ADVOCATING FOR A REGULATORY FRAMEWORK FOR SUSTAINABLE MICROFINANCE SYSTEMS

The lessons from Bolivia and the Philippines

By Daiki Mochizuki

> Lasting peace cannot be achieved unless large population groups find ways in which to break out of poverty. Micro-credit is one such means. Development from below also serves to advance democracy and human rights. Grameen Bank has been a source of ideas and models for the many institutions in the field of micro-credit that have spring up around the world. – Nobel Peace Prizeannouncement 2006

In 2006, a Bangladeshi banker Muhammad Yunus (Founder of Grameen Bank) received the Novel Peace Prize for "efforts through microcredit to create economic and social development from below."[1]He has developed the concept of microcredit (also known as microfinance), which can be defined as financial services, particularly small loans given to poor people to establish an income-generating activities, and it has been the one of the fastest growing financial industry for poverty alleviation.[2]In fact, the success of the microfinance movement went far beyond 13 million people in 2000 and estimates reachingover 190 million clients in developing world in 2012.[3]128 million clients were classified as poor, and 81.7 percent were women in the world.[4]In addition, microfinance has rapidly become a global $43 billion industry since 1980s, which increases 20,000 percentin comparison with 0.2 billion industry in 1984.[5]

The rapid growth has required a large-scale investment from a wide range of organizations, such as informal, semi-formal, formal microfinance institutions, and

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[1]"Nobel Peace Prize for 2006 to Muhammad Yunus and Grameen Bank - Press Release". Nobelprize.org. Nobel Media AB 2013. Web. 21 Sep 2013<http://www.nobelprize.org/nobel_prizes/peace/laureates/2006/press.html>

[2]Robin Gravesteijn, and James Copestake. "Microfinance and Social Performance." The International Studies Encyclopedia.Denemark, Robert A. Blackwell Publishing, 2010. Blackwell Reference Online. 21 September 2013 <http://0-www.isacompendium.com.opac.sfsu.edu/subscriber/tocnode.html?id=g9781444336597_chunk_g978144433659713_ss1-7>

[3]Maesand Larry R. Reed. "State of the microcredit summit campaign report 2012." Microcredit Summit Campaign, 2012. Page 3.

[4]Maes and Larry. 2012. Page 3.

[5]Constantinou, Dinos, and AshtaArvind. "Financial crisis: lessons from microfinance." Strategic Change 20, no. 5-6 (2011): 187-203.

commercialbanks.[6] As a matter of fact, there has first been a conversion from supply orientation to demand adaptation, and microfinance also has been commercialized via practice of new legislation by some organizations.[7] Second, microfinance has provided their services to not only deal with credit but also a broader range of financial services, for example, insurances, savings, payment, and support management.[8] Third, to put it simply, the ideas and means of microfinance services have become an international movement, leading to commercialization and transformation of MFIs.[9]

Microfinance has gained much attention from both domestic and international actors in the 1990s as "revolutionary financial service."[10]However, due to lack of effective supervision of commercial microfinance industry in some locations, the financial market led to massive negative effects on poor micro entrepreneurs, as well as some microfinance institutions (MFIs) went bankruptcy.[11] For instance, commercial MFIs in Bolivia have made clients not only over indebted, leading to high delinquency rates, but also pursued high profit increases.[12]Hence, the purpose of this paper is to show and analyze an effective micro-lending model for practicing microfinance services.This paper defines that such a model is via independent market driven forces and self-sustaining microfinance institutions with access to national and international market for capital with a legal regulatory framework by a state government, cooperating with

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[6]Daley-Harris. State of the Microcredit Summit Campaign Report. Washington: Microcredit Summit Campaign. 2004.
[7]Drake Deborah and Rhyne Elisabeth. The commercialization of microfinance.Kumarian Press, 2002.
[8]Robin and James. 2010. Page 1.
[9]Robin and James. 2010. Page 1.
"[10]Roodman, David Malin. Due diligence an impertinent inquiry into microfinance. Washington, D.C.: Centre for Global Development. 2011.
[11]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 114-137.
[12]Rhyne and Elisabeth. 2012. Page 114-137.

international organization, such as Asian Development Bank for sustainable development of MFIs and poverty alleviation based on the research question: what factors lead to an effective micro-credit lending model and system?

I will study two situations of microfinance: The first case study is liberated microfinance market in Bolivia, which has suffered from a microfinance crisis in the late 1990s. Because many NGOs and other MFIs have shifted into commercial MFIs or private financial funds too rapidly, the Bolivian microfinance sector hadtoo many institutions that operate as loan sharks.[13] By 1997, over 300,000 microfinance loans existed in Bolivia. As a result, the clients were able to easily access to credit from many institutions perceiving multi-loans to be much better investment on their business.[14]Also, after the economic shocks in 1999, the lack of regulation and supervision of commercial microfinance sector had too much debt and shrunk in demand. For instance, a commercial bank BancoSol lost 25 percent of clients.[15]

The second case study is commercial microfinance market in Philippines, enabling an appropriate regulation and supervision systems. Reacting to the rapid growth of several types MFIs in the world especially South East Asia, the Philippines' central bank and the Asian Development Bank has tried creating legal systems and regulatory framework through a wide range of informal, semi-formal, formal MFIs, and commercial banks.[16] This approach has been very effective for the development of sustainable microfinance in the Philippines by clearly

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13Marconi, Reynaldo, and Mosley Paul. "Bolivia during the global crisis 1998–2004: towards a 'macroeconomics of microfinance'." Journal of International Development 18, no. 2 (2006): 237-261.
14Marconi and Mosley. 2006. 237-261.
15Drake, Deborah, and Elisabeth Rhyne. *The commercialization of microfinance*.Kumarian Press, 2002. Page 127-129.
16Hennie Van Greuning,Joselito Gallardo, and BikkiRandhawa. "A framework for regulating microfinance institutions." *World Bank Policy Research Working Paper 2061* (1998). Page 3.

identifying NGOs, semi-formal MFIs, and legitimate commercial institutions.[17] As a result, the regulatory framework has provided an opportunity for NGOs to enter licensed financial institutions.[18] As a matter of fact, commercialization steps at entry were supervised by the local government division Bangko Sentralng Pilipinas (BSP) to determine whether the commercial level is too high or not.[19]

This paper's structure will consist of six sections. The **literature review** will demonstrate overview of microfinance literature and history, mentioning microfinance academic community's prominent works and authors. I will then describe two debates on whether commercialization of microfinance leads to positive impacts on financial market for poverty alleviation or not, as well as referring to the importance of enabling a regulatory framework in commercial microfinance sector for sustainable development. I will finallycharacterize the three levels of analysis framework: client (poverty alleviation), institution (commercialization and transformation), and financial system level (regulation and supervision). The **first case study** will demonstrate a Bolivian microfinance situation, which is liberated microfinance industry showing that how commercial microfinance industry had difficulties due to the lack of effective regulatory framework for commercial development. The **second case study** will survey a commercial microfinance situation with an effective regulatory framework in the Philippines, showing that how a state government has tried various approaches to create public policies and the regulatory framework on the commercial sector with the Asian Development Bank for the sustainable development of commercial MFIs and poverty alleviation. The **analysis** will evaluate

[17] Hennie, Joselito and Bikki. 1998. Page 3.
[18] Hennie, Joselito and Bikki. 1998. Page 22.
[19] Hennie, Joselito and Bikki. 1998. Page 22.

the findings of the paper and compare the results of both countries' approaches on the commercial microfinance industry. Finally, the **conclusion** will suggest specific recommendations based on current research for commercial development of MFIs.

Overview of Microfinance Literature and History

> Whenever you are in doubt, recall the face of the poorest and weakest man whom you may have seen, and ask yourself if the step you contemplate is going to be of any use to him. Will he gain anything from it? Will it restore him to a control over his life and destiny? True development puts those first that society puts last. – Mahatma Gandbi

Microfinance and microcredithave become a slogan among human development promoters, academics, donors, and international communities. The General Assembly announced 2005 as the International Year of Micro Credit.[20] The terms of microfinance and microcredit are sometimes mixed up.In the literature, microcredit refers to only "small loans". On the one hand, microfinance as defined by a scholar Otero Maria is "the provision of financial services to low-income poor and very poor self-employed people."[21] Scholars Schreiner and Colombet characterize it as "the attempt to improve access to small deposits and small loans for poor households neglected by banks."[22]Also, Kelleher and Klein mention that microfinance is a strategy providing "loans to poor people so they can begin their own local business."[23] Hence, microfinance enables poor clients to access many kinds of financial services, such as small loans,

[20]Ann Kelleher and Klein Laura Frances. Global perspectives: a handbook for understanding global issues. Prentice Hall, 1999. Page 107.
[21] Otero Maria. "Bringing development back, into microfinance." Journal of Microfinance/ESR Review 1, no. 1 (1999): 8-19.
[22]Schreiner Mark, and ColombetHéctorHoracio. "From urban to rural: Lessons for microfinance from Argentina." Development Policy Review 19, no. 3 (2001): Page 339.
[23]Kelleher and Klein. 1999. Page 107.

insurance, savings, and payment services from MFIs in order to improve their living standards on their own.

Microfinance and microcredit are considered as new terms in the human development field. Even though microfinance has got much public attention in the 2000s, various approaches to development have been prominent over the last couple decades.[24] For example, Otero emphasized developing infrastructure and financing large capital-intensive projects during 1960s. In the 1970s, the approach focused on dealing with people's basic need in poor communities. In fact, the Grameen Bank originated in 1976 as an action-research project in an area in order to test the hypothesis that "If the poor are supplied with working capital they can generate productive self-employment without external assistant."[25] The bank then was established in Bangladesh in 1983 by government order to provide small loans for improving poor people's economic condition. The Grameen Bank project had been very effective with many successful stories of poor entrepreneurs who used the tiny lending and had opened 298 branches and 250,000 household clients that is 6 percent of the villages in the country.[26]The strategy emphasized "market base" defined as a social business, which gave small credit (approximately $20 - $50) to poor clients to manage their own business.[27]

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[24]Roodman, David Malin. 2011. Due diligence an impertinent inquiry into microfinance. Washington, D.C.: Centre for Global Development.

[25]Hossain, Mahabub. Credit for alleviation of rural poverty: The Grameen Bank in Bangladesh. No. 65. Intl Food Policy Res Inst, 1988. Page 9.

[26]Hossain. 1988. Page 9

[27]JonathanMorduch. "The role of subsidies in microfinance: evidence from the Grameen Bank." Journal of development economics 60, no. 1 (1999): 229-248.

In the 1980s, the priority had shifted from basic needs approach to structural adjustment andstabilizing economies.[28]Microfinance then gained prominence in mainstream during 1980s as a "response to doubts and research findings about state delivery of subsidized credit to poor farmers" because government agencies of microfinance occupied the industry, giving credit to poor.[29]Therefore, the poor clients had been forced to pay high interest rates. Beginning in the mid - 1980s, the subsidized lending model by the government had suffered massive loan losses and required commercialization to continue operating.[30]In other words, the market-based settlement was required more and more in the comparison with the 1970s.[31] This led to a modern approach that places microfinance as part of a formal financial system. For example, local NGOs started to try more long-term approaches. ACCION international has supported low-income clients providing microfinance services, including equity investment and technical assistance by using the development of union group lending to urban venders.[32] Their strategy promoted commercialization of microfinance defining as "to develop commerce and manage on a business basis."[33]

In the 1990s, Robinson observed that a lot of MFIs were created and emphasized on reaching many clients.[34] That is, commercialized MFIs have become very popular among the microfinance sector. For example, a commercial MFI, BancoSol, undertook an initiative in

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[28]Otero. 1999. Page 8-19.

[29] JoannaLedgerwood. Microfinance handbook: an institutional and financial perspective. World Bank-free PDF, 1998. Page 2.

[30] Joanna. 1998. Page 2.

[31] Joanna. 1998. Page 2.

[32] Joanna. 1998. Page 2.

[33]Drake Deborah and Rhyne Elisabeth. The commercialization of microfinance.Kumarian Press, 2002. Page 3.

[34] Robinson, Marguerite S. The microfinance revolution: sustainable finance for the poor. Vol. 1. World Bank-free PDF, 2001. Page 54.

accessing domestic and international financial market and profit motive investors in Bolivia.[35] Hence, appropriate regulation and supervision was desired for developing microfinance industry. By the late 1990s, commercial microfinance was no longer based on small groups. It was a massive industry to attract profit operations.[36] In fact, United Nations Secretary General's 1998's reports that there are 3,000 MFIs in developing countries, and more recent estimate says that 7,000 to 10,000 institutions exist in both developing and developed nations as well.[37] Now, microfinance is a $70 billion industry, attracting tens of thousands of people, predominantly managed by a small group of funds with private capitals.[38]Therefore, today's attempt is to create sustainable development framework in the commercial microfinance industry.

What is the commercialization and transformation of microfinance?

> Once poverty is gone, we'll need to build museums to display its horrors to future generations. They'll wonder why poverty continued so long in human society and how a few people could live in luxury while billions dwelt in misery, deprivation and despair.
> – Muhammad Yunus (Founder of Grameen Bank/Novel Peace Prize recipient)

With the creation of BancoSol in 1992, the microfinance sector has had a new trend of institutional development: the transformation of NGOs into regulated financial institutions.[39] The concept was created over a decade ago with two goals that increasing the number of the

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[35]Robinson, Marguerite S. The microfinance revolution: sustainable finance for the poor. Vol. 1. World Bank-free PDF, 2001. Page 54.
[36]Robinson, Marguerite8 S. The microfinance revolution: sustainable finance for the poor. Vol. 1. World Bank-free PDF, 2001. Page 55.
[37]Kelleher and Klein. 1999. Page 107.
[38]Sinclair, Hugh. Confessions of a Microcredit Heretic: How Microlending Lost Its Way and Betrayed the Poor. Berrett-Koehler Store, 2012. Page 3.
[39]Campion, Anita, and White Victoria. "NGO transformation." Microenterprises Best (2001). Page 3.

poor clients and reducing donor dependence. The spectacular goals have stimulated unification with the formal financial sector, guiding many NGOs into privately owned and regulated entities.[40]Christen and Drake refer to commercialization of microfinance as “the movement of microfinance out of the heavily donor-dependent arena of subsidized operations into one in which microfinance institutions manage on a business basis as a part of the regulated financial system”.[41] Furthermore, Joanna and Victoria defines transformation is one of the ways an MFI can commercialized, stating that “institutional process whereby an NGO microfinance provider or a microfinance project creates or converts into a share-capital company and becomes licensed as a regulated financial institutions”.[42]

In the early 1990s, Promotion and Development of Microenterprises (PRODEM) created the first regulated MFIs called BancoSol in Bolivia, demonstrating new possibilities for other microfinance NGOs and stimulating a great debate within the microfinance community.[43] As a matter of fact, much NGO commercialization has occurred around the world.[44] An MFI is able to commercialize in various ways. For example, one is to transform a nonprofit organization into a formalized and regulated MFI. If it is licensed, the formal or regulated MFI can get investment from public. This method of commercialization has become very popular across the globe. [45] Second is to originate a commercial MFI from scratch. In fact, a lot of commercial MFIs, especially micro banks in Eastern Europe were created this method by the German firm

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[40]Campion, Anita, and Victoria White. 2001. Page 3.
[41]Drake and Christen. 2002. Page 4.
[42]JoannaLedgerwood and Victoria White. Transforming microfinance institutions: providing full financial services to the poor. World Bank Publications, 2006. Page xxviii.
[43]Joanna and Victoria. 2006. Page xxvii.
[44]Joanna and Victoria. 2006. Page xxv.
[45]Joanna Ledgerwood and Victoria White. Transforming microfinance institutions: providing full financial services to the poor. World Bank Publications, 2006. Page xxvii.

Internationale Projekt Consult (IPC).[46] Third way is that traditional banks become involved in microfinance sector. For example, Sogebank in Haiti founded a subsidiary microfinance organization, Sogesol to enter the market. Fourth, the downscaling approach develops a special unit or segment within the back in order to focus on microfinance. At last, merging between two existing nonbank financial institutions is the way to commercialize, such as Xacbank in Mongolia.[47]

However, once MFIs become more commercial entities, commercial microfinance has been at the center of a worldwide controversy reflecting a conversion of integration microfinance into the formal financial sector.[48] In realities, there have been various books and scholarly journals on commercialization and transformation, but the most prominent debates are on how commercial development efforts affect poverty alleviation and they really reach the poor. On the one hand, a significant number of people in the commercial microfinance sector refer to commercialization as a necessary step to provide high quality financial services to the poor.For example, the commercialization of MFIs had led to competition, which improves the quality of services, diversification in lending products, broadening the target group, and decreasing the interest rates charged on micro-loans.[49] In fact, early leaders who brought microfinance closer to commercial banking sector in Latin America have agreed to the huge amount of funds needed in order to reach the more poor clients.

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[46]Joanna and Victoria. 2006. Page xxvii.
[47]Joanna and Victoria. 2006. Page xxvii.
[48]Drake and Rhyne. 2002. Page 3.
[49]Drake, Deborah, and Elisabeth Rhyne. *The commercialization of microfinance*.Kumarian Press, 2002. Page 5.

Scholars Gonzalez-Vega, Schreiner, Meyer, Rodriguez and Navajas state that commercialization and transformation has conducted possibilities of rapid growth, number of challenges, and new adjustments for poverty alleviation. For instance, the commercial growth of microfinance sector has three positive influences for MFIs and poverty alleviation.[50] There first has been a key element for success of microfinance: Outreach. Increase reaching numbers of clients enable MFIs reach more good quality of services and a lot of people are able to access to financial services for poverty alleviation. [51]Second, the growth is a significant factor for improving another microfinance element: Sustainability. Because of the growth, the poor clients were able to access new and better financial services in addition to satisfying more demands. Also, it encouraged the image of commercial MFIs that enables these organizations attracts more capital from banks or private funds.[52] Third, the growth reduced MFI's operating costs. As a result, MFIs would increase both outreach and sustainability for poverty alleviation. [53] However, there have been many negative effects for poverty alleviation. Liberalization of Bolivian microfinance sector has lad to extreme level competition by the aggressive consumer lenders and commercial MFIs.

In addition, according to Joanna and Victoria, Promoters of commercial MFIs claim that the number of loan clients served by commercial MFIs has increased. Robinson also states that

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[50]Gonzalez-Vega, Claudio, Schreiner Mark, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas. "BancoSol: The challenge of growth for microfinance organizations." Microfinance for the Poor (1997): Page 129.
[51]Gonzalez-Vega, Claudio, Schreiner Mark, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas. 1997. Page 129.
[52]Gonzalez-Vega, Claudio, Schreiner Mark, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas1997. Page 130.
[53]Gonzalez-Vega, Claudio, Schreiner Mark, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas.1997. Page 129.

among the poor entrepreneurs in the developing world, there were strong demands for small-scale commercial micro financial services.[54] Christen and Drake describe that commercial MFIs can provide many more financial services for the micro entrepreneur clients than traditional microfinance NGOs. Experience has shown that the wide range of financial services, including insurance, payment system, and savings should be developed by larger commercial MFIs, which has strong infrastructure and financial strength.[55] In fact, scholars argue that dealing with the larger numbers of clients reduces the transaction cost. One of the ways reducing the cost is to expand their financial services to larger clients.[56] The author concludes, "The best way to reach a large number of the truly poor with financial services will be through commercial banking institutions, not microfinance NGOs".[57]

On the other hand, others regard commercial microfinance as the beginning of the profit motive leading an exploitation of the poor and tending to invest richer clients for their profit increase.[58] In fact, as the founder of Grameen Bank Muhammad Yunus describes, "I never imagined that one day microcredit would give rise to its own breed of loan sharks", there have been negative effects of competition, which causes over indebtedness on some clients, and management risk for MFIs. Also, innovative MFIs have smaller opportunities that competitors

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[54]Robinson, Marguerite S. The microfinance revolution: sustainable finance for the poor. Vol. 1. World Bank-free PDF, 2001.Page 6.

[55]Drake Deborah and Christen Robert Peck. Commercialization: The new reality of microfinance. Kumarian Press, 2002. Page 14.

[56]Drake Deborah and Christen Robert Peck. Commercialization: The new reality of microfinance. Kumarian Press, 2002. Page 14.

[57] Drake Deborah and Christen Robert Peck. Commercialization: The new reality of microfinance. Kumarian Press, 2002. Page 14.

[58]Drake Deborah and Christen Robert Peck. Commercialization: The new reality of microfinance. Kumarian Press, 2002. Page 4.

copy their means of microfinance services.[59] For example, they witness commercialization as decreasing the quality of financial services to maximize financial returns. In fact, Scholar Webster refers to commercialization as “Loses quality to gain profit.”[60] Additionally, opponents of commercial MFIs fear that the profit motive guides zero sum game, which is more profit facilitates less services and fewer benefits to the poor clients.[61] They also believe that commercial motive makes MFIs will move up the market with focusing the less poor clients. In fact, the average loan model of commercial MFIs is so much higher than non-profit MFIs, which targets the poorest of the poor.[62]

As a response profit-focus assumption, there has been a debate on the subject of whether the microfinance has really contributed to the poorest of the poor.[63] This resulted to publishing prominent books against commercial MFIs model. Human development first approach has been strongly advocated by the World Bank, other international organizations, and Muhammad Yunus (Founder of Grameen Bank/Novel Peace Prize recipient). The Human Development model defines basic needs approach (participatory development) is the reason microfinance has been successful for poverty alleviation and improving the living standard for borrowers and their families.[64] As a result, MFIs are able to achieve social and financial goals by providing outside help directly. Hence, the advocates of human development state that commercial microfinance unable the society to reach the poorest of the poor.

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[59]Drake and Elisabeth. 2002. Page 5.
[60]Drake and Elisabeth. 2002. Page 6.
[61]Drake and Elisabeth. 2002. Page 6.
[62]Drake and Elisabeth. 2002. Page 6.
[63]Hulme, David, and Mosley Paul. *Finance against poverty: Volume 1*. Routledge, 1996.
[64]Ann Kelleher and Laura Klein. Global perspectives: a handbook for understanding global issues. (Pacific Lutheran University. Longman.) Page 107.

For instance, the founder of Grameen Bank, Yunus argues that microfinance institutions should pursue financial and social goals as “social business”. It means any profit should be re-invested into the company to achieve their social performance. In addition, many critics of commercial MFIs believe that commercialization of microfinance lead to profit motive rather than the social mission (the idea is referred to as “mission drift).[65] As a result, these MFIs may shift services away from the poor clients and try to maximize financial returns for external investments.[66]Accordingly, this debate meets heated whether the process of commercialization is good for the industry and clients.

What is Regulation and Supervision of Microfinance?

> Hey mister, what are you looking for under that light? My keys. Why did you lose them there? No, I lost them across the street. Then why don’t you look for them across the street? Because the light’s better over here.

The microcredit and microfinance movement exist for poverty alleviation. However, some say that commercial MFIs only focus the profitability of micro lending and quality of financial services, and they don’t tell us whether the clients become less poor or not.[67] In recent years, there have been a discussion on regulatory concerns of microfinance sector exist. Thus, the existence of an effective enabling regulatory and supervisory environment is important to the success of MFI commercialization and transformation.[68]Scholars Joanna and Victoria define

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[65]Joanna and Victoria. 2006. Page xxvii.
[66]Drake Deborah and Christen Robert Peck. Commercialization: The new reality of microfinance. Kumarian Press, 2002. Page 14.
[67]Cheston, Susy, and Larry Reed. "Measuring transformation: assessing and improving the impact of microcredit." Journal of Microfinance/ESR Review 1, no. 1 (1999): 20-43.
[68]Joanna and Victoria. 2006. Page xxviii.

regulation as the “binding rules governing the conduct of legal entities and individuals, whether they are adopted by a legislative body or an executive body” and supervision as “external oversight aimed at determining and enforcing compliance with regulation”.[69]To put it simply, regulation is rules to manage micro financial operations and supervision as making sure the compliance with those rules. Scholars Armstrong, Cowan, Vickers, and Majone state the necessity of regulation and supervision in the economic activities and reform measures to restrain the effects of market failures.[70] Chaves and Gonzalez regard regulation as “a set of enforceable rules that restrict or direct the actions of participants and as a result alter the outcomes of this action.”[71] Additionally, the regulation in the formal micro financial sector intends “to maintain a balance between shareholder and debtor/depositor interests, arises from information asymmetries that are due to the peculiar nature of the assets of the banking firm.”[72]

Enabling a regal framework and policy environment is generally believed as a one of the better way to increase the depth and breadth of access to financial services rather than governments directly participate in microfinance industry.[73] In addition, the regulatory framework is required as requirements for the development of financial viable and commercial financial institutions. However, there are no arrangements for how to create the regulatory framework in the financial sector, and it led to some issues in some locations. Hence, the financial crisis in various

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[69]Joanna and Victoria. 2006. Page xxviii.
[70]Arun, Thankom. "Regulating for development: the case of microfinance." The Quarterly Review of Economics and Finance 45, no. 2 (2005): Page 346.
[71]Chaves, Rodrigo A., and Claudio Gonzalez-Vega. "Principles of Regulation and Prudential Supervision: Should They Be Different for Microenterprise Finance Organizations." Economics and sociology occasional paper 1979 (1992). Page 4.
[72]Chaves and Gonzalez.1992.Page 4.
[73]Joanna and Victoria. 2006. Page 21.

countries hasactually conducted the debate of regulation and supervision into financial sector reforms front line in order to assuring systemic stability and protecting depositors.[74] However, appropriate regulation and supervision of financial markets rely on the country's orientation, such as institutional capacities.[75] In fact, due to inappropriate regulation or supervision of commercial microfinance industry in Bolivia, it caused massive damages in micro financial market and over lending issues by poor micro entrepreneurs, as well as some MFIs went bankruptcy, which will be explained in detail later in case studies.[76]The more recent debate on regulatory policies with focusing on means of provide appropriate relation between economic and social objectives as well as the connection between political and economic system.[77]

According to Joanna and Victoria, the Consultative Group to Assist the Poor's (CGAP's) by the World Bank and the Asian Development Bank also advocates the idea of regulation and supervision stating regulations and supervision are a regulatory framework to govern financial activities.[78] Some argues that credit-only services are not necessarily to be regulated. Once commercial MFIs begin taking deposits, the regulations should be applied. There have been two main aspects of financial intermediation below:[79]

1. Need for a sound and reasonable regulatory environment and capable supervision by the central bank or relevant regulatory authority.[80]

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[74]ArunThankom. 2005. Page 347.
[75]ArunThankom. 2005. Page 347.
[76]Rhyne and Elisabeth. 2012. Page 114-137.
[77]ArunThankom. 2005. Page 347.
[78]Joanna and Victoria. 2006. Page xxviii.
[79]Joanna and Victoria. 2006. Page xxviii.
[80]Joanna and Victoria. 2006. Page xxviii.

2. The institutional capacity and culture required to be a true financial intermediary taking deposits from the public, on-lending these deposits, and in doing so, complying with regulations and being supervised by a regulatory body.[81]

Hence, many scholars say that an appropriate regulatory framework is an essential element in the commercial microfinance factor in order to support MFI's sustainable financial services to the poor such as savings.

Furthermore, the World Bank stressed a market-oriented approach to increase financial sustainability. The strategy includes a number of key legal and regulatory frameworks, establishing institutional capacity and financial systems infrastructure.[82] Thus, the regulation and supervision of MFIs should be an integral part of a strategy to develop a market-driven financial system.

Microfinance and Development

Microfinance is the provision of financial services for poverty alleviation by NGOs, MFIs, commercial MFIs, private financial funds, and commercial banks. Their practice has included not only social development concept but also financial and commercial markets.[83] This cross-sectional element has guided to the creation of a growing number of microfinance institutions in the developing world.[84] When microfinance industry keeps the right balance between two frameworks development and commercial finance, microfinance will continue to bring

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[81]Joanna and Victoria. 2006. Page xxviii.

[82]Van Greuning, Hennie, Joselito Gallardo, and BikkiRandhawa. "A framework for regulating microfinance institutions." *World Bank Policy Research Working Paper* 2061 (1998).

[83]Otero Maria.1999. Page 1.

[84]Otero Maria.1999. Page 1.

international development and poverty alleviation.[85] In the scholarly journal "Bringing Development Back, into Microfinance", Otero Maria argues that microfinance plays three key roles in development strategy: client, institution, and financial system level.[86]

The first point, microfinance's main objective is to alleviate poverty at a client level. MFIs require breaking a cycle of poverty for people living in slums, lacking access to basic services (health, education, and infrastructure) and provide essential skills to enter mainstream economy. Microfinance enables poor clients access to productive capital, basic needs, and human capital to get out of the poverty cycle.[87] Many of them are women who poorly trained, and the poor clients also have no access to clean sanitation. Once natural disasters hit in developing countries, the poor people would be affected the most. In addition, rural clients tend to be poor, so opportunities for urban employment are hard to get to. In fact, many work activities just create the enough cash to survive.[88] Many rely on their children for work and suffer from the cost of sending them to school. Hence, microfinance requires satisfying their shortage of material capital, capital investment, and productive capital as well as an attempt to establish assets and create wealth (basic needs) among the poor clients.[89] The client approach claims that promoting local organizations, democratic systems, and encouraging human rights

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[85]Otero Maria.1999. Page 1.
[86]Otero Maria. "Bringing development back, into microfinance." Journal of Microfinance/ESR Review 1, no. 1 (1999): Page 10.
[87]Otero Maria.1999. Page 10.
[88]Otero Maria.1999. Page 10.
[89]Otero Maria. "Bringing development back, into microfinance." Journal of Microfinance/ESR Review 1, no. 1 (1999): Page 11.

enable the poor to get out of the poverty cycle, such as reaching productive capital. That is, microfinance is an essential tool to reduce their level of weakness.[90]

Second, microfinance and development are linked at the institutional level, which this paper refers to commercialization and transformation. Microfinance desires to create private institutions to provide financial services with the poorest people, and commercial MFIs become part of the infrastructure of the nations.[91] In other words, these MFIs are circulation channels for providing services that the poor clients need. In fact, this creation of distribution channel toward the poor clients is one of the hardest challenges governments face. However, the lack of effective infrastructure or microfinance's distribution channel drives the country to low economic growth. Hence, in the situation, microfinance offers to establish private, sustainable institutions dealing with wider range of financial services to the poor.[92] The sustainability of MFIs is really important to increase the country's economic growth. If MFIs are untrustworthy in terms of financial capital, their quality of services decrease over the long term, they become temporary financial services for poverty alleviation and development strategy. Therefore, In order to attain self-sufficiency in their operations, MFIs need to create a link between commercial microfinance and development.[93]

The final junction between microfinance and development breaks out at a financial system level in a country, which this paper refers to regulation and supervision of MFIs.[94] This intersection will achieve once MFIs become a regulated institution, as part of the country's

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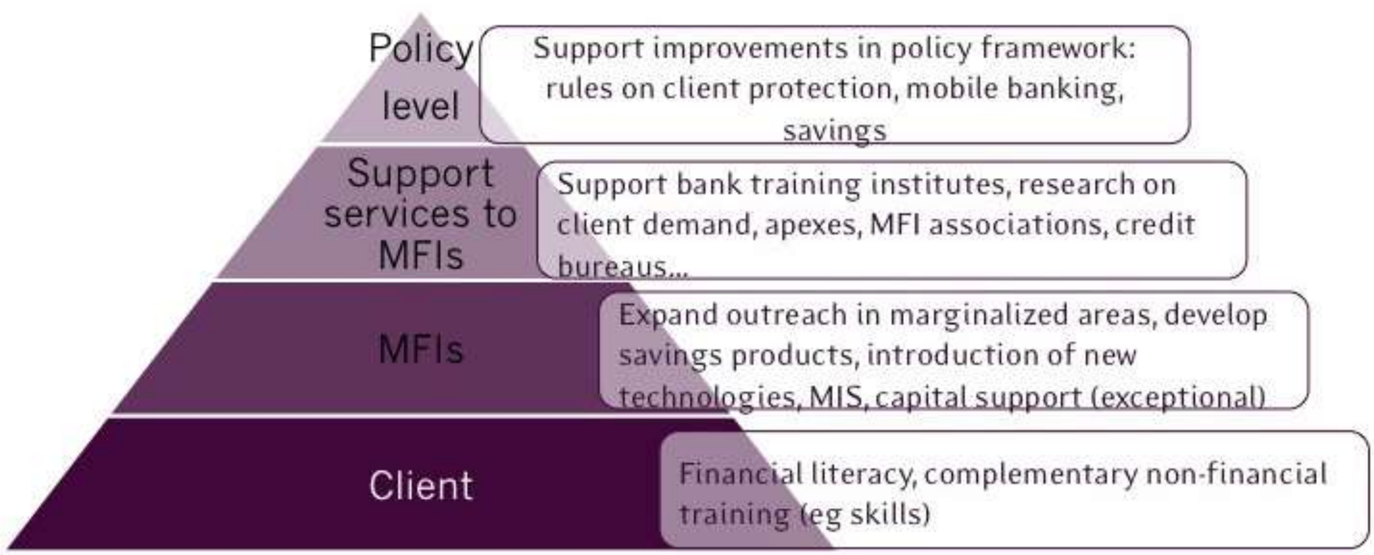
[90]Otero Maria.1999. Page 11.
[91]Otero Maria.1999. Page 11.
[92]Otero Maria.1999. Page 12.
[93]Otero Maria.1999. Page 11.
[94]Otero Maria.1999. Page 12.

financial system. It is really important to address healthy financial systems that have played key role in sustainable development. This approach also refers to financial sector development and the reform should be a priority in all developing states.[95] Once these MFIs become regulated institutions, they are able to access more capital markets and private funds to invest their micro lending, which enable them boost reaching the number of poor people.[96] It has led to capturing their savings, providing other essential financial services to poor and accessing another source of capital which is deposits. Hence, MFIs has encouraged the creation of a wider and deeper financial system in a country, which has no restriction of capital and no dominance of microfinance sector by a few group or individuals. The healthy financial system becomes possible once commercial MFIs can manage risk effectively on their own and avoid systemic risk to the system. Improvement and reforming of the country's financial sector must be a priority in all developing countries.[97]

Figure 1.[98]



[95]Otero Maria.1999. Page 11.
[96]Otero Maria.1999. Page 13.
[97]Otero Maria.1999. Page 13.
[98]ACP/EU. Microfinance vision. http://www.acpeumicrofinance.org/en/history/vision

According to ACP Secretariat funded by the Europe Union (See figure 1), characterizes the three key elements: client, institution (Support services to MFIs), and financial system level (Policy level), which I described above. The three analysis levels address key point to create the financial infrastructure and distribute wealth and resources among the poor people.[99] Therefore, Otero believes that these three levels must perform well to make microfinance a powerful development tool for poverty alleviation.[100]

Using the three levels of analysis framework, next section will analyze and evaluate two commercial microfinance industries, Bolivia and the Philippines. Institutional level has been highly successful in Bolivia, but other two levels have missed its marks. In fact, the lack of effective regulation and supervision lead to a microfinance crisis in the late 1990s, and the clients suffered from over-lending issues. On the other hand, the commercial microfinance market in Philippine represents a cohesive policy approach that addresses all three levels are. The Central bank of the Philippines with the Asian Development Bankhas set a policy level framework for regulating microfinance institutions with having a wide range of informal, semi-formal, formal MFIs, and commercial banks As a result, Philippines overall performance has ranked one of the best practice models for poverty alleviation in terms of business environment and regulatory framework.

[99]Otero Maria.1999. Page 13.
[100]Otero Maria.1999. Page 14.

Background of Case Study: Features of Microfinance in Asia and the Latin America

> This is not charity. This is business: business with a social objective, which is to help people get out of poverty. - Muhammad Yunus

The two cases being analyzed in this paper will be liberated commercial microfinance industry in Boliviaandcommercial microfinance sector in the Philippines with alegal microfinance system and regulatory framework. Both countries have features in common with each other: "commercial orientation."[101]These countries had subsidized micro-lending model and strong government interventions in financial market before, but they recognized the inefficiencies and ineffectiveness of these microfinance systems. As a result, they started rebuilding the financial system for more commercial development and poverty alleviation.[102]

Even though both countries have commercial orientation, the microfinance sector has progressed in Asia and the Latin America under different economic conditions and political situations. For instance, according to this table 1,[103] the data illustrates that Latin America MFIs

	Average Loan Balance per Borrower ($US)	Average Saving Balance per Saver ($US)
Africa	228	105
Asia	**195**	**39**
Eastern Europe/Central Asia	590	N/A
Latin America	**581**	**741**
Middle East/North Africa	286	N/A

[101]Weiss, John, and Montgomery Heather. "Great expectations: Microfinance and poverty reduction in Asia and Latin America." Oxford Development Studies 33, no. 3-4 (2005): 391-416.
[102]Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 1.
[103]Microbanking Bulletin Issue #9, July 2003

focus on more financial viability. In other words, by comparison with Asia, scholar Rutherford argues, “The Bolivia microfinance intervention was typically urban rather than rural, less concerned with poverty and more focused on micro-enterprise.” It targeted the ‘economically active poor’ people with established businesses that needed capital to grow. From the start, Bolivian microcredit was itself seen as a business, potentially as a branch of commercial banking.”[104]On the other hand, another data shows that Asian MFIs have one of the highest of breadth (number of clients) and depth of outreach (poverty clients).[105] According to the Microfinance information exchange (MiX), the Philippines is clearly among the top leaders all over the world in reaching down to its poorest citizens with financial services.[106]

This paper defines the lack of an effective regulatory framework is the reasonwhy Bolivian commercial microfinance sector has had the microfinance crisis in the late 1990s, while the Philippines’ commercial microfinance industry has been successful, enabling the regulatory framework with the Asian Development Bank. Both countries made the liberalization and transformation success, but the regulatory framework was a significant element for sustainable development of commercial sector and poverty alleviation. Therefore, the first case study analyzes the performance of Bolivian commercial microfinance industry when Bolivia underwent a major economic and microfinance crisis as well as evaluates the performance of

[104]Rutherford, S. “Microfinance’s evolving ideals: how they were formed and why they’re changing”, paper presented at ADBI Annual Conference, Microfinance in Asia: poverty impact and outreach to the poor, Tokyo, (2003).

[105]Weiss, John, and Montgomery Heather. "Great expectations: Microfinance and poverty reduction in Asia and Latin America." Oxford Development Studies 33, no. 3-4 (2005): 391-416.

[106]Weiss, John, and Montgomery Heather. "Great expectations: Microfinance and poverty reduction in Asia and Latin America." Oxford Development Studies 33, no. 3-4 (2005): 391-416.

commercial microfinance institutions, using the three level of analysis framework. The second case study will analyze how the Philippines has liberated the microfinance industry. I will then evaluate the importance of regulatory framework by state government andthe Asian Development Bank has had positive impact on development of commercial microfinance sector in the Philippines in terms of the three levels of analysis framework.[107]

Case Study: Bolivia

In recent years, microfinance services have highly progressed by MFIs the outreach of the financial system to many poor people who would be normally excluded traditional financial institutions in Latin America, especially Bolivia.[108]Bolivia is officially known as the Plurinational state of Bolivia located in central South America.[109]The main economic activities include fishing, agriculture, forestry, mining, and manufacturing, and the Bolivian populations are estimated at 10 million people.[110]Agriculture accounts for 9.6 percent of the total GDP while industry accounts for 38.3 percent and services sector 52.1 percent (2012). 49.6 percent people live in below poverty line (based on percent of population living on less than the international standard of $2/day).[111] In the international development community, Bolivia has been considered as the best practice model for commercial microfinance. Bolivia is well known for

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[107]Charitonenko, Stephanie, and S. M. Rahman. "Commercialization of microfinance." Manila, Phillipines: Asian Development Bank (2002).

[108]Weiss, John, and Montgomery Heather. "Great expectations: Microfinance and poverty reduction in Asia and Latin America." Oxford Development Studies 33, no. 3-4 (2005): 391-416.

[109]"The world fact book: Bolivia". Central Intelligence Agency. https://www.cia.gov/library/publications/the-world-factbook/geos/bl.html

[110]"The world fact book: Bolivia". Central Intelligence Agency. https://www.cia.gov/library/publications/the-world-factbook/geos/bl.html

[111]"The world fact book: Bolivia". Central Intelligence Agency. https://www.cia.gov/library/publications/the-world-factbook/geos/bl.html

successful MFIs that have transformed from their original status as NGOs into commercial microfinance institutions.[112]For example, the first and best-known commercial MFI is BancoSol, which established in 1992 by a NGO PRODEM and other investors. These commercial entities contributed to boost commercial microfinance industry operating on commercial principles though the mid 1990's. This Bolivia's experience led microfinance sector to a new direction in the 1990s and caused the rapid growth of commercial MFIs to a level that made the market for prime urban microfinance clients and entry of consumer lending.[113]

Modernizing the Financial System in Bolivia

Bolivia's initiation of commercial microfinance approach has started after a period of hyperinflation in the mid-1980s that had caused major financial and economic instability.The inflation was the most horrible in Latin America history and highest in world history.[114]For example, during a year period between August 1984 to August 1985, prices kept up by 20,000 percent, and while the final month of the inflation, the prices surged 60,000 percent, including GDP fell by 18 percent in 1985. In order to control the inflation, a new government's comprehensive stabilization program was enforced on August 29, 1985.[115] As a result, within 10 days the hyperinflation concluded, and the prices went down as well. The stabilization program contained macroeconomic policy, such as fiscal reform, trade liberalization, internal price

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[112]RhyneElisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): 114.
[113]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 114.
[114]Sachs, Jeffrey D. "The Bolivian hyperinflation and stabilization." (1986). Page 1.
[115]Sachs, Jeffrey D. "The Bolivian hyperinflation and stabilization." (1986). Page 1.

decontrol, and privatization of public enterprises.[116]In addition, the reformation aimed to restore the confidence disappeared during Bolivia's 1984 -1985 hyperinflation, which left the overall Bolivian banking sector with only US$60 million in outstanding loans.

The Bolivia's reform of financial system had a significant role to encourage Bolivian state's development because single individual, business group and family occupied banking sector in Bolivia. Furthermore, donor and government interventions in microfinance had caused market failures.[117] This led to insufficiencies and inefficiencies for economic development. Hence, the Bolivian financial market was liberated to modernize the financial sector with inflation control and setting a favorable condition for commercial entities into the financial market.[118] For instance, the liberalization of microfinance sector included closure of government-subsidized banks, removal of control over interest rates, and other government interventions.[119]In addition, the new government modified the legal framework for the banking system and provided independence from political control, as well as removed undercapitalized banks from the financial marketto attract wide range of business entities for private sector, consolidating ineffective state-own banks.[120]The Bolivian government finally decided to allow foreign

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[116]Sachs, Jeffrey D. "The Bolivian hyperinflation and stabilization." (1986). Page 4.
[117]Navajas, Sergio, and Mark Schreiner. Apex organizations and the growth of microfinance in Bolivia.Rural Finance Program, Department of Agricultural, Environmental, and Development Economics, Ohio State University, 1998.
[118]Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 1.
[119]Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 12.
[120]Sachs, Jeffrey D. "The Bolivian hyperinflation and stabilization." (1986). Page 4.

commercial banks to enter alone or local partners in the financial market in Bolivia due to the lack of supply and equity capitals.[121]

As a result, these reformations took depositors back into the financial system. For instance, the total amount of outstanding loans reached US$4.9 billion at the end of 1999 in comparison with a few million dollars in 1985.[122] The entry of foreign commercial banks and private entities increased so much competition by providing lower interest rates. Microfinance has become an important part of the financial sector, and some MFIs have provided their services with large number of people more than mainstream financial institutions.[123]Hence, their motivation toward the liberated microfinance industry started due to the hyperinflation, and it led to massive impact on microfinance sector as well.[124]Following the key elements why the Bolivian microfinance sector has had so much commercial development in terms of the liberalization.[125]

- Liberalizing interest rates
- Closing state banks
- Permitting financial institutions to accept deposits in foreign currency

121Rhyne Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 115.
122Rhyne Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 115.
123Loubière, Jacques Trigo, Patricia Lee Devaney, and Elisabeth Rhyne. "Supervising & regulating microfinance in the context of financial sector liberalization." Report to the Tinker Foundation (2004). Page 1.
124Loubière, Jacques Trigo, Patricia Lee Devaney, and Rhyne Elisabeth. "Supervising & regulating microfinance in the context of financial sector liberalization." Report to the Tinker Foundation (2004). Page 1.
125Loubière, Jacques Trigo, Patricia Lee Devaney, and Rhyne Elisabeth. "Supervising & regulating microfinance in the context of financial sector liberalization." Report to the Tinker Foundation (2004). Page 11.

- Instituting a universal bank system

These reformations provided a significant basis for the development of commercial microfinance sector.Responding to the liberalization, non-profit entities (NGOs), such as Prodem, FIE and ProCredito started to provide credits to micro entrepreneurs.[126] Then, commercial banks were able to join in the field because the Bolivian financial regulator the Superintendencia de Bancos y EntidadesFinancieras (SBEF) changed from traditional focus to new type of policy framework, which was becoming more flexible requirements for loan collateralization.[127]

Performance of a Commercial MFI: BancoSol

In Bolivian microfinance sector, formal and private financial institutions have provided most microfinance services. The Bolivia's financial sector reform has encouraged commercial MFIs, which were originally NGOs with donor support to enter the financial market.[128] These transformed MFIs enable Bolivian financial sector as one of the biggest microfinance market in the world. In other words, the process of commercialization and transformation (from NGOs to commercial institutions) has played the most significant role for Bolivian commercial microfinance movement.[129]The formalization of the financial system brought the great

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[126]Loubière, Jacques Trigo, Patricia Lee Devaney, and Rhyne Elisabeth. "Supervising & regulating microfinance in the context of financial sector liberalization." Report to the Tinker Foundation (2004). Page 12.
[127]Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 12.
[128]Rhyne Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 115.
[129]Rhyne Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 115.

possibility of more rapid growth. For example, BancoSol demonstrates outstanding success in terms of breadth, depth, quality of outreach and sustainability.[130]

BancoSolidario S.A. (BancoSol) is a private, fully chartered commercial bank. After the earlier success of PRODEM, BancoSol began operations in 1992. They provide microfinance financial services through a profit maximizing strategy of commercial viability as well as BancoSol's shareholders expect profits, and they will reinvest for additional outreach.[131]BancoSol has encouraged its core product "solidarity-group lending" defined as a lending method that small groups borrow the funds collectively and other group members encourage one another to repay.[132] In 1999, the newspaper headlines describe, "BancoSol was the best local financial entity."[133] In the mid-1990s, BancoSol was ranked for the top three of key bank performances: return on assets (5.2 percent in 1998), asset quality, and capacity adequacy.[134]Once BancoSol has maintained incredible performance for both social and profit motive, many MFIs in Bolivia and even international entities tried to counterfeit their business model.[135]

As a matter of fact, BancoSol has an amazing performance in term of the outreach and sustainability. Outreach represents the provision of a wide array of financial services to large

130Gonzalez-Vega, Claudio, Mark Schreiner, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas. "BancoSol: The challenge of growth for microfinance organizations." Microfinance for the Poor (1997): 129-170.

131Gonzalez-Vega, Claudio, Mark Schreiner, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas. "BancoSol: The challenge of growth for microfinance organizations." Microfinance for the Poor (1997): 129-170.

132Armendáriz de Aghion, Beatriz, and Morduch Jonathan. "Microfinance beyond group lending." Economics of transition 8, no. 2 (2000): 401-420.

133Rhyne Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 117.

134Gonzalez-Vega, Claudio, Mark Schreiner, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas. "BancoSol: The challenge of growth for microfinance organizations." Microfinance for the Poor (1997): 129-170.

135Rhyne Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 117.

numbers of the poor. First, the average of the monthly loan portfolios from 1994 to 1995 was US $30 millionin comparison with US $4 million in 1992.[136]That is, in the beginning of 1992 to the end of 1994, BancoSol's portfolio increased about eight times. Second, the portfolio growth had a rapid development in the number of clients with active loans, showing from the 14,300 in 1992 to over 60,000 by 1994. In terms of the number of client and active loans, BancoSol is one of the best performances MFI in Latin America.[137] Third, the rapid development enabled BancoSol set up more its portfolio to many new borrowers, which is 23,510 in 1993 and 30,021 in 1994. With no doubt BancoSol's clients are not among the poorest of Bolivians because the precondition that the poor clients must have operated a business for at least a year before entering for the loan.[138] However, the poor clients were able to never expect to obtain to access to traditional formal financial institutions previously. Thus, BancoSol's main target is economically active poor.

A financially viable MFI produces enough revenue to cover the all costs under its command, and it is able to operate without any subsidies. Furthermore, their equity capital is commercially profitable.[139]According to Yaron's subsidy dependence index, BancoSol has had remarkable

[136]Gonzalez-Vega, Claudio, Mark Schreiner, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas. "BancoSol: The challenge of growth for microfinance organizations." Microfinance for the Poor (1997): 129-170.

[137]Gonzalez-Vega, Claudio, Mark Schreiner, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas. "BancoSol: The challenge of growth for microfinance organizations." Microfinance for the Poor (1997): 129-170.

[138]Gonzalez-Vega, Claudio, Mark Schreiner, Richard L. Meyer, Jorge Rodriguez-Meza, and Sergio Navajas. "BancoSol: The challenge of growth for microfinance organizations." Microfinance for the Poor (1997): 129-170.

[139]Dacheva, Petra. "Commercialization in Microfinance–A Study of Profitability, Outreach and Success Factors within the Latin American Context." (2009).

performance as well, and they are truly self-sustainable.[140]As a matter of fact, BancoSol has been independent from subsidy since 1994. Also, before BancoSol established, PRODEM (PRODEM transferred to BancoSol) had made an important improvement toward self-sustainability, declining from 115 percent in 1988 to 18 percent in 1991. Led by BancoSol, other commercial MFIs, for example, Centro de Fomentoa Iniciativas Economicas (FIE) and Caja de Ahorros y PrestamosLoas Andes also have operated the microfinance services via the commercial orientation.[141]

The Rise of Consumer Credit

In term of poverty alleviation, the primary goal of microfinance is to improve the welfare of poor households via better access to small loans.[142]Comparisons with other MFIs, non-government organizations (NGOs) are essential parts for poverty alleviation in Bolivia because The NGOs tend to become a more poverty-oriented and rural focus rather than other commercial entities, which are the exact opposite. Even though NGOs have dealt with only 17 percent of the total microloan portfolio, some NGOs have grown rapidly and have had 38 percent active microfinance clients.[143] Most of organizations has continued their financial services as NGOs but influenced by commercialization and transformation around them.[144]For

[140]Yaron, Jacob. "What makes rural finance institutions successful?." The World Bank Research Observer 9, no. 1 (1994): 49-70.
[141]Rhyne, Elisabeth, and Robert Christen. Microfinance enters the marketplace. USAID, 1999. Page 8.
[142]Navajas, Sergio, Mark Schreiner, Richard L. Meyer, Claudio Gonzalez-Vega, and Jorge Rodriguez-Meza. "Microcredit and the Poorest of the Poor: Theory and Evidence from Bolivia." World development 28, no. 2 (2000): Page 1.
[143]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 123.
[144]Rhyne, Elisabeth, and Robert Christen. Microfinance enters the marketplace. USAID, 1999. Page 8.

example, due to the Bolivian financial regulator liberated the commercial sector too rapidly, Bolivia also experienced another trends on the financial market, which is consumer lending. It had been growing really quickly than commercial MFIs. Because of their similar loan products, the consumer lenders also targeted the microfinance market.[145]

The rise of consumer credit has led to massive impact on microfinance sector in Bolivia, and this lending methodology was imported into Bolivia from developed world of salaried workers arrived in Bolivia via Chile. The Consumer lenders provide loans of almost same size as microcredit loans very quickly and flexibly.[146] The first large consumer lender in Bolivia was Acceso FFP. They reached a total of 90,000 loans outstanding during first three years even though BancoSol has achieved that numbers of portfolio in the twelve years. This has stimulated other consumer lenders to adapt the business strategy quickly in order to gain market share and the introduction of profit motive.[147] In fact, Bolivian commercial banks also began consumer credit operations using the techniques. Because of the rise of consumer credit, microfinance sector also received the influence of delinquency and over lending.[148]

The consumer lenders enlarged risk via aggressive marketing. They finally began moving into the microfinance sector without altering their method of lending. Instead of adopting lending techniques designed for microenterprises, consumer lenders took advantage of the micro lenders.The technique was so simple: “lure the good clients away from micro lenders by

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[145]Rhyne, Elisabeth, and Robert Christen. Microfinance enters the marketplace. USAID, 1999. Page 9.
[146]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 117.
[147]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 117.
[148]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 123.

offering them larger loans with faster and lower rates."[149] In fact, the consumer lenders thought they would be secure if they targeted clients in a good standing among micro lenders, which low risk strategy to invade the microfinance market. This aggressive method is one of the reason Bolivian microfinance sector has had the crisis.

Table 2. Economic condition.[150]

	1998	**1999**	**2000**	**2001**	**2002**	**2003**
Economic condition						
GNP Per Capita (in current US $)	1070	1023	1016	949	883	870
Real GDP Growth (%)	5.2	0.4	2.4	0.0	2.5	2.6
Investment/GNP (%)	23.8	18.4	17.3	17.0	15.0	12.5
Savings/GNP (%)	16.0	12.5	11.8	12.7	13.4	
Urban unemployment rate (%)	5.3	6.1	6.8	7.3	7.4	8.0

Under the push of structural changes after the hyperinflation, the liberalization allowed many microfinance NGOs transformed themselves into commercial banks or private funds.[151]The Bolivian microfinance sector had attained not only rapid growth but also serious profits with consumer lenders, pursuing highest rates of profit, such as the FFPs ACCESO and FASSIL. The entry of these new players was so rapid without any regulations, and they provided larger loans than commercial MFIs and banks for the purchase of durables products such as Television

[149]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 123.
[150]Marconi, Reynaldo, and Paul Mosley. "Bolivia during the global crisis 1998–2004: towards a 'macroeconomics of microfinance'." Journal of International Development 18, no. 2 (2006): 237-261.
[151]Marconi, Reynaldo, and Paul Mosley. "Bolivia during the global crisis 1998–2004: towards a 'macroeconomics of microfinance'." Journal of International Development 18, no. 2 (2006): 237-261.

rather than business capital.[152] These events finally led to the financial crisis in microfinance industry in Bolivia in late 1999 to 2001. In fact, according to table 2, the microfinance crisis caused serious damage to Bolivian economic development with low economic growth.

Table 3. The number of commercial banks

	1997	1998	1999	2000	2001	2002	2003
Commercial Banks	3185	4023	3786	3174	2769		2827

In addition, the number of commercial banks decreased so rapidly, therefore, both commercial MFIs and poor clients had several issues. For example, Liliana Bottega of Caja Los Andes stated "Acceso and CrediAgil have closed, but the damage has been done to the system. The end of growth in numbers of clients, rising portfolios as micro lenders go up market, the highest delinquency in the history of Bolivian microfinance and dramatic fall of profits."[153]

Client Level: Poverty alleviation

It is true that the clients were able to take advantages of commercial MFI services. For instance, the competition lad to lower interest rates comparison with subsidized micro-lending model in the mid-1980s, as well as enabling them to reach many kind of financial services, such as insurance, payment and management. However, due to the lack of effective regulatory policies, some commercial MFIs pursue high profit motive, operating as loan sharks. In addition, the emergence of consumer lending caused serious issues between borrowers and lenders. As a

[152] Marconi, Reynaldo, and Paul Mosley. "Bolivia during the global crisis 1998–2004: towards a 'macroeconomics of microfinance'." Journal of International Development 18, no. 2 (2006): 237-261.
[153] Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 126.

matter of fact, by 1997 there were nearly 300,000 available microfinance loans in Bolivia, with the number of consumer loans also approaching that level.[154]MFIs and their investors are able to easily shift from micro lending to loan-sharking and drove Bolivians' microfinance market to be chaos. In 2000, over 400,000 to 1 million microenterprise loans were available. Due to taking loans form several institutions at once, there was no way to make sure how many MFI's loan existed at the time. The total active loan portfolio was US$379 million, and it occupies over 10 percent of the overall portfolio in the Bolivian financial sector. The most of MFIs provided loans without any external subsidies.[155] The clients also were able to access credit easily and quickly from many institutions at a time as "the logic of clients is that they will earn more by investing more. Multiple loans have even become a status symbol."[156]In worst cases, clients began bicycling loans to pay off another loans."[157] In other words, the clients reduced their risks by widening their choices.

This behavior seriously damaged constructed culture of repayment in microcredit. In fact, a study demonstrated that 28 percent of clients and 34 percent of the portfolio accompanied with more than one institution. When the microfinance industry was reaching impregnation in 1999, Bolivia suffered the serious economic setback after some year of progress starting with Brazil and extending throughout South America. As a result, Bolivian

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[154]Marconi, Reynaldo, and Paul Mosley. "Bolivia during the global crisis 1998–2004: towards a 'macroeconomics of microfinance'." Journal of International Development 18, no. 2 (2006): 237-261.
[155]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 123.
[156]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 123.
[157]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 123.

economic market experienced massive social unrest, including mass protests claiming human basic needs, such as water and electricity. Commercial MFIs tried to get their money out from clients.

Institutional Level: Commercialization and Transformation

With no doubt increasing competition and commercialization have been very effective for MFIs and their clients because these elements have led to lower prices, quicker and easier services, and a variety of new products to customers. The liberalization created the space for development of microfinance. For instance, compare with other commercial banks all over the world, BancoSol has had excellent performance in terms of outreach and financial sustainability. In realities, by the mid to late 1990s, interest rates on Bolivian microloans were the lowest in Latin America.[158]The commercial MFIs in Bolivia have encouraged universal funds for poor micro entrepreneurs. This major contribution must not be forgotten as the commercial microfinance challenge to help the poor. However, when the competition and commercialization in microfinance lose the balance of power between lenders and borrowers due to the lack of effective regulatory framework, many serious problems will come out. For example, during 1999 and 2000, none of the MFIs grew as they had in the past. BancoSol lost their 25 percent clients, and they return on equity dropped from 29 percent in 1998 to 4 percent in 2000.[159] In addition, Prodem lost 45 percent clients during the two years.As FOSSIL loan officer stated, “Before, the institutions selected clients. Now the client selects the

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[158]Loubière, Jacques Trigo, Patricia Lee Devaney, and Elisabeth Rhyne. "Supervising & regulating microfinance in the context of financial sector liberalization." Report to the Tinker Foundation (2004).
[159]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 123.

institution."[160] In other words, when clients have a choice, they choose the lenders, which offer the cheapest rates. Hence, this paper defines when commercial MFIs has provided financial services with a effective regulatory framework and legal policies to restrain such as the consumer credit, both commercial MFIs and the clients are able to take advantages. Therefore, commercial MFIs industry must require policy level (regulatory framework) for sustainable development of MFIs as well as poverty reduction.

Financial System Level: Regulation and supervision

The Bolivian financial regulator, SBEF adept the new policy framework, which enables MFIs reach more flexible for their loan portfolio with lower capital requirement, and this was key factor that Bolivian microfinance sector went to chaos. Because they liberated too rapidly, the emergence of consumer credit happened.[161] In realities, the members of microfinance community then concerned about the consequences of growing delinquency among the consumer lending.[162] The superintendence of Banks published regulations in early 1999 to prevent the fall of consumer credit. The most significant regulation limited the clients' total debt service to 25 percent of salary. As a result, some consumer lenders, for example, FASSIL reduced the portion of consumer lending and switched into microfinance industry.[163]

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[160]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 126.
[161]Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 12.
[162]Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 12.
[163]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 126.

However, the regulation came too late in the financial market. By mid 1999 the consumer lending movement crashed. The two largest consumer lenders, Acceso FFP and CrediAgil had huge debt at the time, and the BSP finally intervened directly in those institutions. In fact, at the end of 1998, Acceso had had eighty-eight thousand clients with the portfolio of US$93 million and delinquency of 19 percent. In 2000, Acceso had only eighty-four hundred active clients and a portfolio of US$5.4 million.[164]The consumer-lending model could be working in middle class Chile but not suited in Bolivia. They failed to recognize that their techniques lacked essential element that made lending to micro entrepreneurs work.

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[164]Rhyne, Elisabeth. "Commercialization and crisis in Bolivian microfinance." The Commercialization of Microfinance, Drake D, Rhyne E (eds). Kumarian Press: Bloomfield (2002): Page 126.

Case Study: The Philippines

The Philippines is officially known as the Republic of the Philippines in a Southeastern Asia and seventh-most populated country in Asia.[165] Agriculture stands for 11.8 percent of the total GDP while industry accounts for 31.1 percent and services sector 57.1 percent. The Philippines has a population of about 105 million, has been growing at 1.7% per year. Some 26.5 percent people live below the poverty line. 18.5 percent of all urban families are poor as well as around 40 percent of rural families stay in poverty line.[166]Unemployment rate keeps 7 percent. The Philippines' poverty trends have been dropping during the past decade, but some urban areas are still into cycle of the poverty.[167]

Similar with Bolivia, The Philippines had a long history of subsidized micro-lending system and strong government interventions in the financial market.[168] Before 1997, 86 subsidized directed credit programs existed by government non-financial agencies. However, they recognized the inefficiencies and ineffectiveness of these microfinance systems, so the government has been working to create a policy environment and legal regulatory framework for sustainable development of MFI, such as interest rate deregulation and allowing commercial banking.[169] As a result, the Philippines have a various range of informal, semi-formal, formal MFIs and NGOs,

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165The world factbook. "The Philippines." Central Intelligence Agency.
https://www.cia.gov/library/publications/the-world-factbook/geos/rp.html

166The world factbook. "The Philippines." Central Intelligence Agency.
https://www.cia.gov/library/publications/the-world-factbook/geos/rp.html

167Van Greuning, Hennie, Joselito Gallardo, and BikkiRandhawa. "A framework for regulating microfinance institutions." World Bank Policy Research Working Paper 2061 (1998).

168Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 12.

169Charitonenko, Stephanie, and S. M. Rahman. "Commercialization of microfinance." Manila, Phillipines: Asian Development Bank (2002). Page 2.

providing many financial services to poor people with the legal systems and regulatory framework.[170]For example, in 1997, the government issued a national strategy for microfinance sector, which addressed the goal of establishing a financially viable and sustainable market via the adoption of market based-principles, such as changing to market-based interest rates and no government interventions.[171]

There were four main principles as the government new policy framework. First, the government enabled policy environment that encourages the increased participation of the private sector in microfinance sector.[172] Second, "market-oriented financial and credit policies." Third, non-government interventions in implementation of credit and programs. Fourth, the policy facilitates the greater role of the private sector. These principles were just managed as a milestone for policies and regulatory framework in order to help commercial MFIs attain their goals of outreach and sustainability.[173] As a result, Commercialization of microfinance is strongly advocated with demand by the clients for sustainable expansion of outreach. Also, the Philippines government acknowledged various advantages of commercialization for providing microfinance services. For example, Executive order No. 138 in 1999was proclaimed that government subsidized credit programs to be transformed to MFIs by February 2002.[174]

170Charitonenko, Stephanie, and S. M. Rahman. "Commercialization of microfinance." Manila, Phillipines: Asian Development Bank (2002). Page 2.
171Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 15.
172Habaradas, Raymund and Umali Mar Andriel. "The microfinance industry in the Philippines: Striving for financial inclusion in the midst of growth." Center for Research & Development. 2013. Page 4.
173Habaradas, Raymund and Umali Mar Andriel. "The microfinance insutry in the Philippines: Striving for financial inclusion in the midst of growth." Center for Research & Development. 2013. Page 4.
174Charitonenko, Stephanie, and S. M. Rahman. "Commercialization of microfinance." Manila, Phillipines: Asian Development Bank (2002). Page 10.

Then, under the general banking of 2000, the Bangko Sentralng Pilipinas (BSP: Central Bank of the Philippines) published rules and regulations, which promoted participations of commercial MFIs for development and growth of microfinance in the Philippines.[175] For example, the bank law of 2000 specialized a structure of licensed financial intermediaries and financial regulation provided proper space for commercial banks to have foreign equity (allowed 40 percent of the voting stock of a bank).[176]In addition, some section of the general banking law 2002 adjusted to elaborate appropriate regulation and supervision of commercial microfinance operations. As a result, in 2000, there were almost 2,000 microfinance institutions, including commercial MFIs, rural banks, cooperatives and NGOs provided finance services to many clients.[177]

Table 4.[178]

Overall microfinance business environment ranking – Top 10 countries, 2012
Weighted sum of category scores (0-100 where 100=most favourable)

Rank	Country	Score	Change (from 2011)
1	Peru	79.8	+12.0
2	Bolivia	71.8	+7.1
3	Pakistan	67.4	+4.6
4	Philippines	63.3	+4.8
5	Kenya	62.8	+2.5
6	El Salvador	56.3	- 2.5
7	Colombia	56.0	-
8	Cambodia	55.7	+4.8
9 -10	Mexico	53.6	-
9 -10	Panama	53.6	-

175Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 15.
176Gallardo Joselito. "A Framework for regulating Microfinance Institutions. The experience in Ghana and the Philippines." The World Bank. Financial Sector Development Department. 2001. Page 20.
177Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 16.
178Habaradas, Raymund and Umali Mar Andriel. 2013. Page 4.

Due to the creation of policy environment and regulatory framework for commercial MFIs, the Philippines has had powerful commercial oriented MFI model, having hybrid combination of various MFIs such as NGOs, semi-formal, rural banks and cooperatives. As a matter of fact, in 2012, the Philippines ranked No.4 in the world in term of microfinance business environment (see table 4). Also, the Philippines microfinance sector has grown over the past decade. According to table 5, the number of active borrowers boosted almost 25 percent from 2.88 million at the end of 2009 to 3.6 million in 2011, as well as outstanding loans increased by 25 percent during two years.[179] In terms of active borrowers, NGOs stood for 68 percent in 2011, and banks accounted for around 29 percent. Therefore, the Philippines' microfinance services have contributed for poverty alleviation.

Table 5.[180]

Microfinance outreach, loans, and savings (2005, 2007, 2009, 2011)

Selected indicators	2005	2007	2009	2011
No. of active borrowers ('000)	1,508	2,143	2,887	3,600
Banks	597	779	883	1,032
NGOs	839	1,353	1,985	2,478
Cooperatives	72	11	19	90

[179] Habaradas, Raymund and Umali Mar Andriel. "The microfinance industry in the Philippines: Striving for financial inclusion in the midst of growth." Center for Research & Development. 2013. Page 7.
[180] Habaradas, Raymund and Umali Mar Andriel. "The microfinance industry in the Philippines: Striving for financial inclusion in the midst of growth." Center for Research & Development. 2013. Page 7.

The Asian Development Bank: Microfinance Development Program

The Asian Development Bank (ADB) is a regional development bank constituted in August 1966 to facilitate economic development of countries in Asia. Headquarters locates in Manila, the Philippines. The bank is a part of members of the United Nations Economic and Social Commission for Asia and the Pacific (UNESCAP). ADB was framed similar with the World Bank and has almost same weighted voting system, which votes are separated with members.[181] Both Japan and the United States keep the largest proportions of shares each at 12.78 percent, and China holds 5.45 percent as well as India retains 5.36 percent.

The ADB agreed the microfinance development program (MDP) in 2005 in order to support microfinance sector with the government of the Philippines and achieve the Millennium Development Goals.[182] To accomplish this, the goals of program were organized to "enhance the enabling policy and regulatory environment to promote market efficiencies and a better outreach of microfinance services to the poor at competitive prices." Second, "build viable microfinance institutions". Third, "Strengthen regulatory and supervisory capacity and oversight for the microfinance sector." Fourth, "Increase financial and consumer protection for users." In other words, the ADB tried to create regulatory framework for self sustaining MFIs, as well as focusing on consumer protection.[183]

The program was completed in October 2009, and the performance program overall was rated as highly successful.In the microfinance development program, BSP with the ADB issued the

[181]Asian Development Bank. http://www.adb.org/about/main
[182]The Asian Development Bank. "The Philippines: Microfinance Development Program. Performance Evaluation Report. " 2012. Page 11
[183]The Asian Development Bank. "The Philippines: Microfinance Development Program. Performance Evaluation Report. " 2012. Page 11.

regulatory framework for sustainable microfinance systems. For example, on December 2005, Circular No. 505 allowed microfinance banks to establish branches anywhere in the country under the criteria and framework set by BSP. They also promoted electronic banking to facilitate electronic payment transactions.[184] In addition, Cicular No. 542 included the rules and regulations on consumer protection for electronic banking. Then, on January 2006, they issued Circular No. 2, mentioning NGOs requires to show their operations, so BSP was able to understand their overall performance to prevent market failure. Also, The ADB program established performance standards for MFIs with government regulatory agencies and MFI associations. Hence, the ADB tried to create public policy and regulatory framework for MFIs operations with the BSP. The program reached 2.1 million borrowers with rated highly successful, including housing loans and micro insurance, mobile banking services.

Table 6.[185]

Regulatory framework and practices – Top 13 countries, 2012
(Weighted 50% in the overall index)

Rank	Country	Score	Change (from 2011)
1 – 2	Peru	80.0	+10.0
1 – 2	Philippines	80.0	+5.0
3 – 5	Kenya	75.0	+5.0
3 – 5	Pakistan	75.0	-
3 – 5	Uganda	75.0	-
6 – 7	Bolivia	70.0	+5.0
6 – 7	Cambodia	70.0	-
8	Paraguay	65.0	+5.0
9 – 13	El Salvador	60.0	-5.0
9 – 13	Kyrgyz Republic	60.0	-
9 – 13	Mongolia	60.0	-
9 – 13	Rwanda	60.0	-
9 – 13	Tanzania	60.0	-

184The Asian Development Bank. "The Philippines: Microfinance Development Program."Performance Evaluation Report. 2012. Page 11.
185Habaradas, Raymund and Umali Mar Andriel. "The microfinance industry in the Philippines: Striving for financial inclusion in the midst of growth." Center for Research & Development. 2013. Page 5.

According to table 6, the data illustrates the Philippines has kept to rank highest along with Peru in the world for the best practice of regulatory framework.

Client Level: Poverty alleviation

The Philippines is clearly one of the best leaders in the world, reaching down to the poorest people.[186] In 2011, they had around US $600 million in microfinance loans and 3.2 million active micro borrowers.[187] The average loan size is under US $200 in comparison with Bolivia's under US $700. Thus, the micro lendingis favorable reaching down to the poorest Filipinos.The average of deposit size is under US $100 even though the Latin America countries have the average of US $740. Also, in terms of total active borrowers, NGOs have excellent performance that accounts for 68.82 percent in 2011 since banks just accounts for 28.67 percent. Thus, the Philippines has had one of the best hybrid of the business entities and non-profit organizations.[188]

The ADB approach to poverty alleviation has had positive impacts on the Philippines industry as well. They promoted electronic banking to encourage electronic payment, which enables both lenders and borrowers save the operation costs. In addition, the ADB with BSP emphasized applying borrowers protection so that the Philippines has never got serious over-lending issues like Bolivia. Thus, this paper defines that the Philippines microfinance sector, including commercial entities, reaches down to the poorest of clients.

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[186]MIX. "The Philippines market profile." http://www.mixmarket.org/mfi/country/Philippines/report
[187]Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 16.
[188]Habaradas, Raymund and Umali Mar Andriel. "The microfinance industry in the Philippines: Striving for financial inclusion in the midst of growth." Center for Research & Development. 2013. Page 7.

Institutional Level: Commercialization and Transformation

The Philippines has market-oriented principles in the microfinance sector, which is significantly self-funded via deposits, having almost US $400 million in deposits from 4.3 million depositors.[189] Before 1997, 86 subsidized directed credit programs were carried by government agencies. After the liberalization under the general banking law and the ADB approach, the government transformed those programs to MFIs, especially private sector. As a matter of fact, over 2,000 MFIs were providing microfinance services to several million clients in 2000. Thus, the process of transformation and commercialization has been highly successful with effective regulatory framework and legal systems, for example, general baking law 1997 and 2000. However, in terms of access, the BSP reports that 609 out of 1,634 municipalities (37.3 percent) still do not have a banking office in the end of 2011.[190]These 609 municipalities are populated by nearly 14 million clients, which accounts for 15.2 percent of the total population.[191] Therefore, the Philippines' market-oriented approach is still on the way to achieve several million clients to access to banks and other MFIs.

Financial System Level: Regulation and Supervision

The Philippines globally ranked amongst the top microfinance markets in terms of policy, regulatory framework and business environment.[192] In fact, the Philippines government and the

189Robert C. Vogel. "Microfinance Regulation: lessons from Bolivia, Peru and the Philippines." Multilateral investment fund (MIF). 2012. Page 16.
190Habaradas, Raymund and Umali Mar Andriel. "The microfinance industry in the Philippines: Striving for financial inclusion in the midst of growth." Center for Research & Development. 2013. Page 5.
191Habaradas, Raymund and Umali Mar Andriel. "The microfinance industry in the Philippines: Striving for financial inclusion in the midst of growth." Center for Research & Development. 2013. Page 5.
192MIX. "The Philippines market profile." http://www.mixmarket.org/mfi/country/Philippines/report

central bank have played a significant role, establishing the legal system with the Asian Development Bank. As a result, the BSP liberated the branching of banks related of microfinance and promoted electronic banking system with consumer protection under the objective "enhancing policy and regulatory framework." Also, the national Anti-Poverty Commission (NAPC) published an "industry advisory containing guidelines and model business development services manuals" in order to build viable MFIs.[193] Overall, these programs were evaluated highly successful. Thus, the Philippines' financial system level approach has worked really well, and it leads to positive effects on client and institutional levels as well.

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[193]Habaradas, Raymund and Umali Mar Andriel. "The microfinance industry in the Philippines: Striving for financial inclusion in the midst of growth." Center for Research & Development. 2013. Page 12.

Analysis

Both counties Bolivia and the Philippines had nearly a parallel microfinance structure previously, defined asgovernment subsidized micro-lending model, and the industries were supported by government interventions. However, the governments recognized that these subsidized programs were one of the greatest obstacles to sustainable microfinance development because it caused institutional inefficiencies, less innovative and disappointing natural market mechanisms. Also, it had become less clear how donor subsidies are able to assist the operating advances in the microfinance industry. As a result, the governments made these industries more commercial-oriented for more institutional sustainable development for poverty reduction.

Both countries appropriately modernized the financial system, and many NGOs were able to transform themselves into commercial MFIs and private funds, operating as self-sustainable institutions, for example, the converting of a NGO PRODEM into a commercial bank BancoSol in Bolivia. BancoSol has successfully provided sustainable large-scale outreach this paper mentioned in the first case study, and the process of transformation has been very effective and influenced the region development as well. This is one of the great achievements to send poverty to a museum for future generations. After the adaptation of market-driven principles, nevertheless, one country Bolivia had its microfinance market failure, which led to a microfinance crisis. The average of micro-loan size is close to $700, and some commercial MFIs only targeted at economically active poor. On the other hand, the Philippines are clearly among the leaders in the world, reaching down to the poorest of Filipinos, and the average micro-loan size is under $200.

What are the differences between the two countries? Various scholars assert that commercialization itself has critical issues, such as leading to exploitation, indebtedness on some clients and targeting at the less poor people. In realities, issues of microfinance commercialization are featured in nearly every single article since in the mid-1990s due to the rapid growth of commercial sector as international movement. Sound true but it is not. The argument has digressed from the essence of the problem.

The essential distinction between a country making it success or failure is whether the country has effective regulatory framework and policy environment by a state government and central bank for microfinance sector. The final junction between microfinance and development, decision-making at the Policy level strongly affects institutional level and client level. In other words, the growth of commercial MFIs and increased reaching down to the poorest clients is under the control of financial system level. Furthermore, it is true that many countries have limited capability in order to regulate and supervise their financial institutions and systems, plus developing nations usually possess less sufficient policy environments of the formal financial sector. Consequently, the reformation of financial system is the most priority for developing countries to assure systematic stability and protect borrowers.

The regulatory framework then operates at full efficiency to maintain the healthy financial system, which leads to right balance between not only borrowers and lenders but also commercial and non-profit microfinance sector for sustainable development. As a matter of fact, Once these MFIs become regulated institutions under the effective regulation system and policy environment, they are able to access more national and international markets for capital to invest the more funding, which enables reaching down to the poorest people more and more.

Accordingly, this paper defines that commercialization of microfinance is operated successfully only under the effective regulatory framework and policy environment by a state government. Plus, in order to promote greater efficiency and effectiveness, this paper advocates that the state government should cooperate in creating the framework with international organizations, for example, the Asian Development Bank and the World Bank since enabling regulatory framework usually only depend on a country orientation under their features of the distinct, such as institutional capability. Also, some developing countries have a little experience of financial reformation and creating a policy environment in the financial sector. It is really important to keep stable financial system and regulation to prevent the financial crisis from an international point of view. Hence, the cooperating strategy is one of the best solution strategies to create greater regulation and supervision system and establish favorable conditions for commercial microfinance sector.

In the end, Commercialization of microfinance is absolutely necessary step. The most important thing for poverty alleviation is sustainable development, which means "profitable". An institution is impossible to become sustainable until it is commercialized. Subsidy gives temporarily benefit for both institutions and clients like an adrenaline shot but can never get sustainable development for poverty alleviation. It is true that commercialization has various challenges. However, microfinance strongly needs commercialization to satisfy people's latent worldwide demand that would be normally excluded from traditional financial institutions. In fact, there has been strong transition from supply orientation to demand adaptation. MFIs reached down only 25 million people in 2000 but went over 190 million clients in 2012. To achieve greater sustainability, depth, quality and breadth of outreach, commercial-oriented

MFI model with the effective regulatory framework and policy environment is the best practice to send poverty to a museum.

Conclusion

> The difference between transformation by accident and transformation by a system is like the difference between lighting and a lamp. Both give illumination, but one is dangerous and unreliable, while the other is relatively safe, directed, and available.
>
> - Ferguson and Naisbitt

The microfinance revolution has innovatively changed attitudes toward helping the extreme poverty and actually have unparalleled positive influence in poor people's lives. The rapid growth of commercial sector has shownincreased efficiency, sustainability and large-scale outreach but also confronted difficulties and obstacles in some countries. On the one hand, microfinance sector in Bolivia operated accidentlyin the late 1990s as "lighting." The ineffective regulatory framework and supervision system drove the microfinance industry chaos, for example, indebtedness and over-lending on some clients.On the other hand, microfinance sector in the Philippines with the Asian Development Bank worked really well as "a lamp." The country has been at the leading edge of commercial microfinance with allowing the regulatory framework and policy environment. The Philippines has given a crucial insight for sustainable microfinance development; Creating rules and regulation at the policy level is the most significant factor for microfinance poverty alleviation.

Even though innovative financial services are about to embrace the whole world, there has been still no universal-consensus concerning how to create the regulatory framework and supervision system. Consequently, IOs ought to exercise a joint initiative for setting the global common regulatory framework and supervision system as effective poverty reduction strategy.

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