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SBP Governor launches Key Microfinance Sector Development Initiatives

Dr Shamshad Akhtar, Governor State Bank of Pakistan (SBP) today launched important initiatives for the growth and development of microfinance sector, at an event at SBP Karachi. The event was attended by all stakeholders including donors, Presidents/CEOs of Commercial/Microfinance Banks, and representatives of the Pakistan Microfinance Network and Pakistan Bankers Association.

These measures are expected to ease liquidity constraints of microfinance providers in view of the tighter liquidity conditions and sudden spike in inflation which has severely affected the poor and marginalized segments of the society. SBP has launched three facilities to support the microfinance sector:

- (i) The Microfinance Credit Guarantee Facility;
- (ii) The Institutional Strengthening Fund; and
- (iii) The Improving Access to Finance Services Fund.

These initiatives are part of the GBP 50 million 'Financial Inclusion Program' (FIP) supported by the UK Department for International Development (DFID) and an endowment fund worth US\$ 20 million under the ADB's Improving Access to Financial Services Program.

The **Microfinance Credit Guarantee Facility** is expected to increase the flow of credit to microfinance sector. The facility aims to incentivize banks/DFIs to channelize funds to MFBs/MFIs for on lending to low income segment of the population. The facility will provide credit guarantees of up to 40 percent of the funding provided by Banks/DFIs and aims to develop market and graduate poor borrowers to mainstream financial service providers. Banks/DFIs will lend to MFBs at the SBP policy discount rate plus 200 bps. The funds channelized under facility to MFBs /MFIs shall be deductible from Demand and Time Liabilities of the banks/DFIs for the purpose of SLR and CRR calculation.

The facility will be established at State Bank of Pakistan (SBP) with the help of the UK Government Financial Inclusion Program grant funds equivalent of up to GBP 10 million to be used as the guarantee fund. The State Bank has issued necessary guidelines for operationalizing the facility which were finalized after due consultation with stakeholders.

The MCG facility is expected to help raise local currency funds for eligible MFIs/MFBs. The loans portfolio under the guarantee scheme will be administered by banks. The facility will also help building links between micro borrowers and formal financial institutions. The familiarization of the bank with the client should eventually lead to the "graduation" of the borrower. The facility shall provide partial Guarantees to minimize the perceived risk premium by covering part of the losses incurred on funds made available to MFBs/MFIs with the advantage of leveraging the guarantee fund a number of times while keeping the incentive for banks/DFIs to collect the loan. The lending of MCG facility will help these institutions to play their role in the growth of micro credit more effectively.

The **Institutional Strengthening Fund** designed to build capacity of the microfinance sector. The fund is expected to enhance potential for growth and create depth in outreach by improving human resource quality, service delivery and increasing service availability to potential microfinance clients. The fund is established at the State Bank under the UK Government's Financial Inclusion Program that involved funds equivalent to Pound Sterling 10 million for institutional strengthening. The fund will provide grants for capacity building to generate on-lending resources through commercial sources, equity investments or deposit mobilization strategy through improvement in management, governance, internal controls and functions. The fund will also provide grants for employing cost

reduction mechanisms for increasing outreach in rural and remote areas through product innovation, development or use of technology. In addition, the fund will provide grants for business development services to MFI clients or improving quality of services; and developing capacity for transformation of MFIs into licensed microfinance banks.

SBP has developed detailed guidelines, selection criteria and application format for ISF. The fund will primarily focus on institutions that are already regulated, or are in the process of seeking a license or have solid plans for restructuring in the near future. SBP regulatory oversight will ensure transparency and good governance practices, which will ultimately lead to greater investment in the microfinance industry. Moreover, ISF is capped at US\$1 million per year per grantee and subject to at least 25% matching grant from the grantee. Grants may be made on an annual basis and institutions that qualify for funding in a year may also qualify for funding in another year subject to good performance and submission of another successful proposal through the approved application procedure.

The **Improving Access to Financial Services** is also designed to enhance capacity of the microfinance sector and promote financial literacy. The fund has been established at the State Bank with help of an endowment of USD 20 million under the ADB-supported "Improving Access to Financial Services Program – IAFSP". The fund will provide benefits for and have positive impacts on rural and urban communities, in particular the poor & the women.

These benefits are quantitative and qualitative in nature and include (i) capacity building and training of financial services providers to promote expansion into rural areas; product and service innovation, including savings, remittances and Islamic financial services; adoption and integration of new technologies and applications for improving access to financial services; (ii) capacity building and training of Government and regulatory authorities to support development of an inclusive financial sector and implementation of measures under the Program; and (iii) literacy programs (financial and basic) conducted by or on behalf of financial services providers for clients and potential clients to improve access to financial services and the utilization of finance.

It may also be mentioned here that in Pakistan there are about more than 30 million people living below the poverty line. Despite the consensus that microfinance is an effective tool to alleviate poverty, the gap between demand for and supply of financial services for the poor and marginalized segments of population is very wide. The current microfinance outreach of 1.8 million customers is limited to only around 5% of the potential market. The SBP and the Government of Pakistan are committed to increasing the number of microfinance borrowers to 3 million by the end of 2010 and 10 million by 2015 as documented in the national Microfinance Strategy adopted in 2007. In order to achieve the outreach target the microfinance industry would need substantial additional funding.
