UNITED NATIONS CAPITAL DEVELOPMENT FUND
Myanmar

Policy Brief

FX-Denominated Offshore Debt Finance Agreements for Microfinance Institutions in Myanmar: Regulations and Procedures

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1. Acronyms

AML	Anti Money Laundering
AOA	Articles of Association
ADB	Asian Development Bank
CBM	Central Bank of Myanmar
DG	Director General
FRD	Financial Regulatory Department
FX	Foreign Exchange
IFI	International Financial Instituion
MDF	Market Development Facility
MOA	Memorandum of Association
MSME	Micro Small & Medium Enterprises
MFI	Microfinance Institution
MFSC	Microfinance Supervisory Committee
MoPF	Ministry of Planning and Finance
MIC	Myanmar Investment Commission
MMFA	Myanmar Microfinance Association
PAR	Portfolio at Risk
UNCDF	United Nations Capital Development Fund
UNOPS	United Nations Office for Project Services
USAID	United States Agency for International Development

2. Introduction

The issuance of new Microfinance Institution (MFI) Directives on 29 August 2016 has opened the door for MFIs to attract debt finance and grow their organisations and credit portfolios, potentially very rapidly. Myanmar has the benefit of being home to more than a dozen international MFIs that have already been successful in their home markets of Japan, Cambodia, India, Bangladesh, Sri Lanka and some African countries. The expertise and systems these MFIs have developed and refined over years, combined with the large network of financially sound owners and financiers, allows Myanmar MFIs to skip years of learning and to upscale operations fast.

This brief aims to contribute to the success of MFIs in Myanmar by enabling international financial institutions (IFIs) that have the potential to support MFI growth to find their way in the new regulatory and procedural environment. Secondly, the brief aims to open a discussion between stakeholders in MFI debt finance to identify and advocate for ways to improve regulations and procedures for the benefit of all – regulators, supervisors, shareholders, IFIs, MFIs and their advocacy platform, the Myanmar Microfinance Association.

3. Market Actors

Microfinance Supervisory Committee

The main MFI regulator is the Microfinance Supervisory Committee (MFSC). Like the many other committees that are so typical in the public administration system of Myanmar, the MFSC isn't embedded in a ministry like a department is but can have members from various governmental organisations. It has a strong connection to the Ministry of Planning and Finance (MoPF).

The MFSC's Chair is the Minister of Planning & Finance and its Secretary is the Director General (DG) of Financial Regulatory Department (FRD) of MoPF. The MFSC meets irregularly and often unannounced, perhaps about four to six times per year. The MFSC as such can't be visited, other than through its Secretary or Chair . In addition to determining MFI regulations, the MFSC also decides on applications for MFIs licenses and on approval of debt finance agreements. The MFSC Secretary is housed in Building 34 in Nay Pyi Taw and can be reached at +95 67 410 254 or mmse34@gmail.com.

Financial Regulatory Department

The FRD has six divisions, or sub-departments. One of these departments - the MFI Supervision Division - is responsible for what its name suggests, day-to-day on and off-site supervision of MFIs.[1] This MFI Division also supports the MFSC decision process, for example by ensuring appropriate documentation of requests for approvals, including that of MFI debt finance agreements.

The FRD's Director General, as MFSC Secretary, functions as entry point for the MFSC, and closely cooperates with the MFI Supervision Division's Director on MFI-related issues.

Central Bank of Myanmar

The Central Bank of Myanmar (CBM) is not responsible for MFI regulation or supervision. CBM does determine the setting for financial markets, including that for retail finance and foreign currencies. Its long-term objective is to liberalise the financial markets, allow pricing be determined by market forces and ensure financial sector stability.

Currently, pricing in the market for retail finance is determined by CBM's bank-lending rates, which set interest at a maximum of 13% nominally per annum in Myanmar Kyat and 8% in US Dollar (www.cbm.gov.mm).

CBM also regulates the market for foreign currency and monitors Myanmar's foreign currency position. Based on that responsibility CBM needs to pre-approve any offshore FX-denominated debt finance agreements for companies located in Myanmar, including

[1] Others are divisions on the supervision of the insurance sector; inspection of state-owned banks; inspection of the State Lottery Enterprise; policy, research and training; and administration.

funding for MFIs. CBM's approval decision is based on criteria outlined in a regulation issued on the topic. The responsible department is the Foreign Exchange Management Department.

Myanmar Microfinance Association

Although the Myanmar Microfinance Association (MMFA) doesn't have a formal position or legal status, it does have a very important role in the processes related to communication between MFIs and regulators, especially in advocacy. The MMFA was instigated by the forerunner of the FRD as a platform to represent the MFI community in its communication with the regulator. Until today, the FRD and MFSC consider the MMFA as representative of its MFI constituents. The MMFA board is the democratically elected representative of the informal association of MFIs. The MFSC and FRD consider requests and recommendations made by the MMFA as highly relevant, and as guidance for possible regulatory change.

4. Procedures

This is the procedure for an MFI to gain approval for off-shore sourced, FX-denominated debt finance. It gives an overview of required documents and expected checks.

First step: CBM

The MFI should apply at Central Bank of Myanmar, Office Building No. (55), Nay Pyi Taw - the Foreign Exchange Management Department.

Documents and information to provide

- ✓ Corporate Documents (Certificate of Incorporation, Form VI, Form XXVI, MOA and AOA)
- ✓ If a company has been incorporated, the annual financial statement of the relevant fiscal year and the most recent annual financial statements of the company which have been properly audited by an audit team recognised by the Government;
- ✓ Loan Agreement (Draft) including complete information regarding loan (and Repayment Plan and Schedule);
- ✓ Credit Advice that shown the equity has been brought in for the paid-up capital of the company;
- ✓ Other necessary documents.

CBM checks

- ✓ Whether the company has brought in minimum US$ 500,000 as equity or capital brought-in into Myanmar;
- ✓ Whether the company that obtains an offshore loan is a business that regularly obtains income in foreign currency in accordance with the provisions of Foreign Exchange Management Law and Foreign Exchange Management Regulations;

- ✓ Whether the company is able to make full repayment with income in Myanmar Currency
- ✓ Whether there are any FX hedging arrangements in the event that the company does not have regular income in foreign currency;
- ✓ Whether the minimum 80 % of foreign capital (equity amount) stated in the MIC Permit has been brought in;
- ✓ Whether the ratio of debt to equity is between 3:1 and 4:1;
- ✓ Whether the terms and conditions of the loan stated in the loan agreement and supporting documents of the company are accurate or not;
- ✓ Whether the tenure of repayment stated in the loan agreement occurs within a medium-term period or a long-term period and the repayment schedule is in accordance with the loan agreement; and
- ✓ Whether the interest-rate is within the limits set by the maximum bank-lending rate.

Second Step: MFSC

Application should be made to MFSC through FRD of MOPF, Building 34, Nay Pyi Taw, Myanmar - DG of FRD and Secretary of the MFSC.

Documents and information to provide

- ✓ The loan agreement
- ✓ Approval letter of CBM.
- ✓ Information on the MFI:
  - Most recent profit-loss account and balance sheet checked by the auditor.
  - Details on non-performing loans or portfolio at risk (PAR)
  - Details on business performance, areas of operation, number of clients, portfolio size, paid-up capital.
- ✓ Information on utilisation of funds from the debt finance agreement:
  - Business plan for the use of funds borrowed (e.g. expansion, bigger loan sizes for clients, upgrading service with information technology)
  - Statement of commitment to utilise the funds in microfinance services
- ✓ Information on the trustworthiness of the lending organisation.
- ✓ Statement that loan will not exceed the prescribed solvency ratio (i.e. Total Equity/Total Assets greater than or equal to 12%).

MFSC checks

- ✓ Whether the lender a formal and reliable institution
- ✓ Whether Anti Money Laundering (AML) rules are met.
- ✓ Whether the MFI will stay within prudential ratio limits
- ✓ Whether the MFI has sound business practices.
- ✓ Whether the MFI will use funds for on-lending.

Duration

As the decisions are made in committee meetings that take place irregularly, prior contact should be sought with the financial sector authorities to get a sense of when committee meetings will occur, and to pre-check if documentation is considered complete and appropriate.

Very rough indications of involved timelines would put the estimate at between one and two months for CBM and between two and three months for the MFSC. However, as meetings do not have a regular schedule and depend on many unpredictable factors, timelines could on occasion may be much shorter/longer.

5. Regulatory changes: assessment and future

Assessment

In recent years the regulatory space for MFIs has strongly improved. Limitations on taking on debt finance and deposits have been relaxed and MFIs are no longer forced to lend to rural areas if this doesn't align with their business model. The move to allow provision of mobile-banking services (if approved by CBM) will give a green light for MFIs to provide remittance services (if approved by the MFSC). CBM has allowed debt finance providers to charge 13% on Myanmar Kyat, further enabling development of this market.

The progress made has been catalysed by the strong role played by the MMFA and the open attitude of the regulator to consider issues for improvement. Communication between MMFA and FRD is good, open and constructive. Strong technical support to FRD as supervisor by a range of development partners including the ADB, World Bank, USAID and UN agencies UNCDF and UNOPS, has also been beneficial for sector development.

The new government has issued strong support for inclusive, market-based economic development and access to finance for Micro Small & Medium Enterprises (MSMEs) and the agricultural sector. This leads to a credible expectation that the pace of recent progress will be maintained in the near term.

Future

Ongoing regulatory reform is expected, including a review and reform of the MFI Law, supported by the World Bank. Conversations are ongoing between MMFA and FRD to further detail and specify the requirements of the deposit-taking scheme.

IFIs will start lending to MFIs, catalysing expansion of their operations and branch networks and creating rapid increase in outreach. Some of the bigger and stronger MFIs will start preparing for deposit-taking, and other smaller ones for merging.

As a result of competition by new MFI entrants and liberalisation of funding markets, there will be a transition from overwhelmingly donor-driven MFI delivery to market-based MFI delivery. UNCDF's Market Development Facility (MDF) will also aid in this transition process.

The newly issued regulations to allow MFI delivery of remittance and mobile-financial services will be tested, as well as the quality and effectiveness of MFI supervision.

The introduction of a local-currency-based, small-scale Apex lending facility is expected for 2017 and liberalisation of lending rates in the retail market thereafter (though still without a clear timeframe).

Sources

Microfinance Business Law (2011)

Law on the Central Bank of Myanmar (2013)

Financial Institutions Law (2016)

CBM (Foreign Exchange Management Department: Criteria for Offshore Loans)

MFSC Directives 2016/1-4 of 29 August 2016.

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