A winning development strategy?

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Replicating Grameen in the Philippines

Grameen banking offers small loans - microcredit - for people too poor to qualify for traditional bank loans, to enable them to start up income generating activities. Originating in Bangladesh in 1976, the Grameen Bank has reversed conventional banking practices by removing the need for collateral, lending to groups rather than individuals, and by creating a banking system based on mutual trust, accountability and participation.

Yet in many developing countries, Grameen-style banking has failed to reach significant numbers of rural poor people mainly because it relies heavily on financial support from donors and is thus unsustainable. Today, in the Philippines however, where 24 million people cannot afford food, shelter or clothing and need a steady source of income, Grameen banking is at last making headway. An increasing number of poor people living in rural areas - women especially - are taking out small loans to start up micro businesses: rural banks are making a profit which enables them to meet the added costs of providing financial services to poor rural areas. How has this been possible?

Rocky road to replication

With the advent of democracy in 1986, many NGOs began providing financial services for the rural poor. In 1989, the government backed a Grameen Bank Approach Replication Project run by local non-government organisations (NGOs). Evaluated in 1993 by the Philippine Agricultural Credit Policy Council, it was noted however, that despite high repayment rates and a significant positive impact on the standard of living of its beneficiaries, internal resource mobilisation was minimal, the costs very high, interest rates inadequate, and outreach to poor people insignificant. Grameen-style banking was deemed financially unsustainable: 'any attempt … to replicate or expand it should be carried out with great caution', concluded the report.
Then in 1995, the People's Credit and Finance Corporation (PCFC) was established by the government of the Philippines as the executing agency for the Rural Micro-enterprise Finance Project (RMFP), jointly funded by the Asian Development Bank and the International Fund for Agricultural Development (IFAD). Initially however, with the PCFC re-financing NGOs and cooperatives as Grameen replicators through loans, effective outreach to poor rural areas was slow. The turn-around came in 1997 when the Centre for Agriculture and Rural Development (CARD), a local NGO, established a rural bank along Grameen lines and started sharing its knowledge and experiences.

Pro-poor banking?

CARD had begun organising poor rural people into groups for lending purposes in 1988. After eight months, it had just 150 borrowers and a meagre repayment rate of 68 percent. Then, in late 1988, CARD introduced the Grameen discipline of weekly meetings and repayments: 89 poor women agreed to participate in a pilot venture and repayment surged to 100 percent. In 1990 CARD began modifying Grameen techniques to suit local needs in the Philippines. Over the next six years it introduced life and accident insurance and voluntary withdrawal savings for all borrowers, non-business loans (for house repairs and education for example) for prime borrowers, and an incentive scheme to encourage Grameen staff to improve outreach and loan repayments. The number of CARD borrowers increased from 307 in 1990 to 6,844 in 1996; its operational self-sufficiency ratio (income/costs including loan-loss provision) grew from 31 to 77 percent in the same period. A year later CARD set up a rural bank, preparing the ground for its self-reliance and future independence from donors, and began accepting deposits from the general public. By 2002, it had expanded its outreach to 92,500 depositors and 56,400 poor women borrowers, using both clients' deposits and PCFC loans as sources of funds. Repayment rates are now 99.7 percent, its operational self-sufficiency ratio 145 percent, its return on assets 5.2 percent and on equity 18.8 percent. Growth looks set to continue.

Grameen-style banking, with its focus on group-lending and mutual trust, is effective. Other local NGOs have established rural banks and existing banks are replicating Grameen approaches to mobilise poor peoples' savings and to ensure profitability and financial self-reliance. The Enterprise Bank in Mindanao, for example, was initially unsuccessful in lending to individual poor people. Adopting Grameen practices, however, including charging higher interest rates, enabled it to expand its outreach from 6,404 to 20,944: sixty percent of its profits in 2001 came from the Grameen portfolio, profits that can help cover the extra costs involved in lending to poor isolated areas. So too, the People's Bank in Caraga, originally an NGO and rural bank in trouble, adopted Grameen practices and expanded its outreach from 5,121 to 11,543 borrowers.

Policy incentives pave the way

Crucial changes to microfinance policy have also proved conducive to the success of rural banks in the Philippines. A national strategy for microfinance was launched in 1997; the special characteristics of microfinance (the absence of the need for collateral, for example) were recognised in the Banking Act of 2000 and in 2001 the moratorium on banks being allowed to expand was lifted. So too, the removal of ceilings on interest rates, which had hampered Grameen replication in the early 1990s, and the phasing out of subsidised public agricultural credit programs were equally helpful. Sound banking practices are clearly a prerequisite for successful Grameen replication.

Making microfinance work for the very poor

A key strength of the Grameen approach is its focus on community-level social capital, the strong moral commitment of group leaders, the insistence on regular repayment at compulsory, weekly group meetings, and the fact that repeat loans (that can get progressively larger) are contingent upon satisfactory repayment of previous loans.

For microcredit initiatives to reach poor people in remote areas, rural banks need to experiment with the classical Grameen model. They need to adapt it to suit local needs, especially those of poor women, to dovetail it to those very people traditionally considered 'unbankable' – with no assets, no collateral, and no savings. This can be done by:

- offering a variety of deposit products such as group savings, voluntary and compulsory deposits and current accounts
- offering a variety of loan products such as non-enterprise loans and group and individual loans that cover all costs and yield a profit
- offering deposit products to non-poor members to generate additional loan capital for poor people
- offering a combination of loans and training services to improve outreach to the poorest households in remote areas

- providing opportunities for the enterprising poor to graduate to individual loans for larger investments thus enabling them finally to move out of poverty.