<u>National Roll-Out of Microfinance-exclusive CIB</u>
Key Note Address by:
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Distinguished Guests,

Ladies and Gentlemen,

I am extremely delighted to be part of this historic event of the launch of the national roll-out of microfinance dedicated CIB, and I congratulate all the stakeholders, Pakistan Microfinance Network, Pakistan Poverty Alleviation Fund, DFID, DataCheck, Microfinance Banks and MFIs, and my colleagues at SBP on this great achievement which will modernize and strengthen the 'industry infrastructure' of microfinance in Pakistan.

SBP has been actively supporting microfinance in Pakistan through policy, regulatory and program-based interventions to make major breakthroughs in reaching out to millions of underserved people who require a wide variety of financial services. The efforts to mainstream Microfinance into the formal financial

system started in 2000-2001 when the Government promulgated the Microfinance Institutions Ordinance. Presently, nine MFBs are operating in Pakistan. All these MFBs are privately owned and reflect diversity of ownership and approaches to microfinance banking. Considering that the market has potential and the regulatory framework is supportive, the ownership in MFBs has flowed both from local and international investors including banks, development agencies, investment funds, mobile network operators, and largest transformed MFIs. With the collective wisdom and efforts of all key stakeholders, the microfinance sector has spawned its own innovation, and the success of microfinance in Pakistan is widely acknowledged by the international community. Our microfinance regulatory framework has been ranked globally at the top in 2010 and 2011 by the independent "Economic Intelligence Unit" of UK's 'The Economist' Magazine. And Pakistan is the fastest developing market for branchless banking.

SBP has played a sterling role in the development of the microfinance sector as an alternative to conventional banking to serve the lower end of the market. However, there is a global shift from microfinance to inclusive finance, *that is*, from supporting microfinance initiatives in isolation to building an inclusive financial sector. Inclusive finance recognizes that a continuum of financial services providers work within their comparative advantages to serve the poor and low-income people, as well as micro and small enterprises. Financial inclusion is a core component of SBP's financial sector development strategy. It envisages transforming the financial market into an equitable system with efficient market-based financial services to the otherwise excluded poor and marginalized population including women and young people.

SBP's financial inclusion agenda is supported by a multi-pronged strategy. First, the regulatory framework to enable commercial microfinance in Pakistan is well-developed. The most recent regulatory innovation includes the introduction of the bank-led model for branchless banking. Second, SBP's commitment is

reflected by the in-house Development Finance Group, dedicated to increasing access to financial services. The Development Finance Group consists of departments that focus on key areas of financial inclusion including microfinance, agricultural credit, SMEs finance, and housing finance. Third, SBP has partnered with DFID to launch a GBP 50 million "Financial Inclusion Program" (FIP) to tackle financial exclusion among poor and marginalized groups head-on through a variety of supply-side funds and facilities. FIP focuses on market-based, sustainable financial services for low income people and small enterprises and to move away from a donor dependent model. In addition, FIP aims to enhance delivery of financial services through technology based branchless banking solutions, financial innovation, and remittances. Fourth, in line with the evidence (Access to Finance (A2F) Survey of 2008) that lack of financial literacy is a major constraint in advancing financial inclusion, SBP launched the first-ever Nationwide Financial Literacy Program (NLFP) in January 2012 to tackle this issue. The program focuses on different themes such as savings, budgeting,

debt management, investment, consumer protection and branchless banking to impart awareness and understanding of basic financial concepts to the low-income and unbanked population. Lastly, a number of initiatives have been taken to promote access to finance in the SMEs, agriculture, housing and microfinance sectors that largely focus on creating an enabling environment by addressing regulatory barriers, market failures and industry bottlenecks, and ensuring consumer protection.

Despite having in place internationally acclaimed regulations, innovative delivery channels, credit enhancement mechanisms and industry-wide initiatives for institutional and capacity development, and consumer protection, the growth in microfinance has remained stagnant at around 2 million borrowers in Pakistan in recent years, indicating that our success in achieving financial inclusion leaves much to be desired. This partly explains why Pakistan has one of the lowest financial penetration levels in the world with 56% adult population totally excluded, and another 32% informally served. Therefore, it is imperative that we all endeavor to bring these

segments into the formal banking channels to achieve our collective vision of 'access for all'.

The stagnancy in microfinance growth is attributable to various factors; most notably among them is the risk of multiple borrowings by clients. In a period of high growth during 2007-08, the staff of some MFIs followed unhealthy practices of clients vying and poaching that caused negative repercussions on loan portfolios of such MFIs. As the competition increased, the MFBs and MFIs became increasingly sensitive to the fact that without an information sharing mechanism, aggressive credit growth would lead to worsening of repayment performance, thereby creating systemic risk for the sector. The lack of a complete information sharing mechanism was due to the fact that only MFBs (regulated by the State Bank) had access to SBP's e-CIB; and non-regulated MFIs were neither posting nor retrieving credit history of their borrowers through SBP or a private CIB. Clearly, the lack of an exclusive credit bureau was contributing to the 'imperfection' of the credit market. At the same time, the experiences of borrowers' revolts and

government interventions in neighboring countries, such as Andhra Pardesh in India, were also forcing the lenders to pursue a risk-averse approach in Pakistan.

Taking a proactive approach in Pakistan and recognizing the potential risks in absence of a sound risk management framework nor a credit information sharing mechanism, policy makers and other key stakeholders explored different options to develop a long-term solution of credit information sharing. Finally, in May 2010, PMN and DataCheck in collaboration with SBP and PPAF, launched a pilot of MF-exclusive CIB at Lahore. The idea was to test and develop the reporting structures, MIS, and data storage/processing capabilities of lenders in the pilot and then prepare for a national roll-out at the appropriate time. Here, I would like to congratulate the leadership and team of DataCheck/PMN for their commitment and hard-work in making the pilot a successful project, and paving the way for the development of a dedicated national CIB for microfinance.

Currently, four CIBs are operational in Pakistan, three private and one public, all with varying stages of development. The largest and oldest is e-CIB, which is housed in the State Bank of Pakistan and requires all regulated financial institutions to report data on all loans and debt instruments, both disbursements and repayments. According to an IFC's paper on credit bureaus released in 2007 "Private credit bureaus are found in approximately 60 countries and in nearly every developed country. Public credit bureaus, usually set up by central banks and found mostly in developing countries, exist in approximately 70 countries." It is a matter of great satisfaction that Pakistan has credit bureaus both in the public and private sector. Having a private sector credit bureau exclusively for microfinance in particular is a source of both encouragement and pride for all of us. Let me assure you that SBP is fully supportive of private sector credit bureaus. However, presently private bureaus are non regulated entities. SBP believes that a policy framework for credit bureaus is essential for their smooth and long-term growth. In fact, the Government and SBP are already

working on the development of a legal framework that will strengthen private CIBs by establishing criteria for licensing, issuing regulations, and creating an oversight mechanism. All this will result into stakeholders' satisfaction, and, most importantly, it will boost public confidence.

A nation-wide MF-CIB will be a major step with positive impact for both lenders and borrowers. As the CIB expands its operations across the country, the quality and efficiency of the loan appraisal process will improve significantly. The CIB will help microfinance banks and institutions in developing robust risk management system and practices, thus reducing the risk of multiple borrowing and loan defaults. On the clients' side, the CIB will open access to credit for millions of potential poor borrowers. Availability of the CIB will also reduce the credit risk cost of the lender, thus also lowering the loan price for the borrowers. At present, the successful borrowers of microfinance institutions also face difficulty in accessing larger loans from MFBs or commercial

banks due to non-availability of their long history of loans and timely repayments with a microfinance institution. The MF-CIB will facilitate the 'graduation' of such livelihood-based workers into small entrepreneurs.

Although there are numerous benefits of a fully functional credit bureau to all stakeholders, successfully operating a national CIB will not be without challenges. Ensuring timely and accurate reporting by all members will be crucial for maintaining the impartiality and integrity of the CIB. I believe PPAF will make it mandatory for its partner MFIs to report accurate and timely data on their clients. At the policy level, it will be a priority to ensure that consumer rights remain protected. They should not become victims of inaccurate reporting of their data, and/or breach of data confidentiality by the CIB. As customers, it is their right to have an accessible redressal mechanism. I am sure the leadership of MF-CIB will take into account all these concerns, and build the CIB on strong fundamentals.

I will now highlight few recent developments in the microfinance sector that, we hope, can turn the existing stagnant curve into a steeper growth curve. First and foremost, many of our MFBs have undergone recapitalization and restructuring in the last two years. Resultantly, strong and strategic investors have now entered and are entering in the microfinance sector. Secondly, adoption of new technologies and alternative delivery channels such as mobile phone and agent-based banking have radically transformed the distribution channels and retail capacity of the sector. Finally, SBP continues to invest in various large-scale initiatives in areas of funding, financial literacy, capacity building, institutional strengthening and innovation. In the interest of time, I will not go into the details of these initiatives. However, I will emphasize that all these initiatives, including MF-CIB, have now set a platform for MFBs and MFIs to attain high growth momentum. SBP encourages that credit growth should be fairly distributed across all economic, social, and geographic segments of the target market. The MFBs and MFIs should develop innovative credit

methodologies and appropriate risk management policies to maintain growth and quality of loan portfolios. In particular, SBP encourages financing micro enterprises that so far have been neglected by both the microfinance sector and commercial banks. In this regard, SBP has already issued necessary regulations to allow MFBs to extend loans of up to Rs. 500,000/- to microenterprises.

Now I wish to address the CEOs/Presidents of MFBs and MFIs specifically? In my view, the ball is now in your court. What has so far been achieved in the arena of microfinance in Pakistan may best be described as an 'enabling environment for attaining scale and sustainability'. However, achieving scale and sustainability is a huge task. I would urge you to improve corporate governance, management structures, and institutional and HR development in your respective organizations. Your organizations should also have in place adequate systems and policies for ensuring the protection of consumer rights. SBP is already in the process of revising regulations to ensure that MFBs follow best standards in these

critical areas. We count on your wisdom and commitment to reach out to millions of financially excluded people. On our part, SBP will continue to support your efforts to advance financial inclusion.

In conclusion, I would like to congratulate PMN, DataCheck and all key stakeholders on the national roll-out of MF-CIB, and we look forward to its success and expected outcomes of this mega initiative. I believe after global recognition of Pakistan's MF regulations, it is now the turn of our MF-CIB to earn appreciation worldwide.

Thank you!