47

October 2004

PERSPECTIVES

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THE PROVISION OF MICROFINANCE SERVICES BY SAVINGS BANKS

Selected experiences from Africa, Asia and Latin America

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WORLD SAVINGS BANKS INSTITUTE

EUROPEAN SAVINGS BANKS GROUP

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Contents

1. FOREWORD

In developing and emerging economies a lot needs to be done to improve access for people, households and enterprises to financial services. Leading international institutions increasingly recognise the importance of access to financial services for providing a launch pad for development and contributing to poverty reduction. But also in advanced economies, financial exclusion is a reality. Increasingly governments are acknowledging the social impact of this phenomenon and call upon the financial sector to address this issue.

As no country is exempt from this problem, WSBI perceives 'access to finance' as a global challenge and is convinced that the provision of sustainable microfinance, based on the mobilisation of savings represents one of the most important solutions to this challenge.

Defined as the range of ‘small-scale’ financial services that are provided to the lower income strata of the population, microfinance is an important tool to improve these clients’ capacity to take their development in their own hands. Building inclusive financial systems is therefore critical to the massification of pro-poor financial services as large-scale sustainable microfinance requires an integration at all levels (micro, meso and macro).

As proximity banks, savings banks have essential assets that make them ideally equipped to provide microfinance services: They are accessible because of their *geographic proximity* given their wide spread branch networks and nationwide coverage and compared to other formal financial institutions they also tend to have relatively *low requirements for accessing their services* (such as low minimum balances for savings accounts). Savings banks as formal financial institutions also provide a whole range of financial services in a sustainable manner, a clear difference from several microfinance institutions who depend on donor funding and offer limited credit services.

This paper selects six examples from across the developing world to highlight savings banks' activity in microfinance. These six examples, however, are just that – examples of a much wider commitment to extend access to affordable financial services to as many people and enterprises as possible. In a coming edition, examples will be drawn from across the advanced industrial world, where savings banks remain in places that other banks will not serve and run specialist schemes to foster enterprise among disadvantaged groups.

Around the globe, savings banks and postal savings banks service significantly more than a billion accounts – enough, in the developing world, for every third adult to have one. Indeed these institutions probably provide around three-quarters of all accessible savings and payments services in the developing world. These numbers are as much a challenge to the movement as they are an undoubted validation of its importance – if there is so much infrastructure for mass access, why then is access still perceived as such a problem?

As an official Microfinance Partner of the *United Nations' International Year of Microcredit(YoM) in 2005*[1], the WSBI is both promoting savings and postal savings banks' capabilities and advocating an enabling environment for the increased involvement of formal financial institutions in the provision of microfinance.

Such an environment encourages institutions to lend, it offers flexibility with regard to interest rates and recognises the high volumes of small-scale transactions inherent to microfinance by obliging both reasonable reporting requirements and supervisory rules.

In addition, for the proximity banking sector to flourish, WSBI calls for the fundamental promotion of a pluralist financial sector, where the basic principles of competition encourage a diversity of financial services that can cater for all strata of our society.

Chris De Noose
Chairman of the Management Committee, WSBI

1 For further information, visit www.yearofmicrocredit.org

2. EXECUTIVE SUMMARY

It is increasingly recognised that providing financial services to disadvantaged people can help them break the vicious circle of poverty. Numerous initiatives have therefore been established and supported to provide microfinance services, albeit some more sustainable than others. With the Millennium Development Goals[2] in mind and the huge challenges related to reducing poverty by 2015, there is an increased awareness among policymakers and practitioners that the involvement of the formal financial sector is required for the massification of financial services to the poor in a sustainable manner and to achieve a significant reduction of financial exclusion.

Since savings banks' primary concern is to mobilise financial resources and, where possible, invest these in the economy, they differ from microfinance initiatives that were created with a credit focus. In most countries they have built up a reputation as solid institutions that have proven effective in times of crisis and are *trusted by savers*. Although not in all cases equally successful, savings banks generally provide a sense of security for low income clients thanks to their formal character and explicit (or implicit) guarantee on deposits.

These days there is also a growing recognition among academics, practitioners and policymakers that the underprivileged need not only credit, but a wider range of financial services including savings, insurance and payment services. This paper portrays the experiences of a selection of savings and socially responsible retail banks in the provision of these services to the poor, highlighting the characteristics of flexible, affordable, convenient and safe services that are demanded by this client group.

2 The Millenium development goals include the aim to reduce poverty by 15% by 2015
They are: (1) eradicate poverty and hunger; (2) achieve universal primary education; (3) promote gender equality and empower women; (4) reduce child mortality; (5) improve maternal health; (6) combat HIV/AIDS, malaria and other diseases; (7) ensure environmental sustainability; and (8) develop a global partnership for development.

The paper argues that savings and socially responsible retail banks have an important role to play in diversifying financial services and making them more viable for poorer clients. This is the conclusion of an analysis of experiences of a selection of members of the WSBI (World Savings Banks Institute) that are already active in microfinance (Banco del Estado, Chile; Banco Caja Social, Colombia; National Bank for Development, Egypt; Caja Muncipales de Ahorros, Peru; Postal Bank, Tanzania and Government Savings Bank, Thailand).

Institutional commitment is a prerequisite for providing low-income people with financial services. The commitment of savings banks to provide financial services to underserved markets distinguishes them from most other formal financial institutions. In addition to that, the distribution of their profits, educational initiatives and efforts to support initiatives aiming at social inclusion are other expressions of their *social responsibility*.

The savings and retail banks studied mobilise deposits from their customers to fund their microcredit programmes and are therefore less dependent on commercial borrowing sources giving them a comparative advantage over those institutions that are legally prohibited from capturing savings.

As proximity banks, savings banks have essential assets that make them ideally equipped to provide microfinance services. They are accessible because of their *geographic proximity* given their wide spread branch networks and nation-wide coverage. Compared to other formal financial institutions, they also tend to have relatively low requirements for accessing their services (such as low minimum balances for savings accounts).

Although each savings and retail bank applies a different methodology to its microlending programme, the experiences included as case studies in the annex have shown that within successful retail banks, a specific focus on low-income clients is often translated into a separate programme, cost centre or entity. The advantage of this approach and clear market segmentation is that there is relatively more freedom and flexibility to take decisions that are essential for the development of microfinance products and services. Special measures for instance, with regard to staff recruitment and training, distribution channels for services as well as product development, can be decided more easily.

To ensure that low-income clients are reached on a sustainable basis, operations in this market segment need to be commercially viable and attractive. This market segment can be profitable, and it depends on the bank's capacity to achieve high levels of efficiency. On the cost side, this implies the implementation of appropriate measures to control costs and streamline internal processes. Standardisation of certain products and processes can create economies of scale and thereby reduce a bank's operating costs, as well as a client's overall transaction costs. On the revenue side, a diversification of products and services can contribute to achieving profitability and risk diversification, being more competitive and resistant to macro-shocks. Savings banks that are successful in microfinance manage to create cross-selling opportunities ensuring the bank-client relationship is broadened both to the benefit of the bank that generates more business and the client who has access to more services.

Recognising that savings banks and socially responsible retail banks have the potential for downscaling and diversifying their operations to offer a range of financial services to currently underserved markets, this paper also highlights a number of challenges for those willing to enter into the microfinance business or strengthen their existing operations in this field. The challenges include the design of appropriate products, the availability of the required skills and capacity among staff, high efficiency to compensate higher costs per volume of transaction and adherence to good corporate governance principles.

This paper emphasises that the right enabling environment is needed to encourage banks to develop such operations. This environment would include amongst others a liberal interest rate climate, reasonable reporting requirements and attention to the peculiarities of microfinance operations when setting capital requirements and provisioning rules. For countries where publicly owned savings banks are operating as narrow banks and not allowed to lend, the removal of these legislative and regulatory barriers could contribute significantly to increasing access to financial services to this under-served segment. That is to say on the condition that the banks build up the necessary capacity to manage microcredit programmes, are subject top prudential supervision and are managed independently to avoid political interference in the decision making process.

In addition to the right enabling environment, there are other ways in which to encourage savings and retail banks to further explore the possibilities of microfinance. Donor funds have in some cases been instrumental in introducing a microlending programmes to a savings or retail bank. Successful experiences have illustrated the positive impact of a donor contribution to capacity building programmes and efforts aimed at institutional development. But as the case studies show, whenever donor assistance came at the inception or triggered downscaling experiences, the savings banks have become rapidly self-reliant and expanded their activities in this area. It has to be understood however that donor assistance will only result in sustainable efforts if there is a commitment at all levels within the bank. In some cases, guarantee schemes that cover a part of the risk for microloan portfolios can also encourage banks to move into this business.

In addition to these efforts, alternative ways need to be found to deepen the outreach of savings and retail banks to where their distribution channels cannot currently reach. Alliances between savings banks, microfinance institutions and community-based organisations could for instance be explored. Pull tactics such as public-private partnerships that increase the underprivileged's awareness of financial services and their benefits can assist in deepening the outreach of savings banks. For example, the Senegalese Ministry of Family, Youth and Women supported an agreement between the postal savings service and the UNCDF/ILO in 1988 whereby savings and transactional services were extended to women groups[3]. In some cases, lack of information is the underlying reason why people do not find the way to banks, in particular with their savings. Several savings banks have positive experiences in developing client educational programmes or advice to accompany their financial services. The Government Savings Bank of Thailand can illustrate an interesting example of experience developing financial literacy.

3 This project aimed at promoting income-generating activities carried out by women groups. It was funded by the United Nations Capital Development Fund (UNCDF) and monitored by the International Labour Organisation (ILO).

3. INTRODUCTION

There is a broad consensus among academics, governments and donors that the lack of access to banking services for the disadvantaged impairs economic growth and a better distribution of its benefits. For many underprivileged households, the possibility of accessing financial services constitutes a chance to build wealth. We can see three effects of providing the disadvantaged persons with financial services[4]: Firstly, it can augment the expected value of income and thus increase potential for consumption, future investment and asset accumulation. Secondly, it can limit the downward spiral of earning insufficient income to satisfy basic consumption needs. Thirdly, it can facilitate the constitution of precautionary savings for facing risks and uncertainty that can affect income levels, thus helps smooth consumption levels (Kimball and Weil, 2003)[5]. In spite of the acknowledged advantages of using financial services, many households still remain 'unbanked' for various reasons.

Table 1: Statistics highlighting several countries where a significant proportion of the population is 'unbanked'

Country (Year)	Number of (non-savings) bank deposit accounts	Number of savings bank accounts
Benin (2002)	162,614	360,033
Burkina Faso (2002)	328,994	323,000
Chili (2001)	1,093,000	11,052,000
Colombia (2001)	N.A.[6]	1,100,000
Côte d'Ivoire (2002)	659,642	875,000
Kenya (June 2003)	1,970,536	1,907,000
Senegal (2002)	339,589	141,327
Tanzania (2003)	1,400,000	1,000,000
Togo (2002)	180,413	200,000

Source: Various[7]

3.1 Microfinance

Microfinance today can be defined as the range of 'small-scale' financial services that are provided to disadvantaged persons with the aim to improve their capacity to take their development in their own hands. The microfinance industry can be characterised by its clients, their specific needs and the alternatives they have in access to financial services.

Microfinance clients are typically people on low-incomes, who are self-employed or salaried, such as factory workers. In rural areas they may generate some income from farming, food processing or trading at the local markets, whereas in urban areas they tend to be shop keepers, street vendors, entrepreneurs, service providers, craftsmen, etc. They generally have numerous income generating activities that are somewhat unpredictable and may be seasonal but appear more or less stable. It has increasingly been recognised that not all people may be helped with microcredit but that all are deposit worthy and need to make payments.

Microfinance services are characterised by the fact that they are tailor made for this target group and that the financial services take into account the needs and restrictions of these people. The perception of these needs within the microfinance business has evolved over time. Whereas in the beginning microfinance was considered as microcredit, in recent years microfinance providers have come to appreciate the needs of poorer households to have access to other financial services, such as savings, insurance and payments. The financial services provided to low-income households need to take into account some basic aspects that characterise these people such as irregular income flows from numerous activities in some cases seasonal, activities of an informal nature, a lack of collateral and low basic reading and writing skills.

4 Zeller, Manfred (2000) *Product Innovation for the Poor: The Role of Microfinance, Rural Financial Policies for Food Security of the Poor*, Policy Brief N° 3, International Food Policy Research Institute.

5 Kimball, M and Weil P. *Precautionary Saving and Consumption Smoothing Across Time and Possibilities*, No 4005, CEPR Discussion Papers.

6 Available information on the Colombian banking system refers to the value of deposits rather than the number of accounts. BCS has a 2-2.5% market share in deposits, but given the fact that almost one third of its accounts has a balance below 2,115 US$ whereas the system as a whole only has 12% of its deposits in such accounts, its share in the number of accounts is larger.

7 Annual Report of the Banking Commission of the West African Economic and Monetary Union (2002), Payment System in Kenya by the Central Bank of Kenya (Sept 2003), Passing the Buck-Money Transfer Systems: The Practice and Potential for Products in Tanzania and Uganda, Microsave Africa (May 2003), WSBI Statistics.

Partly due to these reasons, in emerging and developing economies there is a tendency not to cater for such disadvantaged persons in the formal financial sector. That is to say, where conventional financial institutions impose conditions on the provision of their services that are unlikely to be met by poorer households, financial exclusion arises. The consequence is that most low-income people therefore obtain financial services through informal arrangements in the market that are generally expensive, not so safe or unsustainable in the long run.

Recognising the evolution of financial exclusion, many institutions have started to provide microfinance services, be it out of a development consideration or a business opportunity or a combination of both. It is difficult to classify microfinance providers. Operating in the domain of microfinance are grassroot organisations, financial NGOs, non-bank financial institutions, credit unions, co-operatives, private commercial banks and state-owned banks. And among these, are the savings and retail banks that are affiliated to the WSBI. Each institution may differ in objectives, focus on financial services, business orientation, target group within the microfinance segment, ownership structure, capacity to mobilise savings, or regulation etc, but all share the same commitment to providing services to an otherwise 'unbanked' population.

In fact in recent years, we have witnessed a broadening and deepening of the microfinance industry. Deepened, because several traditional and commercial banks, recognising the market opportunities have started to downscale their operations to target low-income customers. Broadened, because several institutions that formally only offered a limited range of financial services, mainly credit, are expanding their operations by providing other banking services such as the collection of savings. Parallel to this some typical deposit-taking institutions such as postal savings banks are experiencing a similar trend in the other direction. Some of them are diversifying into microcredit and other financial services.

3.2 Savings banks providing microfinance services

What distinguishes savings banks from other microfinance providers in developing and emerging economies is that they are all formal financial institutions that are in the first instance committed to the mobilisation of savings. Typically, clients of savings and retail banks are households, microenterprises and SMEs.

As demonstrated by the case studies in this paper, the ownership structure of these savings and retail banks varies. Some are privately owned, others state-owned. There are postal savings banks, savings banks owned by municipalities and financial institutions with a more co-operative ownership structure. As with other formal financial institutions, they are regulated as opposed to most microfinance providers that operate as informal institutions. This informal character does provide a sense of security for low-income clients. The fact that banks are regulated and supervised by government agencies and have to comply with financial prudential rules, increases the stability of the financial sector. As with other banks, savings and retail banks contribute when it exists, to a deposit guarantee scheme that protects the small savings.

In most countries savings and retail banks have built up a reputation as solid institutions that have also proven effective in times of crisis. Confidence in well-established savings and retail banks is therefore relatively high in many economies. Savings banks are characterised by large distribution networks to reach out to the clients nationwide. They are often known as 'proximity banks' a concept that will be further developed in the following chapter. Thanks to their decentralised nature they can address the needs of the local people and use mobilised resources to invest in the local economy. Savings banks are committed to regional economic development and often have a social mandate within their charter.

3.3 The paper

This paper argues that the demand for microfinance services is still considerably larger than the supply and that institutions like the savings and retail banks can contribute to the massification of microfinance that is needed in order to satisfy this demand. It also stresses the diversity of financial services that is needed by those with low incomes and underlines the importance of the mobilisation of local resources and the stimulation of a savings culture. The characteristics of savings banks and their way of operating as 'proximity banks' respond to the needs of microfinance clients. It is their commitment to society that makes the provision of microfinance services a natural progression in their development.

These comparative advantages of savings banks for the provision of financial services to low income clients will be further developed in the next chapter.

In chapter 3, the different types of microfinance services offered by savings banks in developing and emerging economies: credit, savings, insurance and payments, will be analysed. This chapter draws heavily upon the experiences of a number of savings banks that already have specialised in microfinance services, and who were studied for this paper. More about these institutions and experiences can be found in the case studies in the annex.

The fourth chapter will conclude with an overview of challenges and some recommendations that could contribute to enabling savings banks as well as other institutions that share the same commitment, to bring microfinance services to the people through an effective and mass medium.

4. COMPARATIVE ADVANTAGES OF SAVINGS BANKS IN MICROFINANCE

Savings banks and socially responsible retail banks can be described as 'proximity banks'. In general terms this means that they are close to their customers and serve the best interest of the community they operate in. In the following sections the four main characteristics that make them ideally equipped for providing microfinance services are outlined: geographic proximity, accessibility, sustainability and social commitment. The description of the comparative advantages is based on the in depth study of 6 savings banks that are particularly active in the provision of microfinance services and furthermore on information gathered from other WSBI member banks that have started with these services or are keen to provide them recognising their potential.[8]

4.1 Geographic proximity

The accessibility of financial services for poorer households is in many countries related to the physical distance between them and the institution that provides the service. In many developing countries a large proportion of the poor population live in rural and remote areas of the country. Moreover, due to inadequate infrastructure and a lack of affordable transport, people have to invest time and money, which are scarce, in crossing this distance. Also in some urban areas, traffic or other difficulties may prevent people from easily accessing banking facilities, meaning that they have to turn to other alternatives. It is for this reason that widespread distribution channels are essential for providing microfinance services.

8 Of the 74 WSBI members in emerging and developing economies at the end of 2002 more than half reported to provide microcredit services.

Savings banks recognise this and are committed to maintaining branches in rural and structurally weak urban areas even though many commercial banks choose leave these places. Due to the fact that savings banks are not driven by the objective of profit maximisation alone, but also aim to serve the general interest, they are prepared to incur the costs related to maintaining a large retail network, unlike commercial banks that tend to concentrate their activities in prosperous urban areas.

Table 2: Banks and savings banks' branches (approximate data)

Country (Year)	Savings bank	Number of outlets of the savings bank	Number of outlets other banks
Benin (2002)	Caisse Nationale d'Epargne	92	34
Chile (2003)	Banco del Estado	378	1535
Colombia (2003)	Banco Caja Social	122	3364
Côte d'Ivoire (2002)	Caisse d'Epargne et des Chèques Postaux	194	150
Kenya (2003)	Post Office Savings Bank	471	512
Malaysia (2002)	Bank Simpanan Nasional	424	3000
Peru (2003)	Cajas Municipales de Ahorro y Crédito	167	806
Senegal (2002)	Caisse Nationale d'Epargne	137	103
Tanzania (2003)	Postal Bank	153	140
Thailand (2002)	Government Savings Bank	573	4000

Sources: WSBI, Central Bank of West Africa States + various, including reports from the IMF, the World Bank and the Asian Development Bank.

In Africa, the dominance of postal savings banks is a legacy of colonial times. The choice of the postal distribution network is logical given the nationwide coverage of post offices. As such, savings banks are able to cost-effectively implement the policy of financial citizenship, relying on the convenience of post offices to deliver pseudo-banking facilities to a large segment of the population and to reach remote communities. In many countries, postal savings banks are the only institutions operating a nationwide network of retail branches.

In Kenya and Senegal for instance, postal savings banks rely on a distribution network, which is by far larger than banks' facilities. The Kenya Post Office Savings Bank (KPOSB) operates through 471 outlets, while commercial banks manage altogether approximately 512 outlets. While roughly 80% of commercial bank branches are located in main cities, only 45 out of 471 outlets managed by KPOSB are located within Nairobi (capital) region. Likewise in Senegal, with approximately 126 outlets (of which 23 are located in the Dakar region), the postal retail network outnumbers commercial banks branches (103 branches concentrated in main cities). Since commercial banks concentrate predominantly in attractive and lucrative urban areas, (postal) savings banks are a key vehicle for the delivery of retail financial services in rural communities.

In developing countries in Asia, the banking industry has experienced an impressive development over the last two decades. Commercial banks have expanded their retail network to better serve national economies. However, with (or without) the post brand, and even in countries with developed banking industries, savings banks have been able to distinguish themselves from other banking institutions by their strong physical presence. For instance, with 573 branches of the 4,600 nationwide branches for the whole Thai banking sector, the Government Savings Bank (GSB) manages one of the largest networks, just behind the Bank of Agriculture and Agricultural Cooperatives, which includes 629 branches in its network.

Also in Latin America savings banks are characterised by strong local roots and a decentralized network of retail branches. Banco del Estado in Chile operates in more communes (106 of 341) than any other financial institution in the country. In fact, more than one third of its 304 branches are located in remote areas. Additionally, the bank has 74 mobile branches. Other savings banks use existing retail outlets (for instance shops) to provide some of their financial services. This is the case for instance in Brazil where in addition to its 1693 branches, Caixa Economica operates 291 Bank Service Stations (called PABs), 2053 banking correspondents, and also provides services through 8870 lottery shops and simplified lottery units. It is the only bank that is present in all 5561 municipalities of Brazil. In Cuba, Banco Popular de Ahorros has the largest network of offices in the financial system on the island with its 500 offices.

Knowing that a large branch network is costly, savings banks have been innovative in establishing alternative ways of getting closer to the people. Making good use of modern technology and economies of scale, some savings banks introduced mobile branches with agents who are well equipped to render services directly to the people.

In Chile for example, microfinance agents visit people in their businesses or homes to sell them credit and savings services using palm pilots that can be connected to computers in the branch, saving them time and increasing efficiency.

In addition to their local presence, savings banks can also guarantee a nationwide coverage by themselves as is the case for many postal bank networks, or in conjunction with other savings banks they are associated with, as is for instance the case for the Peruvian municipal savings banks. In comparison with many smaller microfinance institutions that work locally, the savings banks have the advantage that they can provide services throughout the country, something that particularly suits payment services. In some cases, services go even beyond that and provide links with foreign institutions, which can be relevant in countries where remittances are a relatively important ingredient for economic growth. Banco Caja Social is for instance catering for remittance services between Spain and Colombia through an alliance with the Spanish savings bank 'la Caixa'.

4.2 Accessibility

Related to the geographical proximity of savings banks to their clients is the regional orientation and identification with the customer. As proximity banks, savings banks are more aware of the needs of their customers and the decentralised nature of their institutional operations allows them to adapt to these needs. Given the specific characteristics of microfinance clients as mentioned in the introduction, this is a particular advantage of savings banks.

In designing the products and services to be offered, savings and socially committed retail banks take into account the special needs and limitations of low-income households together with that of the more affluent customers. Examples of this in microsavings and microcredit services offered by savings banks are numerous.

With regard to deposit services, the minimum amount required for opening and holding an account is often too high and unaffordable for a large proportion of the population. In some countries, savers are required to deposit more than their annual per capita income in order to open a deposit account with a bank. In Benin and Senegal, commercial banks often ask at least between US$90 and US$180 in local currency to open a savings account.

The clients are also requested to maintain a minimum balance, ranging between US$50-100. In addition, bank fees to hold an account exceed often interest paid for small deposit amounts.

At the postal savings bank in Benin Burkina-Faso, Kenya and Tanzania in contrast, people can open a savings account with less than US$10 and an even lower amount in fees is required to keep this account active. In some countries like Cameroon, Côte d'Ivoire, and Tanzania, the minimum amount to open a deposit account with the postal savings bank is a bit higher and ranges between US$10-20. Although this amount varies across countries, it rarely exceeds US$25 in Africa and in general, this amount represents less than 5% of the per capita Gross National Income (GNI).

The figures for Latin America are relatively higher due also to a higher Gross National Income (GNI) per capita. Banco Caja Social asks for a US$25 deposit to open a savings account, which is well below the average requirement of the banking system in Colombia. In Peru, the minimum amount to open an account varies among municipal savings banks but remains around US$10. Banco del Estado of Chile does not have a minimum requirement to open a savings account.

Table 3: Minimum fee to open a savings account

Country	Savings bank	US$ value	% of per capita GNI (2002)
Benin	Caisse Nationale d'Epargne	9.00	2.3
Burkina Faso	Caisse Nationale d'Epargne	9.00	4.09
Chile	Banco del Estado	No minimum	No minimum
Colombia	Banco Caja Social	25.00	1.36
Côte d'Ivoire	Caisse d'Epargne et des Chèques Postaux	16.00-32.00	2.6
Kenya	Kenya Post Office Savings Bank	7.00	1.9
Malaysia	Bank Simpanan Nasional	0.27	0.007
Peru	Cajas Municipales de Ahorro y Crédito	10.00	0.48
Senegal	Caisse Nationale d'Epargne	22.4	4.76
Tanzania	Postal Bank	5.0	1.8
Thailand	Government Savings Bank	No minimum	No minimum

Source: WSBI, World Bank and various

Likewise in developing Asia, driven by technology solutions, savings banks have shown an impressive capability to capture small depositors and to overcome underlying operational inefficiencies. In Malaysia, an individual can open an ordinary savings account with only RM 1.00 (US$0,27) at Bank Simpanian Nasional. In Thailand, the Government Savings Bank does not require a minimum amount.

On the lending side, most banks perceive microlending as a risky business. In fact, extending loans to low-income people is regarded as too costly and inefficient because the atomistic and short-term structure of loans entails excessive administrative costs. Other concerns that explain commercial banks reluctance to extend microloans are problems of asymmetric information and a lack of bankable assets.

In the cases of the savings banks analysed for this paper, they have succeeded in minimising conditions and attracting low-income clients. In general, where the microcredit programme is dealt with by a separate unit (Tanzania, Egypt, Thailand and Chile) it shows that their entire loan portfolio is taken up by these clients. In the case of Banco Caja Social (BCS) and the Municipal savings banks in Peru, it is more difficult to distinguish within the loan portfolio among the clients but the proportions of borrowers with low income levels also proves that these banks offer credit products and services accessible to the poor. According to the official Colombian definition of microcredit, 5% of BCS' total loan portfolio was in the hands of microenterprises[9]. The loans extended by BCS composed 16% of all microcredits outstanding in formal financial institutions in 2002. In Peru, around half of the borrowers have an income level that is below the per capita GDP of the country (around US$2,000) and a quarter lives on less than US$1,000 a year.

4.3 Profitability

Although the outreach of institutions providing microfinance services is of great importance, this should be combined with concerns for profitability of the institution. Profitability is essential for the continued access to financial services for those people that are not being served by traditional banks.

9 Official government definition 'microcredit': credit provided to microenterprises counting less than 10 workers with assets up to 501 minimal monthly salaries around US$60,000 and an outstanding loan balance with the respective financial institution less than 25 minimum salaries.

For savings banks, which in general finance microfinance programmes from their own resources rather then with subsidies from international donor organisations, it is a key concern.

For a selection of savings banks that are active in microfinance, information on profits was collected for the preparation of this paper, although it has proven difficult to single out the microfinance activities as a separate business unit in the statements provided. Table 4 shows the return on assets and operating income for the entire institution or group of institutions, as is the case for Peru.

Table 4: Profitability of a selection of savings banks active in microfinance (as of 01/01/2002)

Savings bank	Country	Return on Assets (1) (%)	Operating Income/ Average Assets (%)
Banco del Estado	Chile	0.64	4.86
Banco Caja Social	Colombia	2.96	18.85
National Bank for Development	Egypt	0.91	2.23
Peruvian Savings Banks affiliated to FEPCMAC	Peru	3.83	4.39
Tanzania Postal Bank	Tanzania	2.17	13.90
Government Savings Bank	Thailand	1.98	3.21

Source: WSBI. (1) Adjusted return on assets for all except Peru where ROA was not adjusted.

Savings banks can in general use mobilised resources for reinvestment in credit and are therefore not so dependent on commercial borrowing sources. This gives them a comparative advantage over banks that have a lower capacity to mobilise savings, or over those institutions that are legally prohibited from capturing savings.

Apart from the cost of capital, the profitability of the financial services offered is influenced by the operational expenses and loan loss provisioning. In the microfinance sector, the debate on the issue of financial sustainability has shifted from a focus on cost recovery (with high interest rates as a result) to a cost minimisation approach.

"Microfinance managers, especially those working in more competitive markets, increasingly recognise the importance of streamlining operations and cost management for long-term viability"[10]. The costing exercise is key for product design, delivery mechanisms and pricing. These factors play an important role in strategic planning. Because, costing can be an efficient tool for tracking hidden costs and other operational inefficiencies, it should contribute to lower administrative and operating costs for microfinance operations, hence bring down sustainable interest rates.

Keeping operational costs down is a general concern among banks and increasingly among microfinance institutions, maybe less so among microfinance programmes in a stage where they receive donor subsidies for operations. Savings banks attempt to reduce the costs of microfinance activities by increasing efficiency, introducing a massification of the operations and making use of appropriate technology and methodological tools. Especially in the offer of savings products, standardised and simple products allow for economies of scale that can reduce costs.

What is also key is also the preservation of low levels of default payments in credits since the loan loss provisioning can have a significant impact on costs structures. In the cases studied, the default rates (portfolio at risk >30 days) were all between 1 and 7% with the exception of the credit programme in the National Bank for Development, which disclosed a high rate of non performing loans (19.5%) at the end of December 2002.

Table 5: Delinquency and interest rate

Savings bank	Delinquency rate (month/year in parentheses)	Nominal interest rate per annum
Banco del Estado (Chile)	1% (04.03)	23.76-17.4%
Banco Caja Social (Colombia)	6.3% (04.03)	29%
National Bank for Development (Egypt)	19.5% (12.02)	29.7%
Cajas Municipales de Ahorro y Credito (Peru)	4.79% (03.03)	55.6%
Postal Bank (Tanzania)	1.5% (12.02)	47.1%
Government Savings Bank (Thailand)	3.81% (12.02)	19%

10 Brigit Helms 'Microfinance Product Costing', Paper presented at the World Council of Credit Unions Conference on '*Best Practices in Savings Mobilisation*', November 2002, Washington D.C.

On the income side, the banks are committed to charging and offering correct interest rates that cover their costs in order to achieve sustainability of the microfinance services separate from the other activities of the bank. In general, nominal interest rates charged on microloans are higher than those applied on conventional loans. Often, they are charged as flat rates and calculated as fixed amounts including the capital to be paid back each term. In the microcredit experiences included in this study, only Banco Cajas Social, the Peruvian savings Banks and Banco del Estado charge their interest rates on the remaining balance.

An important advantage savings banks have over microfinance institutions is that they have in most cases a diversified retail-banking portfolio of services to offer. Therefore they are able to raise income in different areas of the banks' business, such as through commissions on payments and insurance. On top of the variety of products, the diversified client base on which savings banks can generally count assists in the profitability of the institution as a whole. Saying that of course, 'cross-subsidisation' of services and clients needs to be addressed with care.

4.4 Social commitment

The commitment of savings banks to the provision of financial services to underserved markets distinguishes the banks from many other formal financial institutions. The decisions to provide affordable financial services and maintain a broad retail distribution network distinguish savings banks from purely profit-seeking and maximising financial institutions. The proximity to underserved customers and conviction of their commercial potential translates itself into a strategy with a strong commitment to microfinance. But there are other ways in which the savings banks demonstrate their commitment to society and their socially responsible approach. Around the world, savings and socially committed retail banks have different ways of investing in social economic development in the communities in which they operate.

4.4.1 Channels for government policies

In several countries the savings bank is used as a channel for government policies. Banks are used to administer funds or execute payments for instance. Managing such tasks poses important challenges to the independence of the decision-making of the bank, but when done in line with good governance principles the banks can effectively use their position to the benefit of society.

The Government Savings Bank (GSB) in Thailand is a good example: GSB's social activities encompass various projects. The Thai Government has entrusted GSB to administer a Regional Urban Development Fund (RUDF) and a Social Investment Fund (SIF). The RUDF is a revolving fund set up to extend loans to municipalities for financing public utilities projects. In administering the RUDF, GSB aims to enhance the project management capability of selected municipalities and improve public services. On the other hand, the SIF finances projects of mutual interest to the community and of particular interest to underprivileged groups within the society. The activities eligible for financial support are in the area of income generation, environmental protection, local economy development and community welfare.

Another example can be found in Brazil, the Caixa Federal Economica's network and operations play a key role in the federal government programmes to fight poverty, promote social inclusion and minimize inequalities. Caixa is the largest distributor of welfare payments in the country. It plays a prominent role in uniting all federal government welfare revenue transfer programmes, involving more than 10 million social security accounts and benefiting approximately 43 million people. These accounts will be transformed into bank accounts, which will be an important step in promoting financial inclusion and providing access to other banking services.

4.4.2 Distribution of profits

Some savings banks are required by law or their statutes to reinvest a part of their profit in socio-economic development. Despite the fact that there are unfortunate cases in which the bank's profit is taken by the government to fill holes in its budget, in most instances the reinvestment is well stipulated and managed under strict rules of good corporate governance. This is for instance the case in Peru, where it is stipulated in the law that created the municipal savings banks that up to 50% of the profit generated by the bank can be invested in socio-economic development in the region through the municipalities that own the savings banks. In 2001, US$13.5 million net profit was generated, of which 90% was reinvested in the CMACs and the US$1.35 million given to the municipalities for investment in the society.

In some cases the ownership of the savings bank also guarantees that profit earned is reinvested in the community. In Colombia, the savings banks' majority shareholder is a Foundation called 'Fundación Social' which runs community development programmes.

In 2002, Banco Caja Social generated a profit of US$11.8 million of which US$262,850 was reinvested in the bank and US$11,5 million were paid out in dividends of which almost US$10 million corresponded to the Fundación Social that invested the entire amount in community development projects that are directly targeted to assist the poorest.

4.4.3 Education

Policy-oriented savings banks often go further than other financial institutions in taking responsibility for their educational role when it comes to the mobilisation of savings. They set up campaigns that are not only innovative but also have an added value on top of the marketing aspect. Risk taking and the provision of advice are important investments that savings banks undertake in this respect. Such an example is the 'school based banking scheme' of the Government Savings Bank of Thailand (See Box 1).

Box 1: The Government Savings Bank of Thailand 'School-Based Banking Scheme'

What is the school-based bank?

The school-based bank is a model bank operated by students with their teachers and GSB staff playing an advisory role. Selected students who behave well and have a sense of responsibility and thoughtfulness act as the manager, finance officer, counter service officer, and teller. Deposit and withdrawal services are provided before the morning class or during the lunch hour. The GSB branch that plays an advisory role performs auditing and collects savings after the banking hours of the school-based bank.

Support from GSB

GSB's support for the school-based bank includes training on banking operations and the provision of equipment. Passbooks and printed forms are specially designed for the purpose. It is important that the administrators of the participating schools are aware of the value of the scheme and give their full cooperation. GSB also provides the students who participate in the scheme with scholarships, educational material, and organises study tours for them.

5. THE RANGE OF FINANCIAL SERVICES PROVIDED TO THOSE WITH LOW-INCOMES

In a broad spectrum, we can reasonably identify four pillars in microfinance. Within this view, microfinance means the provision of financial services; mainly savings, credit, insurance and payments services to individuals as well as micro and small enterprises. Savings mobilisation is often referred to as '*the forgotten half of rural finance*', but the microfinance community has become increasingly aware of the importance to mobilise small savings. Learning from field experiences, academics and practitioners are now going beyond savings and credit services to recommend an extension of micro-insurance services to the most vulnerable groups. Indeed, the poor are more exposed to risky situations (droughts, floods, etc.) that can severely affect their livelihoods. Seibel (1997) even claimed that micro-insurance has been '*the forgotten third*' of microfinance. Finally, those with low incomes also need to have access to convenient payment services. They might have to issue money orders or money transfers for business purposes. They also receive money from relatives living in urban centres or abroad.

5.1 Savings mobilisation

The lack of savings has usually been raised to explain weak economic growth in developing countries. Savings are low said the '*vicious cycle theory*' because personal incomes are too low and because of that investment levels are also too low, leading to low production levels and low incomes. This is what is often called the poverty trap. The lack of savings also explains and justifies why external funds are needed and helpful for poor economies to trigger economic growth and achieve poverty reduction. The lack of savings in poor countries has become a controversial assumption since various studies indicate that savings exist but are rather held outside the banking system.

5.1.1 Rationale of small savings collection

Although savings and credit practices differ from common practices encountered in modern societies, small savings do exist in developing economies and are even abundant[11]. In general, poor people face irregular income streams, therefore deposit services can play a critical role in buffering any emergencies. Access to secure deposit services enables those with low-incomes to smooth their consumption over time. Vulnerable groups even show a higher propensity to save. They save to meet the various needs of their life cycle, such as birth or death, marriage, or to be able to face emergencies like illness or floods, large sums such school fees as well as religious and social obligations and investment.

It is often due to the lack of convenient, secure and flexible financial services that poor people encounter difficulties that cripple their savings ability. "*… when poor households' desire and need to save meets a safe, easily accessible opportunity to do so, their commitment to saving, and the amounts they manage to save, are remarkable*"[12]. The importance that poor people attach to savings is obvious through the various ingenious, but costly, solutions they rely on to save. In general, informal savings practices are the only way for poor savers to put a little aside. They accumulate through various informal means (hoarding, the purchase of livestock, money guards, rotating savings and credit associations, etc.).

Informal savings and credit practices have also been invigorated by weak regulations, unstable economic or political environments (inflation, conflicts, etc.), financial repression and public distrust of banks following banking crises. However, the inconveniencies associated with these informal practices should not be neglected, the satisfaction provided notwithstanding. Informal savings forms are generally indivisible, quasi-illiquid and high-risk bearing even though for clients there are clear advantages such as accessibility, convenience and the actual fact of it not being formalised (especially with banks now having to follow KYC rules more strictly).

To protect and encourage small savings entails not only a civic duty to the more vulnerable strata of the population, but also an expression of a moral obligation to help people to use accumulated resources wisely.

11 A key distinction should be introduced between 'savings' and 'deposits'.
Savings encompasses all forms and practices related to holding assets while deposits represent that portion entrusted with financial institutions.

12 SUM/UNDCF/UNDP, *Savings Policy Statement*, June 1998, p. 1.

In many developing countries, apart from the informal sector, savings banks have been the only financial institutions mobilising small savings. In Africa and Asia, some postal savings institutions (Benin, Burkina Faso, India) have been very successful in capturing household savings. In Latin America, recent progress in regulating financial cooperatives has been very beneficial to small savings mobilisation as those institutions are allowed to provide savings schemes to their members. Indeed, people will deposit their surplus capital with financial institutions, if these are adequately structured and offer clients affordable and adequate deposit services[13].

In the past, MFIs stressed the acceptance of compulsory savings schemes by their clients/members as a well-accepted means to set aside funds for long-term purposes. Compulsory savings is an integral part of many micro-credit programs and some savings banks that launched microcredit programmes have compulsory savings schemes, such as in the case of Tanzania Postal Bank and the National Bank of Development in Egypt. However, the compulsory saving, which is often deducted from the loans is usually considered as part of the cost of the credit and for that reason there is substantial evidence that compulsory savings schemes are not liked by clients nor form a sustainable stimulator for increasing savings. Indeed, people rather prefer properly designed voluntary savings schemes to protect the little they are able to set aside.

Compared to those non-bank institutions that are not allowed to capture savings, savings banks' comparative advantage lies in their legal mandate and their operational ability to collect and protect small deposits from the public. Over time, savings banks have, like cooperatives, rural banks and other financial institutions alike, developed and commercialised a wide range client-friendly deposit facilities.

As a result of the low minimum requirements imposed by savings banks, a relatively large number of accounts are being kept open with low balances. The structure of ordinary savings accounts in Benin and Burkina Faso for instance shows that the balance does not exceed €15 for 62% and 36% respectively. Evidence from Kenya shows that the balance for 44% of passbooks was less than US$2.5 in 1997 while 20% ranges between US$2.5-8.33. Only 12% of passbook balances exceeded US$66.7 at that time.

13 M. Fiebig, Alfred. Hannig and Silvia. Wisniwski 'Savings in the Context of Microfinance: state of knowledge', CGAP, Working Group on Savings Mobilisation, 1999/ p. 1, pp. 28.

In Banco Caja Social (BCS) in Colombia, which has around 1 million clients, 75% of the deposit accounts have a balance below US$80. When compared to the financial system as a whole, BCS had nearly 30% of all its deposits in accounts with balances up to US$2,115 (compared to a GDP per capita of US$1,842) whereas the financial system as a whole only captured 12% of its deposits in these accounts. The Municipal Savings Banks in Peru had more than 325,000 savings accounts in June 2002, of which 60% had a balance of less then US$100 and another 20% between US$100 and US$500, whereas the per capita income for that year was US$2,127 in Peru.

5.1.2 Variety of savings instruments

To cope with their clients' needs for deposit services, savings banks have developed different types of flexible products in order to encourage and capture voluntary savings. *Savings accounts* are typically interest earning accounts, opened in a bank's books with a minimum initial sum which must be left in deposit at all times. There are various options in savings accounts. The *passbook* allows the customer a high degree of freedom to deposit and withdraw money the limit being fixed by the availability of funds and quite often, interest is tax-exempted. Almost all savings banks offer this product, which in the case of some postal savings banks is their only product or concentrates the bulk of the deposits with the bank. Clients are particularly interested by the flexibility associated with this product, which can also be used as security for a loan or an overdraft.

Some banks have introduced restrictions to the open access function of passbooks. Restrictions on transactions can take various forms. For instance, the Tanzania Postal Bank has derived two products from the passbook. With the postal product account (PPA), deposits and withdrawals can be made in any outlet, but once a week and in accordance with a limit on different categories of post offices and branches as stipulated by the authorities. In contrast, deposits and withdrawals with the domiciled savings account (DSA) are limited to one branch, but without size or frequency limits on transactions.

Likewise the Government Savings Bank in Thailand offers a special savings account (SSA). With this scheme, each deposit or withdrawal must not be less than BHT 1,000 (€22.7) except for the withdrawal of interest, which accrues on a daily basis and is exempt from tax. A second and subsequent withdrawal is subject to a fee of 1% of the transaction amount but these should be no less than BHT 500 (€11.3) each.

Unlike passbooks and domiciled passbooks, which are designed basically for the general public, special schemes present particular features and are for instance, tailor-made for particular segments of clientele. There are a variety of *special savings accounts* (i.e., youth savings accounts, women savings accounts, premium savings certificates, etc.).

Banco Caja Social has introduced such products that are self-explanatory and have memorable names. One of these savings accounts is called '*cuenta de ahorros progrese*' which has a didactic element orienting people to save in a progressive manner. The minimum amount to open such an account is double that for a traditional savings account after which people can save in amounts of around US$15 at a time. The savings account offers preferential access to loans of up to 3 times the balance of deposit, when held for at least 6 months and when a balance of around US$140 has been reached in the account.

The 'save-as-you-earn' (SAYE) is a savings scheme whereby the customer remits a specific amount of money on a monthly basis and for a fixed period. The SAYE account holder is required to deposit a fixed minimum in return for a lump sum at the end of the contractual period with tax exempted accumulated interest. The SAYE targets customers who receive regular but low-income flows and aims to accumulate their savings to meet a certain future demand (school fees, purchase of assets, etc.). The SAYE mainly attracts low-income salaried people and those who run small businesses. The SAYE has been introduced by the Kenya Post Office Bank and is known at the Tanzania Postal Bank as 'WADU'. At the *Bank Simpanan Nasional* in Malaysia a similar scheme is called SEDAR.

The '*Tontine savings account*' is a declination of the 'SAYE' in the cultural context of West Africa where Rotative Savings and Credit Associations (ROSCA) are very active. Although aiming to encourage small savers to accumulate capital to meet a certain demand, this scheme however, enjoys more flexibility than the SAYE. In Benin where this scheme has been introduced, any account holder can choose to remit on a daily/weekly/monthly basis any amount above CFAF 2,000 (€3.09) and for a contractual period of twelve months. He is also allowed to open several accounts, but not to make any withdrawals during this contractual period. In return, the savings bank pays a higher and tax-exempted interest rate on sums remitted.

Table 6: Sample of savings schemes offered by savings banks

Schemes	Features
Passbooks	Designed to cater for small depositors, most popular product in the savings banks community, allows very low minimum balance for opening and maintaining accounts, high administrative costs.
Youth and school savings plan	Aims to inculcate the habit of thrift and saving among school children, attract parents to become clients, allow small minimum balances for and maintaining accounts, high administrative costs. School children are encouraged to save and some prizes (scholarships, educational materials,) are awarded to children/schools for their participation/cooperation.
Institutional savings accounts	Designed for institutions such as small enterprises, public entities (i.e., schools, hospitals,...), NGOs, associations (i.e., women groups, farmer groups,...), high administrative costs.
Save-as-you-earn	Savings accumulation for specific goals and targets, restrictions on withdrawals imply low transaction costs, predictable and stable liquidity flows costs, higher return compared to the interest rate on passbook.
Savings certificates and fixed deposits	Net savers looking for high return, term fixed at the opening of the account and withdrawal at maturity unless incurring penalties, very low administrative costs and very stable funds for financing medium and long-term investments.
Premium bonds, prize bonds	Savers are eligible to participate in regular draws with major prizes, deposits are interest-free, withdrawals are not allowed within a certain period of time, cheap and stable funds that can be used for interest bearing investments.
Pension and retirement savings accounts	Designed for savers looking for reliable deposit facilities and an attractive return on a long-term deposit plan, stable funds, high interest rates, low administrative costs, withdrawals are restricted except for at high penalties, contract cancellation fees are very high.

Some savings banks encourage the collection of '*institutional savings*' thereby attracting larger amounts of deposits. Deposit facilities are provided to institutions (i.e., self-help groups, NGOs, SMEs, etc.). The provision of institutional savings accounts has been critical to the implementation of some poverty reduction programmes and a gateway into microfinance for some savings banks. Community-based development projects often request from beneficiary populations partial funding maintenance costs. The convenience of institutional savings accounts allows groups to pool together tiny amounts of individual savings for accumulation purposes and contribute to the empowerment of local populations. An example of such a savings product can be found in Senegal (See box 2).

Box 2: Rural savings accounts for women promotion groups in Senegal

Since 1985 the National Savings Bank (NSB) in Senegal has opened savings accounts for womens' groups that were granted some equipment (i.e., millet mills, boreholes). The objective was to enable these women to accumulate capital for the maintenance and the renewal of their equipment. The NSB offers the groups convenient procedures and organisation through its post offices networks that provide access to the remote communities where groups are present.

By mid-2002, the NSB included within its customers 1,000 women's groups distributed throughout all regions of Senegal, totalling an outstanding deposit balance of over CFAF 506 million (€750,000). These groups gather around 80,000 to 100,000 women spread over 28 subdivisions. The Women Promotion Groups (WPG) themselves counted more than 410 Unions, 30 sub-divisional Federations and 10 regional Federations with a national Federation at the helm.

Gradually, the Federations have introduced reciprocity by offering credit facilities to WPGs. In general, the Federation lends the WPGs a minimum of CFAF 25,000 (€37.5) and a maximum of CFAF 500,000 (€750) repayable over 5 months with the possibility of a one-month deferred payment and 5% interest-rate. The amount of the loan is linked to the amount of accumulated savings and thereby considered as a revolving credit.

Box 2 continued

The NSB, in addition to its role in securing deposits, plays the role of intermediary between the Federation and Women Promotion Groups with regard to the processing of the money granted (administration – funds delivery). The promotional activities managed by the Post in favour of womens' groups have resulted in:

- An assessment of the accumulated savings and of the productive activities undertaken by the womens' groups carried out together with the supervisory Ministry on a quarterly basis.
- A yearly subsidy of CFAF 1,500,000 (€2,250) to the womens' groups that have achieved recognition for their significant efforts in savings and in diversifying their activities.

Ceremonies have been organised every year to offer bonuses and award 'best savers diplomas' to the womens' groups that have distinguished themselves the most (75 groups have been awarded prizes). Moreover, this initiative has had a snowball effect at government level with the introduction of the contest that awards subsidies to the most effective groups.

Contractual savings schemes are savings plans whereby a customer is committed to saving regularly over a contractual period and thereby accumulates term illiquid financial assets. On one hand, contractual savings schemes allow the depositor to enjoy higher returns while safeguarding their savings. On the other hand, intermediaries use contractual savings schemes to attract stable financial resources.

The definition of contractual savings can be extended to all savings schemes with a contractual period, e.g., fixed deposit, save as you earn, accumulation of the down payment of a house, education savings plan, wedding savings plan, funeral savings plan, etc.) with some schemes linked to the promise of obtaining a loan facility[14].

14 Gregorio Impavido and Alberto R. Musalem 'Contractual savings, stock and asset markets', the World Bank, FSSD, p.3.

For example, the holders of fixed deposit accounts with Bank Simpanan Nasional (BSN) in Malaysia are eligible to apply for a loan under this scheme. The minimum loan is RM 1,000 (€243) and subject to a maximum of 90% of the value of fixed deposit certificates pledged as collateral. The interest rate charged is 2.5% above the interest on pledged fixed deposit certificates. A SEDAR account holder is eligible to apply for a personal loan not exceeding twice the amount saved if he has deposited at least RM 500 (€121) for a period of one year. The minimum loan is RM1,000 (€243) and the maximum is RM 5,000 (€1,215). The loan is offered for housing, education, medical expenses and other purposes determined by the *Bank Simpanan Nasional*.

Most common contractual savings schemes are however pensions and life insurance assets, which are usually available only upon the occurrence of a particular event (e.g., retirement, disability, death). Pension schemes offered by savings banks are contractual savings plans whereby the holders remit regularly a certain sum and thereby accumulate a capital amount (principal + interests) available at retirement age.

In Benin, for instance, any individual is allowed to open a pension savings account with a minimum deposit and a minimum account balance respectively of CFAF 5.000 (€7.62) and for contractual period of 5 to 25 years. Another example is the National Savings Bank of Burkina Faso, whose scheme is accessible to any individual who commits to save regularly a pre-determined amount of money for minimum contractual period of 2 years where deposits with the pension savings account enjoy a yearly interest rate of 6% (2 percent above passbook rate).

The conditions of these schemes are adapted in order to offer them to poorer clients by allowing small minimum deposits in particular. In reality however, pension schemes attract mainly formal sector workers (wage earners). By end 2002, the savings bank in Benin managed 1,000 pension savings accounts representing 1% of total liabilities. At the end of 2000, the savings bank in Burkina-Faso had approximately 4,200 pension savings accounts representing an accumulated amount of CFAF 1.4 billion (€2.18 million) and 5,6% of total bank liabilities.

5.2 Lending services

Access to finance and in particular, credit is one of the most often quoted constraints to business development by the self-employed and micro-entrepreneurs. The definition of microcredit has evolved over the years and its interpretation is still wide ranging across countries and institutions. In some countries, where the microfinance industry has grown into a competitive business, central banks have established a definition of what can be considered as a microcredit by taking into account the borrower (e.g. size of enterprise in terms of turnover, assets, employees, etc.) and characteristics of the debt (size of loan, number of loans, etc.).

Some definitions are rather narrow and strict and only consider a micro-credit when it is a loan invested in an entrepreneurial activity. In other circumstances and more often it is accepted that the money lent is fungible and that it can be invested to respond to any need the household might have. In this case the level of income of the borrower or average loan size is more determining for whether a loan is a microloan or rather a typical retail loan. Considering the different interpretations of microcredit that exist, we have relied on the definitions as used by each savings bank when presenting figures and analysis.

Although some postal savings banks are prohibited from lending, in general savings banks are characterised by the fact that they offer a whole range of lending products and that these products are segmented depending on the customer group and the investment purpose[15]. The exception to this may be the postal savings banks that are often restricted by law in their lending operations. In general, microlending programmes are included within regular retail banking operations, but may operate as separate programmes, cost centres or even subsidiaries such as is the case for Banco del Estado de Chile, with specific methodologies adapted to the microcredit operations.

Savings banks apply diverse methodologies for administering their micro-lending programmes. Most apply individual lending methodology as an extension of their mainstream retail lending business. Evidence from the case studies indicates that only Tanzania Postal Bank applies a pure group lending methodology.

15 The WSBI counts 36 postal savings banks of which 22 are not allowed to provide lending services.

In the case of the People bank project of Government Savings Bank (GSB), the loans are extended to individuals who are required to be in a group of three (3) members with two of them guaranteeing the borrower. No methodology is by itself a guarantee for success and can therefore preferable. Each institution has to design and administer its programme according to their domestic economic, social and cultural context.

5.2.1 Weight of programmes

The weight of microloans in the total loan portfolio of savings banks varies from modest to significant. In the case of the Government Savings Bank in Thailand, this is 2% and for Banco Caja Social in Colombia taking into account the narrow definition held by the Central Bank[16] and for Banco del Estado in Chile it is around 5%. The Peruvian Cajas Municipales de Ahorro y Credito consider half of their total loan portfolio as consisting of microcredits. In the case of the Tanzania Postal Bank, which was only granted permission to lend a few years ago, the microcredit portfolio is the bulk of its loan portfolio. The actual fact that savings banks, like other formal financial institutions providing microcredits, are able to offer credit to a wide range of clients with different levels of income helps diversify their risk and thereby lower costs.

Table 7: Microlending portfolio as % of total loans

Institution	Outstanding microlending portfolio (US$million) (1)	Outstanding loans (US$million) (2)	Ratio (1)/(2)
Banco del Estado (Chile)	300	5,384	5.57%
Banco Caja Social (Colombia)	18	360	5%
National Bank for Development (Egypt)	4.4	1,100	0.4%
Cajas Municipales de Ahorro y Credito (Peru)	133.7	267.3	50%
Postal Bank (Tanzania)	1.9	4.0	49%
Government Savings Bank (Thailand)	134	5,991	2,2%

Source: WSBI and member banks

16 According to the bank's own standards this figure is around 20%.

Although for some of the bigger savings banks, the relative importance of the microcredit portfolio may be small, it is clear that compared to many microfinance institutions they are considerable. In a recent survey, the *Microfinance Information eXchange (MIX) bulletin* benchmarked large Latin American microfinance institutions as those with an outstanding loan portfolio above US$15 million[17]. The savings banks that were looked at in Latin America (in Peru, Colombia and Chile) all have portfolios larger than that and can be compared to some prominent microfinance providers such as Mibanco in Peru (US$92.3 million), Bancosol in Bolivia (US$80.9 million), Cooperativa Emprender in Colombia (US$62.2 million).

The experience of the Government Savings Bank (GSB) is also a good example of how the re-targeting of retail banking operations to provide microfinance services can have an immediate and considerable impact. After two years in operation, the 'People Bank project' had achieved a tremendous expansion with an outstanding microloan portfolio above US$130 million. This amount represented 10% of the outstanding micro-loans extended by Bank Rakyat Indonesia (BRI) Unit-Desa (US$1,319 million) and half of the loan portfolio of Grameen Banks (US$250 million).

Even in Africa, where microloan portfolios are generally a lot smaller due to loan sizes and number of customers, it is worthwhile noting that the experiences of National Bank for Development in Egypt (US$4.4 million) and the Postal Bank in Tanzania (US$1.9 million) are quite significant in average if compared to the size of the loan portfolio of some of the medium-size microfinance institutions[18].

In order to succeed in the massification of microfinance services it is generally recognised that a larger involvement of formal financial institutions, is needed. However, in order to analyse the actual (and potential) contribution of savings banks in this respect, it is not enough to highlight only the size of the loan portfolio but also the outreach of the bank is of importance.

17 *Benchmarking Latin American Microfinance*, published by the Microfinance Information eXchange (MIX) bulletin www.mix.org

18 Microbanking Bulletin, July 2003, Bulletin Tables, p. 54.

5.2.2 Outreach assessment

Outreach indicators that are provided in table 8 refer to the breadth and depth of these programmes. The breadth refers to the number of small borrowers served while the depth indicates the capacity of the services to target underserved and disadvantaged people. Among these experiences the performance of the Government Savings Bank (GSB) has been the most impressive in terms of growth in breadth. In only two years time GSBs People Bank managed to achieve more than 550,000 active borrowers.

The depth of the outreach can be measured by dividing the average loan balance by the country per capita Gross National Product (GNP). Generally speaking, a lower depth ratio implies deeper outreach. In the particular case of selected experiences, it is worth noting that the estimates in some cases outperform international standards. The average balance per borrower for the People Bank project is nearly 12% of the GNP per capita in Thailand. Measured like this, the outreach for the National Bank for Development (NBD) microcredit programme in Egypt is similar. In the case of the Postal Bank in Tanzania, the ratio of depth falls between 33-55% (depending on how many group members took up the group loans). In Latin America, the municipal savings banks in Peru scored best with 33% with Banco del Estado and Banco Caja Social both having 68%.

Table 8: Outreach indicators

Institution	Active borrowers	Average loan balance in US$ (1)	Per capita GNP in US$ (2)	Ratio (1)/(2)
Banco del Estado (Chile)	96,000	3,125	4,590	0,68
Banco Caja Social (Colombia)*	52,700	1,300	1,890	0,68
National Bank for Development (Egypt)	18,577	318	1,470	0,22
Cajas Municipales de Ahorro y Credito (Peru)*	205,450	650	1,980	0,33
Postal Bank (Tanzania)	4,235 groups (3 to 5 people)	448 per group	270	0,33-0,55
Government Savings Bank (Thailand)	555,934	241,5	1,980	0,12

* *These percentages may actually be higher when only the microcredit clients are concerned, but no separate figures exist.*

5.2.3 Gender analysis

When looking more closely at the types of customers served with microcredits by these savings banks, it is evident that more than 40% of all clients are female. As these institutions provide conventional loans in parallel to their microlending programmes, it may well be that the proportion of the female population receiving microloans is slightly higher. This percentage is as high as 80% in the case of Tanzania Postal Bank, which is the only bank in the sample with a policy that prioritises women. The bank has consistently reported better loan repayment rates by women than for men.

Table 9: Female presence

Institution	Percentage of female clients
Banco del Estado (Chile)	45%
Banco Caja Social (Colombia)	43%
National Bank for Development (Egypt)*	24.6%
Cajas Municipales de Ahorro y Credito (Peru)	45%
Postal Bank (Tanzania)	80%
Government Savings Bank (Thailand)	NA

* *This ratio refers to loans to women as a proportion of the number of outstanding loans on 31, December 2002.*

5.2.4 Profitability

Available information indicates that all the above-mentioned microlending programmes are profitable. However, it is difficult to get beyond available data because the information is in general consolidated in regular financial statements. Three of the case study programmes have been isolated as income centres (Tanzania Postal Savings Bank, Government Savings Bank of Thailand, National Development Bank of Egypt). Although they are most often declared profitable, there is no clear indication of the full costs of these programmes. The Tanzania Postal Bank recorded an additional income of about US$197,000 meanwhile the Government Savings Bank of Thailand disclosed an amount of US$13.4 million as the interest received under the People Bank project. The National Bank for Development (NBD) of Egypt has recorded a cumulative net profit of about US$2.7 million over a decade. The microenterprise subsidiary of Banco Estado, which has its own balance sheet became profitable in 1998 (having been launched in 1996) and generated a profit of US$20,882 in 2002.

5.3 Insurance services

Microinsurance has emerged as the third pillar in the range of microfinance services and relevant tools to address the vulnerability of less affluent people. It can be defined as "*the protection of low-income people against specific perils in exchange for premium payments proportionate to the likelihood and cost of the risk involved*"[19]. Access to small credits does not significantly reduce the vulnerability of microentrepreneurs and low-income. Microinsurance may help soften the adverse impact of various risks, which can jeopardise their income streams.

In practice, microinsurance products take different forms. Here we will divide them in 3 groups:

1. insurance policies linked to credit products;
2. insurance policies linked to savings products including life insurances;
3. insurance policies covering risks other than death and permanent invalidity, but people and their properties in general.

For banks or microfinance providers in general, microinsurance schemes can help mitigate the negative effects of bad debts on the quality of the loan portfolio since death and illness generally result in outstanding payments. A step further is offering insurance to low-income people to protect them from risks and vulnerabilities other than death and invalidity, such as health, education or fire with no specific link to a credit or savings product.

5.3.1 Insurances linked to loans

Most common and often obligatory in the microfinance industry is the credit life insurance that covers the repayment of a microloan in case of death or permanent invalidity. When offered by MFIs this is generally linked to a special reserve fund the MFI generates from fees charged to clients. This commission is normally included in the cost of the loan. There are also insurance policies that protect people for a temporary incapacity, for health reasons for instance or loss of a (part of a) crop due to a natural disaster, and repay a part of the loan when these occur. Pricing of these schemes can sometimes be a problem incurring excessive costs on clients, however some vulnerability remains with the MFI in case a natural disaster for instance affects a region and several clients die at the same time. Therefore some MFIs have opted for outsourcing of this risk to specialised insurance agents or companies.

19 Michael, McCord and Sylvia, Osinde. 'Reducing Vulnerability: the Supply of Health Insurance in East Africa', Microsave Africa 2003.

Box 3: Characteristics of insurance schemes offered by savings banks

- Clear and simple rules about what is covered and what not;
- No or limited requirements in terms of medical tests for life and health insurances;
- Low cost;
- Easy accessibility: in bank offices, with little paperwork and instantaneous cover;
- Brand name of product is easily recognisable and information is clear;
- For account holders only or with preferential conditions for account holders;
- Premiums are paid easily through bank accounts or automatically included in cost of a loan;
- Payment installments are generally flexible and adapted to income generated by beneficiaries.

Though all policies differ, some general characteristics of many insurance products offered by savings banks that make them especially suitable for low-income households are related to their coverage, timeliness, accessibility and affordability.

Savings banks generally outsource the design and administration of insurance schemes to a separate entity, often an insurance company owned by the bank or the same group. This has the advantage of specialisation in a rather complex and risky business, and offers the possibility to diversify in terms of products offered and cross-selling opportunities.

Banco del Estado has a subsidiary called 'Banestado Corredores de Seguros', which provides amongst others insurance products to middle and low-income people that are generally linked to a credit or savings product. The credit life insurance they offer is compulsory and automatic with receipt of a loan. In addition to that they offer microentrepreneurs and self-employed people like farmers voluntary insurance that could protect people in the case of temporary or long-term illness or ('*Seguro Salud*') or loss of investments in agricultural crops due to adverse weather conditions ('*Seguro Agricola*').

There is also an insurance policy that protects against damage to the productive assets of a micro or small enterprise, called '*Empresa Protegida*'. In the latter case the insurance repays a number of quotas depending on the damage done to the company due to fire, theft or accidents.

The National Bank for Development (NBD) is also providing mandatory life insurance services to its borrowers. The fees represent 2.7% per year of the principal amount of loan. The policy holders are protected against unforeseen risks or unexpected adverse conditions that might threaten their business and cause a loan default. In case of misfortune, the NBD provides assistance to the beneficiary of up to US$120 for funeral and burial expenses. The bank also assumes the remaining part of the loan.

5.3.2 Insurance linked to savings products

The second type of insurance is that which is linked to contractual savings products of which the life insurance is the most common product offered by savings banks. It provides designated beneficiaries with a payout that assists them in coping with their hardship upon the death of a family member, often the breadwinner. A typical example is that of '*Casa segura*', which offers in case of the death of the policy holder who saves for the purchase of a house, to his or her beneficiary the amount that would have been collected in case the person would not have died and completed the savings scheme plan. This allows the beneficiary to purchase the house even though the saver has not been able to meet his commitments because of an early death.

Along the same lines, the 'Seguro para sus estudios' policy is linked to a parent's savings plan for the education of children. Government Savings Bank (GSB) in Thailand offers a similar educational insurance, though in this case, the policy holder is insured for the death of the child. Upon maturity of the policy, the beneficiary will receive the sum insured in a series of instalments suited to the children's educational plan. In case of death of the beneficiaries during the policy period, GSB will pay the total (or partial) sum insured to the policy holder depending on the age of the child when it dies.

Box 4: Life insurance offered by the Government Savings Bank (GSB)

GSB has a well-developed insurance portfolio and is market leader for life insurance in Thailand with currently more than 600,000 policy holders. These products are in fact life insurance-like deposit schemes. Its basic life insurance product '*Perm Poom Sub Endowment Scheme*' offers the insured person several benefits after he or she has paid premiums for two years or more, such as a loans in the same amount as the cash value at an interest rate of only 8% per annum; withdrawal of cash in an amount up to the cash value; and tax deductible premium payments.

Another GSB scheme called '*Ronsai Endowment Insurance Scheme*' combines the features of the above scheme with savings features. It differs in the fact that the policy holder is required to pay small premiums to be entitled to the maximum benefits on a progressive basis. Also, bonus is paid in cash every certain period of time and a maturity bonus is paid upon maturity of the life insurance policy. Upon the death of the policy holder prior to the maturity of the policy, GSB will pay the beneficiary/beneficiaries the sum insured plus an additional benefit.

An alternative to this is the '*Endowment and Life Annuity Insurance*' of GSB which offers two benefits during the policy period – life protection and maturity bonus payment – though the policy holder is not yet retired and not a government official. The policy holder is allowed to indicate when he would like to receive the annuity and may opt for a lump sum. Moreover, GSB provides this scheme in two options, with dividends and without dividends. The policy holder can apply for accident coverage and pay premiums at the lowest rate. A special coverage is applied in case of disability, no matter whether it results from sickness or an accident.

Indeed, life (and invalidity) insurance products are most common among savings banks, including postal savings banks. For instance, the national (postal) savings bank in Senegal has combined a life insurance policy with its pension savings plan. In Benin, the postal savings bank offer 'Postassur' which is not linked to any other product as it protects policy holders (rather than account holders) against a death or disability following an accident. However, account holders get better conditions with a similar insurance policy scheme called 'Yebomi', thereby stimulating savings. In Burkina Faso only account holders have access to Postassur life insurance offered by the postal bank there. Banco Caja Social offers a life insurance called 'Proteccion Creciente' which is administered by 'Liberty Seguros' and covers apart from death also severe illnesses and total and permanent invalidity.

Table 10: Examples of premiums and compensation for life insurances

Bank and insurance product offered	Range of premium paid per year	Corresponding compensation in case of death (disability is generally a % of that)
Sonaposte, (Burkina Faso), Postassur	€10.67	€762
Remarks: Amount is doubled in case death results from an accident (no coverage for disability)		
Postal Savings Bank (Benin), Yebomi	€11.74	€152.5-7,623
GSB, (Thailand) Perm Poom Sub Endowment scheme		€108-43,200
Remarks: Periods insured between 10 and 20 years, additional benefits for insured person after having paid premiums for 2 years. Additional coverage can be obtained of disability		
Banco Estado (Chile) 'Seguro de vida e invalidez'	€6.72-166	50-2000 UF (equivalent of USD)
Remarks: Covers sports and activities of high risk		
Banco Caja Social (Colombia)	€35	US$1624-24,368
Remarks: Also covers serious illnesses and total and permanent invalidity		

5.3.3 Other insurance

A third category of insurance is commercialised independent of savings and loan products offered by the bank. The savings bank in Benin offers for instance an '*assurance risques scolaires*' that covers families for possible damage or accidents caused or suffered by school children. Banco Caja Social in Colombia offers an integral insurance called 'poliza del hogar' which covers risks of damage to property and personal risks, including civil liability towards third parties.

5.4 Payments facilities for less affluent people

Payment services are increasingly recognised as an essential component of the whole package of financial services that are required by those on a low-income. Like all customers, they need to pay bills and transfer money. These interests are in principle no different from those of the typical retail client apart from the fact that their accessibility needs to take into account issues such as standards of education and client location. Low-income customers generally require payment services that are low cost, secure and fast, convenient and easy to use.

5.4.1 Domestic payments

Access to these services not only depends on the financial institution but also on the overall domestic payment system and related policies in place. For savings banks, payment transactions are a central factor in the relationship with their clients. Their general strategy is based on a multi-channel alternative offering a range of payment services through different instruments.

Savings banks have become aware of the potential of the domestic market of money transfer services and the need to address it. In several countries, they are developing strategies and identifying cost-efficient technologies to serve this market. A relevant development has happened in the West African Economic and Monetary Union (WAEMU) where in the framework of a partnership with a local service provider, savings banks are providing an electronic money transfer service on the domestic and regional mass market since early 2003. The business took off rapidly in Cote d'Ivoire where the 'Caisse d'Epargne et des Chèques Postaux' (CECP) carried out more than 80,000 transactions for an approximate value of €5.9 million for the first eleven months of 2003.

Most payment transactions by low-income customers are still undertaken in cash partly because they have limited access to other services, but also because they generally do not trust other payment instruments offered. The acceptance of alternative payment instruments and the necessary marketing that needs to accompany their introduction has proven essential in the experiences of savings banks. A related survey that was undertaken with clients of Banco Caja Social in Colombia also reflected that for the use of cheques, debit cards and credit cards, the cost of transactions (and interest rate in latter cases) was one of the major issues deterring low-income customers from opting for these products.

Table 11: Interest of clients and financial institutions with regard to payment instruments

Interest of client	Interest of financial entity
Low cost	Quality of service delivery
Convenient and easy to use	Cost reduction
Secure and reliable	Standardisation
Fast	Building customer-bank relation

From the perspective of banking institutions, moving away from cash operations to more electronic forms of payment is however desirable. By switching to electronic payment services, banks can provide a fast and quality service also outside of office hours while reducing processing costs and standardising operations. Electronic payment instruments also tend to strengthen the relationship between the client and the bank and build loyalty. Other services can also more easily be linked to those payment instruments.

In the case of low-income customers, making a payment transaction is for some, their first introduction to the banking system and by attracting customers in this way, savings banks contribute to their bancarisation. The capturing and processing of recurrent payments of low-income customers is for many savings banks a potential growth market. Savings banks can make use of their assets such as their branch network for this purpose and where the network does not reach, alliances can be created.

Revitalised postal savings banks can offer valuable alternatives in places where people previously only had the possibility to transport cash or to send money by - rather bureaucratic- postal money orders. Some postal banks (or postal financial services divisions) have even introduced plastic cards. For example, *DinarPost* has been introduced by the postal financial services' division in Tunisia to facilitate withdrawal services through 300 existing ATMs in the country. In South Africa, the Postbank *Flexi Card* service formerly known as *Telebank* is a card based transactions account. The minimum for opening and maintaining this account is R 50 (€5) and the transactions are made possible at the terminals in over 300 post office counters and at some 7,200 ATMs of other banks.

Several savings banks, especially in Latin America and Asia have introduced plastic cards on a large scale and acquired their own ATMs with inter-connection to home facilities. *Caixa Econômica Federal* in Brazil, which performs many payment transactions also for the government (welfare programmes etc.) has developed a large and nationwide network of ATMs with almost 12,500 machines. It has also issued around 19 million debit cards. Another example is Banco Caja Social in Colombia, which has issued more than 270,000 debit cards. In Colombia, only 12% of the bancarised population (6%) has a debit card and only 5% a credit card. The growth potential in the low and middle-income segment of the population is large.

Table 12: Payment facilities with some savings banks

Country	Institution	ATMs (number)	Debit cards (number)
Brazil	Caixa Econômica Federal	12,473	19,041,658
Chile	Banco Del Estado	768	347,194
Colombia	Banco Caja Social	133	271,801
China	Postal Savings and Remittance Bureau	4,690	28,310,740
Costa Rica	Banco Popular y de Desarrollo Comunal de Costa Rica	127	678,433
Cuba	Banco Popular de Ahorro	52	52,500
Malaysia	Bank Simpanan Nasional	602	NA
Thailand	Government Savings Bank	281	NA
Tunisia	La Poste Tunisienne	80	15,000

In the particular context of the microcredit business, savings banks have an advantage over microfinance institutions in the sense that they can offer alternative services for the repayment of loans, including through ATMs and other electronic channels. However this advantage can also be used to create synergies between savings banks and more grass roots level MFIs. For instance, savings banks can team up with microfinance institutions and issue a payment card with both brands that can be distributed to clients of the MFI. The client can use the card to collect the loan disbursed by the MFIs and repay the loan, and on the other hand save with the savings bank and make payments. The bank thereby has a cost-efficient way to reach out to more clients that would otherwise have difficulties reaching the branches. The MFI can achieve lower transaction costs and improved security by using this system. The client wins because of the increased access to financial services.

5.4.2 International money transfer services: Remittances

Global official figures estimate that 100 million migrants support half a billion people every year through remittances worth US$100 billion. This figure doubles if we include unrecorded flows. In many developing countries the remittance flows exceed aid, and often represent an important source of income. Savings banks are also active in this business and more in particular in the transfers of migrant workers' earnings sent back to their countries of origin to support their families and communities.

Savings banks have a natural role to play in the remittances business because of their retail orientation. The main originators and beneficiaries of the lower value payment transactions around the world are individuals and small businesses, the traditional target client group of savings banks. Capturing these flows in recipient countries would allow savings banks to offer complementary banking products and services on both sides (such as savings accounts, plastic cards, insurances, loans, etc).

Some savings banks have connected with multinational wireless money transfer networks such as Western Union, Money Gram, Vigo, etc. which provide reliable solutions that are responsive to the market-demand. By channelling more of the remittances into the financial system and intermediating the flow of these resources, savings banks are able to contribute to leveraging the positive impact of the transfers.

However, it is recognised that often the costs charged to customers are relatively high although these partnerships result in additional income from fees and commissions on these services. The cost is especially an issue in places where competition is low or non-existent. Fee and commission charges can be as high as 20-25% in cases where the market is monopolised by commercial remittances companies. In those countries where competition among remittances companies or banks providing these services has grown, such as the traffic between the USA and Mexico, fees and commissions have fallen by 58% since 1999.

In several savings banks, efforts are undertaken to encourage those that live abroad to save at home. This may be done in local currency or hard currency (if allowed by the central bank) such as the case of the savings bank in Cape Verde. Some savings banks in countries that experience large inflows of remittances have set up special inter-bank agreements and develop specialised products and services for attracting these flows. Banco Caja Social in Columbia has established such agreements with savings banks in Spain where many Colombian emigrants live. It has established several products adapted to the needs of their migrant customers and family members. In 2003 when Banco Caja Social started its remittances service, it quickly reached more than 1200 transactions a month with an average of US$500 per transfer. In 2002 the Kenya Post Office Savings Bank managed 420,740 remittances transactions worth US$11.66 million. The Tanzania Postal Bank sent US$37.67 million worth of remittances on behalf of its customers in 2003.

Linking remittances flows with microfinance products is an area of increased interest in savings banks. Not only the cross-selling opportunities but also the social responsibility of the banks make them look for ways to channels these resources into productive investments. At a microlevel, mechanisms are developed to allow direct payment of microcredits with remittances income. Arrangements to use the remitter’s assets as collateral are also being explored though still difficult for the legal aspects that are involved in such cross border transactions. A microloan with such guarantees can be higher or less costly. At an institutional level, remittances can offer opportunities for the refinancing of microcredit portfolios. Credits that are backed by regular cross-border payments could be grouped and traded at a lower cost allowing the bank to charge less for such credits and increasing the added value for the customer.

Table 13: Senders and beneficiaries: their interests and profile

	Sender	Beneficiary
Priorities	■ Transaction fee ■ Security	■ Duration of transaction ■ Security
Other important factors	■ Proximity of transaction points ■ Duration of transaction ■ Exchange rate	■ Conditions and requirements for obtaining the money transferred (simple processes, little information and documents required) ■ Amount finally received
Profile	■ Migrants workers employed in the informal sector mainly ■ Little spare time (work up to 90% of their time) ■ Intention to legalise stay in resident county and continue to earn for personal benefit and that of the family back at home	■ Direct family members of the migrant ■ Receive remittances in order to cover mortgage payments, reimbursement of travel loan, basic needs or investments ■ Generally no significant stable income, time is not an issue ■ Interested in obtaining additional bank products

Source: Results from survey among families of Colombian migrants in Spain, Banco Caja Social.

The fact that remittance flows generally benefit the low-income segment of the population increases their significance to economic development and poverty reduction. These, as well as the reduction of the costs of the transfers remain the principle challenges of the remittances business. Savings banks are prepared to act in a competitive environment and are encouraged to design targeted products and services for the migrant customers and beneficiaries of remittances. Establishing partnerships will be of key importance in order to deliver end-to-end value[20].

20 Because of the above mentioned initiatives and potentials, the savings banks have an interest in influencing the remittance business both at the level of policy formulation as well as in enhancing the service delivery. The WSBI is working with international organisations with the aim to improve the remittance business; make it more transparent, reliable, less costly and with a higher development impact.

6. CHALLENGES AND RECOMMENDATIONS

It is increasingly accepted that in order to achieve the massification of microfinance, donor funds and discounted credit lines from governments and central banks can no longer form the main source of funding for microfinance programmes. Even though donor funding can be a support and catalyst in some cases to develop and expand microfinance services, more commercially viable programmes should be encouraged. Experiences of some savings banks and other formal financial institutions show that institutions that have the capacity to mobilise deposits or commercial funds can be sustainable in providing these services.

A key factor in the successful delivery of the microfinance services, as in any type of institution, is the fact that there is an institutional commitment to develop these services on a commercial and sustainable basis. Only then can the bank dedicate the appropriate resources to make it work.

6.1 Challenges

It is recognised that savings banks as socially responsible retail banks have the potential for downscaling and diversifying their operations to offer a range of financial services to currently underserved markets. However, there are a number of challenges for savings and other retail banks willing to enter into the microfinance business or strengthen their existing operations in this field. They include amongst others (in no particular order): product development and human resources, efficiency, corporate governance and for some, legal obstacles.

6.1.1 Product development and human resources

The market segmentation earlier mentioned is of key importance to meet the challenge of appropriate product design. Examples given from the savings banks included in this paper show that microfinance products, even though they belong to the retail product family, have specific characteristics that make them attractive to low-income clients. Also the marketing of these products and services is very well targeted with well-defined, ‘easy-to-understand-and-remember’ concepts.

Savings banks have, thanks to their long-standing tradition and institutional commitment, developed a range of microsavings instruments that are adapted to the needs of the poor. They are used to handle numerous small transactions in managing small deposit accounts. As mentioned in the case studies, generally 80% of the people hold 20% of the deposits. Many savings banks have also been able to downscale their retail lending operations in microcredit programmes by adopting methodologies suited to reach out to low-income clients.

As is particularly demonstrated in the cases of Chile and Colombia, savings banks that are successful in microfinance manage to create cross-selling opportunities, ensuring that the bank-client relationship is broadened both to the benefit of the client who has access to more services, as well as that of the bank that generates more business. The view of savings banks that a client has an integral need of financial services is a strong asset that allows microfinance services to grow into commercially viable operations.

Without contradicting what was said before about the need to view microfinance as a specialised business and the importance of market segmentation, it is also relevant for savings banks to view microfinance clients as banking clients that can upgrade into the retail banking services. This up-scaling process has happened in some savings banks, even though it only involves a small percentage of the microfinance clients.

However, savings banks fully recognise that microfinance operations differ from conventional banking practises in several ways and that they therefore require specific skills and capacities. It is indeed advisable for banks going into microfinance to attract skills outside the bank by recruiting practitioners, even if some are not highly educated. A good combination of professional bankers and microfinance experts is required for starting a downscaling experience.

Intensive training programmes should also be undertaken to change the mind of conventional bankers and to introduce them to microfinance techniques and methodologies. The advantage for savings banks and retail banks in this respect is the fact that they are often used to micro-savings products and already deal with clients that are potential clients for microloans.

6.1.2 Improving overall efficiency

Taking into account the outreach and depth of services, it has to be recognised that microfinance has in general a higher costs per volume of money or per transaction operating as efficiently as possible to bring down the cost of services delivery where and when possible is of strategic importance. Downscaling experiences have shown that initial cross-subsidisation of microfinance operations might be necessary. On this particular point, banks with a diversified asset-portfolio can subsidise microlending charges with other interest income earned.

But, cross-subsidisation is relevant for a limited period only after which it becomes essential for large banks to create microfinance cost centres in order to operate a cost-allocation process and to measure the subsidies. Cross-subsidisation does not always work without creating in-house opposition and conflicts. For these reasons, public and donor funds in particular have played and will probably continue to play an instrumental role in guiding mainstream banks through the process of experimenting in microlending activities.

6.1.3 Corporate governance

Government interference can in some cases prevent banks from moving forward dynamically. In the cases where banks are state owned it is especially important that they are managed independently. The variety of ownership structures among the case studies shows that the ownership structure itself is not so much an issue, but rather the governance of the institution. For instance, it is obvious that politically-motivated microlending decisions would quickly lead to substantial losses and threaten the protection of deposits. Therefore, guidelines for good corporate governance are very important. Also with regard to the use of the bank as channel for government policy and the distribution of the bank's profit as was mentioned earlier, these guidelines have to be taken into account to avoid a politicisation of the bank's decisions.

For certain postal savings banks, prudential supervision is an issue. Those banks that are governed by postal laws rather than falling under banking/financial regulations need to adapt themselves and introduce measures responding to supervisory requirements in order to better serve the needs of their clients and become more integrated in the financial system as a whole.

6.1.4 Overcoming legislative obstacles

Some savings banks and most often postal savings institutions continue to operate as narrow banks. Among them, some are policy-based financial institutions that are required to invest their liquidity in government debt instruments. Others have been allowed to diversify in low risk financial instruments. But, most of them invest in government guaranteed debt instruments issued by public sector companies, while a small number further diversify their investments in money markets debt instruments (i.e., commercial papers, bonds).

Several governments, especially in Africa, are considering extending a permission to those banks to enter into more specific microlending business on a small scale in order to stimulate the microfinance sector and expand financial services available to the poor. These institutions will be allowed to introduce microlending operations with a minimum capital far lower than that which is required for commercial banking. It is understood by postal banks operating in these countries that notwithstanding the removal of these legislative barriers, they will still need to build up the necessary capacity and introduce the right technology to manage microlending programmes.

In other circumstances, such as in Senegal, the postal savings bank is undergoing a restructuring process for becoming a licensed bank. When allowed to lend, the postal savings banks foresee using mobilised resources for investing in other financial institutions that lend to those on low-incomes. In that case, the savings banks will operate as a kind of wholesale lender for the microfinance sector.

6.2 Recommendations

Public authorities and supervisory agencies can support the downscaling of banks into microfinance operations by ensuring a favourable legal and regulatory environment and encouraging the partnerships with grassroot financial institutions to deepen the outreach of these banks.

6.2.1 Enabling environment

One aspect of an enabling environment was already touched upon for those institutions that are currently not allowed to lend. But such an environment should also include flexibility with regard to interest rates as well as reasonable reporting requirements and supervisory rules that recognise the specificities of microfinance operations, particularly their high volume of activity undertaking small-scale transactions.

Liberal interest rates: An important aspect of the enabling environment is a liberal financial system that refrains from fixing interest rates and allows banks to charge the cost of the transactions and build viable and sustainable microfinance operations. Evidence from the National Bank for Development, the Tanzania Postal Bank and Municipal Savings Banks in Peru amongst others shows that interest rates on microloans are higher (at least double and in case of TPB even three fold) than on conventional loans in order for these institutions to meet associated costs. In some countries, like Colombia, the government maintains controls on interest rates, which can limit the capacity for banks to enter into the micro-finance business in a viable way.

Table 15: Comparison of interest rates

Country	Institution	Average lending basis rate on conventional operations (% per annum)	Microfinancing programme lending rates (% per annum)
Chile	Banco del Estado (Chile)	18-19%	28.5-37.8
Colombia	Banco Caja Social (BCS)	19.7%	29
Egypt	National Bank for Development (NBD)	12-14%	29.7
Peru	Cajas Municpales de Ahorro Credito (CMACs)	24.4%	55.6
Tanzania	Tanzania Postal Bank (TPB)	14-15%	47.1
Thailand	Government Savings Bank (GSB)	8%	19-56.3

Reporting requirements: Microlending programmes imply large numbers of small and even atomistic transactions. Therefore reporting on each loan is indeed costly and burdensome. This can also be the case in relation to low value payment transfers. In countries with advanced microfinance industries (especially in Latin America), supervisory authorities are increasingly recognising the specificities of microfinance operations and their implications for reporting.

Without putting the stability of the financial sector at risk, but while complying with international standards as well as local conditions, supervisory authorities need to adapt their regulations to allow banks to use their infrastructure and capacity to downscale their operations into smaller transactions and report on them in a proportionate manner.

Capital requirements and provisioning: Equally with regard to prudential measures related to the capital base of a bank, the peculiarities of microfinance operations have to be kept in mind. All restrictions based on the capital base systematically restrict the expansion of microlending programmes. In some countries, prudential measures request banks to restrict uncollaterised loans or loans with weak collaterals to a certain limit of their capital.

For example, the central bank requires the microcredit portfolio at the Tanzania Postal Bank not to exceed 25% of the bank's core capital. As microloans are in general unsecured loans, these requirements definitely limit the expansion of downscaling experiences. These issues have to be taken into account if national authorities want to stimulate downscaling of bank operations into microfinance.

The same counts for provisioning requirements; regulatory and supervisory authorities require that banks constitute reserves based on the quality of their loan portfolio. Even though the quality of a microfinance loan portfolio may be good (with low default rates) some authorities have insufficient understanding of the business to allow a reasonable classification resulting in a significant amount of reserves required to cover these loan portfolio.

The example of Tanzania is again of relevance. As a standing regulation from the central bank, all loans under the microcredit programme outstanding for a period of more than 90 days after the expiry date should be classified as loss and a provision made for the full amount (100%) of this loan. However, similar regulations are not applied to conventional loans.

Outstanding loans are downgraded to 'substandard' between 91-180 open days and the bank is required only to make a provision of 10% of this amount. Then the loan shall become doubtful between 181-270 days and a provision representing 50% of this amount has to be built up. It is only after 271 days that any outstanding conventional loan is classified as a loss and the provisioning made on the full amount.

6.2.2 Alliances between savings and retail banks and MFIs

An alternative for savings and retail banks to offering microfinance services directly to the end beneficiary could be to establish alliances with successful microfinance institutions, or work together with grass roots level organisations. Various options could be developed in implementing this approach.

First, the microfinance institution (MFI) and savings bank can share responsibilities of a part of the services offered to the clients, building on each other's comparative advantage. The MFI has a closer contact with the client and can have a better knowledge and understanding of his financial situation. The expertise that microfinance institutions have built up in analysing the repayment capacity of clients makes them especially suitable for evaluating loan applications. On the other hand, the savings bank can complement the efforts by investing its mobilised deposits in microloans and offering its infrastructure and services to disburse the loan and collect loan repayments. In such an arrangement, cross selling opportunities are not so easy to achieve and require training of MFI staff about other products than loans that they are used to offer.

Another possibility is for the savings bank to specialise in wholesale lending to MFIs for onlending to their microborrowers. Savings banks could refinance well-functioning MFIs individually or indirectly through a second tier institution. In order to screen MFIs to identify potential partners, savings banks can increasingly rely on microfinance rating agencies. These agencies help to reduce information costs and set standards by which MFIs are easily comparable.

Public authorities and donors in particular can help to promote independent and reliable rating agencies for the microfinance industry. They can also be supportive of such initiatives by offering guarantee schemes to back these alliances.

7. CONCLUSION

The microfinance industry is at a very critical stage. Despite recent progress the needs remain immense with roughly only one-third of the potential market currently served. Donor and publicly subsidised funds have helped to launch many programmes but can no longer continue to drive the industry forward. There is an increased awareness that the microfinance industry should rely more on commercial funding sources to ensure expansion and this leads to the recognition that banking institutions are potential players in this industry.

Savings and socially committed retail banks have experience in dealing with disadvantaged groups of society and can find in microfinance a further opportunity to demonstrate that they are customer-driven institutions. In order to do so, savings banks should continue to introduce pro-low-income financial products and services (loan, insurance, remittance and payment facilities) to complement existing deposit services for these customers.

Offering microfinance services is potentially a good strategy for savings and retail banks that have management capacity and full board or management commitment to expand their services, which fulfil the institutional conditions needed for full banking services. Delivering microcredit services for instance can contribute to generating higher returns on their investments. It is indeed questionable whether some savings banks will remain profitable over the long-term without adjusting their current investment structure because it is somehow hard for them to strike the cost-income balance with such an over concentration of their investments in low-return public sector securities.

Most savings banks manage to create revenue from the provision of other services, including money transfer services and marketing insurance policies. They can be cost-effective solutions for securing and transferring funds from and for other microfinance institutions as well as offering payment facilities in areas where other banks do not reach. Evidence from case studies indicates that if well administered, the introduction of micro-credit programmes can provide reasonable income to savings banks thereby strengthening their financial viability. In the future, the relative capacity to generate non-investment income would for many savings banks be key to ensuring the financial viability.

Donor-backed initiatives can assist savings banks, which have decided to further downscale their operations. However, the focus should not be on granting subsidised credit lines as has been often the case for mainstream banks. Instead, in some cases appropriate guarantee schemes and subsidised technical assistance for capacity building and institutional development can be more instrumental in supporting this process. In order to be sustainable, every microfinance downscaling experience should aim at breaking-even after an experimental phase.

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9. ANNEXES: CASE STUDIES

1. Banco del Estado, Chile
2. Banco Caja Social, Colombia
3. National Bank for Development, Egypt
4. Cajas Municipales de Ahorro y Crédito, Peru
5. Postal Bank, Tanzania
6. Government Savings Bank, Thailand

9.1 Banco del Estado de Chile, Chile

9.1.1 General Information

Chile has 15.1 million inhabitants, most of whom (86%) live in urban areas. The country is spread over 756,626 km^2. Chile has undergone profound economic, social and political change over the past decade, marked by productivity gains, high output growth, and a stronger external position. Today, the country is classified as 'upper middle income country,' which is the highest income category for Latin America (OECD). In 2002, Chile had a GDP of US$66.4 billion and GDP per capita was US$4,414. Around twenty per cent of the population is living below the national poverty line (figures from 1998). According to the figures of the National Bank of Chile, the unemployment rate of September 2002 was 9.7%. Inflation has been in the single-digit range since 1994 and was 2.5% on average in 2002.

The SII (Servicio de Impuestos Internos de Chile) estimated that in 2000, the economy included more or less 530,000 micro enterprises and 94,000 small enterprises, representing 97% of the total number of companies. In addition, it estimated that another 400,000 informal microenterprises exist. Between 1994 and 2000, the number of small enterprises increased by 17%, and the number of microenterprises by 22%. Both sectors offer together around 70% of the jobs/employment at national level. It is estimated that around a quarter of the microenterprises in the country have access to financial services.

Chile's banking system was once relatively exclusive. Only the rich could access banking services; everyone else used department stores to access credit. But in the early 1990s, banks expanded quickly to accommodate new account holders and expand their offering of credit to the new burgeoning middle class and lower income category. Bancarisation rates are now relatively high compared to neighbouring countries some estimates point to as reaching 70%. The Chilean banking system is composed of 27 institutions from which 25 are private banks, of which 16 are foreign. There is 1 financial company and 1 government-owned bank, which is Banco Estado de Chile. There are 9 banks that offer credit to micro and small enterprises. Apart from the banks there are 81 savings and loans cooperatives. Figures from 31 December 2001 show that Banco del Estado de Chile represented 20% of all bank branches in the country and had 13% of the assets of the banking sector making it the third largest bank in this ranking. Banco del Estado de Chile captured 13% of all deposits at the same time. When looking at savings accounts alone, 77% of all deposits in savings accounts in the entire banking are with Banco del Estado de Chile.

9.1.2 Institutional aspects

Banco del Estado de Chile was created in 1953 following the merger of 4 public and mutual savings banks (Caja Nacional de Ahorros & Caja de Crédito Hipotecario & Caja de Crédito Agrario & Instituto de Crédito Industrial), with the two-fold objective: offer competitive banking and financial services that contribute to the national economic development (development objective); enhance access to financial and banking services for all Chileans (social objective). In harmony with its mission, it serves all layers of the Chilean population and in particular households, micro-enterprises, SMEs and public authorities.

The rates of return on assets and capital are generally below the average for the financial system because the bank charges lower commission, maintains smaller financial margins and has higher exploitation costs because of its branch network[21].

Although government owned, it operates as an independent financial entity. As any other Chilean bank, it is supervised by the Superintendencia de Bancos e Instituciones Financieras and contributes to the deposit guarantee scheme.

In 1996 Banco Estado de Chile created a separate subsidiary called 'Banestado Microempresas S.A' dedicated to the provision of credit services to micro entrepreneurs. The provision of these services required a separate entity in order to respond flexibly and dynamically to the needs of microenterprises with adapted technologies and systems, risk analysis methods, specially designed products, different models of client service and professional staff dedicated to working for this sector. Banestado Microempresas has 320 members of staff, including 141 commercial officers, each of whom manages around 450 clients.

These staff members are distributed over 92 specialised offices throughout the country. The distribution network of the Banco Estado de Chile comprises 307 subsidiaries throughout the country and 1,810 ATMs (of which 12 are mobile). There are also 34 Puntos de Atención de Cercania (PAC), which are offices opened for a day, or a couple of hours during the week by staff of the nearest branch in order to service their clients in the more remote areas. These PACs were introduced with the start of the microenterprise subsidiary in 1996. In 176 of the 342 'comunas' in the country that are mostly situated in (very) remote areas Banco Estado de Chile is the only bank offering formal financial services. The bank is present in 83% of the poorest 'comunas' of the country. The full banking system captures only 20% of its deposits outside metropolitan regions where 60% of the people live, whereas Banco del Estado captures almost half of its deposits in these regions.

21 El Sistema Bancario de Chile, Capitulo IV, Banco Central.

9.1.3 Operational aspects

'Banestado Microempresas SA' targets low-income entrepreneurs, both in urban and rural areas. At the end of 2003, the subsidiary had 96,000 clients and a US$300 million loan portfolio. In order to be eligible for a loan from Banestado Microempresas, clients need to be self-employed with a business of at least one year old, as well as have a good commercial history. Almost half of all clients have had their business for more than 5 years and nearly two thirds of the businesses are formal. 50% of the businesses have a turnover less than US$715 a month. Male clients make up 55% of total borrowers, most of whom are between 30 and 65 years old.

Since the start of the programme in 1996, 206,000 loans have been provided to the value of US$230 million at an average of US$1,100 per loan. Just over a third of these loans were for less than US$700. Most of them were microenterprise loans, which may (or may not) have been complemented by additional loans, each with different objectives. For instance the 'quick business credit' allows microentrepreneurs to take advantage of unforeseen business opportunities, like the opportunity to buy raw material at promotional prices, or to pay additional temporary employees for an exceptional business opportunity. Other credit products that have been developed are loans for the acquisition of a vehicle and loans for capacity building and technical assistance. Related to the latter, the bank also provides support to obtain a grant from the government for the reimbursement of costs for capacity building and technical assistance.

The bank offers individual loans and the lending methodology is based on an analysis of the client's activity, the credit need and reimbursement capacity. A loan can be obtained in 48 hours. Additional loans will be allocated only if the borrower has reimbursed the first loan correctly, within a period of at least 12 months. The bank makes use of a website and offers the possibility to apply for a loan on-line.

For savings products, clients of the microenterprise portfolio rely largely on Banco Estado de Chile. At the end of May 2003, more than two thirds of the clients of Banestado Microempresas had savings in the bank, with an average of US$350 per savings account. Together, their deposits amounted to US$13 million. In total Banco del Estado de Chile has 11.5 million savings accounts, holding US$2,650 billion worth of savings. On average this is US$230 per account compared to US$750 for the entire banking system). On top of that, 9 million or 78% of all accounts have a balance of below US$75. There is no minimum amount required to open a savings account.

In June 2003, a current account product was introduced for clients of Banestado Microempresas. Products that are lined up for launch include: credit cards and credit lines attached to electronic purse and to current accounts, as well as a health insurance and a life insurance specifically designed for microenterprise clients.

9.1.4 Financial sustainability

Interest rates charged by Banestado de Empresas are among the lowest in the financial system and range from 1.98 to 1.45% per annum depending on the type of enterprise (micro to medium) and number of financial products purchased by the client. According to the bank, this is possible because of the massification of the service, an advanced risk analysis technology, optimisation of processes, adequate cost control and low default rates. The portfolio at risk is around 1% and 60% of all clients pay their debts in advance.

Since its launch as a pilot programme in 1996, Banestado Microempresas was able to reach break-even in 1997 and started making profit in 1998. In 2002, the profit made was Pesos 14,5 m (equivalent to US$20,882).

9.2 Banco Caja Social, Colombia

9.2.1 General information[22]

Colombia has a population of 43.8 million people of whom 72% live in urban centres spread around the country. The entire territory of Colombia covers 1,142,000 km^2. In 2002, the country had a GDP of US$80.7bn, with US$1,842 per capita. A little less than half of the population, 20.2 million are considered economically active, although 16% of them are unemployed. The National Department of Statistics reckons that more than a third of the economically active population is working in the informal sector. In 2002, around half the population lived on a maximum of 3 minimum wages, or US$360 per month. The inflation rate at the end of 2002 was 7.0%, whereas for the five-year period 1998-2002 it was 10.5% on average.

22 Derived from *The Economist*, Country Briefing Colombia and data from DANE, DNP and other sources quoted by BCS in presentations.

According to a study undertaken in 2002[23] the rate of bancarisation in Colombia is, despite its urbanisation, still relatively low. Less than 37% of the population would receive financial services. This implies that a large potential remains for the development and extension of financial services in the country. In August 2003, Colombia's financial sector included 75 regulated financial intermediaries, which together had 3,600 offices around the country as well as 5,500 ATMs. Most banks have a nationwide coverage. According to sources of the 'Superintendencia Bancaria', deposits collected from the population amounted to US$21,938m of which US$7,710m were held in savings accounts. Around 12% of deposits are held in accounts with balances below US$2,000. Moreover, studies show that 4.86 million people, 80% of those that are 'bancarised,' generate 18% of all deposits.

In terms of assets, Banco Caja Social (BCS) takes 16th position in the Colombian financial system with a share of 2-2.5% of the market in loans and deposits. However, when considering the market for microcredit and consumer credit, BCS ranks third with a market share of 16% and 10% respectively. Compared with other commercial banks in the financial system, Banco Caja Social has a good rate of return. It figures at a second position when considering their return on assets (ROA), which is 2,65. Only Bogota bank, which has an ROA of 3.02, preceded BCS in the ranking. In terms of return on property, BCS ranks third with 21.1 after Megabanco and Bogota.

9.2.2 Institutional aspects

'Caja de Ahorros del Circulo de Obreros,' which preceded Banco Caja Social (BCS) was created by a Jesuit Priest in 1911. Today, Banco Caja Social is a 'sociedad anonima' in which the 'Fundación Social' holds the majority of the shares (79.77%). The Fundación social is a non-profit organisation that owns and coordinates various companies that operate mainly in the financial sector. The second largest investor is the International Finance Corporation of the World Bank group, which owns 9,51%[24]. BCS does not receive government or other subsidies.

23 Estudio Sindicado TGI 2002. More recent studies that exclude the younger generation, less than 18 years, and the poorest indicate that bancarisation is higher, at around 60%.

24 BCS' other investors comprise: Compañia inversora commnea (4.52%), Fundación projuventud (3.82%), ARP Colmena (1.93%), Colmena Capitalizadora (1.44%) and Fundación Colmena (0.01%).

The mission of BCS is to administer in an optimal way the relation with its target clients: low to middle income individuals and microenterprises and SMEs, with the objective to establish long-term relations of mutual benefit. Banco Caja Social mobilises resources by collecting savings from the public, who in turn, are the recipients of loans and other microfinance services. It targets those who are traditionally not served by the formal financial system with the aim of augmenting the degree of 'bancarisation.'

Profit earned is reinvested in the bank and distributed in dividends as decided by the owners. The majority shareholder, Fundación Social, takes into account both the banks' expansion requirements and technical infrastructure needs as well as the needs of the community development, human rights and other programmes it runs. In 2002 for instance, Banco Caja Social generated a profit of US$11,8 million of which US$262,850 was reinvested in the bank and US$11,5 million were paid out in dividends of which almost US$10 million corresponded to the Fundación Social that invested the entire amount in supporting and developing its activities, including community development projects that are directly targeted to assist the poorest.

Following an important reform of the Colombian financial sector, Banco Caja Social was transformed into a commercial bank in 1991. As a consequence BCS is supervised and regulated by the 'Superintendencia Bancaria' and complies with regulations set by this body including international standards for capital adequacy (Basel) and Generally Accepted Accounting Principles (GAAP). BCS contributes to the 'Fondo de Garantias de Instituciones Financieras' (FOGAFIN) like all other regulated financial institutions in the country. This fund operates a deposit insurance scheme that protects savings up to US$10,000. Since their conversion into a commercial bank, Banco Caja Social also pays corporate taxes (37.5%) over the profits it generates.

The proximity to the client is a key advantage of BCS, which has 122 offices in more than 40 cities spread around Colombia. In addition to that they operate 133 ATMs. In total more than 2,500 people are employed at the Bank to serve around one million clients.

9.2.3 Operational aspects

In its early days, BCS operated rather like a traditional savings banks, focussing on the mobilisation of savings, but later on the lending business was introduced. When BCS transformed itself into a commercial bank, it further broadened the variety of products and services offered.

Since its target group in general is the lower income segment of the population, all services are designed to meet the needs of this market, where microfinance of course, plays an important role. Some specific services, such as a special current account and credits offered with IFI support[25] being are more specifically targeted.

At the end of September 2003, the Bank had 1,173,260 clients of whom around 155,000 received a loan. More than forty percent of those clients had an income of less than US$211 per month and another 39% earned between US$211 and US$422 per month, which is less than 4 times the minimum wage. Practically all clients receiving loans of BCS earn less than US$1,268 per month[26]. Forty three percent of all clients are women and two thirds does not have a university degree.

Considering the bank's own estimates, taking into account credits provided to self-employed people with low income (below US$345/month), the microcredit portfolio of BCS is US$68.5 million and represents 21% of the total loan portfolio. A new law in Colombia defines microcredit more restrictively as credit provided to microenterprises counting less than 10 workers with assets up to 501 minimal monthly salaries (around US$60,000) and an outstanding loan balance with the respective financial institution of less than 25 minimum salaries[27]. According to these standards, BCS had at the end of 2002, a microcredit portfolio of US$18 million, which represents 5% of BCS's total credit portfolio. It also represents 16% of all microcredit provided by the formal financial institutions in Colombia.

Segmentation and innovation are strategic pillars on which BCS manages the expansion of its services. Currently, all financial services and products offered by BCS are divided in 3 main areas following a segmentation of BCS's market: 'Banca Personal', 'Banca Microempresarial' and 'Banca PYME'[28]. In September 2003, Banca Personal had nearly 1 million clients representing 81% of all savings captured by BCS. There are 172,800 microenterprise clients and 600 SMEs.

25 BCS has access to special credit lines for development purpose, such as the IFI which targets new private enterprises as well as microenterprises and SMEs.

26 Vicepresidencia de Riesgos de BCS, figures correspond to credits outstanding at 31.12.2002

27 Superbancaria. Circular Externa 011. 05.03.02

28 'Banca Personal': the main clients are salaried people, pensioners, students, house mothers, professionals and independent workers with a maximum of 2 employees including the owner; 'Banca Microempresarial' include all enterprises that have up to 10 workers and assets below US$58,600 and 'Banca PYME' includes small and medium sized enterprises with between 11 and 200 employees with assets of up to US$1,760,000.

Credit products are offered for all three categories and can be related to a specific investment (a house, car, education etc.) or free to the borrower to invest. For microenterprise clients in particular, BCS offers credits for working capital, overdrafts and banking guarantees as well as loans for acquiring equipment, cars or real estate. The credit methodology used for providing microcredits is based on cash flow analysis supported by visits and personal attention rather than based on collateral. All microcredit loans are provided to individuals, no group based lending is done. An analysis of the credit portfolio at the end of 2002 showed that 20% of the outstanding loans were between US$422 and 1,268. Only 9% received more than US$8,459.

Banco Caja Social has a strong reputation in mobilising savings of the poor. Nearly 30% of BCS's deposits are held in accounts up to US$2,115 in which the financial system as a whole keeps only 12% of the deposits collected. Three quarters of all clients had between US$0 and 80 in their savings account in June 2002.

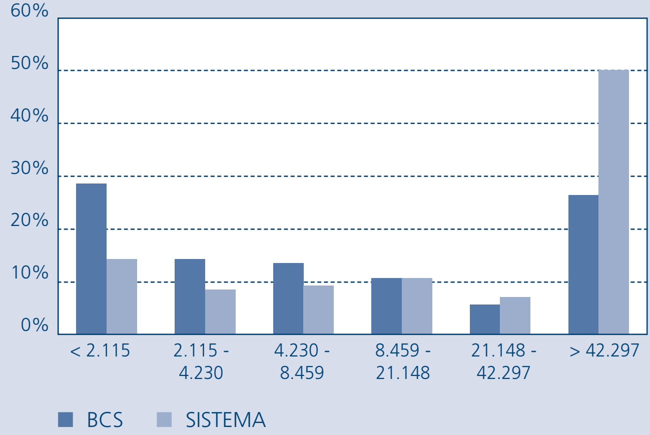
Savings products vary in terms and remuneration offering different combinations to meet different clients' needs as well as flexibility in withdrawals for certain products. For the traditional savings account, the minimum requirement to open a savings accounts is relatively low compared to other banks. In order to open a savings account, a minimum deposit of COP 75,000 (US$25) is required in the ordinary savings account, well below the average requirement of the banking system at large. Also the cost for maintaining such an account is relatively small COP 4,750 (US$1.7), and is charged monthly due to a debit card issued to the account holder, to support transactions in other channels such as ATM's. In order to attract savers, BCS also provides other incentives, such as lotteries.

The success of mobilising savings is partly thanks to the design and development of appropriate products. These include products with self-explanatory and memorable names, easy access and constant advice. For instance, there is a savings account called 'cuenta de ahorros progrese' which has a didactic element orienting people to save in a progressive manner. The minimum amount to open such an account is around US$50 after which you can save in parts of around US$15 at a time. The savings account offers preferential access to loans of up to 3 times the balance of deposit when held for at least 6 months and when a balance of around US$140 has been reached in the account.

So far, 7% of the 60,000 clients have received a loan. Another example is the 'Ahorro programado alcance su casa,' which assists clients in saving for buying a house and at the same time complies with requirements the government poses for its social housing finance programme.

Growth in savings has been positive and increased up to the middle of 2002. Since then, BCS lost a part of its market share due to a crisis in the internal debt market, which encouraged people to transfer money from fiduciaries to the banks of the same financial group. On average, BCS saw a growth of 19.6% in savings compared to 21.1% for the whole financial sector in 2002.

Savings mobilised, ranges US$



Source: BCS, based on figures of 'Superbancaria,' 31.03.2002

In addition to microcredit and savings, Banco Caja Social also offers payment and insurance services. As regards insurance, a life insurance policy covering the homes to insure individuals against patrimonial and personal risks is provided by Liberty Seguros. For payments, clients can count on BCS for their debit card and automatic transfers. In 2001, 72,539 payment transactions were registered. The bank also operates a telephone banking service however this is not for transactions, only for consulting information. In recent years, BCS has added services such as credit card facilities and operations to facilitate remittance transfers, in particular from Spain.

Emigrants living in Spain can make use of the Spanish savings banks network to send money home while BCS ensures its distribution to family member clients of the bank. For BCS, this is another way to attract clients and make them loyal to the bank as well as to contribute to the bancarisation of people who would otherwise not make use of the banking system.

9.2.4 Financial sustainability

Interest rates charged by BCS for their loans are close to the maximum fixed by the state, as administrative costs for the microcredits and low average consumer credits are high. In 2002 this rate was 29% per annum compared with an inflation rate of 7% registered for the same year. With this rate, BCS is no exception in the banking sector in Colombia.

In April 2003, BCS's default rate was below the average for the entire financial system. The portfolio at risk was 6.3% compared to 12% for the average.

9.3 National Bank for Development, Egypt

9.3.1 General information

Egypt is a lower middle-income country according to international standards. By 2001, the country has over 65.2 million inhabitants for about US$98.5 billion in GDP and US$1,530 in per capita GDP. Egypt is considered as an emerging economy with a well-diversified financial industry. About 100 banks operate in Egypt with nearly 2,400 branches nationwide. The banking sector includes 63 commercial banks and many non-bank financial institutions. However, the 'big four' public sector commercial banks account for roughly 57% of banking assets, 59 percent of all loans and 70% of deposits[29].

About 23% of the population is considered as poor by any standard and another quarter lives on the edge of poverty. There is an unbalanced distribution of poverty in Egypt, 42% of the poor live in urban areas whereas, 58% live in rural areas. The economy includes approximately 2 million microenterprises. Although microfinance is far more active in Egypt than in other countries in the region, estimates indicate that no more than 5% of the demand is being met. Entrepreneurial people tend to rely on self-financing or costly informal financing for their operations.

29 The 'big four' are: National Bank of Egypt, Banque Misr, Banque du Caire and Banque of Alexandria.

Although four banks have recently established microentreprise lending credit programmes, commercial banks in Egypt as in many developing economies have traditionally shied away from microfinance. Non Governmental Organisations (NGOs) are predominant in the Egyptian microfinance industry with government and donor-subsidised credit lines being their main source of funding. However, the National Bank for Development (NBD) has successfully introduced and managed a micro-credit programme for over sixteen years. An investigation from the United Nations Development Programme (UNDP) carried out in collaboration with the World Bank found that the NBD experience was a model for best practice techniques in microfinance for the entire Middle East.

9.3.2 Institutional aspects

NBD was incorporated in 1980 as a joint stock company with a capital of US$15 million. NBD's authorised capital has since been raised to the equivalent of US$111,1 million and the paid up capital stood at US$53,7 million. NBD's total assets were estimated at US$1.56 billion in 2001 while its net profit reached US$13,9 million in the same period showing an increase of 6% on pervious years. NBD is regulated under the Provisions of the Bank Act. The bank has a mixed and fragmented capital structure with about 20,000 shareholders, including individuals, companies and other organisations. NBD's investment policy aims to finance development projects with a private sector-led approach in the different sectors of the economy.

NBD's microcredit programme started with the recognition of the vital role played by microenterprises in the Egyptian economy and that the major constraint for these activities was both the access to reliable sources of funds and the unwillingness of the classic banking system to recognise this sector. The bank aims at increasing small enterprises' access to credit services thereby supporting job creation and alleviating poverty in the country.

NBD launched this programme in collaboration with the USAID, the Ford Foundation, UNICEF and CIDA. The bank established an SME division and started to operate the programme through 4 branches, extended in 1993 to 13 branches. At inception, USAID agreed to incur administrative costs and operating expenses under this programme and disbursed a revolving fund of US$11 million, but once it broke even, NBD financed this programme with its own resources[30].

30 R. Dhumale, A. Sapcanin and W. Tucker '*Commercial Banking and Microfinance in Egypt: National Bank for Development*', case study, UNDP, 1999, p. 26.

The bank does not receive any incentive from the government for its social function, but hopes that in the long run, these small borrowers will become clients under conventional banking conditions.

9.3.3 Operational aspects/outreach

The target groups for NBD's microcredit programme are small-businesses and self-employed people. Following the programme guidelines, loans are not provided to start-up new businesses. However, NBD has extended its program to informal groups and enterprises who have no previous experience with the conventional banking system. In fact, most of the borrowers operate in the informal sector and their business is usually carried out from their home. The number of employees in small businesses financed through this programme ranges between 2-12. Typically, they include extended or close family members and a few outside workers. Clients come from various sectors of activity (craftsmen, small-traders, etc.)

Over the past years, the NBD's microcredit experience went through a steady growth process. By June 1998, 188,000 microloans had been extended for an accumulated disbursed amount estimated at US$133.0 million. Loan terms are for up to 10 months. By mid 2003, the bank had disbursed a total amount of US$144 million for almost 337,000 microloans. During the same period, the bank was dealing with 18,577 active borrowers for an outstanding balance of US$4.4 million. The programme is designed and administered to benefit those on low incomes. These microloans used to range between US$50 to 2000 (LE 250 to 10,000) for an average loan size of about US$400-600 (LE 2,000 to 3,000). In 2000, the management of NBD decided to reach even poorer clients by lowering the maximum loan size to around US$500 (LE 3000). Since then, the average loan size has decreased to US$480 far below the average level of expenditure for a typical poor household in Egypt, which is estimated at US$1358 (mid-2003).

Although emphasis is not provided as to gender balance, NBD is running a few women-oriented initiatives, which are gaining significance. By April 2003, women had received 69,581 loans representing almost 21,34% of all loan applications financed under this program. The value of women disbursed loans were worth US$21 million and represented 15.2% of the total value of disbursed microcredit under this program. The outstanding number of active loans to women amounts to 4,582 loans and was worth US$1.16 million (December 2002). Late repayments and overdue loans have been however significant reaching nearly 19.5% of the entire loan portfolio.

Table: Basic data on NBD microcredit program

	1998	Dec 2001	Dec 2002
Total value of disbursed microcredits (US$ million)	131.0	176.1	144
Number of disbursed microcredits	188,000	282,859	321,496
Number of disbursed microcredits to women	13,522	58,717	69,581
Women loans			
Value (US$ million)	-	25.7	21.56
% of disbursed value of microcredits	-	-	15.0
% of disbursed number of microcredits	13.5	14.58	21.6

Source: UNDP (1999), www.nbdegypt.com/microfinance.htm, NBD 2002

NBD has adopted an individual lending approach applied to conventional banking operations. Loans are un-collateralised and repayment schedules adapted to borrower conditions. However, recipients are requested to sign a promissory note for a timely repayment of their loan before the final disbursement occurs. Nevertheless, loan officers scrutinize client's credit needs, type of activity, income cycle, cash flow, etc. and enforce close monitoring principles in order to minimize delinquency rates.

Besides microcredit services, NBD has also introduced savings schemes. Savings are compulsory because NBD would like to enhance savings awareness among its microcredit clients. The aim is to encourage its borrowers to better manage their financial resources. A precondition to loan approval is for the applicant to deposit an equivalent of 10% of the requested loan in an interest-bearing savings account with the NBD.

This amount is often added to the amount loaned to the borrower. It is a symbolic act, which shows however that the borrower commits to the goals of the programme. The reward on this savings account is fixed at 8% per year and the borrower is free to retrieve his money after having paid back the loan. However, given that most clients depend on the programme for initial and continued access to finance, they often accumulate their savings. In fact, borrowers renew their loans to run their business and even apply for larger loans. The compulsory savings balance under this programme stood at US$667,000 at December 2002.

NBD has 66 branches of which 44 have implemented this programme, the objective being to operate this programme through the whole network. Remarkable for NBD is the introduction of mobile banking services points that achieve geographical proximity. Cars with a driver, a teller and a loan officer visit areas of Cairo where the bank does not have locations. These mobile branches carry out routine operations normally available in regular branches. Currently, NBD's microcredit programmes employ 367 permanent staff out of a total of 2707 employees. However, due to financial constraints, the bank did not find it feasible to set up separate credit windows, but instead offers these services as one product among many handled by regular staff.

9.3.4 Financial sustainability

Revenues from NBD's microcredit programme are derived from direct and indirect sources. The bank allows weekly repayments of interest and monthly repayments of capital (depending on the nature of the activity). Overall, NBD charges a 29.7% yearly effective interest rate. Direct revenues are mainly provided by interest income on lending operations, which include a flat annual interest rate of 16%, plus an additional 4.7% for transportation costs (representing the cost of mobilising loan officers). Indirect incomes are derived from the mandatory life insurance fees of 2.7% and a 6% penalty fee paid in advance for delinquency. After the final payment of the loan, the borrower is refunded this penalty fee as well as the overpaid interest from advance reimbursement.

The costs incurred by NBD for its microcredit programme are mainly related to staff remuneration. This is indeed a labour intensive activity as 13,5% of banks' staff are in some extent involved in microcredit operations, which however represent less than 1% of the total outstanding loan portfolio. NBD has managed to maintain staff remuneration at a reasonable level (salaries vary between US$88 to 150) and loan officers are paid on a performance-based reward system. Although, profit maximisation is not the prime focus, NBD has professional operations and works according to cost-recovering principles. Among the factors that have led to success of the NBD's microfinance programme are commitment, vision and the drive of its senior management.

9.4 Cajas Municipales de Ahorro y Crédito (CMACs), Peru

9.4.1 General Information

Peru has a population of 26.7 million people of which around 73% live in urban areas. A large concentration of are located in Lima and its surrounding area. The country measures 1,285,000 km^2 and is divided into 24 departments.

Almost half of the population is considered as economically active, but unemployment is high (over 40% of the economically active population). In 2002, Peru's GDP was US$56.9bn and US$2,127 per capita. According to World Development Indicators, almost half of the population (49% in 1997) - of which the majority are indigenous people - live below the national poverty line. The country is rich in natural resources (copper, silver, lead, zinc, oil and gold) but due to political instability the economy and infrastructure have been neglected. Inflation was only 0.2% in 2002 and the five-year average between 1998 and 2002 ranged at 3.3%.

In Peru there are more than 3 million microenterprises[31], which offer jobs to more than 6 million people, or 75% of the active population. Three quarter of all enterprises in Peru are micro or small enterprises and they are estimated to account for 42% of total GDP[32]. Half of these enterprises are located in urban areas, the other half in rural areas. Of the urban micro- and small enterprises, 40% are in Lima.

According to a recent study of the central bank, the bancarisation in Peru is insufficient considering credit only amounted to 28% of GDP in 2001. In addition, the demand and offer of this credit is very concentrated: 68% of all credit goes to 3,000 medium sized enterprises and 200 large corporations (which alone already make up 42%) whereas 245,100 small producers and microenterprises receive only 5% of all credit[33]. Compared with the estimated number of microenterprises it means that less than 10% of them receive credit from a regulated financial institution.

31 Defined officially in Peru as enterprises that have less than 10 workers, annual sales below US$50,000 and fixed assets of US$200,000 or less. This definition applies both to agricultural as to non-agricultural enterprises.

32 Figures of 1999.

33 Banco central de Reserva, El Costo del Crédito en Perú, November 2002.

Peru's banking system is composed of 15 banking institutions and several non-banking financial institutions of which 14 are municipal savings banks (Cajas Municipales de Ahorro y Crédito – CMACs, including Caja Municipal de Crédito Popular de Lima) and 12 rural savings banks (Cajas Rurales de Ahorro y Crédito – CRACs), 5 'Financieras' and 13 'EDPYMEs' (Entities for the Development of SMEs). There are also three government-owned entities: the central bank (Banco Central de Reserva del Peru), a deposit-taking institution (Banco de la Nación), and a development bank (COFIDE). The banking system is very concentrated. The banks operating in the country were good for almost 95% of the credits and 97% of deposits of the formal financial system at the end of 2001. On top of that, as a result of mergers and restructuring, the number of banks is decreasing and a high concentration of the market share currently rests in just 4 entities.

Looking at financial services provided to microenterprises in particular, in June 2002 around 42 financial institutions specialised in providing credit to microenterprises[34] of which 2 were banks, 1 'Financiera' and all the EDPYMEs and savings banks. In the middle of last year, the credit portfolio of the sum of these institutions amounted to US$546 million of which the CMACs represent almost 50%. In addition, 170 savings and loan cooperatives actively managed a portfolio of US$101 million.

9.4.2 Institutional Information

The Cajas Municipales de Ahorro y Credito (CMACs) were created under the decree-law 23039 of May 1980 that aimed to decentralise economic development. The objective of the the CMACs was to increase local savings to support productive activities in the provinces, i.e. micro- and small enterprises and creation of jobs in this sector. The law therefore foresaw the creation of CMACs in the departments outside of the capital, where a savings bank already existed. The first municipal savings bank was created in 1982 in Piura. Today there are 13 savings banks in the provinces, which operate through 130 offices. In June 2002 the CMACs had 1845 members of staff.

34 Apoyo de COFIDE a las Microfinanzas en Peru, Marco Castillo Torres, V Foro Interamericano de la Microempresa.

The CMACs are financial intermediaries owned by the local authorities of the cities where they operate. They have a separate legal entity, with economic, financial and administrative autonomy. The Board of Administration of the CMACs is composed of representatives of different economic actors, including the private sector and the church. The members of the board are nominated by the respective municipality and also include some direct representatives of the municipal council.

The capital structure of the whole CMAC system in Peru, including the 13 savings banks, reached US$50 million at the end of 2001. Following a change in the law CMACs became joint stock corporations (sociedades anonimas) in 2001. This allows them to attract new capital from external investors. The CMACs largely mobilise their own resources in the regions where they operate. In addition they manage credit lines provided by the development bank of the government (COFIDE) and other specialised government agencies for onlending to microenterprises and households. Some CMACs, such as CMAC Arequipa, have received loans and subsidies from donor agencies or investment funds.

The ownership of the CMACs guarantees in a way that the banks' activities benefit the local economy, but also by statute, the CMACs are obliged to invest in socio-economic development by financing projects in the region. Up to 50% of the profit generated by the bank can be invested in these kinds of projects through the municipalities that own the savings banks. In 2001, US$13.5 million net profit was generated, of which 90% was reinvested in the CMACs as capitalisation and the rest given to the municipalities for investment in the community. Decisions about the distribution of profit are taken annually by the General Assembly of each savings bank. Like the banks, the CMACs pay taxes on their profit and contribute to the deposit insurance fund that protects deposits up to US$5,000.

In line with legislation and special laws, the CMACs are regulated by the Banking and Insurance Superintendence (Superintendencia de Banca y Seguros) and subject to the norms and regulations of the Central Reserve Bank. Additionally as they were created and are owned by the Municipalities, they are supervised by the General Comptroller of the Republic. The federation of the CMACs, FEPCMAC, which was created in 1987 has an external auditing role. FEPCMAC provides advisory services, capacity building, control, and represents the CMACs.

9.4.3 Operational aspects

The creation of the CMACs was undertaken with the specific objective to have decentralised financial institutions oriented towards those segments of the population who lack access to the formal financial system. In June 2002 all CMACs together had 402,288 clients. All CMACs are situated in the provinces but most clients are situated in urban areas (only one fifth of the clients operate in rural areas). Forty five per cent are women. Around half of the microenterprise clients of CMACs have an income level below the per capita GDP and a quarter earn less than US$1000 a year. In the microenterprise and SME client base, CMACs attend mainly enterprises active in commerce (54%) and to a lesser extent services (26%). Only 11% of the clients are active in agriculture and 9% in other productive activities[35].

Financial services offered by the CMACs are basic. All started off by providing pledge credit with gold or silver jewels as guarantees. Then, consumer credits and microenterprise credits were introduced. Since 1999 the CMACs have also provided agricultural credit. Housing finance was only introduced in 2002. At the end of June 2002, the credit portfolio of CMACs was US$267,3 million, distributed over 410,904 loans. The average amount of credit was US$650 at that time. Most loans are provided for more than 6 months and around 2 thirds of all loans are invested by clients in working capital. Just over half of the loans are to clients categorised as micro or small entrepreneurs, another 16% are to medium sized enterprises and almost one third are consumer loans.

On the liabilities side, the CMACs mainly offer ordinary savings accounts and fixed deposits (two thirds of the deposits). In 5 years time the level of deposits has quadrupled. At the end of August 2003 the CMACs held US$359.9 million in deposits. They were spread over 407,354 accounts with an average of US$883 held per account. However, 93% of all clients hold only 21% of all deposits in value terms and 65% of all accounts have a balance less than US$100.

Deposits are still growing, although not as fast as the demand for credit. Entry barriers for deposit accounts are kept low to attract the lowest income savers. The minimum amount to open an account varies at around US$10 depending on the CMAC. The CMACs do not charge a commission on savings accounts and interest rates paid on savings result in positive rates in real terms.

35 Figures at 30.06.2002, Report of the Federación Peruana de Cajas Municicpales de Ahorro y Crédito.

Other initiatives that are taken to attract savers are more promotional. For instance, there are lotteries organised for which clients can obtain tickets having saved a certain amount in a brief period or reached a certain balance.

The CMAC provides basic payment services in their offices where clients can pay their bills and make transfers to other CMACs around the country. Outside the normal opening hours of the CMACs, several of them provide access to their services through 'CajaMatico', which is a small counter with one bank employee for basic services. Some CMACs offer electronic bank cards, but they are only to consult balances, not for payment or other transactions.

9.4.4 Financial sustainability

The average nominal interest rates that CMACs charge for their loans are relatively high compared to the banking sector as a whole and considering low inflation rates, but similar to banking rates when compared in their particular segments. In July 2002 banks charged on average 24.4% for loans in local currency whereas CMACs rates were 55.6% on average. However, when looking at the microfinance services offered in Peru, CMACs interest rates are, at 48%, below the average which is 58.6%[36], more that half of which the central bank in Peru estimates is for operational costs. Between 1999 and 2001 the interest rate has been continuously reduced.

The default rate on loans is fairly low with a portfolio at risk of 4.79% in March 2003[37]. When compared at the end of 2001 with other non-bank financial service providers, CMACs appeared to have the best credit portfolio quality with 5.28% compared to 7% on average. In general CMACs have had default rates below the banking sector.

Compared to the banks, CMACs have higher ratios of operational costs over assets, but they have been reducing this ratio in 13 to 9% between 1998 and 2001. Compared to the banking system the return on patrimony of CMACs is considerably higher: 27% in December 2001 compared to 4% for the banks.

36 Banco central de Reserva, El Costo del Crédito en Perú, November 2002.
37 Credit portfolio with arrears over the entire credit portfolio in March 2003.

9.5 Tanzania Postal Bank, Tanzania

9.5.1 General information

Tanzania is among the poorest nations in the world. By 2001, the country has an estimated gross domestic product of US$9.3 billion for approximately 34,5 million people, giving a per capita income of about US$270. According to reliable estimates, between 15 and 18 million of Tanzanians – over half the total population – live below the poverty line, i.e. less than US$1 per day. It is also estimated that 80% of country's poor live in rural areas.

The development of the rural sector is therefore crucial in any strategy aiming at invigorating output growth, promoting employment and alleviating poverty in Tanzania. Financial sector reforms launched by the Government in the early nineties resulted in the closure of many rural bank branches and the interruption of many rural credit schemes. Currently, the challenge remains to enable the main sectors of the rural economy, agriculture and microenterprises, to achieve sustainable growth.

The country's banking system includes 21 licensed commercial banks, 9 non-bank financial institutions and many exchange bureaus. To that you can add approximately 650 savings and credit cooperatives (SACCOs) and several hundred microfinance institutions (MFIs) structured foremost as non-governmental organisations (NGOs). The central bank is the regulator and supervisor of banking operations in the country.

The banking system has an over concentration of commercial banks, which controlled 94% of the system's assets at December 2002. The three large domestic banks account for 49% of the system's assets while four subsidiaries of major foreign banks account for a further 41%. The Tanzania Postal Bank is very small compared to these major players with a market share of approx 2.5%. However according to the Household Budget Survey 2000-01, in 6.4% of all households (or about 450,000 people) there was a member with an account in a commercial bank highlighting the importance of the Tanzania Postal Bank (TPB) and the SACCOs as depository institutions. Nationwide, TPB manages over 1 million savings accounts.

Together, commercial banks in Tanzania operate only 180 branches (95 branches are controlled by the National Microfinance Bank and the three largest domestic banks represent 85% of the whole branch network). TPB's services are available through 133 outlets. This covers 4 own branches, 15 regional offices, 1 district office and the wide network of Tanzania Post Corporation (TPC) in 113 locations on agency agreement.

9.5.2 Institutional aspects

TPB was established by the Parliament Act No. 11 of 1991 and amended by Act No. 12 of 1992 as the successor of Tanganyika Post Office Savings Bank. The establishing act changed the status of the bank into a legal entity with its own capital, Board of Directors and Management. Furthermore, the TPB Act stipulated that, the bank shall operate through the network of Tanzania Post Corporation on an agency agreement. This arrangement is the key to the bank's accessibility to rural population.

The objectives and functions as stipulated in the TPB Act are:

- To mobilise local savings and to promote savings habits of the population;
- To provide in accordance with the provisions of the Banking and Financial Institutions (BFI) Act of 1991, adequate and proper banking services and facilities throughout the United Republic;
- To mobilise resources by accepting deposits, floating bonds, debenture and other monetary instruments;
- Subject to the Act, to administer such funds as may be placed at the disposal of the bank from time to time;
- To undertake any other function as performed by commercial banks.

TPB was established with an authorised share capital of US$1 million. In 1993, it secured a non-bank financial institution license from the central bank allowing TPB to undertake any banking business except the provision of check accounts. In 1994, the authorised share capital was raised upwards to US$2 million to enable the bank to finance its expansion programme. The current paid-up capital position stands at US$1.040 million with share holding distributed as shown below:

The Government of the United Republic of Tanzania	45.3%
The Revolutionary Government of Zanzibar	11.0%
Tanzania Post Corporation	33.2%
TP & TC SACCOS	10.5%

The primary mission of Tanzania Postal Bank is "*Total quality commercial banking to meet and exceed the expectations of the existing customers and to acquire new ones while ensuring continuous growth and profitability.*"

The idea to introduce a microcredit scheme came as a support to the government policy towards poverty reduction. Microcredit has important social and economic implications in terms of employment creation and poverty alleviation. Microcredit has also been used as a means to widen the bank's investment avenues and to increase its income. Small loans help the poor or low-income persons to improve their livelihoods, reduce vulnerability and foster social as well as economic empowerment through self-employment projects that generate income.

9.5.3 Operational aspects

Broadly speaking, TPB microfinance activities encompass three aspects: savings mobilisation, microcredit and money transfer services under an agency arrangement with Western Union. TPB started as a deposit taking institution, mobilising savings and investing in profitable ventures. Deposits are mobilised through the extensive outreach in both rural and urban areas. Cumulative customer deposits increased six-fold over the ten years reaching US$49.6 million at the end of 2002 as compared to US$8.1 million in 1992. TPB has maintained a low and affordable minimum balance and minimum account opening requirement, which currently stands at US$5.

The microcredit scheme for micro-entrepreneurs and low-income households both in rural and urban areas started in 2001 on a pilot basis in one district. A successful operation in the pilot location has enabled TPB to roll out the scheme to other locations. TPB microcredit policy allows both individual and group-based lending methodology. However, only group-based microcredits have been extended. This was done in the initial period of the programme with the purpose to deal with the problem of asymmetric information and lack of quality collateral. The group-based lending has the following features and mechanisms:

- Individuals take the first step in the microcredit process by organising themselves into groups of five known as G 5. Men and women form preferably separate groups.
- Members in a particular group are strictly limited to people who enjoy mutual trust and confidence, and live in the same area. Spatial and social cohesiveness developed among the individuals of the same gender, residing in the same area, has proved to be important in smooth functioning of these groups.
- The group members of five people elect group leaders (chairperson, secretary and a treasury). Four groups of five people form one larger solidarity group of a maximum of twenty people called a Microcredit Members Centre (MMC). This composition has greatly eased administration and enhanced the group guarantee mechanism.

- After the formation of groups and training of group members by TPB officers, credit is issued to individual groups. But this is done only if all of the group members have deposited their guarantee savings (forced savings) and have conformed to the conditions of the loans.
- No tangible collateral is required to secure microloans under group methodology. The groups' self-selection, guarantee, forced savings, monitoring and peer pressure reduce problems or moral hazard and allow substitution of joint liability for individual collateral.
- The group-based methodology has enabled the program to circumvent potential adverse selection problems in the informal and imperfect world, where information is costly to collect. Through the group's self-selection, members of the same community have generally proved to have excellent knowledge about who is reliable and who is not.

People are very careful about who they admit into their group, given the threat of losing their own access to credit or having their savings (group guarantee funds) confiscated. Microcredit customers are mobilised through a series of information meetings organised in villages and urban centres. After the constitution of the groups, the interested group members would together approach the respective loan officer to apply for their loan facility. After providing more details about the terms and conditions of the programme, the loan officer will then visit the businesses of all group members. Then, he will send the application with his remarks to regional office for decising making. In average it takes a total of ten days to study a new application and to disburse the money. However, it may only take an average of 5 days to complete the study and disburse the money for a repeat loan application. Under this scheme, microloan principal amounts are offered from US$50-600. The repayment period for all the schemes ranges between 6 to12 months. Repayment is made in equal installments over a period of six months to one year as may deem suitable.

TPB also operates an agricultural input supply revolving fund scheme where eligibility requires the clients to be engaged in agricultural production activities[38].

38 TPB has also introduced a scheme for the employed known as Consumer Credit. In practice, TPB enters into an agreement with the employer to deduct the repayment from the salary of the employee at the end of each month. The scheme also requires no traditional collateral. By the end of 2002, the bank had distributed a total amount of US€2 million under this scheme.

The purpose of the scheme is to enhance working capital and purchase of light raw materials/inputs and meet other expenses associated with agricultural production. The scheme requires no tangible security for loans below US$2,000, however for loans above this amount, the bank requires a traditional/non traditional collateral in addition to the Seed Growers Association (SGA). SGA is a small self-selected group of three (3) people who will guarantee each other.

By 31 December 2002, the total value of disbursed microloans stood at US$1.9 million extended to 676 groups. These groups have a total of 4,235 clients out of whom 80% are female. 41 groups have fully liquidated their first round loans. The total income earned stood at US$197,100. Also relevant is the compulsory saving aspect of the scheme, which has enabled the mobilisation of US$96,500.

As unsecured loans, the central bank requires caution that a microcredit portfolio should neither exceed 25% of the bank's core capital nor 100% of the entire bank's credit portfolio. In addition, as a standing regulation from the central bank, all microloans that remain outstanding for a period of above ninety (90) days after the expiry date shall be classified as loss.

9.5.4 Financial sustainability

To meet the high administrative and transaction costs of microcredit operations, the bank charges interest and commission. During the pilot phase, the interest rate was 2.5% per month. Other charges for borrowing under this scheme are the loan application fee of US$1, the loan processing fee of US$5 and a charge of 1% on the approved amount as a monitoring fee.

The bank offers incentives to good borrowers in terms of interest expenses. For group lending, the group that makes repayment on their due dates, receives a rebate of 5% of the interest after loan liquidation. If repayment is made before loan expiry date, the borrower receives a refund of 25% on interest owing. The schemes provide for full repayment of a loan as a condition to access another credit facility. If one member of the group defaults, other members of the group will not be able to borrow and will therefore put pressure on him/her to pay. TPB's microcredit schemes have a default rate of 1.5%. The bank is now rolling out the programme in other regions in Tanzania.

9.6 The Government Savings Bank of Thailand, Thailand

9.6.1 General Information[39]

The Thai economy is recovering from the Asian financial crisis and therefore remains fragile. Exports are the main driver of growth and private investment has shown signs of improvement in selected export oriented industries. The Bank of Thailand has maintained an accommodative monetary policy and opted for low interest rates. The inflationary impact of oil price increases is likely to be neutralised by increases in productivity, low industrial capacity utilisation, and wage increases which remain modest given the still relatively high unemployment rate. The inflation rate reached an average of 4.2% between 1996 and 2000.

The social impact of the Asian financial crisis is still being felt. A large share of the Thai population is clustered around the official poverty line. Poverty is concentrated among certain population groups. Households headed by farmers, the elderly (aged 70 and over) and people with less than primary schooling are particularly vulnerable. Children under the age of 17 years, accounting for 38% of the total poor, are at a much greater risk of poverty than adults. To this purpose, the Royal Thai Government has issued the Ninth National Economic and Social Development Plan for 2002 to 2006. The Plan specifies the goal of reducing poverty rates from 14.5% in 2000 to less than 12% of the population by 2006.

As regards the composition of the financial sector, commercial banks have traditionally dominated the Thai financial system. There are about thirty commercial banks in Thailand, 13 domestic and 21 operating as foreign banks. In addition, the Thai government controls four specialised banks, each serving a particular mandate (The Bank of Agriculture and Agricultural Co-operatives, The Government Housing Bank, The Government Savings Bank and The Export-Import Bank of Thailand). Both the government-owned and commercial banks are supervised by the Bank of Thailand.

A tendency that has been observed within the Thai banking sector in recent years is an increased customer orientation with more products tailored to specific needs, greater convenience through new technology and lower fees and costs resulting from higher competition. State-owned commercial banks, and more specialised institutions such as the Government Savings Bank and the Government Housing Bank have been aggressively raising their lending profile, to the point where they now all match that of privately owned banks in outstanding credit.

39 Sources: The World Bank and The Bank of Thailand respectively.

With total assets of nearly US$13,000 million, the Government Savings Bank of Thailand (GSB) is the fifth largest bank in Thailand, after domestic commercial banks like Bangkok Bank (US$31,000 million), Krung Thai Bank (US$26,000 million), Thai Farmers Bank (US$19,000 million) and Siam Commercial bank (US$18,000 million). The GSB has the second largest network with 573 branches nationwide, just after Krung Thai Bank (647 branches) and before other domestic commercial banks like Bangkok Bank (526 branches) or Thai Farmers Bank (533 branches).

9.6.2 Institutional aspects of the Government Savings Bank

GSB, formerly called the Savings Office, was founded in 1913 under the jurisdiction of the Royal Treasury Department to encourage people to save and to provide safe depository for their property in accordance with the Savings Office Act. The Savings Office was later transferred to the Post and Telegraph Department. After the end of World War II, the Government enacted the Savings Bank Act, which created the Government Savings Bank that became operational on 1 April 1947.

At present, the GSB is a state enterprise guaranteed by the Government and operating under the supervision of the Ministry of Finance. GSB conducts its businesses independently under the guidance of its Board of Directors, which is appointed by the Minister of Finance.

The identity and philosophy of the bank is to commit itself to three major roles: as a development bank, as a commercial bank and as a social contributor. In line with the Government's concern for poverty reduction in Thailand, GSB was given the mandate by the Government to provide the 'unbanked' low-income population with microfinance services at relatively low lending rates. To this purpose, it launched the *People Bank project* on 25 June 2001[40].

In each branch of the GSB, a person was recruited to be dedicated to the operation of the People Bank. The People Bank Department at the GSB head office employs 20 staff with an average of 5 employees in each branch that have been trained for this project including a manager and his/her assistant, a credit officer, an accounting officer and a support officer. Apart from its 573 branches, GSB has 281 ATMs and employs deposit collectors and loan officers who travel by foot or by the means of a motorbike in order to visit customers on a regular basis.

40 The Government strongly supports the promotion of the project provided it is in line with one of its major policies.

The People Bank is the core microfinance activity conceived, developed and operated by GSB. However, GSB also operates an additional microcredit scheme in line with government policy: the *National Village and Urban Community Fund (NVUCF)*. The NVUCF is a microcredit revolving fund to finance projects of mutual interest to the communities and of particular interest to the poor, the underprivileged groups and the returned labour[41].

9.6.3 Operational aspects and outreach of GSB's microfinance activities

The establishment of the People Bank project is an effort to provide low-income people with a source of loans and to wean them off non-conventional sources (such as loan sharks), which usually tax them heavily and trap them into debts all their lives. In spite of this social role as a development bank, the People Bank project is a profit making social activity. The People Bank is included in the GSB's balance sheets and overseen by the People Bank department. The project consists of micro-credit services for small entrepreneurs, both in the urban and rural areas countrywide. These clients are also provided with savings and insurance facilities as well as training services[42].

9.6.4 Lending operations

The loans are extended to individual customers who are required to form a group of 3 members with two of them guaranteeing the third one. However the guarantor could equally be a government official of a certain rank or be in the form of real estate. Loans are extended to eligible members. Loans granted can be either repaid in cash or by direct debit. The borrowers are insured under a personal accident insurance plan.

41 The Fund is provided for village residents to be used as a revolving fund or for occupational promotion investment. Through this project, GSB coordinates with village level committees to ensure that benefits are rapidly generated for the local people and local economies are hence improved. In this framework, the GSB has secured a loan of BHT 80,000 million (US$1,883 million) for the Government. GSB, in collaboration with the Bank for Agriculture and Agricultural Cooperatives (BAAC), has transferred through its branch offices 1 million BHT (US$23,534) to each one of the nearly 80,000 villages nationwide.

42 Occupational and management training is provided to the members of the project with a view to enhancing their managerial and entrepreneurial skills. The purpose is to educate microentrepreneurs (and in particular those with no or low professional education) on how to set up and run their microenterprise. This responds to one of the main objectives of the People Bank project, which is to encourage vocational knowledge and skill development among the target group so that they can run a sustainable business and therefore develop their capacity to become regular customers of the bank.

At the early stages of the project, the maximum amount of the loan without collateral was set at BHT 15,000 (US$346) with a twelve months repayment period and an optional grace period for deferred payment of one month. Provided that the customer proved timely in their repayment and managed the borrowed amount responsibly, he/she would be entitled to a second loan of up to BHT 30,000 (US$692) with a 24-month repayment period and an optional grace period for deferred payment of one month. These conditions were later revised and have resulted as of February 2002 in a maximum loan amount for first time borrowers of BHT 30,000 (US$692) with a 24-month repayment period, followed by a second loan (provided the customer proves responsible) of an amount up to BHT 50,000 (US$1,153) and a maximum repayment period of 36 months. Both loans offer an optional one-month grace period for deferred payment. The interest rate of the loan has been fixed by GSB with the government's consent at 1% per month (in contrast to an average of 10% per month charged by loan sharks).

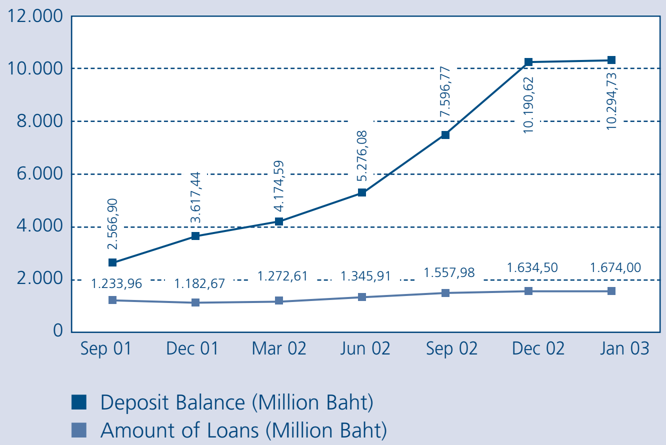
At the end of 2002, the People Bank project had a membership of 566,515 people (an increase of around 80,000 new members in less than one year) for a total of 554,740 loans representing a cumulative amount of BHT 10,258.42 million (US$245 million) and an average of US$441 per person. The outstanding loan portfolio stood at BHT 5,685.25 million (US$134 million).

9.6.5 Savings services

The People Bank does not only extend loans but also promotes savings habits and collects savings from the customers. The savings habits of the individual, reflected by both the deposited amount and the frequency of deposits is taken into account for eligibility for the microloan. The savings products offered by GSB are classified under standard and special savings accounts. The first one accrues interest on a daily basis and is exempt from tax. The savings account can be used as collateral for a loan or an overdraft. Not only is it possible to transfer funds from the savings account to a current account, but also payments of utility bills can be deducted against the savings account. The particularity of the special savings account is that each deposit or withdrawal must be of BHT 1,000 minimum (US$23), except for the withdrawal of interest. Second and next withdrawals are subject to a fee of 1% of the transaction amount but not less than BHT 500 each (US$12). The deposit interest rates differ depending on the amount deposited and the time for which the deposit has been fixed.

For retail customers this ranges from 2% for a savings account up to 4.5% per annum for a tax-exempt monthly fixed deposit account. But, this rate is slightly lower and fixed at 1.25% for savings deposits made under the People Bank project. In January 2003, the deposit balance of the 568,431 members of this project stood at BHT 1,674.50 million (US$38 million).

Comparison between total amount of deposits and loans (September 2001 - January 2003)



9.6.6 Financial sustainability and performance

At the end of 2002, outstanding loans with defaults over three months amounted to BHT 214,37 million (US$5 million) and corresponded to a number of 21,506 people. The share of non-performing loans, considered as defaults for over three months to outstanding loans, stood at 3.81% by the end of 2002. The default for over three months to total loans ratio was 2.10%[43]. The total interest received from the inception of the project until 15 January 2003 totalled BHT 580,728,112 (over US$13 million).

43 The 1997 financial crisis resulted in non performing loans in the (commercial) banking sector reaching a peak of 47% of total outstanding loans in May 1999, compared with around 10% by the end of 2001.

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The opinions expressed in this paper are the responsibility of the authors and do not necessarily reflect the views of any of the above-mentioned people or an official position of the WSBI.

11. EPILOGUE

WSBI represents savings and retail banks throughout the world and to this extent, is also developing a series of case studies from European savings and retail banks.

In its pursuit however, to disseminate current and relevant information, it has been decided to issue this 'Microfinance provisions by savings banks illustrated by selected experiences from Africa, Asia and Latin America,' before the European case studies have been concluded. The analysis of provisions of microfinance services by savings banks using European examples, will follow.

About WSBI (World Savings Banks Institute) and ESBG (European Savings Banks Group)

WSBI (World Savings Banks Institute) is one of the largest international banking associations and the only global representative of savings and retail banks. Founded in 1924, it represents savings and retail banks and associations thereof in 84 countries of the world (Asia-Pacific, the Americas, Africa and Europe -via the European Savings Banks Group).

It works closely with international financial institutions and donor agencies and facilitates the provision of access to financial sectors worldwide - be it in developing or developed regions. At the start of 2004, assets of member banks amounted to more than €7,300 billion.

ESBG (European Savings Banks Group) is an international banking association that represents one of the largest European retail banking networks, comprising about one third of the retail banking market in Europe, with total assets of €4,345 billion (1 January 2004). It represents the interests of its members' vis-à-vis the EU Institutions and generates, facilitates and manages high quality cross-border banking projects.

WSBI-ESBG members are typically savings and retail banks or associations thereof. They are often organised in decentralised networks and offer their services throughout their region. For decades WSBI members reinvest responsibly in their region and are one distinct benchmark for corporate social responsibility activities throughout Europe and the world.

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