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Mainstreaming Grameen banking

How rural banks combine sustainability with outreach to the poor in the Philippines

By Hans Dieter Seibel & Fabrizio Felloni

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In many countries, Grameen replication has not fared well in terms of outreach and sustainability. There is no country where the Grameen Bank, reaching two million poor women in groups of five and centers of 30 in Bangladesh, has been truly replicated. In The Philippines, rural banks and NGOs-turned-rural-bank have made Grameen banking a highly profitable product with rapidly expanding outreach to the enterprising poor and ultra-poor, mostly women. How did they do it?

Poverty in the Philippines

According to the national statistics office, 24 million people, 28.4% of the population, cannot provide for minimum basic needs. Twice that number are underemployed, subsisting on less than \$100 a month. In rural areas, financial services are mainly provided by rural banks, rural cooperative banks and thrift banks as well as cooperatives; but the very poor have been largely beyond their reach.

Grameen replication by credit NGOs: unsustainable operations at minimum outreach

Since the beginning of democracy in 1986, civil society institutions have played an important role in The Philippines. An increasing number of NGOs provided financial services to the poor, estimated at 600 in the mid-1990s. While the markets of rural banks and NGOs overlapped, the rural banks served the middle and lower sections, and NGOs made a determined effort to reach further down. Since 1989, that role was officially recognized by the government through its support to the Grameen Bank Approach Replication Project implemented by the Agricultural Credit Policy Council (ACPC) through NGOs. In 1993, ACPC evaluated the performance of 23 replicators. It noted high repayment rates and a significant impact on the standard of living of its beneficiaries, but found the program donor-driven, internal resource mobilisation minimal, costs exorbitant, and interest rates inadequate. As the NGOs were found combining minimal operational self-sufficiency rates (below 25%) with minimal outreach. ACPC warned that, “*any attempt... to replicate or expand it should be carried out with great caution*”.¹

PCFC: expanding Grameen banking with great caution

This is what the People’s Credit and Finance Corporation (PCFC) did: *expanding Grameen banking with great caution*. PCFC was established by the government in 1995 as a wholesale financial institution for poverty alleviation and funded by an ADB/IFAD loan. Refinancing NGOs and cooperatives as GBA replicators, outreach at the beginning grew only slowly. The turn-around came in 1997, when the Center for Agriculture and Rural Development (CARD), a Grameen replicator and disseminator, established a rural bank and started sharing lessons, learned the hard way, among rural banks.

CARD: mainstreaming a credit NGO

The story of CARD is worth telling, as it stands for lessons that ought to be learned by many. CARD had been established in 1986 as one of many new NGOs at the onset of a new era. In January 1988, it began organizing the poor into groups of 15-45 men and women and provided microloans at negotiable repayment terms. After eight month, it had reached 150 borrowers, at a repayment rate of 68%: obviously a false start. In late 1988, the president of CARD visited the Grameen Bank in Bangladesh, was deeply impressed, introduced the Grameen discipline of weekly meetings and repayment schedules – but met with stiff resistance by the men. Only 89 poor women agreed to participate in a pilot venture: with great success, as repayment surged to 100% and stayed close to that figure ever since. During 1990-96, CARD modified the Grameen technology. It substituted first-loans of six months for one-year loans; requested from repeat borrowers a self-financing ratio of 25%; introduced mutual life and accident insurance; replaced group funds by center funds; offered multipurpose loans to prime borrowers; added voluntary withdrawable savings; and introduced a staff incentive scheme. Active membership grew to 307 in 1990, 1,711 in 1993

¹ ACPC, Evaluation of the Grameen Bank Replication Project in the Philippines. Manila, 10/1995.

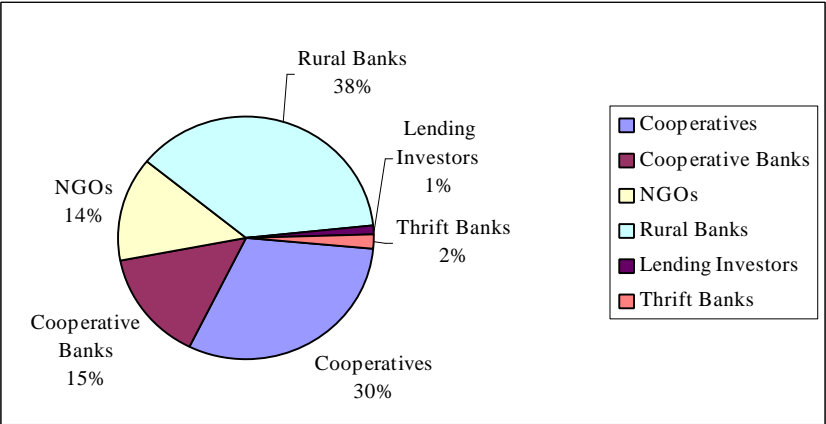
and 6,844 in 1996; the ratio of operational self-sufficiency, an indicator of cost coverage, grew from 31% to 46% in 1993 and 77% in 1996 – impressive gains, yet far from satisfactory. Then, in 1997, CARD established a rural bank, accepted deposits from the general public, and entered into unprecedented growth. By May 2002, it had expanded its outreach to 92,500 poor and non-poor depositors and 56,400 poor women-borrowers, using both deposits and PCFC loans as sources of funds. Its repayment rate was 99.7%; its operational and financial self-sufficiency ratios stood at 145% and 119%, respectively; return on assets was 5.2%, return on equity 18.8%. Its growth continues unabated.

The two-fold impact of the CARD miracle: mainstreaming NGOs and Grameen banking

The CARD miracle has initiated a process of conversions of credit NGOs into rural banks; and it has attracted banks as Grameen replicators in increasing numbers. As of June 2002, banks account for 55% of the 162 active intermediaries in the project. Highlights are:

- During the recent phase of rapid expansion of the project, the early emphasis on NGOs and cooperatives has shifted to banks
- The shift in emphasis to banks, including the establishment of banks by participating NGOs, constitutes the mainstreaming of Grameen banking in the Philippines
- In terms of repayment, rural banks and thrift banks performed best (with collection rates of 97.6% and 99.5%, respectively).

Distribution of Grameen replicators in the project, June 2002



Grameen banking as a financial product

To the banks, Grameen banking is but a financial product: highly effective in terms of outreach and profitability. Producers Rural Bank Corporation in Cabanatuan (Nueva Ecija Province), established in 1994, may serve as an example. For two years, 1996-98, it experimented with microfinance, but suffered delinquency problems. These were solved when the staff were trained at Card Rural Bank and GBA was adopted: “word by word,” as its owner and CEO put it. During four years of testing Grameen and non-Grameen products in parallel, it has embraced banking with the very poor with increasing enthusiasm. While most rural banks are unit banks of limited outreach, Producers Bank now has, thanks to Grameen:

- ✓ 12 branches
- ✓ 51,700 depositors (21,000 of them in GBA, accounting for 4% of deposits)
- ✓ 17,258 borrowers (12,519 of them in GBA, accounting for 13% of loans outstanding)
- ✓ a return on assets of 5.3% on Grameen and 1.5% on non-Grameen operations
- ✓ a return on equity of 105.6% on Grameen and 11.2% on non-Grameen operations.

It attributes its success in outreach and profitability to the quality of GBA training at Card Rural Bank; the adoption of GBA credit discipline, value formation, group and leadership training; vigorous marketing at doorsteps, taking the bank to the people; recycling deposits at the local level as its motto. Encouraged by this breakthrough in rural banking, Producers Bank now embarks on transferring key elements of GBA to its regular banking operations; graduating up to 30% of Grameen clients to individual loans; and building a Grameen

franchising/Build-Operate-Transfer business as a rapid expansion strategy across the country. In November 2002, the CEO of Producers Bank addressed the Microcredit Summit in New York, disseminating his message of *sustainable outreach to the poor by rural banks*.

Lessons learned... and disseminated

There are several important conclusions from the case studies which are, in contrast to earlier findings, of great relevance to the international debate over group vs. individual technologies and of sustainability vs. outreach:

- Mainstreaming GBA as a product of regulated financial institutions is feasible.
- GBA as a product of healthy financial institutions can be highly profitable and produce a share in profit far in excess of its share in the loan portfolio; but in weak institutions, both Grameen and non-Grameen banking do not pay off, neither in terms of outreach nor in terms of profitability.
- Compared to 1993, transaction costs have gone down, in CARD, from 47% to 35%; in Producers Bank's GBAR program, they stand at 12.3%.
- The high profitability is due to high repayment rates, high interest rates, and, in banks, economies of scope.
- Outreach could be substantially increased by stronger support to branching out through institutional loans.
- The restriction of loans to productive purposes and microenterprises (e.g., excluding agricultural and educational loans) interferes with institutional autonomy.
- GBA as a group lending methodology is flexible: clients may stay in the groups, graduate to individual lending, or do both
- Institutional sustainability and rapid increase in outreach to the poor are not only compatible, but also mutually reinforcing.
- Not every methodology is for every bank: non-collateralised group lending works in some, collateralised individual lending in others: for reasons of management preference or others.
- In either case, sound banking practices and adequate monitoring, guidance and staff training are necessary.

The social capital of Grameen banking in The Philippines

Successful replicators share a least the following three sound practices, constituting the core social capital of the original Grameen approach:

- high moral commitment of leaders based on values enforced through training
- peer selection and peer enforcement, precluding adverse selection and moral hazard
- credit discipline, including weekly instalments; rigid insistence on timely repayment; and repeat loans of growing sizes contingent upon repayment performance.

The most promising replicators are those who have experimented with modifications to the classical replication model, constituting additional social capital dimensions:

- (rural) bank status
- deposit mobilisation through differentiated products
- differentiated loan and insurance products which cover all costs and yield a profit
- client differentiation through larger-size loan and deposit products for non-poor members (generating additional loan capital) and graduation opportunities for the poor.