



Bangko Sentral ng Pilipinas

MAYNILA, PILIPINAS

OFFICE OF THE GOVERNOR

Circular No. 273
Series of 2001

The Monetary Board, in its Resolution No. 147 dated 25 January 2001 approved the partial lifting of the general moratorium on the licensing of new thrift and rural banks to allow the entry of microfinance-oriented banks, as follows:

Section 1. Microfinance-oriented banks may be established on a very selective basis, preferably in places not fully served by existing rural banks or in areas not fully serviced by microfinance-oriented banks, subject to the following additional criteria (in addition to standard licensing requirements):

1. That the microfinance-oriented bank to be established shall either be a thrift bank or a rural bank;
2. That the capital of the microfinance-oriented banks to be established should be owned by private persons, multilateral entities or a combination thereof;
3. That in the case of a rural bank to be established as a microfinance bank, the minimum paid-in capital shall be P5 million or the applicable existing capitalization requirement for a new rural bank, whichever is higher. The capitalization requirement under existing regulations shall apply to thrift banks;
4. That the organizers must have the capacity to engage in microfinancing, which may be indicated by the following:
 - a. At least twenty percent (20%) of the paid-in capital of the proposed bank must be owned by persons or entities with track record in microfinancing.
 - b. Majority of the members of the board of directors have experience in microfinancing with at least one member having actual banking experience.
 - c. The proposed bank must have as a minimum, an adequate loan tracking system that allows daily monitoring of loan releases, collection and arrearages, and any restructuring and refinancing.

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5. In addition to the requirements for the establishment of banks, in general, the application for authority to establish a microfinance-oriented bank must be accompanied by the following documents:
 - a. A vision and mission statement with clear expression of the commitment to reach low-income clients.
 - b. A written manual of operations, which shall include the administrative and credit program systems and procedures. The Manual must be consistent with the core principles, characteristics and features of microfinance, attached as Annex A.
6. At least fifty percent (50%) of the bank's gross loan portfolio at all times shall consist of microfinance loans as defined under existing Bangko Sentral ng Pilipinas regulations.

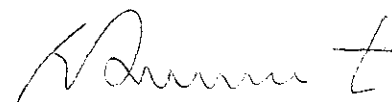
Section 2. The requirement that the President, Chief Operating Officer or General Manager of a rural or thrift bank must have at least two (2) years experience in banking and/or finance may be substituted with microfinance experience in cases of officers of a microfinance organization applying for authority to establish, or convert into a rural or thrift bank provided that the concerned officer is a college graduate.

Section 3. Subject to the standard branching requirements, microfinance-oriented banks are also hereby exempted from the general moratorium on the establishment of bank branches. After one year of profitable operations, a microfinance-oriented bank may apply for establishment of a branch but the Monetary Board may require additional capital to be put up for every branch in addition to the minimum capital of the thrift bank/rural bank.

Section 4. Existing microfinance organizations applying for authority to establish, or convert into a rural or thrift bank may be allowed to also convert their existing branches/offices into branches of the bank proposed to be established by simultaneously applying for authority for the purpose. However, the standard requirements for the establishment of branches, particularly the capitalization requirement, have to be complied with. Moreover, there must be a showing that the area is not fully served by any existing rural bank.

This Circular shall take effect immediately.

FOR THE MONETARY BOARD:


RAFAEL B. BUENAVENTURA
Governor

27 February 2001

NOTES ON MICROFINANCE

A. Definition of Microfinance

Microfinance is the provision of a broad range of financial services such as – deposits, loans, payment services, money transfers and insurance products – to the poor and low income households, for their microenterprises and small businesses, to enable them to raise their income levels and improve their living standards.

B. Core Principles for Microfinance

- The poor need access to appropriate financial services
- The poor has the capability to repay loans, pay the real cost of loans and general savings
- Microfinance is an effective tool for poverty alleviation
- Microfinance institutions must aim to provide financial services to an increasing number of disadvantaged people
- Microfinance can and should be undertaken on a sustainable basis
- Microfinance NGOs and programs must develop performance standards that will help define and govern the microfinance industry toward greater reach and sustainability

C. Characteristics and Features on Microfinance

Characteristics	Distinguishing Features
Type of Client	• Low income • Employment in informal sector; low wage Bracket • Lack of physical collateral • Closely interlinked household/business activities
Lending Technology	• Prompt approval & disbursement of micro loans • Lack of extensive loan records • Collateral substitutes; group-based guarantees • Conditional access to further micro-credits

	• Information-intensive character-based lending linked to cash flow analysis & group-based borrower selection
Loan Portfolio	• Highly volatile • Risk heavily dependent on portfolio management skills
Organizational Ideology	• Remote from/non-dependent on government • Cost recovery objective vs. profit maximizing
Institutional Structure	• Decentralized • Insufficient external control & regulation • Capital base is quasi-equity (grants, soft loans)

D. Definition of Microfinance loan

Microfinancing loans are small loans granted to the basic sectors, on the basis of the borrower's cash flow and other loans granted to the poor and low-income households for their microenterprises and small businesses to enable them to raise their income levels and improve their living standards. These loans are typically unsecured but it may also be secured as the case may be.

E. Level of Microfinance loan

Average microfinance loan of an NGO microfinance institution or of a cooperative bank or credit union in the Philippine case is about P25,000. To be realistic, the maximum principal amount of a microfinance loan can be pegged at P150,000. This is equivalent to the total resources of a microenterprise per **Small and Medium Enterprise Development Council Resolution No. 3, Series of 1995**.

F. Collateralization of Microfinance Loan

A microfinance borrower is not likely to be able to borrow from a large commercial, thrift or rural bank but from an NGO microfinance institution or perhaps from a small rural or cooperative bank. Thus, microfinance loans are typically unsecured, for relatively short periods of time (180 days) with monthly (or more frequent) amortizations of interest and principal, and often featuring a joint and several guarantee of one or more other persons and, certainly, seldom with tangible collateral. But in some cases, they can also be secured, depending on the capacity of the borrower to offer collaterals acceptable to the lending institution.

G. Interest on Microfinance Loans

Great caution should be exercised in drawing up regulations about interest rate ceilings on microfinance loans.

The old (and by now highly discredited as ineffective) approach to loans for low-income borrowers emphasized subsidized interest rates and did not recognize that subsidized below-market interest rates did not necessarily result in opening up access to financial services for low-income households and microenterprises.

The new approach which has been demonstrated by global experience is characterized by a market-based interest rate regime which permits the institution providing microfinance services to cover administrative costs, provisions for loan losses and intermediation/funding costs. This basis is consistent with financially sustainable rural finance and microfinance. Invariably, the global experience continues to validate the proposition that what matters most to the poor and underserved segments is access to financial services rather than their interest-rate cost – most especially because microenterprise and small business borrowers will take a microfinance loan whose period (monthly repayments) match the additional cash flows they hope to generate.

Therefore interest on such microfinancing loans shall be reasonable but shall not be lower than the prevailing market rates. This is to enable the lending institution to recover the financial and operational costs incidental to this type of microfinance lending.

H. Segments of Demand for Micro-credit

1. The landless who are engaged in agricultural work on a seasonal basis and manual laborers in forestry, mining, household industries, construction and transport: requires credit for consumption needs, but also for acquiring small productive assets, such as livestock.
2. Small and marginal farmers, rural artisans, weavers and those self-employed in the urban informal sector as hawkers, vendors and workers in household microenterprises: requires credit for working capital, including a small part for consumption needs. *This segment largely comprises the poor but not the poorest.*
3. Medium farmers/small entrepreneurs who have gone in for commercial crops and others engaged in dairy, poultry... Among no-farm activities, this segment includes those in villages and slums engaged in processing or manufacturing activity... *These persons live barely above the poverty line and also suffer from inadequate access to formal credit.*

(Source: IFAD Draft Appraisal Report, National Microfinance Support Programme, May 2000)