delivered via mobile phones (mobile money) in 147 developing countries.

⁴¹ MABS is a USAID-funded project that assists rural banks to develop the capability to profitably provide financial services to microenterprises.

⁴² G-Cash is the service of Globe Telecom that turns a mobile phone into an electronic wallet. It allows the following: i) buy & sell goods and services; ii) send/receive remittances locally or from abroad; iii) pay bills and taxes; school tuition fees; iv) load cell phone airtime credit; and v) transfer money from one person's phone to another.

households and are usually used to improve or repair existing homes, construct and purchase new homes, buy land, or install or improve utilities and other basic services.⁴³

To enable banks engaged in microfinance to provide this type of loan, the *Bangko Sentral ng Pilipinas* issued Circular 678 on 6 January 2010 recognizing loans for housing to microfinance clients as part of a wide range of financial services to the sector. Since the risk profile of the new product may be different from regular microfinance loans, banks are required to carefully study the ability of clients to repay the loan, especially the new customers.

Microfinance in Agriculture

More than 50 percent of the poor who are considered clients of microfinance live in the rural areas where agriculture (farm, non-farm or off-farm) is one of the main economic activities. In view of this, a number of microfinance institutions have developed loan products for clients engaged in agriculture. Some MFIs are already implementing microfinance for agriculture. For example, TSPI Development Corporation has launched The Palayan Program (TPP) which has served more than 800 small farmers in just one year. Alalay Sa Kaunlaran, Inc. (ASKI), on the other hand, also offered an agricultural loan program to clients who have good loan repayment records for two consecutive years. Spouses of clients with good track record are also qualified to apply. A maximum loan amount of PhP150,000 is allowed per borrower depending on his or her capacity to pay.

Meanwhile, some rural banks engaged in microfinance operations have also started to provide agricultural microfinance. In 2004, RBAP-MABS developed the Micro Agri loan Product (MAP) where the amount of loan is determined through a cash flow analysis of the household income and expenses and not on pre-determined financial requirements of an agricultural commodity. A MAP client has an option to pay the loan by means of a straight amortization scheme or through a payment scheme that combines regular amortization and a balloon payment at the time of harvest/marketing. A micro-agri loan using the MABS approach finance a variety of farm and fishing activities that include grains, fruits, vegetables, livestock and marine products.⁴⁴

Since it was pilot tested in 2004, there are now 18 rural banks with more than 58 branches all over the country that offer MABS' micro-agri loan product. Over 43,000 loans totaling more than PhP583 million (about US\$13 million) have been disbursed to small farmers in the Philippine countryside.⁴⁵

Microfinance for Safe Water Supply and Sanitation

As of 2008, only about 84 percent of the population has access to safe water supply (NSCB MDG Watch, 2010). Of these, only about half (44 percent) are connected to Level 3

systems that are deemed as the safest and most convenient source of water supply. Of those who do not have access to safe water supply, many are from the poor communities. More recently, there has been an interest into looking at the feasibility of using microfinance services to provide the necessary financing for low-income households in the Philippines to have access to piped water connection. The USAID-funded Philippine Water Revolving Fund Support Program (PWRP-SP) has recently commissioned a study to introduce the concept of microfinance in expanding water supply and sanitation services to poor households. The study looked at various options for possible collaborative arrangements between an MFI and a water service provider.⁴⁶

In the various options identified, the MFI as partner shall provide the necessary financing. Microfinance principles and methodology shall be used in developing the appropriate loan product.

At present, ASKI has indicated its willingness to pilot-test the partnership with the local water district in their area of operations. Focus group discussions are currently being conducted to determine demand for microfinance for safe water connection.

Social Performance Management

A number of MFIs are apprehensive of mission drift in view of the growing commercialization of the sector. In view of this, there has been a deliberate focus on social performance, which is defined as the effective translation of an MFI's mission into practice in line with commonly accepted social values.⁴⁷ A number of MFIs have recognized the importance of implementing Social Performance Management (SPM) where it is defined as an institutionalized process which involves setting clear social objectives, monitoring and assessing progress towards achieving these, and using information to improve overall organizational performance.⁴⁸

As a result of this awareness, the Microfinance Council of the Philippines (MCPI) embraced SPM as one of its major agenda in 2006. It embarked on a three-year project that will, among other things, raise the level of awareness on SPM among its network members and build their capacities to manage their social performance.

To increase the level of awareness on SPM, MCPI has conducted promotional meetings participated by more than 75 institutions to date. As a result, there has been an increasing uptake of SPM among several local networks, MFIs, local donors/funders and other

⁴⁶ Water service providers referred to here are the local water districts. In areas where WSPs have existing water supply services but households lack funds to connect, MFIs may provide loans to individual households to finance their water connection fees and the related infrastructure (e.g. reticulation pipes) needed. In areas where there is no existing water supply service provided by any water service provider: i) households may be organized into a water association where the MFI will provide the necessary social preparation and capacity building activities to the members of the association and provide needed financing; ii) water kiosks or water stations may be established where the water association may establish and manage a water kiosk from where the members of the poor community shall buy their safe drinking water; or iii) LGUs may be enjoined to participate for communities that need huge investments for constructing the required infrastructure (e.g. transmission and distribution lines) for water connection.

⁴⁷ As defined by the Social Performance Task Force.

⁴⁸ With SPM, an MFI looks into its social goals -- whether it is reaching their target clients, meeting their clients' needs, and effecting positive changes in the lives of its clients. SPM is also the process by which an MFI attempts to achieve its social goals, necessarily ensuring that operations (i.e., service delivery, HR, MIS, finance) and strategy (vision, mission, social objectives, range of products and services) are aligned with its avowed social goals.

⁴³ Culled from the UN HABITAT Technical Assistance to the HUDCC for Housing Microfinance.

⁴⁴ See <http://www.rbapmabs.org/home/index.php/mabs-approach-training-and-technical-services/courses-and-training-offered-as-part-of-the-full-mabs-technical-assistance-package/introduction-to-microfinance>

⁴⁵ www.rbapmabs.org

support organizations. Updates and MFI practices on SPM are also regularly provided to network members while peer exchange and learning for 'advanced' MFIs are also regularly conducted.

In terms of capacity building, MCPI has established a pool of trainers on SPM (of the 19 trained, half have been already certified as SPM trainers). More than 50 MFIs have participated in the SPM training—11 of which are participating in a peer learning community, 5 MFIs have undergone social audit, and 6 MFIs have completed client protection assessments. Furthermore, there were 15 MFIs that submitted Social Performance Reports in 2010 to the MIX and to MCPI.

Business Development Services (BDS)

Aside from providing financial services, there is a growing number of MFIs that support the business endeavors of their clients and their microenterprises. MFIs also facilitate client's access to Business Development Services (BDS). These refer to the wide array of non-financial services critical to the entry, survival, productivity, competitiveness, and growth of enterprises. BDS are provided to assist individuals and entrepreneurs to enhance their business skills and market access to improve their income generation and asset-building capacity. These services include training, consultancy and advisory services, marketing assistance, market information, technology development and transfer, and business linkage promotion.⁴⁹

BDS are provided by MFIs using any of the following modalities: i) direct provision; ii) forming strategic alliance with existing BDS providers; or iii) establishing specialized, subsidiary or "spin-off" firms to handle the BDS requirements of clients.

When there are no other organizations that offer the services to the microfinance clients, the MFI usually considers developing a complementary BDS program. The following are MFIs that provide BDS to their clients: the Center for Agriculture and Rural Development (CARD); Alalay Sa Kaunlaran, Inc. (ASKI); and Taytay Sa Kauswagan, Inc. (TSKI). All of them have used the third option in providing BDS.

Partnership between Microfinance Institutions and PhilHealth (KaSAPI)

To enable the Philippine Health Insurance Corporation (PhilHealth) to reach its goal of universal coverage, it has to reach out to both those employed formally and those within the informal sector. Thus, in 2005, PhilHealth launched the *Kalusugang Sigurado at Abot-Kaya sa PhilHealth Insurance* or KaSAPI Program. KaSAPI is an innovative scheme of PhilHealth that enables it to reach out and enroll the informal sector under the National Health Insurance Program (NHIP) by partnering with big MFIs, such as cooperatives, rural banks and other organized groups. Organized groups with more than 1,000 members and with strong operational, management and financial capacities were invited to become KaSAPI partners.

Under the scheme, the collection mechanism of the MFIs (e.g., the weekly center meetings held to collect loans) is used to implement the flexible alternative payment scheme. This payment scheme made the PhilHealth premium contributions

⁴⁹ *Business Development Services for Microenterprises: A Guide for MFIs*, DOF-NCC and NAPC; developed under the ADB-TA Support to the Microfinance Development Program.

affordable to the informal sector.

From only four organized group-partners in 2006 (i.e., three MFIs and one rural bank) there are already seventeen organized groups that have signed a Memorandum of Agreement (MOA) with PhilHealth as of December 2009. Only nine organizations, however, were able to meet the required minimum number of actual enrollees. This translates to an enrollment of 27,853 in 2009 to the NHIP through KaSAPI.

RESPONDING TO THE CHALLENGE OF RISK PROTECTION: MICROINSURANCE

After several cycles of microfinance provision (i.e., savings and credit services), MFIs have realized that gains resulting from continued access to savings and credit services are usually eroded when contingent events arise. The poor are vulnerable to risks such as illness, physical injury, accident, or death; basic business risks; loss of property; loss of job; theft; and abrupt swings in the economy. Those belonging to the low-income sector have inadequate, or in some cases, no access to risk protection services. Most of the times, they are financially unprepared to cope with and mitigate these risks. Because of this, MFIs realized the need to assist their clients with financial products that will help them manage these risks and/or provide financial relief when contingent events occur.

The National Strategy and the Regulatory Framework for Microinsurance

Recognizing that the poor need to be protected against risks and having learned that the private sector has the technical and financial expertise in providing the poor sustained access to financial services, the government launched and issued the National Strategy and the Regulatory Framework for Microinsurance in January 2010. These documents provide the pillars for the development of the microinsurance market in the Philippines. Both documents were crafted in partnership with the private sector and generally call for increased private sector participation in the provision of risk protection to the low-income sector.

In line with the National Strategy for Microfinance, the National Strategy for Microinsurance also envisions the development of a viable and sustainable microinsurance market. This shall be achieved through the establishment of an appropriate policy and regulatory environment for the safe and sound provision of microinsurance by the private sector. Under the strategy, informal insurance and insurance-like activities shall also be mainstreamed into the formal system. To encourage and promote microinsurance to both providers and potential clients, a financial literacy campaign on microinsurance shall likewise be launched and institutionalized.

To delineate microinsurance from the regular insurance products offered by most insurance providers,⁵⁰ microinsurance is defined as a financial product or service that meets the risk protection

⁵⁰ In the Philippines, insurance companies (life and non-life), cooperative insurance societies and mutual benefit associations licensed by the Insurance Commission are the only entities allowed to provide insurance products and services.

needs of the poor where:

- i. the amount of premiums, contributions, fees or charges, computed on a daily basis, does not exceed five percent of the current daily minimum wage rate for non-agricultural workers in Metro Manila;⁵¹ and
- ii. the maximum sum of guaranteed benefits is not more than 500 times the daily minimum wage rate for non-agricultural workers in Metro Manila.⁵²

The National Strategy for Microinsurance highlights the distinct roles of the government and the private sector in protecting the poor against risks. Under the strategy, government's role is limited to the provision of an enabling policy and regulatory environment for greater private sector participation in the provision of microinsurance products and services. In line with this, the Insurance Commission has recently issued several circulars providing a regulatory space for the provision of microinsurance.⁵³

Recent and On-going Developments for Microinsurance Development

Establishment of Performance Standards for Microinsurance

Recognizing that an increasing number of institutions shall be interested in the provision of microinsurance products and services, the government through the National Credit Council (NCC) and the Insurance Commission, in partnership with concerned industry associations, developed the standards of performance for microinsurance. These performance standards shall set the benchmark for prudential and market conduct behavior to ensure that the poor is adequately protected. The performance standards shall be used by the regulators and provide them the necessary information that will enable them to determine the viability and sustainability of entities engaged in the provision of microinsurance products and services.

Financial Literacy (Microinsurance Literacy)

Since "insurance is sold rather than bought", the government, in partnership with the donor community and the private sector, shall conduct a massive insurance literacy campaign.⁵⁴ The literacy and awareness campaign aims to develop a strong insurance culture among the Filipino people, especially those in the low-income sector. It is expected to change the mindset of concerned stakeholders towards insurance for the low-income and informal sector. Participation of the local government units shall also be enjoined in the campaign.

⁵¹ The five percent ceiling for premium for microinsurance considers improved efficiency in the Insurance Industry resulting from better and improved mortality rates and technology, and the increased number of insured thereby spreading risks to a greater number and lowering costs of insurance delivery.

⁵² The maximum coverage can provide 16.5 months (500 days) of lost income resulting from any unforeseen or contingent event happening to the insured. This is deemed sufficient to augment the needs of the family of the insured. This insurance coverage can be provided with the maximum 5% ceiling.

⁵³ As a first step, the Insurance Commission has issued on January 29, 2010 Insurance Memorandum Circular 1-2010 providing for the regulation of microinsurance products and services.

⁵⁴ The Asian Development Bank (ADB) Developing Microinsurance Project and the German Technical Assistance (GTZ) Microinsurance Innovations Project for Social Security are both providing technical assistance and funding support to the government in the development and implementation of the "Roadmap to Financial Literacy on Microinsurance".

Product Development

Considering the peculiar needs of the low-income sector, simple, innovative and affordable microinsurance products that are tailor-fitted to the needs of the poor are now being developed. Recently, the Insurance Commission has approved a prototype policy contract for non-life microinsurance product. A prototype policy contract is also currently being developed for life microinsurance product. Unlike the traditional insurance policy contracts, these policy contracts are short, simple, and easy to understand.

DONOR SUPPORT TO THE MICROFINANCE SECTOR

Various donors supported the development of the Philippine microfinance sector. Among others, technical and funding assistance were provided by the United States Agency for International Development (USAID), the United Nations Development Programme (UNDP), the Asian Development Bank (ADB), and the European Union (EU).

United States Agency for International Development (USAID):

USAID has provided a three-pronged support to microfinance development in the Philippines. The first is the implementation of the Credit Policy Improvement Program (CPIP), a technical assistance to the National Credit Council (NCC) under the Department of Finance. CPIP provided technical assistance to the government (DOF-NCC in particular) in establishing a policy and regulatory environment that encouraged the private sector to participate in the provision of microfinance services. CPIP was implemented from November 1996 to February 2006. This assistance resulted in the adoption of key policy reforms that provided commercialization impetus to the sector.

In addition to the policy level support, USAID also provided assistance to rural banks through the Microenterprise Access to Banking Services (MABS) Project. The MABS program is an initiative that supports the Philippine rural banking industry to significantly expand microenterprise access to bank-microfinance services. Specifically, the program provides technical assistance and training in various areas of microfinance operations to partner rural banks. Partner rural banks offer microfinance loans and deposit services specially tailored to microenterprise clients. Since its inception in 1998, the MABS Program has helped more than 230 rural banks and branches in the Philippines.

Aside from rural banks, USAID also provided assistance to cooperatives engaged in savings and credit operations through the Credit Union Enhancement and Strengthening (CUES) Program. The main objective of CUES is to identify and transform credit cooperatives into safe and sound institutions. Aside from enjoining partner-cooperatives to adopt the model credit union approach⁵⁵ in their operations, CUES also implemented a microfinance component—the Savings and Credit with Education (SCWE) component. Under the SCWE, women in the

⁵⁵ The Model Credit Union Approach focuses on instituting financial discipline among the partner cooperatives. Among other things, financial discipline focuses on the importance of efficiently managing its operations and properly managing its loan portfolio by implementing appropriate policies and procedures for maintaining good portfolio quality.

rural areas are organized into village centers and are provided microfinance services through the partner-cooperatives. Upon project completion, the partner-cooperatives had organized the Model Cooperative Network (MCN), which continued to provide similar technical assistance to its members.

Asian Development Bank (ADB): In 2006, the ADB provided a US\$150 million Microfinance Development Program loan to the Philippine government. The assistance focused on the following: strengthening the regulatory and supervisory capacities of concerned institutions for a sound microfinance sector; building the capacities of MFIs to provide cost-efficient microfinance services to the poor; and improving financial literacy and increasing consumer protection for the poor. Accompanying the program loan is a technical assistance and two grants that assisted concerned government agencies in implementing the needed reforms. The technical assistance focused on the following areas: i) development of consumer protection and business development services guidebook for MFIs; ii) development and implementation of training modules for various types of MFIs on the use of the PESO performance standards; iii) development of the National Microfinance Literacy Program Framework and conduct of relevant training courses; and iv) provision of technical assistance to the National Credit Council (NCC) and the National Anti-Poverty Commission (NAPC) in implementing the relevant reforms to strengthen the regulatory environment for the microfinance sector.

United Nations Development Programme (UNDP): In 1998, the Philippines became one of the recipients of the “Microfinance Support Project” (MSP) under UNDP’s Global MicroStart Programme. The MSP assists partner MFIs to have efficient and sustainable microfinance operations using the ASA methodology.⁵⁶ Phase 1 of the program covered 20 MFIs (mostly start-ups and small NGOs).

Carrying the lessons learned from the first phase, the second phase of MSP was launched in January 2003. Phase 2 focused on providing technical assistance to three big MFIs that showed capacity for exponential growth and commitment to adopt the ASA system, namely CARD NGO, CCT Credit Cooperative, and LifeBank. The second phase ended in June 2004.

International Fund for Agricultural Development (IFAD): Apart from financing projects related to agricultural development, IFAD also funded a program for microfinance in the Philippines—the Rural Micro-Enterprise Promotion Program (RUMEPP). It has two components: micro-credit and support component and the microenterprise promotion and development component. The first component provides loan funds and capacity building assistance to MFIs. Loan funds are provided at market rates through the Small Business Corporation (SBC) while capacity building includes training, systems development, and provision of institutional loans and matching grants to enable MFIs to open new microfinance

windows in the program target areas. The second component provides efficient, cost-effective and demand-responsive business development services to rural micro-enterprises.

European Union (EU): The EU provided assistance to specific area-based development programs. In addition to the development components of the programs, the EU also provided capacity building funds for partner-MFIs in the project area. For some projects, microfinance loanable funds were deposited as trust funds in and administered by the PCFC. The funds are then provided to their partner MFIs at market rates using the eligibility and creditworthiness criteria of the wholesale lending institution. The partner-MFIs then lend to the program participants in the area.

Aside from these, the EU has also provided funding to improve financial inclusion and build social impact towards food security in Southeast Asia. The Philippines is one of the countries in the region that was given financial assistance. The program aims to build the capacity of MFIs and their networks to increase financial inclusiveness in rural areas in order to help farm households improve their food security. The program is being implemented in partnership with the Microfinance Council of the Philippines, Inc. (MCPI). It has the following components: i) strengthening MCPI’s capacity to serve its members & stakeholders; ii) strengthening MFI operations through customized on-site coaching and mentoring of MFI staff using the social performance management (SPM) approach; iii) providing support for the development and testing of new or improved financial services for farm households; and iv) training rural households on their rights and responsibilities as microfinance clients.

International NGOs and Foundations. Aside from the Official Development Assistance (ODA) provided by foreign donors through the government, a number of international NGOs also provided assistance to the Philippine microfinance sector. Assistance is usually coursed directly to MFIs or network of MFIs (e.g., MCPI, cooperative federations, and regional microfinance councils). These include, among others, the following: Interchurch Organisation for Development Cooperation (ICCO), CORDAID, Small Enterprise Education and Promotion Network (SEEP), ECLIF, and Oikocredit.

⁵⁶ The ASA methodology is touted as a unique low-cost, fast expansion microfinance technology.

ADDRESSING MULTIPLE BORROWING

The growth of microfinance in the Philippines has largely been demonstrated by the profitability of the sector enabling MFIs to expand their operations. As profitability is demonstrated, an increased number of financial institutions have become interested in microfinance. This resulted in competition among MFIs and more recently, a growing concern for multiple borrowings, or worse, credit pollution.

Anecdotal evidences in other countries show that there are a number of reasons why clients borrow from multiple sources: to finance their investment and microenterprise expansion plans (Krishnaswamy 2007); to cope with unexpected economic shocks (Chaudhury and Matin 2002); to take advantage of the lower interest rate loans to pay higher interest rate loans (Venkata and Veena 2010). Some analysts even point out that competition for borrowers between and among MFIs served as an incentive for microfinance clients to engage in multiple borrowing.⁵⁷

While there are yet no hard evidence that multiple borrowing has resulted or results in borrower' over indebtedness, the lack of a centralized information system that provides information on borrower's current level of indebtedness coupled with the aggressiveness of loan officers at the MFI level are sector concerns that need to be addressed.⁵⁸ Credit bureaus, however, are not necessarily "silver bullets" that would prevent borrower over-indebtedness. Lender's policy on how data coming from credit bureaus is used is still an important consideration in preventing borrower over indebtedness.

Considering that there is already an enabling law for the establishment of a central credit information system, this concern should be given importance not just by the government but also by the network of MFIs looking after the viability of the sector and the welfare of the MFI clients.

LOOKING FOR THE RIGHT DESIGN FOR FINANCING THE POOR IN AGRICULTURE

Studies have shown that the growth of the microfinance sector has been biased towards the urban areas. Majority of the

⁵⁷ See, for instance, Krishnaswamy, Karuna, 2007, "Competition and Multiple Borrowing in the Indian Microfinance Sector," Institute for Financial Management and Research, Centre for Micro Finance Working Paper, September 2007; and McIntosh, C., A. de Janvry, and E. Sadoulet, "How Rising Competition Among Microfinance Institutions Affects Incumbent Lenders," The Economic Journal, Vol. 115(506), pages 987-1004, Royal Economic Society, October 2005. The author wishes to thank Prof. Erwin Tiongson of the Asian Institute of Management for pointing out these references.

⁵⁸ The Asian Institute of Management, in partnership with MCPI, Oikocredit, and Grameen Foundation, is currently conducting a study that aims to determine the incidence of multiple borrowing among MFI clients in an area where there are several MFIs operating. The study, however, does not intend to determine if multiple borrowing leads to over-indebtedness of borrowers.

MFIs are located in the urban areas and have mostly been catering to the urban poor, who are engaged in retail or trading microenterprises. Considering that more than 50 percent of the poor reside in the rural areas, whose economic activities are mostly agriculture-based, the challenge is for microfinance to meet the financial service needs of the rural, agriculture-based poor population.

Lending to the poor in the agriculture sector still remains a challenge to this day. The complexity of agriculture brought about by the risks associated with agricultural economic activities poses some challenges to microfinance. While some MFIs have embarked on designing microfinance products for clients in the agriculture sector, evidence shows that the schemes were mostly saddled by high delinquencies after several cycles. The peculiarities of the agriculture sector make it difficult to design microfinance products that would fit all types of commodities in all localities. While market price fluctuations and systemic risks in agriculture are challenges beyond the microfinance sector, these are considered important factors on how the rural-agricultural based poor can be given continued access to financial services.

More recently, there is a growing interest on how microfinance can participate in value-chain financing. Given the importance of the input and the output market in ensuring profitability and sustainability of income from the agriculture sector, value-chain financing has long been recognized as an important concept in making agriculture profitable. However, value-chain financing in recent past have mostly been focused on small and medium-sized agri-based enterprises. If there were small farmers receiving credit from "value-chain financing", this has mostly been provided through either input-suppliers or trader-lenders. Given this phenomenon and considering that MFIs, especially those operating in the rural areas, are looking at effective means of helping their clients increase their incomes from their agriculture-based economic activities, the challenge is on how MFIs can participate in value-chain financing. This is an area worth looking into.

PROTECTING MICROFINANCE CLIENTS

Clients of microfinance are considered vulnerable groups. They are considered vulnerable in two ways: first, the income from entrepreneurial activities that were financed by microfinance are usually eroded when they are affected by contingent events such as death, illness, fire, earthquake, typhoons and other natural disasters; and second, they are prone to being taken advantage of by unfair and unscrupulous lenders. Oftentimes, they are not prepared to handle contingent events and are at a loss, or worse, not aware when taken advantage of.

Vulnerability to contingent events is now being addressed through microinsurance. Convincing the poor of their need for insurance and prompting them to buy insurance is still a challenge.⁵⁹ Related to this is the challenge for insurance providers to innovate and design insurance products tailor-fitted to the needs of the poor. This includes a reconsideration of their existing underwriting

⁵⁹ Since the poor are more concerned of the present than the future, the challenge becomes increasingly important.

and claims settlement procedures to ensure that these meet the requirements and circumstances of the low-income sector.

As more institutions provide financial services to the poor, the risks of being exposed to institutions that may take advantage of their vulnerability resulting from non-transparency and full disclosure become increasingly real. In view of this, it is always important to educate potential and existing clients of microfinance on the roles and responsibilities of both lenders and borrowers, including their rights and privileges. Recently, the Smart Campaign came up with the following Client Protection Principles (CPPs): i) avoidance of over-indebtedness; ii) transparent and responsible pricing; iii) appropriate collections practices; iv) ethical staff behavior; v) mechanisms for redress of grievances and vi) privacy of client data. Tools have recently been developed that are being made available for MFIs to enable them to consciously be aware of how their institutions are abiding by the CPPs.⁶⁰

Realizing the importance of protecting the microfinance clients from abuse and non-transparent microfinance practices, MCPI, Oikocredit and other institutions, have included client protection in its advocacies. These organizations promote CPP in various fora, provide training on the CPPs, and conduct assessments on the MFI's client protection practices.

These client vulnerability concerns emphasize the importance of financial literacy for microfinance clients. Providing financial literacy for microfinance clients is a major and priority agenda that should not be overlooked as the microfinance sector moves forward.

GRADUATING MICROFINANCE CLIENTS: THE MISSING MIDDLE

As businesses of microentrepreneurs grow from micro to small enterprises, higher amount of working capital is needed. Oftentimes, the amounts required are beyond what some MFIs can afford to lend. The bigger financial institutions that can afford their working capital requirement, however, are not inclined to extend the needed resources inasmuch as the graduating microentrepreneur often cannot comply with or does not have the requirements imposed by big financial institutions.

Aside from financial resources, these graduating microentrepreneurs also have non-financial services requirements that would help them expand their business and venture into better and more stable markets. This calls for improved and more responsive business development services. There is a need to address this gap. The complicated and tedious requirements of financial institutions that have the capacity to lend to graduating microentrepreneur should be reviewed. Along this line, supervision and examination policies and procedures of concerned regulatory authorities should also be reviewed to determine those that may discriminate against small enterprise lending. Also, there may be a need to

⁶⁰ The Client Protection Principles (CPPs) serve as an industry-wide code of conduct and a proactive assertion of microfinance as a double bottom line industry. The principles came from a synthesis of existing codes of conduct from a number of microfinance networks and associations. The main points of agreement became the Client Protection Principles (see, Beyond Codes: Foundation for Client Protection in Microfinance, October, 2010).

review the current system on chattel mortgages that at present does not consider moveables (inventories, purchase orders, warehouse, future produce, etc.) as collateral for lending. It is believed that recognition of moveables as collateral may open up financing to microenterprises graduating to small (the missing middle) enterprises. Similarly, this will also boost value chain financing. In the same manner, the network of MFIs may advocate the establishment of a registry for moveable collaterals.

REGULATING AND SUPERVISING COOPERATIVES ENGAGED IN SAVINGS AND CREDIT OPERATIONS

Cooperatives engaged in savings and credit services perform a significant role in providing financial services to the poor. Cooperative members comprise a sizable portion of the microfinance borrowers in the country, with majority belonging to the low-income sector.

As of June 2010, there are 1,444 credit cooperatives and more than 13,000 multi-purpose cooperatives. About 80 percent of the multi-purpose cooperatives are engaged in savings and credit operations and therefore provide some form of financial services to the poor. At present, there is yet no systematic set of data that provides an accurate set of information on the financial performance of cooperatives engaged in savings and credit operations. Pieces of information indicate though that there are already a few cooperatives that compares with rural banks in terms of resources. Nonetheless, institutional hurdles have hampered the full maximization of the potentials of cooperatives. As the policy paper "Mainstreaming Micro" (PinoyMe Foundation, April 2010) averred:

The current state of the cooperative sector can be traced primarily to a poor regulatory environment and the lack of effectiveness of the CDA as a regulator. For almost two decades, CDA has focused mainly on its developmental functions rather than on its regulatory functions, in part because the CDA Charter is ambiguous and does not grant the CDA the necessary authority to regulate cooperatives. Considering the potential of cooperatives as vehicles for promoting social and economic empowerment in the rural areas, the thrusts of the CDA need to be refocused and its policy and regulatory functions need to be enhanced so that it can help strengthen cooperatives in the areas of governance, management and operations, among others. An amendment to the CDA Charter, the restructuring of its organization, and the professionalization of its staff (following the BSP as a possible model) will create a strong cooperatives sector that can help deliver microfinance services in the rural areas.⁶¹

⁶¹ "Mainstreaming Micro: The State of the Art of Microfinance and Microenterprise Development in the Philippines," sponsored by the Ninoy & Cory Aquino Foundation, Hanns Seidel Foundation, PinoyMe Foundation; April 2010. This paper is a product of the collaborative effort of several individuals and institutions convened by PinoyME through its strategic research initiative. The following participated in the preparation of this paper: Dr. Cayetano Paderanga, Dr. Gilbert Llanto, Prof. Ronald Chua, Dr. Ma. Piedad Geron, Dr. Erwin Tiongson, Dr. Fernando Aldaba, Prof. Salvador Sibayan (UP Institute of Small Scale Industries), Ms. Pinky Abellada (Pulse Asia), Dir. Joselito Almario, (National Credit Council), Danilo Songco and Angelica Espinosa (PinoyME), Ms. Jocelyn Badiola (Agricultural Credit and Policy Council), Mr. Jerry Pacturan (Philippine Development Assistance Program), Ms. Gemma Marin (John J. Carol Institute of Church and Social Issues), Ms. Lalaine Joyas (Microfinance Council of the Phils., Inc.), and Mr. Reuel Virtucio (PUNLA Foundation).

MANAGING MISSION DRIFT

The increasing commercialization of the microfinance sector the world over has provided strong incentives for private capital investors to come in, which triggered to some extent the expansion of MFIs' operations and the consequent increase in the number of microfinance clients. The increase in private investments also resulted in an increased number of institutions that are interested in providing financial services to the poor thereby facilitating greater competition in the sector. This has spurred operational efficiency prompting MFIs to cut costs, provide products that are responsive to the needs of its clients, and generate higher returns from operations. This then pushed a number of MFIs to focus more on profitability; oftentimes neglecting their original mission of using microfinance as a tool for poverty alleviation.

In view of this, the threat of mission drift is a concern. There is a growing concern that commercialization and increased competition could result in too much profiteering to the disadvantaged of the poor.

MCPI in recent years has been advocating for the institutionalization of SPM processes and systems within MFIs that support their social goals and objectives.

MCPI's program on SPM aimed to achieve the following: achieve a significant number of MFIs that are actively managing their social performance; improve practice in SPM; provide further evidence of the contribution of SPM towards the financial bottom line of MFIs; establish SPM as a reliable basis for the reporting of social performance information to external stakeholders; and support and promote the use of SPM within and outside the region. The association employed the following as strategies to achieve its goals on SPM: (1) promotion and advocacy; (2) capacity building; (3) lateral learning, documentation and dissemination; (4) regional capacity program; and (5) social audit and performance review.

Yearend Reports on BSP Initiatives

2006 Official Poverty Statistics. National Statistical Coordination Board

Asian Development Bank. Report and Recommendation of the President to the Board of Directors on a Proposed Loan and Technical Assistance Grant to the Republic of the Philippines for the Microfinance Development Program, October 2005

Asian Development Bank. Enhancing the Efficiency of Overseas Workers' Remittances. Final report. Manila: ADB. 2004.

Asian Development Bank. Philippines: Microfinance Development Program. Asian Development Bank. Program Number: 38579-01. Loan Number: 2199. November 2007

Asian Development Outlook 2009 – Philippines. Asian Development Bank.

Business Development Services for Microenterprises: A Guide for MFIs, DOF-NCC and NAPC. Developed under the ADB-TA Support to the Microfinance Development Program, 2008.

Branchless Banking for Inclusive Finance. Consultative Group to Assist the Poorest. August 2007.

Pickens, Mark, "Window on the Unbanked: Mobile Money in the Philippines," CGAP, December, 2009

Chaudhury, Iftekhar, and Imran Martin, 2002, "Dimensions and dynamics of microfinance membership overlap – a micro study from Bangladesh," Small Enterprise Development, Vol. 13, No. 2.

Clark, Heather, "Beyond Codes: The Foundation for Client Protection", 2010.

Espenilla, Nestor, "Banking Supervision and Examination in the Philippines," Paper presented during the IMF-FSA Conference on *Financial Stability and Financial Sector Supervision: Lessons from the Past Decade and Way Forward* to be held in Tokyo, Japan on 17 December 2007.

Ferguson, Bruce. "Micro-finance of housing: a key to housing the low or moderate-income majority?" Environment and Urbanization. April 1999.

Fernando, Nimal. "Low-Income Households Access to Financial Services." EARD Special Studies. Asian Development Bank, October 2007.

USEFUL WEBSITES

www.bsp.gov.ph

(Bangko Sentral ng Pilipinas)

www.bwtp.org

(Banking with the Poor)

www.cgap

(Consultative Group to Assist the Poorest)

www.mcpi.org

(Microfinance Council of the Philippines)

www.mdgs.un.org

(Millenniums Development Goals)

www.mixmarket.org

(Microfinance Information Exchange)

www.nscb.gov.ph

(National Statistics Coordination Board)

www.nso.gov.ph, www.census.gov.ph

(National Statistics Office)

www.oecd.org

(Organization of Economic Cooperation and Development)

www.ruralfinance.org

(FAO Rural Finance)

www.uncdf.org

(United Nations Capital Development Fund)

www.web.worldbank.org

(World Bank)

www.adb.org

(Asian Development Bank)

www.rbapmabs.org

www.oikocredit.org

(OikoCredit)

www.grameenfoundation.org

www.pinoyme.org

www.micraphilippines.org

www.seedfinance.org

Geron, Ma. Piedad. "Philippine Country Study on Microfinance." MicroNED. October 2006.

JBIC Pilot Study on Sustainable Microfinance for Poverty Reduction in the Philippines. November 2004.

Jimenez E and Roman P. "Electronic Banking: Delivering Microfinance Services to the Poor in the Philippines," 2004

Krishnaswamy, Karuna. "Competition and Multiple Borrowing in the Indian Microfinance Sector," Institute for Financial Management and Research, Centre for Micro Finance Working Paper, September 2007.

Lirio, R. "Central Bank's Regulatory Role over Non-Bank Financial Institutions," 2002.

Llanto, Gilberto M. "Policy and Regulatory Issues and Challenges in Microinsurance: A Philippine Case." Philippine Journal of Development, Number 62, First Semester 2007, Volume XXXIV, Number 1, Philippine Institute for Development Studies.

MCPI Members' Performance Report on Outreach and Loan Portfolio, December 2006.

Microfinance Consumer Protection Guidebook 2007.

Microfinance Council of the Philippines. "Philippine Country Profile on Microfinance," submitted to the Banking with the Poor (BWTP) Network, May 2006.

Microfinance Program for Water Supply and Sanitation, Final Report, Philippine Water Revolving Fund. 2010

National Strategy for Microfinance, NCC-DOF, 2007.

National Strategy for Microinsurance, NCC-DOF, 2010

Sicat, Allan and Scott B. Gaul, "Benchmarking Philippine Microfinance, 2005," Microfinance Information Exchange (MIX), November, 2006.

Ofreneo, Rosalinda, "Policy Brief on Health Insurance," May 2009

Regulatory Framework for Microfinance in the Philippines. NCC, DOF. Unpublished document.

Regulatory Framework for Microinsurance, NCC, DOF, 2010

Venkata, N. A. and A. Veena Yamini, 2010, "Why Do Microfinance Clients Take Multiple Loans?" MicroSave India Focus Note 33 February 2010.

Policy Measures	Key Provisions
<p>Enactment of the Social Reform and Poverty Alleviation Act, December 11, 1997</p>	<ul style="list-style-type: none"> • Defining capacity building to exclude any and all forms of seed funding, equity infusion, and partnership funds from government to microfinance institutions • Deletion of equity funding from the list of specific uses of the People’s Development Trust Fund (PDTF), a trust fund created under the law aimed at funding capability building activities for MFIs • Rationalization of directed credit and guarantee programs • Emphasis on savings mobilization
<p>Enactment of the Agricultural Fisheries Modernization Act (AFMA), December 22, 1997</p>	<ul style="list-style-type: none"> • Phase-out of directed credit programs in the agriculture sector over a four year period (i.e., ending February 2002) • Rationalization of loan guarantee programs • Adoption of market-based interest rates • Non-provision of credit subsidies • Review of mandates and performance of government agencies and government financial institutions in light of the rationalization of directed credit programs
<p>Issuance of EO138 (August 10, 1999) directing government agencies implementing credit programs to adopt the NCC Credit Policy Guidelines.⁶⁵</p>	<ul style="list-style-type: none"> • Non-participation of government non-financial agencies in the implementation of credit programs • Government financial institutions to be the main vehicle in the implementation of government credit programs • Adoption of market-based financial and credit policies • Increased participation of the private sector in the delivery of financial services
<p>Approval of the design of the Agricultural Modernization Credit and Financing Program (AMCFP).</p>	<ul style="list-style-type: none"> • No further implementation of directed credit programs by government non-financial agencies by end 2002 • Limit lending decisions only to banks, viable cooperatives and microfinance NGOs • Adoption of market-determined lending rates to enable conduits to cover their costs and achieve sustainability in the long run • Focus of the Department of Agriculture on monitoring and evaluation of AMCFP, provision of infrastructure, institution building, research and extension and the provision of an appropriate policy environment conducive for increased private sector participation.
<p>Enactment of the General Banking Act (GBA), May 23, 2000, which includes provisions mandating the Bangko Sentral ng Pilipinas (BSP) to recognize the unique nature of microfinance as it formulates banking policies and regulations.</p>	<ul style="list-style-type: none"> • Lifting of the moratorium on branching, specifically for microfinance banks • Issuance of BSP Circular 272 on January 30, 2001, implementing the microfinance provisions of the GBA • Review of the examination process to reflect the special nature of microfinance, e.g., non-collateralized loans
<p>Enactment of the Barangay Microenterprise Business Act.</p>	<p>This law directs the adoption of market-based credit policies in the provision of financial services to barangay or village-based micro-enterprises. Government wholesale financial institutions are directed to create special credit windows adopting market-based interest rates for private financial institutions intending to provide credit to barangay micro-enterprise business.</p>

⁶⁵ EO 138 was repealed by EO 558 on 8 August 2006. The repeal was, however, clarified in EO 558A issued on October 27, 2006. EO 558A states that the repeal provisions of EO 558 shall only apply to the municipalities and barangays where there are no identified and available participating private financial institutions (PFIs) such as banks, cooperatives and non-governmental organizations that serve the needs of the poor and marginalized sectors of the economy.

Institutional Type	Minimum Capital Requirement (Php)	MCR as % of MCR for Regular Commercial Banks
Supervised by BSP		
Commercial Bank – Expanded (Universal)	P5,400 million	192.8 %
Commercial Bank – Regular	P2,800 million	100.0 %
Thrift Bank – within Metro Manila	P400 million	14.3%
Thrift Bank – outside Metro Manila	P64 million	2.3%
Rural Bank – within Metro Manila #	P32 million	1.3%
Rural Bank – within Cebu, Davao #	P16 million	0.6%
Rural Bank – 1st/2nd/3rd class cities and 1st class municipalities	P8 million	0.3%
Rural Bank – 4th/5th/6th class cities and 2nd/3rd/4th class municipalities	P4.8 million	0.2%
Rural Bank – 5th/6th class municipalities	P3.2 million	0.1%
Cooperative Bank - National	P200 million	7.1%
Cooperative Rural Bank – Metro Manila	P20 million	0.7%
Cooperative Rural Bank – Cebu, Davao	P10 million	0.4%
Cooperative Rural Bank – Provincial	P5 million	0.2%
Quasi-bank	No MCR	Not Applicable
Not regulated//not supervised by BSP		
Finance Company - Metro Manila and Other 1st Class Cities	P10 million	0.4%
Finance Company – Other classes of cities	P5 million	0.2%
Finance Company – Municipalities Credit	P2.5 million	0.1%
Union/Savings-Credit Cooperative NGO	No MCR	Not Applicable
Micro Finance Institution	No MCR	Not Applicable

Source: IRIS Final Report. Microfinance Regulation in Seven Countries: A Comparative Study. (2006), SEC MC 13-2001.

CIRCULAR 272

(January 2001) provides the operating guidelines of the General Banking Law Provisions specifically it recognizes cash-flow based lending as a peculiar feature of microfinance, defines microfinance loans and provides for the exemption of microfinance loans from rules and regulations issued with regard to unsecured loans

CIRCULAR 273

(27 February 2001) partial lifting on moratorium on establishment of new banks as long as the new banks are microfinance-oriented

CIRCULAR 282

(19 April 2001) opens a rediscounting facility for rural banks/cooperative rural banks engaged in microfinance

CIRCULAR 324

(2 March 2002) opens a rediscounting facility for thrift banks engaged in microfinance

CIRCULAR LETTER 2002

– requiring reporting of banks with microfinance operations

CIRCULAR 340

(30 July 2002) provides the rules and regulations concerning the establishment of branches or loan collection and disbursement points (LCDPs);

CIRCULAR 365

(16 January 2003) liberalizes select provisions of Circular 340

CIRCULAR 364

(19 January 2003) Reduction to 75% the risk weight applicable to small and medium enterprises (SMEs) and microfinance loan portfolios that meet prudential standards

CIRCULAR 369

(17 February 2003) liberalizes select provisions of Circular 340

CIRCULAR 374

(11 March 2003) guidelines for the implementation of the Barangay Micro-Business Enterprise Law

CIRCULAR 409

(14 October 2003) provides the rules and regulations for the portfolio-at-risk (PAR) and the corresponding allowance for probable losses which depend on the number of days of missed payment

CIRCULAR 505

(22 December 2005) revises branching guidelines by allowing qualified microfinance oriented banks and microfinance oriented branches of regular banks to establish branches anywhere in the Philippines

CIRCULAR 549

(09 October 2006) exempts microfinance from the required submission of additional documents for the granting of loans

CIRCULAR 570

(24 May 2007) – allows wholesale loans of universal, commercial and branches of foreign banks to non-bank microfinance institutions as compliance to the 6% mandatory credit allocation to small enterprises.

CIRCULAR 607

(30 April 2008) – amends Circular Letter dated 2 October 2002 on the reportorial requirements banks' microfinance loans

CIRCULAR 625

(14 October 2008) – provides rules and regulations that govern the mandatory allocation of credit resources to micro, small and medium enterprises

CIRCULAR 649

(09 March 2009) – provides the guidelines governing the issuance of electronic money (e-money) and the operations of electronic money issuers (EMI) in the Philippines

CIRCULAR 669

(22 October 2009) – allows the servicing of limited withdrawals by microfinance/BMBE clients in LCDPs and OBOs of microfinance oriented banks/branches

CIRCULAR 678

(6 January 2010) – provides rules and regulations that govern the approval of banks' housing microfinance products

CIRCULAR 680

(03 February 2010) – provides rules and regulations on the approval of banks' micro-agri loans

CIRCULAR 683

(23 February 2010) – provides rules and regulations in the marketing, sale and servicing of microinsurance products by banks

CIRCULAR 685

(7 April 2010) – provides rules and regulations for the recognition of Microfinance Institution Rating Agencies

Source: http://www.bsp.gov.ph/about/advocacies_micro_circ.asp

ANNEX D PERFORMANCE STANDARDS FOR MICROFINANCE

AREA	INDICATOR	DEFINITION / RATIO	STANDARD	WEIGHT
I. PORTFOLIO QUALITY				40
	Portfolio at Risk	$\frac{\text{Balance of loans with at least one day missed payment}}{\text{Total Loans Outstanding}}$	PAR - 1 5%	20
	Loan Loss Reserve Ratio	$\frac{\text{Total Allowance Provided}}{\text{Total Required Allowance}}$	Required Reserves: Current – 1% PAR 1 to 30 – 2% PAR 31 to 60 – 20% PAR 61 to 90 – 50% PAR 91 & above and/or loans restructured twice – 100%	20
II. EFFICIENCY				30
	Administrative Efficiency	$\frac{\text{Administrative Costs}^{1/}}{\text{Average Gross Loan Portfolio}^{3/}}$ (Direct & Indirect Costs ^{1/})	10%	10
	Operational Self-sufficiency	$\frac{\text{Interest Income from Loans + Service Fees + Filing Fees + Fines, Penalties, Surcharges}}{\text{Financing Costs + Administrative Costs (Direct & Indirect costs)}}$	≥ 120%	10
	Loan Officer Productivity	$\frac{\text{Number of Active Borrowers}}{\text{Average Gross Loan Portfolio}}$	Group – ≥ to 300 Individual - ≥ to 150	10
III. SUSTAINABILITY				15
	Financial Self-sufficiency	$\frac{\text{Operating Revenue}}{\text{Financial Expense + Loan Loss Provision Expense + Adjusted Expenses}^{4/}}$	≥ 100%	10
	Loan Portfolio Profitability	$\frac{\text{Operating Revenue}}{\text{Average Net MF Loan Portfolio}}$	Greater than inflation rate during the period	5

^{1/} Administrative cost should include loan loss provision expense.

^{2/} $(\text{Beginning Gross Loan Portfolio} + \text{Ending Gross Loan Portfolio}) \div 2$

^{3/} Indirect Costs are allocated in proportion to the number of personnel directly dedicated to each cost center. Indirect cost allocated to the microfinance operations is computed as:

$$\text{Indirect Costs} = (\text{Number of Full-time MF Staff} \div \text{Total Number of Personnel}) \times \text{Total Indirect Costs}$$

Where:

- Full-time MF Staff – refers to employees working full-time in the microfinance operations regardless of employment status, i.e., whether contractual or regular.
- Total Indirect Costs – refers to costs shared by both the microfinance and non-microfinance operations. It includes, among others, salaries and benefits, rent, office materials and supplies, publications and publicity, transportation, travel and training for overhead staff, telephone and postage, insurance, utilities, repairs and maintenance, legal, audit and consultant fees, bank charges, taxes, and depreciation.

^{4/} Adjusted Expenses = Total Operating Expense + [(Average Equity – Average Fixed Assets) x Inflation Rate] + [(Market Interest Rate x Average Total Liabilities) – Actual Interest Expense] + Other Implicit Costs. Other Implicit Costs include those costs relevant to the conduct of its business such as grants, rent free building, donor paid technical advisor, or other subsidized expenses.

AREA	INDICATOR	DEFINITION / RATIO	STANDARD	WEIGHT
IV. OUTREACH				15
	Growth in Number of Active MF Clients	$\frac{\text{Ending No. of Active MF Clients}^{5/} - \text{Beginning No. of Active MF Clients}}{\text{Beginning No. of Active MF Clients}}$	Increasing	5
	Growth in Microfinance Loan Portfolio	$\frac{\text{Ending MF Loans Outstanding} - \text{Beginning MF Loans Outstanding}}{\text{Beginning MF Loans Outstanding}}$	Increasing	5
	Depth of Outreach	$\frac{\text{Total Loans Outstanding} + \text{Total Number of Borrowers}}{\text{GNP per Capita}}$	20% or below	5
TOTAL				100

^{5/} Active MF clients shall be those clients with savings and/or loans.

Source: The Philippine Microfinance Standards

Microfinance Council of the Philippines, Inc.
Unit 1909 Jollibee Plaza Condominium, F. Ortigas Jr. Road,
Ortigas Center, 1605 Pasig City
Philippines
Tel. No.: (+632) 631-6184 Telefax: (+632) 631-5920
E-mail: secretariat@microfinancecouncil.org
Website: www.microfinancecouncil.org