

# UNITED NATIONS CAPITAL DEVELOPMENT FUND

Myanmar



## Funding Challenges for the Microfinance Sector in Myanmar

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November 2015



## List of Abbreviations

CSO	Civil Society Organization
DFI	Direct Foreign Investor
FRD	Financial Regulatory Department
FSP	Financial Service Providers
INGO	International Non-government Organisation
LIFT	Livelihoods and Food Security Trust Fund
MADB	Myanmar Agriculture Development Bank
MARC	Myanmar Access to Rural Credit
MDF	Market Development Facility
MEB	Myanma Economic Bank
MFI	Microfinance Institution
MMK	Myanmar Kyat
MOU	Memorandum of Understanding
MSME	Micro, Small and Medium Enterprise
NGO	Non-government Organization
Norfund	Norwegian Investment Fund for Developing Countries
PGMF	Pact Global Microfinance Fund
UNCDF	United Nations Capital Development Fund
UNDP	United Nations Development Programme

## 1. Introduction

The United Nations Capital Development Fund (UNCDF) is the UN's capital investment agency for the world's 47 least developed countries. It creates new opportunities for low-income people and their communities by increasing access to microfinance and investment capital.<sup>1</sup>

UNCDF *MicroLead Expansion* supports the development and roll-out of deposit services by regulated financial service providers (FSPs) in 21 countries. The programme offers grants and loans that incentivize leading providers to start up new, or strengthen existing, financial institutions that target low-income people.<sup>2</sup>

*MicroLead Expansion* in Myanmar is a 4-year (2014–2017), US\$7-million programme funded by Livelihoods and Food Security Trust Fund.<sup>3</sup> MicroLead supports two southern microfinance market leaders to greenfield in Myanmar in addition to working with a regional association of credit unions to create new rural saving and credit cooperatives (SCCs). By the end of 2017, will increase sustainable access to appropriate, demand-driven and responsible financial services (with a focus on savings) to more than 100,000 low-income people in Myanmar, half of whom women and half of whom in rural areas.

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<sup>1</sup> See [www.uncdf.org](http://www.uncdf.org)

<sup>2</sup> See [www.uncdf.org/en/microlead](http://www.uncdf.org/en/microlead)

<sup>3</sup> See [www.lift-fund.org](http://www.lift-fund.org)

This paper is one in a series of financial inclusion knowledge products written by UNCDF, and it sits within the scope of UNCDF *MicroLead Expansion* programme in Myanmar. The series is written to inform the reader on the financial behaviour and preferences of low-income people, development of financial products, management of financial services and financial service providers' greenfield operations in Myanmar.

## 2. Aims and Objectives

This paper tackles the funding challenges that both national and international microfinance institutions (MFIs) face in Myanmar. The 2011 Microfinance Law has criteria that are interpreted by several MFIs, both national and international, to be restricting their access to funding.<sup>4</sup>

### Current MFIs Funding Sources & Challenges

This paper explains how both national and international MFIs are currently funded and what funding challenges they face.

### Ways Forward – Market Development Facility

The paper ultimately aims at presenting ways forward, in particular how a *Market Development Facility* might best help to fill funding gaps in the market.

This paper was written to address funding issues as they stand on 10 April 2015.

## 3. Microfinance Regulations in Myanmar

H.E. U Thein Sein, President of Myanmar, demonstrated the Government's growing commitment to fostering financial inclusion in 2011, when he recognized the development of **micro savings** and **credit enterprise** as two national development priorities aimed at reducing poverty in Myanmar.<sup>5</sup>

The Myanmar Government's political endorsement of the development of micro savings and credit enterprise led to the passing of the 2011 Microfinance Law. Before 2011, the United Nations Development Programme (UNDP) was the sole institution legally allowed to provide micro-lending and micro-savings services to people in rural areas. The Microfinance Law created for the first time in Myanmar a distinct microfinance sector.

The Microfinance Law comes with a set of explicit socio-economic objectives: reducing poverty at the grassroots level, creating job opportunities, cultivating saving habits,

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<sup>4</sup> Myanmar, Microfinance Law, Law No. 13 of 30 November 2011.

<sup>5</sup> In 2011, at the opening ceremony of the Rural Development and Poverty Alleviation Committee in Nay Pyi Taw, H.E. President U Thein Sein presented eight fundamental tasks to address poverty to be performed by ministries and state organs. The development of micro savings and credit enterprises, one of the eight national development priorities, was assigned to the Ministry of Finance and Revenue.

supporting cottage industries, fostering SMEs, and supporting diversification of income-generating activities of farmers.

The Microfinance Law established the independent supervisory and regulatory agency—the Financial Regulatory Department (FRD, formerly the Myanmar Microfinance Supervisory Enterprise). FRD sits under the Ministry of Finance, and is responsible for the licensing, monitoring and evaluation of MFIs, and issuing new directives.

Key highlights from the 2011 Microfinance Law and the five subsequent microfinance directives include the following:

- The interest rate on microfinance loans is 30% p.a. on declining balance.
- The interest rate on savings deposits is 15% p.a. minimum.
- Maximum loan size is \$5,000/year (no more than one loan per household).
- Loans shall not be issued to purchase luxury items.
- Each MFI has to comply with a 50:50 ratio of rural to urban clients.
- MFIs are permitted to apply mobile payment systems (except remittances from local and abroad).
- Local MFIs can borrow only from Myanma Economic Bank (MEB, a state-owned bank), and not exceed a debt to equity ratio of 5:1.
- Local-based foreign MFIs can only borrow from formal financial institutions outside the country, not exceeding a debt to equity ratio of 5:1 and not exceeding \$3 million.
- To access either grant funding or debt financing, MFIs have to seek approval from FRD.
- To access debt financing, international MFIs have to submit a request for approval to the Central Bank of Myanmar.

## 4. MFI Landscape in Myanmar

Potential for growth in the microfinance sector in Myanmar is enormous. Only 30 percent of adults in Myanmar are currently financially included, and only 18.6 percent of adults use formal credit products.<sup>6</sup> See table 1 for a picture of financial inclusion in the country.

Table 1

### Financial inclusion in Myanmar

Percentage of adults financially included	30%
Percentage of adults with an account at a formal financial institution	5%
Percentage of adults with at least one loan outstanding from a regulated financial institution	19%
Percentage of adults with at least one insurance product from a regulated financial institution	3%
Percentage of formal SMEs with an account at a formal financial institution	17%

Sources: FinMark Trust and UNCDF, *FinScope Myanmar 2013: Survey Highlights*; Chamberlain and others, ‘[Myanmar: Demand, Supply, Policy and Regulatory](#).’

<sup>6</sup> FinMark Trust and UNCDF, *FinScope Myanmar 2013: Survey Highlights* (n.p., 2014). Available from <http://www.lift-fund.org/finscope-myanmar-2013-survey-highlights>; Doubell Chamberlain and others, ‘[Myanmar: Demand, Supply, Policy and Regulatory](#),’ Making Access Possible (MAP) (n.p., Centre for Financial Regulation and Inclusion and Bankable Frontier Associates, 2014). Available from [http://www.lift-fund.org/sites/ift-fund.org/files/publication/MAP\\_Myanmar\\_Diagnostic\\_full\\_report\\_Final.pdf](http://www.lift-fund.org/sites/ift-fund.org/files/publication/MAP_Myanmar_Diagnostic_full_report_Final.pdf)

The Myanmar economy is characterized by high levels of informality, with a pervasive unregulated financial sector constituting the largest source of lending. An estimated 9.2 million adults have a loan from an unregulated FSP, with an estimated total outstanding debt as high as MMK 5.4 trillion (US\$5.7 billion)<sup>7</sup> that is primarily due to a lack of credit, forcing people to turn to moneylenders.

In a speech at the Yangon University of Economics, Economic Advisor to the President U Aung Tun Thet noted that “without formal financial inclusion, people often end up dealing with loan sharks.” He went on to point out the historical dimension to financial inclusion, referring to the 1930 Saya San Rebellion as being caused by resentment against moneylenders, and defined the moneylenders thus: “We now call them *chettars*, people lending money at exorbitant interest rates.”<sup>8</sup>

Exorbitant moneylending certainly exists in Myanmar, but precise data on the practice is lacking. Informal lending at low or zero interest rates is common (e.g., family loans, peer-to-peer lending, lending groups). The estimated current demand for microcredit in Myanmar is \$1 billion, though the estimated total loan portfolio of licensed MFIs is closer to \$118 million, less than 1/8 of the potential loan market.<sup>9</sup>

A new class of MFIs has already begun building on the historical experience of UNDP and the international NGO Pact programme. The sector has opened up to a dozen international entrants and greater domestic participation. There are currently 235 licensed MFIs, which is a dramatic increase from microfinance being essentially illegal three and a half years ago.

Most of the MFIs are very small and only a few have the chance to reach significant scale. With 650,000 active borrowers, Pact Global Microfinance Fund (PGMF)—the oldest and largest MFI—was the only institution authorized to operate before 2011, and it has received grant funding from UNDP since 1997. A few other MFIs of moderate size (e.g., Gret, Proximity Designs, Save the Children, World Vision) have been funding themselves to date, using a combination of grant funding, debt, equity and retained earnings.

MFI sector reach (in terms of both number of clients and market share) is still limited. The MFI sector is the second largest in terms of rural branch networks, after the Myanmar Agricultural Development Bank (MADB).

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<sup>7</sup> Doubell Chamberlain and others, ‘Myanmar: Demand, Supply, Policy and Regulatory,’ Making Access Possible (MAP) (n.p., Centre for Financial Regulation and Inclusion and Bankable Frontier Associates, 2014). Available from [http://www.lift-fund.org/sites/ift-fund.org/files/publication/MAP\\_Myanmar\\_Diagnostic\\_full\\_report\\_Final.pdf](http://www.lift-fund.org/sites/ift-fund.org/files/publication/MAP_Myanmar_Diagnostic_full_report_Final.pdf). P. 14

<sup>8</sup> Financial Inclusion speech to Yangon University Students, Yangon University, Convocation Hall, 31 March 2015.

<sup>9</sup> Data is from 2013. Source: Doubell Chamberlain and others, ‘Myanmar: Demand, Supply, Policy and Regulatory,’ Making Access Possible (MAP) (n.p., Centre for Financial Regulation and Inclusion and Bankable Frontier Associates, 2014). Available from [http://www.lift-fund.org/sites/ift-fund.org/files/publication/MAP\\_Myanmar\\_Diagnostic\\_full\\_report\\_Final.pdf](http://www.lift-fund.org/sites/ift-fund.org/files/publication/MAP_Myanmar_Diagnostic_full_report_Final.pdf)



## 5. MFI Funding Challenges in Myanmar

The laws preventing national MFIs from accessing international funding, and international MFIs from accessing domestic funding, have severely constrained the industry. In the case of national MFIs, state-owned MEB requires MFIs to borrow against traditional collateral (e.g., land, immovable property, gold, and agricultural goods) which are not appropriate forms of collateral for their business plan / needs. In the case of international MFIs, after a loan has been negotiated with an international investor, the FRD reviews it and the Central Bank has the final say on its approval. Several international MFIs have already negotiated international funding agreements, though the terms of these agreements are yet to be approved by the Central Bank.

Despite not being a written requirement in any of the microfinance directives, it is current practice for the Central Bank not to approve any international funding agreement with interest rates that exceed 8 percent for US dollar loans and 10 percent for local currency loans. It is not clear whether the Central Bank refers to nominal interest rates or real interest rates. It is important to mention that in February 2015, the Central Bank auctioned 3-month treasury bills at a yield of 8.19 percent. Government treasury bills are supposedly risk free by their very nature. In contrast, national and international MFI lending comes with intrinsic risks such as currency risk, country risk, MFI portfolio risk, etc. Given that risk-free lending is issued at 8.19 percent, it is very unlikely that MFI lending, which does carry risk, can be issued at the same rate.

Essentially, MFIs come in two distinct types:

- Profit-maximizing MFIs: Commercial companies whose focus is to deliver maximum return to investors.
- Impact-maximizing MFIs: Companies whose focus is to expand financial inclusion to low-income and enhance their financial prospects by providing access to credit and savings, combined with financial skills training and other development tools.

The MFI types defined above are a simplified generalization within the sector. MFIs, however, are all individual— meaning that, in the MFI sector, there are grey areas in between these categories. For example, some commercial MFIs have considerable corporate social responsibility programmes, while other commercial MFIs operate no such programmes. Likewise, social businesses exhibit variation. NGOs can use microfinance surpluses to cross-subsidize some of their other development programmes; conversely, NGOs can use surpluses from other development activities to start microfinance programmes. In the current Myanmar context of 235 licensed MFIs, we see MFIs occupying varied positions across the MFI spectrum, with each facing its own funding challenges.

### 5.1 Challenges Faced by National MFIs

According to the third microfinance directive, issued in October 2014, the state-owned bank MEB is the only financial entity legally allowed to lend to national MFIs. In a

workshop organized by the International Finance Corporation in February 2015, MEB officials stated that MEB is still seeking suggestions as to how to move forward in lending to MFIs under the current regulatory environment. MEB officials explained that, although new regulations stipulate that local MFIs can get loans from MEB, MEB has not yet developed the appropriate loan products. MEB sits under the Ministry of Finance and is one of four state-owned banks. According to banking regulations, all loans issued by state-owned banks as well as commercial banks have to adhere to strict collateral requirements.

In theory, national MFIs can access loans from MEB at a 13-percent interest rate provided they offer up traditional collateral (e.g., land, immovable property, gold, agricultural goods). From October 2014 to date, no national MFIs have been able to access debt financing from MEB.

“It would be very good if we could substitute the MEB traditional collateral with our audited loan books, or with an internationally recognized MFI rating.” (Representative, national MFI)

National MFIs are advocating for the introduction of tailored collateral requirements for MFIs, such as their audited loan books, internationally recognized MFI ratings and group guarantees from development finance institutions, as acceptable collateral.

“Besides accessing debt financing from MEB, there are essentially two other ways to access funding for national MFIs: 1) for the national MFI to create a joint venture with an international company; or 2) for the national MFI to allow an international company to become a majority shareholder. In both cases, the MFI would be able to access international funding.” (Representative, National MFI)

Myanmar may appear to be rigid but some innovative practice is taking hold:

- In January 2015, Norwegian Investment Fund for Developing Countries (Norfund) - a fund to combat poverty in developing countries through private sector development - entered into an option agreement with Myanmar Investments International Limited. Its wholly-owned subsidiary Myanmar Investments Limited signed a joint venture agreement for the development of a microfinance business in Myanmar with Myanmar Finance Company Limited. The joint venture company is called Myanmar Finance International Ltd. According to the agreement, Norfund has the option to subscribe for up to a 25-percent stake in Myanmar Finance Company Limited by September 2016. Through the use of subsidiaries, the funds from the international investors can be channelled into a Myanmar National Investment Company, which is not restricted by law and can lend into the MFI sector. This use of international equity is one way for international investors to lend directly to the national MFI sector.<sup>34</sup>
- In December 2014, Pact in partnership with LIFT started the Myanmar Access to Rural Credit (MARC) project. MARC will build the capacity of nine Myanmar-based civil

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<sup>34</sup> Myanmar Investments Limited, ‘Option relating to the microfinance joint venture agreement,’ 27 January 2015. Available from <http://www.londonstockexchange.com/exchange/news/market-news/market-news-detail/12228417.html>; <https://www.norfund.no/investmentdetails/myanmar-finance-international-limited-article10662-1042.html>

society organizations to become national MFIs. MARC MFIs will issue agricultural and business loans to women in rural areas, covering 900 villages in the Delta and Dry Zone regions.<sup>35</sup> The Pact Global Microfinance Fund (PGMF) director noted that Pact is “keeping them under our wings and will support them all through the process of becoming a formally registered MFI.”<sup>36</sup> Since 2014, PGMF worked with each of the lenders-to-be to improve their technical and organizational capacity to offer quality microcredit services, to ensure their sustainability as they grow their loan portfolios, and to convey lessons from Pact’s own microfinance operations.<sup>37</sup>

## 5.2 Challenges Faced by International MFIs

A spectrum of nine international MFIs operating in Myanmar were interviewed for this paper<sup>38</sup>. These nine MFIs are among the largest MFIs by portfolio size. The MFIs were questioned on their past, present and future funding strategies, current funding challenges and ways to overcome funding challenges. Table 2 provides a snapshot of their responses.

**Table 2: MFIs in Myanmar: Funding strategies, challenges and ways forward**

MFI	Type	Funding arrangements to date	Current funding challenges	Ways forward
1	INGO	Grants: 100%	<ul style="list-style-type: none"> <li>- High interest floor on savings (15% p.a.) makes it very difficult to use savings as a funding source</li> <li>- Lack of diversification of MFI funding sources</li> </ul>	<ul style="list-style-type: none"> <li>- Decrease the interest floor on savings</li> <li>- For Regulator to facilitate legalization process for CSOs/NGOs into MFIs</li> <li>- For Regulator to facilitate entrance of socially oriented DFIs</li> </ul>
2	INGO	Loans: 42% Grants: 29% Equity: 15% Ret. earnings: 14% (Loans were approved before current Central Bank restrictions on interest rates)	<ul style="list-style-type: none"> <li>- <b>Central Bank interest rate cap is prohibiting access to international investment</b></li> <li>- Central Bank declined approval of international finance agreement on grounds of exceeding interest cap</li> </ul>	<ul style="list-style-type: none"> <li>- <b>For Regulator to be open to the market allowing MFIs to borrow at market rates</b></li> <li>- <b>To remove Central Bank interest rate restrictions all together</b></li> </ul>

<sup>35</sup> Pact, ‘Pact and LIFT partners lend to Myanmar poor,’ 24 December 2014. Available from <http://www.pactworld.org/press-releases/pact-lift>

<sup>36</sup> Interview with Jason Meikle, PGMF Deputy Director, Yangon Myanmar, March 2015. Interviewer Eleonora Gatti.

<sup>37</sup> Ibid.

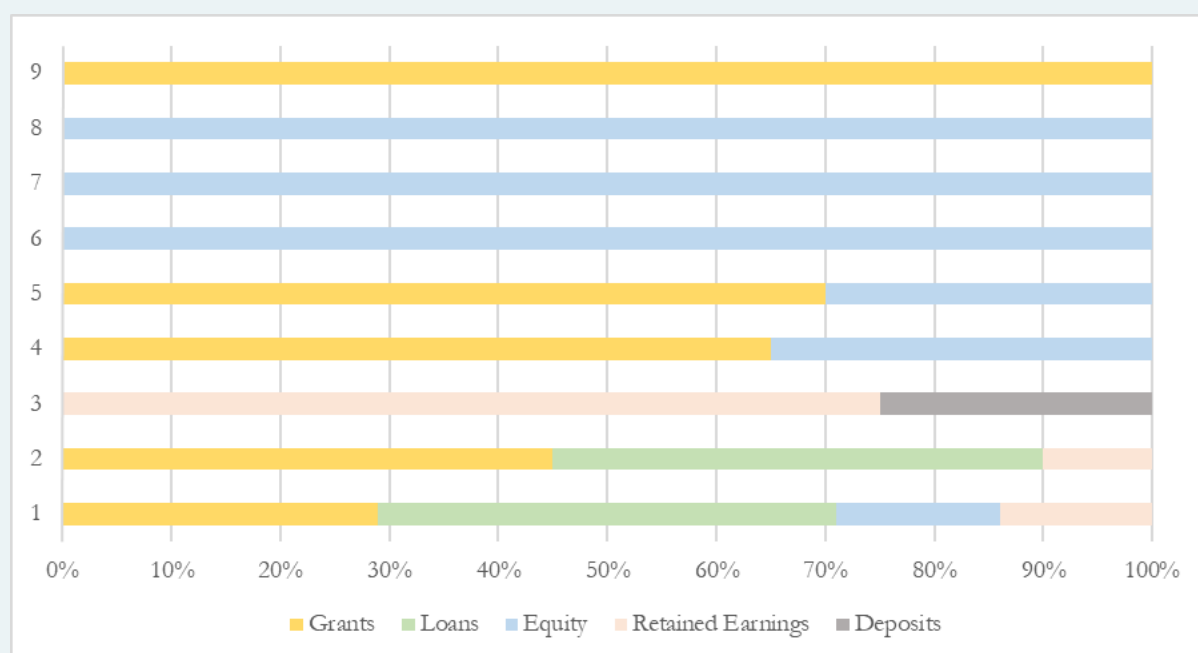
<sup>38</sup> Interviewed by Eleonora Gatti in Yangon between the month of March and April 2015. Names of interviewees withheld.



3	INGO in transition to Limited Company	Grants: 45% Loans: 45% Ret. earnings: 10% (Loans were approved before current Central Bank restrictions on interest rates)	- MFI cannot access adequate international debt financing as legal entity INGO (INGOs in Myanmar have MoU with the Government that might not prove to be a strong enough legal basis to access international debt financing)	- Transition from INGO to limited company <b>- For Regulator to be open to the market allowing MFIs to borrow at market rates</b>
4	INGO	Start-up grant: 100%, reached sustainability. Ret. earnings as equity: 75% Savings: 25%	n/a	- Open up the opportunity to access local currency soft loans from national loan funds to achieve faster growth
5	Limited Company	Grants: 65% Mother company equity: 35%	<b>- Central Bank interest rate cap is prohibiting access to international investment</b>	<b>- For Regulator to be open to the market allowing MFIs to borrow at market rates</b>
6	Limited Company	Grants: 70% Equity: 30%	<b>- Central Bank interest rate cap is prohibiting access to international investment</b>	<b>- For Regulator to be open to the market allowing MFIs to borrow at market rates</b> <b>- Lift restrictions</b> on international companies borrowing from national sources - Set up refinancing facility that can refinance a certain portion of MFI portfolio (e.g. agriculture portfolio, MSME portfolio)
7	Limited Company	Mother company equity: 100%	<b>- Central Bank interest rate cap is prohibiting access to international investment</b> - Central Bank declined approval of international finance agreement on grounds of exceeding interest cap	<b>- For Regulator to be open to the market allowing MFIs to borrow at market rates</b> <b>- To remove Central Bank interest rate restrictions all together</b> - To access grant funding to operate in remote areas
8	Limited Company	Equity from investor: 100%	- MFI is unable to obtain interest rate on capital - MFI cannot open an interest bearing bank account as an international company - MFI cannot buy government bonds as an international company	<b>- Lift restrictions</b> on interest bearing bank account for international companies - Lift restrictions on deposit interest floor for deposits to be used as a source of funding <b>- To remove Central Bank interest rate restrictions all together</b>
9	Limited Company	Equity from mother company: 100%	<b>- Central Bank restrictions on international companies' borrowing</b> from national sources are prohibiting access to local currency loans from national banks or national loan funds	<b>- Lift restrictions</b> on international companies borrowing from national sources - Open up the opportunity to access local currency soft loans from national loan funds

Figure (I) further highlights that, at present, international MFIs use a diverse range of funding mechanisms including grants, equity from their mother companies, debt financing (approved before the current regulation), in-company cross-subsidies, and deposits from clients. It should be noted, however, that the majority of MFIs are yet to reach a well-diversified funding base due to current legal restrictions.

**Figure (I): International microfinance institutions in Myanmar: Funding mechanisms**



The key funding challenges shared by the majority of the MFIs interviewed can be summarized as follows:

- Inability to access international debt financing due to stringent interest rate requirements set by the Central Bank;
- Inability to borrow from national sources due to legal restrictions on international MFI borrowing from local sources;
- Inability to use client deposits as a key funding source due to high interest floor on deposits (15 percent p.a.); and
- Inability to open an interest bearing account to deposit equity capital.

The interviews with MFIs brought up a considerable number of recommendations that, in the view of the MFIs, would contribute to the growth of the sector in Myanmar by overcoming key funding challenges:

- The need for grant money to be used as an operational cushion or disbursement cushion to reach areas where operational expenses are higher;
- The need for a local lending to MFIs in local currency;
- The relaxation of restrictions on borrowing nationally;

- The need to allow commercial banks to securitize MFI portfolios (portfolio buyout);
- The need for a refinancing facility to support a certain portion of the MFI portfolio (e.g., agriculture portfolio, MSME portfolio); and
- The relaxation of the interest floor on deposits so as to leverage client deposits as a reliable funding option.

## 6. Views of international lenders

What concerned interviewed lenders<sup>39</sup> most were the rapidly changing regulatory framework, the country's political instability and the current restrictions on interest rates for lending set by the Central Bank (10 percent for US dollar denominated loans).

"The cap at 10% is several percentage points below the market rate (...) we therefore hope that the 10% cap is only a temporary hurdle and that the government will realise the importance and the need for local currency investments by foreign (impact) investors." (Representative, international impact investor)

Lenders highlighted that the 10-percent cap is inadequate in the Myanmar context, as it does not align with other market signals:

- Three-month (risk-free) treasury bills were auctioned in February 2015 at a yield of 8.19 percent.

"How is [it] then possible for investors to lend long term at 10 percent if risk free for 3-month is at 8.19 percent?" (Representative, international impact investor)

- Banks operating in Myanmar lend on a secured basis at 13 percent for 12 months (14 percent with admin fee).

"How is [it] then possible for investors to lend long term at 10 percent on an unsecured basis?" (Representative, international impact investor)

- It is current practice for the Central Bank not to approve any international funding agreement with interest rates that exceed 8 percent for US dollar loans and 10 percent for local currency loans. There is a 2-percent spread between the set cap at 8 percent for US dollar loans and the set cap at 10 percent for local currency loans.

"This 2 percent spread will provide the wrong incentive to lenders who will make good money in US\$ but leave the MFIs with the currency fluctuation risk due to the difficulty and cost of hedging." (Representative, international impact investor)

<sup>39</sup> Interviewed by Eleonora Gatti in Yangon between the month of March and April 2015.

- Interest floor on deposits to be paid by MFIs to their clients is set at 15 percent p.a.

“How is [it] then possible for investors to lend long term at 10 percent?” (Representative, international impact investor)

Investors show an understanding that the Central Bank is treading a cautious path, but they ask for open dialogue between the Central Bank and core actors in the sector to find a way to satisfy both the Central Bank’s prudent approach and investors’ ability to operate in Myanmar. Investors commented that the Government had every right to restrict international lending if there were concerns that costs would be passed on to clients. Interviewees showed confidence that keeping the 30-percent cap on lending would be a sufficient safety measure. **All investors interviewed called for the 15-percent floor to be lowered or eliminated.**

## 7. Ways Forward

This paper highlighted key funding challenges for national and international MFIs working in Myanmar as well as those challenges faced by international investors. There is no silver bullet to tackle these challenges. – a multi-faceted approach is needed. Such an approach has to address funding challenges of different types of organizations at different stages of organizational growth.

UNCDF is currently setting up a Market Development Facility (MDF), which has been developed to tackle key funding challenges for MFIs operating in Myanmar. The facility will function as a catalytic wholesale financial agent able to take-on risk and leverage outside sources of capital to boost funding to undercapitalized FSPs operating in Myanmar. The fundamental purpose of the proposed facility is to help ‘open up’ what is essentially a donor-driven microfinance sector (i.e. overwhelmingly grant-funded) and support a transition to a more market-driven sector. This will involve the inclusion of domestic and international sources of capital in the form of loans and investments. New sources will be able to help diversify not only the institutions, but also the services available to poor clients – in particular credit, savings and micro-insurance.

UNCDF will use its unique public-private partnership role and capital mandate to leverage maximum donor and impact investment. It will do this in order to achieve the Government policy goals of poverty alleviation, increased agricultural productivity and development of cottage industry sector and Financial Inclusion Roadmap outcomes<sup>40</sup>.

The Market Development Facility will provide direct support for funding needs of international MFIs operating in Myanmar by issuing both local currency soft loans and grant instruments such as performance-based loans, sectorial loans, risk capital grants.<sup>41</sup>

<sup>40</sup> UNCDF Making Access Possible, Centre for Financial Regulation and Inclusion and Finmark Trust, *Myanmar Financial Inclusion Roadmap 2014–2020: Creating financial inclusion through leadership towards a market based approach* (n.p., n.d.). Available from [http://www.uncdf.org/sites/default/files/Documents/myanmar\\_roadmap\\_repro.pdf](http://www.uncdf.org/sites/default/files/Documents/myanmar_roadmap_repro.pdf)

<sup>41</sup> These instruments are to be interpreted as examples.

The facility will also support promising MFIs with technical assistance grants to support the development of new products for microfinance clients, especially savings instruments.

Although geared to support international MFIs with good track records and promising growth potential, the facility also aims at tackling the indirect funding challenges of local MFIs by working in partnership with the Government of Myanmar to support a more conducive lending and regulatory environment. The facility will use a combination of initiatives aimed at supporting MEB in the development of new loan products for national MFIs, and partnership initiatives with international certification bodies to carry out risk-based assessments.

Depending on how the market unfolds, the UNCDF Market Development Facility can be considered a step toward the creation of a Myanmar microfinance apex. Although microfinance apexes take on different forms, they are generally understood as wholesale financial mechanisms used to channel funds to retail microfinance providers. Apex institutions are very common in the South Asia region, with six out of eight countries in the region having an apex.<sup>42</sup>

Around the world, apex institutions have played a strong role in crowding-in commercial microfinance funding.<sup>43</sup> Apexes fill a gap, especially in countries where the microfinance sector is in the early stages of development and there is little interest amongst commercial banks to lend to MFIs. As institutions mature, however, the ratio of apex funding to total debt tends to decrease. There is also evidence of “demonstration effects” whereby commercial banks slowly become comfortable with MFI creditworthiness through sound borrowing history with the apex.<sup>44</sup> Research from this paper tells us that a Myanmar microfinance apex would be considered by the MFIs (as well as by international investors interviewed) a welcome step forward for the sector.

## 8. Further Recommendations

There is no doubt that the microfinance sector will flourish in Myanmar. Huge progress has been made in the short period since 2011 – the year in which Myanmar opened up to the potential for economic growth from microfinance. More progress is to come and will bring increased income to millions, though numerous challenges still remain. The UNCDF Market Development Facility goes a long way towards surmounting the challenges, in a new era of dialogue and progress.

Key issues that all in the sector need to keep close at hand are:

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<sup>42</sup> Qazi Azmat Isa, Yasir Ashfaq and Aban Haq, ‘What Makes a Microfinance Apex Work?’ 2011 Global Microcredit Summit Commissioned Workshop Paper (Islamabad, Pakistan Poverty Alleviation Fund, 2011). Available from [http://www.globalmicrocreditsummit2011.org/userfiles/file/Workshop%20Papers/Q\\_%20Isa%20-%20What%20makes%20a%20Microfinance%20Apex%20Work%201.pdf](http://www.globalmicrocreditsummit2011.org/userfiles/file/Workshop%20Papers/Q_%20Isa%20-%20What%20makes%20a%20Microfinance%20Apex%20Work%201.pdf)

<sup>43</sup> Ibid, p.6.

<sup>44</sup> Ibid.



**1) The microfinance sector should be open and maintain positive dialogue with Regulators.**

Economic prudence and client protection are key principles for the Central Bank, MEB and Ministry of Finance. Expansion and client reach are the shared goals of the sector. Funding is central to balancing everyone's interests. Dialogue is the tool to make this happen.

**2) Internationally-recognized microfinance rating agencies should be introduced to evaluate the performance and risk of MFIs operating in Myanmar.**

In the immediate term, microfinance rating agencies can benefit the Myanmar microfinance sector by: i) supporting the Myanmar Regulator (MEB) to undertake assessments of MFIs using rating certifications of creditworthiness; and ii) aiding international investors in their credit assessments of international MFIs. Examples of microfinance rating agencies include M-CRIL ([www.m-cril.com](http://www.m-cril.com)), MicroFinanza Rating ([www.microfinanzarating.com](http://www.microfinanzarating.com)), MicroRate (<http://www.microrate.com>), and Planet Rating (<http://www.planetrating.com>).

**3) Credit guarantee facilities should be established.**

Credit guarantee facilities will support MFIs, especially national MFIs, to establish credit relationships with local banks and build critical access to local currency financing. They will also deliver a demonstration for local banks to become comfortable with future unguaranteed lending to MFIs.

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