

Ishrat Husain: Strategy for development of Microfinance in Pakistan

Remarks delivered by Dr Ishrat Husain, Governor of the State Bank of Pakistan, as Chief Guest at the launching ceremony of the Financial Sector strengthening program of the Swiss Agency for Development and Cooperation, Islamabad, 26 February 2003.

* * *

I would like to commend the Swiss Government and the Swiss Agency for Development and Cooperation (SDC) for launching the Financial Sector Strengthening Program (FSSP). I believe that the lack of adequate human and institutional capacity, shortage of local expertise and weak coordination among the various stakeholders are indeed the factors inhibiting the growth of microfinance sector in Pakistan. The initiative taken by SDC to overcome these constraints is therefore both timely and appropriate. But I do expect that once the FSSP has successfully demonstrated the business model for capacity building it will be adapted and internalized by our own network without any further recourse to external donors. The transfer of technology and its adaptation to our own circumstances is the most effective way to utilize external resources.

At the outset let me place microfinance in the overall context of the efforts the State Bank is making to expand the outreach of financial services and help the goal of poverty alleviation in the country. The SBP is, in addition to microfinance, encouraging the provision of credit to small and medium entrepreneurs through a newly set up SME Bank, to small farmers through a newly restructured Zarai Taraqqati Bank Ltd and Cooperative Banks, to women entrepreneurs, individuals and small firms through the First Women's Bank. These institutions will work as the prototype in developing the methodology and expertise in these areas and then this prototype will be replicated through the mainstream financial institutions in the country. This is the only durable basis through which the poor can benefit from financial sector of the country.

Pakistan has adopted a sectoral approach to microfinance in Pakistan and assimilated learnings from the experience of other developing countries which have been active in this area for decades. Microfinance is still in its infancy and has a long way to go. Some momentum has been built up during the last three years as bulk of the disbursements has taken place since June, 1999. Although there has been a big spurt in these three years the numbers of the beneficiaries and the volume of credit disbursed is still quite low in relation to the needs and demand of the intended target group. We have therefore decided to adopt a holistic, "let thousand flowers bloom", and inclusive strategy for promotion and spread of microfinance in Pakistan. This strategy consists of the following six elements.

First, there is a strong political commitment towards supporting microfinance as an integral tool of poverty alleviation program. President of Pakistan has taken keen personal interest in the nurturing and growth of this sector and has directed the Ministry of Finance to monitor and track the microfinance sector on a regular basis. The Government has invited the World Bank, ADB and other bilateral donors to actively assist us in this sector. Consequently the enabling environment for development and growth of MF is highly conducive. The constraints, snags and problems faced during the implementation of the program are removed in consultation and full involvement of the stakeholders.

Second, the program involves multiple actors and institutions - community organizations, NGOs, public sector, private sector, Rural Support programs - in the delivery of microfinance. The extent of poverty prevailing in Pakistan requires 'all hands - on the deck' approach rather than an exclusive monopoly of the Government or the public sector as has been the case in the past. Khushali Bank is owned by several leading financial institutions - private, public and foreign - rather than by the Government of Pakistan. This has allowed it to function in a professional manner.

Third, the complementarities between microfinance and other elements of poverty alleviation such as Investment, Infrastructure, Social services and Capacity building are clearly recognized and built in the program. Income generation by the poor cannot take place only through availability of credit if there is no infrastructure, or markets for selling their produce. Similarly without building the knowledge base and enlarging capacity of the poor there won't be any scope for sustainable microfinance.

Fourth, the government is experimenting with a variety of institutional models for delivery mechanisms and outreach to the poor. For example, we have a wholesale organization such as PPAF which is successfully disbursing a \$ 100 million line of credit provided by the World Bank. We have Khushali

Bank which is a retail bank and has already reached out to 100,000 customers and is targeted at 700,000 by 2007. Then there is First Microfinance Bank established in the private sector which is expanding its branch network throughout the country. We have integrated program vehicles such as the NRSP, PRSP etc. which combine Microcredit with other services. There are several single product Microfinance NGOs such as Kashif Foundation in Lahore. Two commercial banks are also providing lines of credit for microfinance. Leasing companies have also begun to take some interest and two of them are already engaged in the sector. In addition there are several self standing donor supported projects delivering microfinance. We don't know as to which particular delivery mechanism will be effective and that is why there is a need to experiment with plurality and diversity.

Fifth, an innovative feature of the Microfinance Sector Development is that as the poor segments of the population are much more prone and vulnerable to shocks they need to be protected. Thus a bad harvest or drought or strikes in the cities or violence completely wipe out the earning capacity of the poor and disable them from repaying their credit obligations on time. As labor is their only asset and the returns on labor are disrupted for no fault of theirs a risk mitigation mechanism had to be created to insulate the poor borrowers from these unforeseen hazards. A Risk Mitigation and Deposit Protection Fund has been created to provide protection to the MFIs borrowers and depositors. They can seek recourse to this fund under adverse circumstances beyond their control.

Sixth, the regulatory regime adopted by the SBP for Microfinance sector is that of a facilitator, guide and problem solver. We do not prescribe for MFIs the same onerous regulations which prevail for other financial institutions. We have a light regulatory oversight and are learning together with the practitioners and adopting ourselves to the changing circumstances. We have a Consultative Group drawn from the representatives of stakeholders who guide us in the development of our regulations and prudential norms.

To conclude, the strategy for microfinance development will undergo continuous review and modification to make it responsive to the needs of the poor. The government, State Bank, NGOs and all other MF practitioners have to work together to make this strategy work and accelerate the speed with which we can reach out to the potential beneficiaries. On the part of the SBP I can assure you our full commitment and support to this strategy. We look forward to working together with you in these endeavors.