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U. S. AGENCY FOR INTERNATIONAL DEVELOPMENT

MID-TERM EVALUATION OF THE SMALL ENTERPRISE CREDIT (SEC) PROJECT

Contract No. AID 492-0443-C-00-2101-00

FINAL REPORT

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EXECUTIVE SUMMARY

The U.S. Agency for International Development Manila Mission requested for technical and advisory services for a mid-term evaluation of the USAID/Philippines Small Enterprise Credit (SEC) Project. This full report, dated August 14, 1992, presents the results of that evaluation.

PURPOSE OF THE PROJECT AND THE MID-TERM EVALUATION

The SEC Project aims to address the economic problem of generating productive employment and increased income of the people by promoting small- and medium-scale enterprises (SMEs). The Project seeks to contribute to the reduction of constraints to SME growth in the Philippines. These constraints are in the form of policy and regulatory structures that favor large-scale business in urban industrial locations and assistance programs that support the weak SMEs. In response, the Project provides support to SMEs outside the Metro Manila area and is designed to channel financing to viable SMEs for accelerated growth in the sector. The SECP also addresses institutional constraints, particularly the structure of the financial system that leaves the SMEs out of the commercial banking system. The project supports financial institutions (IFIs) in the countryside with medium-term capital for increased lending to support SME growth. Finally, institutional development concerns are part of the project design, with efforts allocated to deposit mobilization, technical assistance and training and markets development. In particular, the deposit mobilization feature of SECP is for building the resource base for sustainable lending by financial institutions while technical assistance and training prepare the bank staff for increased support to SMEs.

The purpose of this mid-term evaluation is to assess the implementation of the SECP after more than one year in operation. The effectiveness and impact of the SECP are evaluated relative to the design of the project both as a financing or liquidity assistance to SMEs and as a rural deposit mobilization tool for building the resource base of financial institutions. The project is also evaluated in terms of the efficiency of the credit delivery mechanism using IFIs. Eventually, the mid-term evaluation would determine whether, on the basis of the results of the SECP, additional funding along certain other new lending directions would be justified. Related questions of implementation of any such expanded SECP-like project implementing entity and possible expansion in the financial institutions serving as vehicles of credit delivery, are resolved in the mid-term evaluation.

"This mid-term evaluation was completed through the assistance of the United States Agency for International Development (A.I.D.). The views, expressions and opinions in this report are the author's and are not intended as statements of policy of A.I.D."

FINDINGS

The overall results of the project in **credit delivery** indicate that the SECP achieved success in terms of: a) increased IFI lending to SMEs; b) the high quality of such increased lending in terms of desirable development of IFI capacities and new SME credit markets; c) development of a number of IFIs into stronger institutions that shall sustain the policies of the SECP in the longer term; and d) delivering to the SMEs the financing suited to their needs.

A significant increase in lending to SMEs was observed after the implementation of SECP, and most significantly among the smaller IFIs. New SME borrowers dominated the expanded credit provided under SMEs, showing SECP's development of a formal credit clientele. The increased lending of IFIs under the Project represents generally acceptable credit risks because the IFIs selected SMEs which are successful and undergoing expansion. This policy is consistent with sustainable future growth in lending by IFIs to the SMEs as envisaged under the Project. The SMEs supported by IFIs are about equally distributed between trading and manufacturing or services, reflecting a balanced sectoral development financing impact on SME beneficiaries due to the project.

The findings of key significance to the SME credit system are three reasons found to explain the increased amount, quality and beneficial impact of SECP relending by IFIs to SMEs.

First, SECP's simplicity in design ensured low transactions costs from the SECP to IFIs. Meanwhile, transactions costs from IFIs to SME borrowers are also low because IFIs know their clients and have the quick decision making characteristics of small organizations. The SECP's liberal design and deliberate selection of "community bankers" reduced transactions costs to ultimately benefit the SMEs probably in much the same way that a direct interest subsidy would, but certainly without the latter's distortionary effects on credit allocation. Second, the ready availability of SEC as a source of term lending to SMEs enabled the IFIs to concentrate their efforts in marketing. The main constraint faced by IFIs remains unavailable long-term financing rather than "high" interest cost of financing. Third, the SECP's design allows lending terms to SMEs to be decided upon by the IFIs. It enables IFIs to search for SME projects whose returns meet the commercial financing terms and whose risks are controlled through prudent loan structuring per each bank's policy. Consistent with its institution-building goal, the SECP did not impede the IFIs' efficiency in SME lending decision process — from search, loan structuring to collection.

Some potential weaknesses in credit delivery were found in the Evaluation. Specifically: a) few borrowers accounted for a significant share of SEC financing, which may have constricted the supply to the smaller SMEs; b) SEC-sourced loans are positioned in the credit market only as short- to medium-term facility, explaining a bias observed among IFIs for financing mainly medium- to short-term SME needs; c) the pricing basis using historical yields needs improvement because of observed cases of temporary mispricing of SEC loans to IFIs, leading to distortions in their demand for SECP loans; and d) strong performer-IFIs are constrained by a credit limit policy of SECP that may need review.

The overall results of the Evaluation in **deposit mobilization and institution building** indicate: a) adequate capacities developed for deposit generation but dependent on IFI resource base; and b) some activities in policy research and training were initiated but on balance are inadequate. Size of IFIs' resources remains the factor determining the the IFI's capacity for refinancing and sustained lending through deposit generation. Larger or fast-growing IFIs: a) have strong presence in their deposit markets; b) have loans portfolios that are supported by adequate levels of deposits; and c) show superior profitability resulting in capital build-up and internal funds generation for sustained lending.

The choice of PBSP to implement the Project at the initial stage was a sound one. The IFIs considered PBSP as effectively discharging its functions. PBSP has competently implemented the guiding policies of the SECP, particularly in giving flexibility to the IFIs in loan origination and use of funds.

CONCLUSIONS

The basis for the success of the SECP can be traced mainly to the design of the Project. It is a design that generally reflects sound credit principles as well as the realities of policy constraints to SME development.

SECP demonstrated that interest subsidies are not needed either by the IFIs or by the SMEs. The reasons are due to: a) the flexibility of the IFIs in lending allows them to choose SMEs which are successful and can pay commercial rates; and b) the segmentation of the credit market which allows IFIs to dominate the SME market and exercise their market power over SMEs in lending rates. Instead, SECP showed that the greater benefits to SMEs can come from lowering the transactions costs to IFIs.

Finally, the SECP established the importance of selecting IFIs in implementing directed credit programs. The Project selected IFIs which are committed to, and are already serving, the development targets-SMEs.

RECOMMENDATIONS

1. Conduct policy studies of the SME credit market to assess the structure of SME credit needs and of special SME credit programs to determine their impact on SMEs and IFI channels.

2. Increase funding assistance with emphasis on allocation to strong SME markets and involving other "community bankers" with strong resource base.

3. Improve credit delivery by reviewing: large sub-loans, the interest rate pricing of IFI loans, and the guidelines on credit limits of IFIs.

4. Institutionalize the achievements of SECP by carrying out the recommended expanded phase of SECP with the Development Bankers' Association of the Philippines as project implementor.

5. Strengthen the implementation of an expanded SECP under DBAP by a new organization that remains designed around the existing project concept but augmented by technical assistance for improved direction and monitoring.

LESSONS LEARNED

The success of an SME credit project is determined largely by the degree of orientation of the project design to the needs of the SMEs and the motivation of the IFIs channels through which credit flows.

When an SME credit project channels financing in areas with strong SME-based local economies, it shall achieve superior development results because in those markets, IFIs face a deeper and more diverse lending market. Given such a strong market, a credit project can subsequently raise its development goals to a higher level.

An SME credit project should search for and use existing institutional capacities that are likely to be present even in a distorted financial system. The IFIs used as channels by SECP have already adapted to the transactions costs of the SME market, thus achieving competitive advantage. For this reason, interest subsidies to IFIs are not necessary to "support" SMEs.

SMALL ENTERPRISE CREDIT PROJECT
MID-TERM EVALUATION REPORT

1.0 SCOPE OF WORK

1.1 PROJECT TO BE EVALUATED

The United States Agency for International Aid (USAID) has commissioned PSR Consulting to conduct a mid-term evaluation of the Small Enterprise Credit Project (492-0443). The SECP is a credit mechanism for Small- and Medium-scale Enterprises (SMEs) using Private Development Banks (PDBs) as conduits. Annex A presents a copy of the evaluation scope of work lifted from the Request for Proposal No. 492-92-010.

1.2 PURPOSE OF THE EVALUATION

The purpose of this evaluation is to assess the implementation of the credit mechanism of the SECP. The major areas of the evaluation are the effects of the credit mechanism on the <u>liquidity</u> levels as well as on the <u>rural deposit mobilization</u> efforts of the IFIs. The other areas of evaluation are as follows:

1. New lending directions
2. Additional project funding
3. Inclusion of rural banks or other thrift banks

At the end of the project, the evaluation shall be able to address the following concerns:

1. Effectiveness and efficiency of the SECP in contributing to the greater IFI lending to SMEs and to the SMEs themselves,
2. Adequacy and cost effectiveness of the private development banks (PDBs) as vehicles to deliver credit to SMEs,
3. Effect of the SECP on the IFIs deposit mobilization efforts,
4. Issues on the delivery or usefulness of credit to SMEs,
5. Measures that should be initiated to strengthen IFI rural deposit mobilization and the delivery of credit to SMEs,

6. Feasibility of expanding accreditation to include other financing institutions engaged in SME lending,

7. Appropriateness and usefulness of adding more funds to the IFI credit mechanism, and

8. Appropriate implementing entity for any additional credit funds channelled through a new set of financing institutions.

1.3 PROJECT BACKGROUND

The Project, which started on September 27, 1989, has three components, namely:

1. An expanded intermediate financial institution (IFI) and lending component for Small- and Medium- Scale Enterprises (SMEs),

2. Research and policy analysis to better understand the constraints facing SMEs, and

3. Training and loan development courses to train bankers and entrepreneurs in SME project lending.

The Philippine Business for Social Progress (PBSP) implements the program while the Development Bank of the Philippines (DBP) acts as trustee of the grant funds.

The grant amount of US$ 13.0 million is distributed as follows:

Credit	US$ 12,000,000
Training and loan development	382,000
Research and policy studies	360,000
Project Administration	108,000
Evaluation	150,000

1.4 PROJECT RATIONALE

A major concern of the Philippines is how to alleviate poverty. One solution is to provide productive employment and increased incomes. However, the growth of the country's labor force continues to grow without a corresponding increase in opportunities for gainful employment.

A key sector to the alleviation of poverty is the SME. Small- and medium-scale enterprises are more labor-intensive than large enterprises, generating more employment per unit of capital than large enterprises. These enterprises are also more resilient to economic changes. The country's economic problems include an underdeveloped SME sector.

Several factors contribute to this situation. Policy and regulatory directions of the government, albeit moving towards promoting SMEs, are still biased for large enterprises. SMEs find it difficult to get financing from formal credit sources. The transaction costs involved make SME financing not attractive to these financial institutions. If formal credit is available, these intermediary financial institutions (IFIs) are usually SMEs themselves. This presents a problem as small and medium IFIs do not have sufficient resources to finance the needs of SMEs. On the other hand, SMEs do not have the necessary track record required by large financial institutions. The limited financing available is limited to short-term financing. There are limited funds for medium- to long-term financing which an SME needs for its expansion.

Previous efforts, especially by the government, to remedy the situation concentrated on directed financing programs. These programs lacked components in institution building and policy reforms needed to enable the banking system to sustain SME financing beyond the program. The SECP plans to do better by following a different strategy. It involves the private sector, largely Private Development Banks (PDBs). First, the SECP provides funds to PDBs with financial constraints to make medium- and long-term funds available for lending. Second, it includes an institution building component through the Project design that encourages mobilization of deposits for SME lending. This is an important component of the program. Banking in the Philippines focuses on asset management or creation of loans. The SECP encourages the increase of a bank's capital base and deposit mobilization (liability management) before any loans are made. In short, the SECP attempts to initiate change in a banking culture dominated by an asset management mindset into a liability management orientation.

The design of the program also includes training and policy analysis modules. Bank staff will be given training to strengthen their skills in loan evaluation and project supervision. On the other hand, policy analysis will be done to identify constraints to the delivery of financial services to SMEs and to recommend actions to eliminate these constraints.

1.5 METHODOLOGY

The following evaluation areas guide the assessment of the Project's implementation:

1. Impact of the Project on IFI credit and deposit generation

2. Benefits of the Project on the SMEs

3. Constraints to credit delivery

4. Indicative directions for the project

The study utilizes the following evaluation methods to make sure the evaluation areas are appropriately discussed:

1. Institutional assessment of the IFIs as implementors and PBSP and DBP as Project management and fund trustee, respectively.

2. Review of the IFI's SEC loan portfolio

3. Review of deposit generation performance

4. Assessment of SME lending market potential and other types of financial institutions that are involved in SME lending

5. Review of SEC Project documents at USAID and PBSP

The activities involved in the implementation of the evaluation methods include: visits to IFIs and SMEs; visits to PBSP and DBP; and study of SECP documents and reports at the Project Management

The evaluation techniques utilized in the study include in-depth evaluation approaches and rapid evaluation techniques.

Annex B presents a detailed discussion of the study methodology. Individual reports on each of the thirteen IFIs visited during the study are given in Annex C.

A logical framework for the evaluation was developed based on the necessary information and evaluation methods required to ensure a comprehensive evaluation of the program. The framework, which served as a guide throughout the evaluation, is presented in the next page.

LOGICAL FRAMEWORK
MID-TERM PROJECT EVALUATION

	EVALUATION AREAS (Key Reference to Section 4: Evaluation Questions in Section C: Scope of Work)			
Evaluation Method (Activity, Technique)	A. IMPACT ON IF's' CREDIT AND DEPOSIT MOBILIZATION	B. PROJECT BENEFITS AND IMPACT ON SMEs	C. CONSTRAINTS TO CREDIT DELIVERY	D. INDICATIVE DIRECTIONS FOR SECP
A. INSTITUTIONAL ASSESSMENT . management strategies . management policies . Asset-Liability management (Field Survey; Rapid Assessment)	(A3-A6) IFI management's lending policies (New) Asset-Liability strategy/policies (A7) SEC vs. Other lending programs (A8) Loans vs. Investment policies (New) Deposit generation strategies	(B3) IFI target marketing of SMEs (B5) Significance of SEC in management's access to SMEs (B9) Management capacity for project evaluation	(C1 & C2) Credit delivery capacity of IFIs (C3) Development financing policies and practices of IFIs (C5) Management bottlenecks for project delivery (New) Key examples or case studies of constraints	(D3 & D4) Potential of IFIs other than PDBs to implement SECP (D5) Capacity of existing management set-up for an expanded lending project (D6) Relative emphasis on SECP by participating IFIs
B. IFI LOANS PORTFOLIO (at PBSP and IFIs) EVALUATION . SEC loan portfolio . Special lending programs . Overall and SME loans (Field Survey; In-depth review)	(A1 & A4) Additionality in SME lending (A2 & A3) Additionality in IFI loans portfolio (A5 & A6) SEC fund use (A8) Use of SEC for lending and not for investment	(B3) Types of SME uses of SECP credit (B5) Importance of SME loans under SEC to total IFI portfolio (B9) Capacity of FI to evaluate developmental financing	(C3) Imbalances in participation by IFIs: Manila-based vs. others (C4) Whether SME-SECP loans are development-oriented	(D1 & D2) Geographic breadth of dispersion of SME lending under SECP
C. REVIEW OF IFI DEPOSIT PERFORMANCE UNDER SECP (Field Survey; In-depth review)	(New) Management strategies for meeting liquidity problems (A9) Deposit mix and levels before and after SECP (New) Deposits generation campaigns and track record	(New) IFI deposit performance for SMEs (New) Extent SME-SECP borrowers are deposit clients	(New) Whether IFIs lending to SMEs have liquidity constraints requiring SECP assistance	(New) Track record of various IFIs in generating deposits
D. ASSESSMENT OF IFIs IN THE SME LOANS MARKET . IFIs . SMEs . Other IFIs (Field Survey; Rapid Assessment and In-Depth Review)	(New) Actual SME lending policies and procedures (A1 - A5) Profile of actual and potential SME lending by IFI	(New) IFIs target market policy (B1) Characteristics of SME borrowers: "progressive" or not? (B8) SME needs other than credit (New) Other IFIs serving SMEs: types, importance, apparent lending policies	(C3) Opportunities to Manila-based IFIs allowing SECP use; constraints to rural-based IFIs (C5) Operational bottlenecks of IFI lending to SMEs (C9) Further potentials for SECP lending by IFIs	(D3 & D4) Potential of other IFIs to implement SECP (D5) Capacity of existing project management set-up for an expanded scope (D6) Relative emphasis of FIs: SECP vs. other lending programs (D7) Marketing approach of IFIs for SECP
E. REVIEW OF PROJECT DESIGN AND MANAGEMENT SET-UP . USAID . PBSP (Visit to Project Office; In-Depth Review of Documents)	(New) Project concept, objectives, intended impact on credit and deposit mobilization	(New) Project's intended impact on SMEs' growth and investment	(C5) Administrative and operational bottlenecks in flow of SECP funds to SMEs (C6) Clarity in mandates of implementing scheme and institutions (C8) Role of USAID in project implementation	(New) Whether alternative implementation schemes offer better possibilities given actual results to date

1.6 STUDY TEAM ORGANIZATION

The Study Team is composed of four members. The Evaluation Team Leader provided the general direction and overall coordination of the project implementation. The Evaluation Specialist assisted in the research design and supervision and quality control of the field work and analysis of data. Two Evaluation Assistants joined the team to gather essential information to make a thorough evaluation of the progress of the SEC project. These evaluation assistants implemented the field work and data organization and analysis.

The staff of PSR Consulting were mobilized to provide the necessary support to make sure the Study Team completed the Project to the satisfaction of USAID. Field visits were conducted in teams of two. Staff consultants of the company joined the field surveys whenever a team of two from the Study Team was not possible. This ensured that the targeted field visits were accomplished in the shortest possible time without sacrificing the quality of the field work. Research assistants were also on hand to assist the study team in the gathering and preparation of secondary data for analysis.

2.0 SECP AND THE POLICY AND INSTITUTIONAL ENVIRONMENT FOR SMEs AND SME FINANCING

2.1 SECP FINANCIAL STATUS

The approved budget for the program is US$ 12.85 million or ₱ 269.85 million at the exchange rate of US$. 1:₱ 21. The budget for each project element is as follows (in millions):

	US$	₱
Expanded Financial System Lending (EFSL)	12.000	252.000
Project Officer Salary	0.057	1.197
Other Direct Administrative Costs	0.051	1.071
Loan Development	0.240	5.040
Bank Training	0.142	2.982
Research and Policy Analysis	0.360	7.560
Total	12.850	269.850

The USAID has already advanced ₱ 251.9 for the EFSL. The 17 IFIs were granted a credit line of ₱ 324 million. As of March 31, 1992, total drawdowns and reavailments of the IFIs have reached ₱ 308 million for an average fund utilization of 1.22 times. With repayments of ₱ 115.8 million and an outstanding balance of ₱ 192.2 million, the available balance for drawing is ₱ 59.7 million. A total of ₱ 0.841 million was spent for bank training leaving ₱ 2.1 million for future training seminars. For research and policy analysis, ₱ 0.597 million was expended leaving a balance of ₱ 6.963 million.

The ₱ 308 million drawdown and reavailment of the IFIs was able to finance a total of ₱ 309.3 loans. The SECP contributed ₱ 237.6 million or 77 percent while the IFIs counterpart contribution was ₱ 71.7 million.

2.2 FEATURES OF THE SMALL ENTERPRISE CREDIT PROJECT

The SECP fund came from the US government through the USAID. The grant money was channelled through the Philippine government. The SECP is a wholesale financing facility and as such it does not directly finance projects. It utilizes institutional channels to eventually finance the SME borrower. The Philippine Business for Social Progress (PBSP), a non-profit organization, was chosen to administer the program. The PBSP accredited 16 private development banks and one non-bank financial institution to act as direct institutional lenders for the Program. In turn, the PDBs look for SMEs which have projects that qualify for SECP financing. The PDB submits brief reports covering these projects to the PBSP which authorizes the Development Bank of the Philippines to release the funds to the PDB. Figure 1 shows a diagram of the flow of funds under the SECP.

The SECP is designed as a financing program with "liberal" guidelines and reduced re-lending documentation requirements. Thus, it allows a high degree of flexibility for the PDBs to make loan packaging decisions and to access the financing within a minimal processing period of about two weeks. Under SECP, the IFIs have exclusive discretion over the following lending terms to SME borrowers: 1) the principal amount of the loan to be financed by the SECP, 2) the interest rate to be passed on to the sub-borrower, 3) the term of the loan, and the 4) the collateral requirement. Other major features of the program are: 1) funds are given to IFIs in advance of actual re-lending to SMEs, 2) a loan tenor which is shorter for SEC loans to IFI compared to the tenor of the loan from IFI to SMEs, 3) training component, 4) research and policy component, and 5) various debt instruments. The SECP intended to use this flexibility to attract PDBs to utilize the Program.

A distinct feature of the SECP is its portfolio financing approach. Under this approach, a participating IFI submits a group of projects (portfolio) for financing. While the projects are individually checked if they qualify under the Program, the guidelines are applied to the portfolio and not to the individual projects. The SECP finances up to 80 percent of the total portfolio cost. The participating IFI has the flexibility on the allocation of the fund to different projects. This means that in some instances, the IFI may use the SECP to finance 100 percent of a project in the portfolio. On the other hand, the SECP may be financing less than 80 percent of a project's cost in the same portfolio. The SECP gives the PDB the discretion on how to mix SECP with other sources of funds. For example, the PDB can use other external sources to fund the remaining 20 percent of the portfolio.

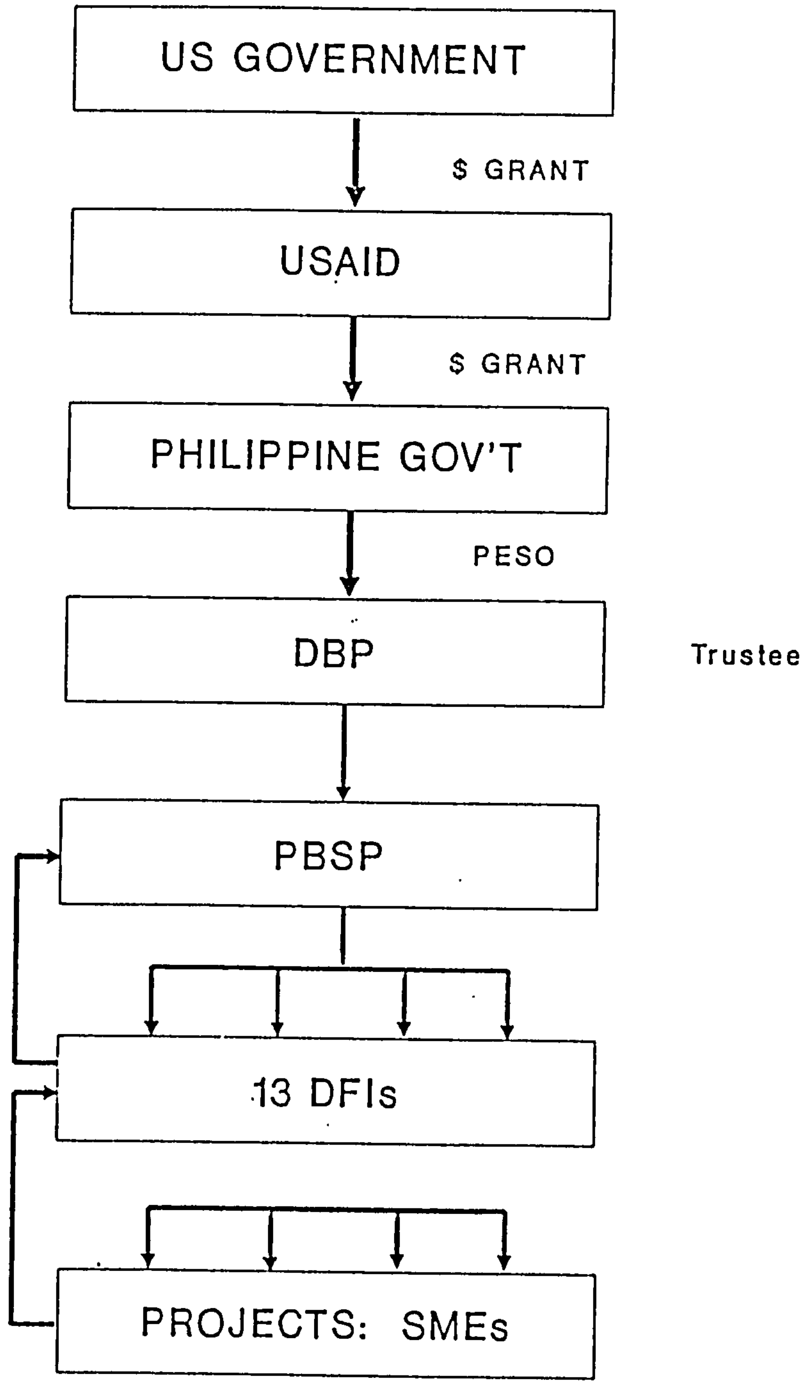
The interest rates charged by SECP to IFI borrowers are market-based and not subsidized. The market rate is calculated as the weighted average rate for the immediately preceding six months of time deposits with more than one year maturities. Instead of using the interest rate subsidies to encourage utilization, the SECP does away with stringent policies and requirements to make funds easily accessible to the IFIs. However, the real intended impact of the market-based interest rate is deposit mobilization and to encourage increased SME lending. Higher costs of fund, such as in the SECP, should encourage the IFI to find cheaper funds such as deposits or capital. The result is a bank that has a growing deposit base built under a sustained SME lending program and funded by maturing SECP funds.

The SECP does not require the IFIs to submit a "collateral" for each project or for the portfolio. SEC financing is effectively a clean loan of the IFI from the SECP. The SECP takes an overall institutional risk on the IFIs because the IFI assumes the liability for the re-lending to SMEs. If the sub-borrower defaults, the IFI must continue paying the amortization to SECP for its portfolio.

Figure 1

SMALL ENTERPRISE CREDIT PROJECT

FUNDS FLOW



Instead of the traditional reimbursement-type financing program, the SECP gives out a cash advance to IFIs for re-lending within 90 days. Hence, the IFI does not need to advance the loan to the sub-borrower before it can apply for a SECP loan. This feature serves as a strong assistance to IFIs in terms of their liquidity. In this respect, the SECP fund is seen by IFIs as a transaction fund, providing immediate liquidity. The benefits are in assisting IFIs in loans marketing and in increasing capability to make timely loan releases to meet SME demand for financing.

Most banks set the loan term to their sub-borrowers to match the term of special financing programs. In the SECP, the term of the PDB loan is based on the average tenor of the IFIs' sub-loans portfolio. A mis-match in the terms of the sub-loans is created by this computation of average tenor. The PDB's loan maturity to the SECP will always be shorter than that of the total sub-borrowers' loan maturities to the IFI. This mis-match creates a funding gap which the PDBs must eventually cover. The SECP was designed to create this gap for the purpose of encouraging the PDBs to mobilize deposits to cover the funding gap. As a result, IFIs need to exercise liability management when they make sub-loans as they need to make funds available once the SECP loan matures.

The SECP also includes a training and a research and policy component. The training component gives the PDBs the opportunity to strengthen their skills in project lending. As of March 31, 1992, a total of 10 training seminars were conducted. These seminars were on the following topics:

1) credit evaluation
2) developing small business relationships for bankers
3) financial management for entrepreneurs
4) basic selling
5) correspondent banking
6) project appraisal
7) management of problem accounts
8) SME lending
9) sourcing and managing funds

Two bankers workshop were also conducted. The first workshop focused on the identification of opportunities and problems in participating in the SECP. The second workshop centered on preparing the PDBs for the 1990's by providing inputs on the planning process, economic environment and finding suitable strategies.

Finally, the SECP offers its IFI-borrowers opportunities to issue alternative debt instruments in availing of the SECP funds. The familiar instrument is the promissory note. However, the IFI can also use commercial papers, bonds and preferred convertible shares. The SECP intended to use this project design feature to contribute to the development of the local capital market. However, only the promissory note has been used by the IFIs so far.

In order to appreciate the features of the SECP, it is best to compare it with a similar program, for example, the Industrial Guarantee Loan Fund (IGLF) of DBP. The IGLF is the most widely used financing program in the DBP.

Field interviews at the DBP point to the liberal terms and the length of the maximum loan tenor (15 years) of the IGLF as the primary reasons for its being attractive to SMEs. Also, it is the only special financing program in the DBP which advances funds to IFIs. The IGLF does not require an environmental compliance certificate which may take months to acquire. It allows loans for working capital purposes, with terms shorter than loans for fixed asset acquisition, but only if there is excess capacity in fixed assets requiring working capital. However, the IGLF remains a financing program only for fixed assets expansion or utilization of excess capacity. Familiarity of the banks with the IGLF, having been initiated in 1952, also contributes to its high utilization.

Table 1 compares the features of the SECP and the IGLF.

2.3 ACCREDITATION STRATEGY

One of the initial activities undertaken at the start of the SECP was the accreditation of financial institutions to implement the Program. USAID did not see a need to create new institutions to act as conduits for the Program. Rather, the Program was designed to work with existing financial institutions. It was required that such institutions demonstrate the following characteristics:

1) An institutional will to participate in SME development

2) An orientation to serving the SME market

3) The availability of existing competent staff

4) Provisions in their lending schemes for "graduating" SMEs business to medium-scale or larger businesses.

5) Profitability or commercial viability of the IFI

The eventual selection of PDBs as conduit banks for the SECP is justified by their orientation towards SME lending. Eventually, the Project Implementation Committee (PIC) chose only 17 banks, out of more than 40 development banks in the country, for accreditation. The eligibility requirements used in the accreditation shows the careful steps taken by the PIC to ensure the selection of the appropriate type of bank and bank management competence for the Project.

There are three measures used to determine the eligibility of a bank for SECP accreditation. These are: 1) management of the bank, 2) statement on SME lending, and 3) financial condition.

Table 1. SEC AND IGLF

LOAN	SEC	IGLF
Purpose	Portfolio Financing	Project Financing
Principal	80% of portfolio. Some projects 100%, others < 80%	72% IGLF, 8% IFI 20% Sub-borrower
Rate	Six months weighted average of time deposit interest rates	60-day WAIR
Term	Average term of the Portfolio. FI pays DBP within average term of Projects.	Matched to project life
Collateral	Clean loan	Any collateral acceptable to the IFI
Advance funds	90 days	Seven days
Training & Research and Policy	Included in grant	none
Debt instrument	Promissory note, commercial papers, bonds, preferred convertible stocks	Special time deposit
Environmental Compliance Certificate	Not required	Not required

An IFI must show sound and efficient management of its operations. It must present a strategy statement indicating interest in SME lending and its potential. Its statement must also evidence its concern as a banking institution in the following development criteria for lending:

1) employment that tends towards more productive labor

2) impact of financing on the poor

3) higher productivity of capital

4) encouraging private sector-led growth industries.

Finally, the bank must pass the following financial tests:

1) Positive net worth

2) Net after tax profit

3) Total SECP borrowings not to exceed 100 percent of its capital base

4) Government ownership of the bank not to exceed 35 percent of total equity

5) Total debt to net worth not to exceed 10 times.

The PIC used two categories to assess the institutional risk and determine the credit lines of banks. Category 1 includes PDBs with head offices and branches in the region. PDBs with head offices in the NCR and branches outside the NCR were classified under Category 2. A special category was created for the Private Development Corp. of the Phil. (PDCP) which is a non-bank financial institution.

Category 1 banks enjoy the advantage of having a credit line equal to its capital base while Category two banks get less than their capital base (66% of capital base).

Private development banks consider SMEs as their target market. However, not all management of PDBs have the inclination or financial resources for greater SME lending. The eligibility requirement seeks to select those banks which can move the funds and at the same time sustain SME lending beyond the project.

3.0 SECP IN THE POLICY AND INSTITUTIONAL ENVIRONMENT FOR SME FINANCING

3.1 CHARACTERISTICS OF SMES AND IMPLICATIONS ON FINANCING PROGRAMS

Various studies have identified some key characteristics of the SME sector, which are themselves results of government policies on the development of SMEs. Certain characteristics are particularly relevant to the issue of financing of SMEs. Size, location and strength or success of SMEs determine the financing requirements of the SMEs and their participation in programs like SECP. Available information indicates that the SME sector is dominated in number by the smaller SMEs of 10 employees or less. There is also a strong concentration of SMEs in the Metro Manila area.

A 1983 NSO Census of Establishments, shown as Table 2, reported that more than 75 percent of firms in the country have 10 employees or less while only eight percent are within the category of more than 50 employees. About 92 percent of all establishments in the Philippines can be classified as "small-and-medium" enterprises, with "small" interpreted as firms with 10 employees or less and "medium" as those with more than 10 but less than 50 employees. The dominance of SMEs in number emphasizes the importance of this sector as an employer. Smaller firms are operated by owner-entrepreneurs with limited capital. The individual financing requirements of SMEs are small but substantial in aggregate for the sector. Because the processing costs of bank loans are primarily fixed costs, the effective cost of financing is high for the individual SME. High transactions costs reduces the demand for and supply of financing through formal credit from banking institutions. Informal credit institutions incur less transactions cost because they can obtain better information about borrowers. They can also efficiently enforce collection because they are close to the business activity of their borrowers.

Business enterprises are concentrated in the Metro Manila area and in the nearby Regions 3 and 4. About 40 percent of all establishments are in the Metro Manila area, with another 23 percent in Regions 3 and 4. The advantages of business location close to the Metro Manila area are well-known, primarily related to superior infrastructure and market access. Even for the SMEs, Metro Manila is the preferred location, representing 38 percent of SMEs and 16 percent for Regions 3 and 4. All other regions, including urbanized growth areas like Cebu, Davao and Iloilo cities, account for only 39 percent of the SMEs. A financing program that "targets" SMEs outside the Metro Manila area, shall find relatively few of these SMEs in other regions. For banks, the search for creditworthy SMEs in these areas is difficult and transactions costs high.

3.2 POLICY CONSTRAINTS IN THE SME SECTOR

The government has recognized the role of SMEs in employment generation, regional dispersal of industries and efficient use of scarce capital. The development of SMEs has been a priority of government policies for some time but development results have been meagre. Government policies have not been as effective in part because SMEs are not viewed in an integrated way with respect to the rest of the industrial sector. There are many policies that promote SMEs but these are negated by other policies that promote large firms located in Metro Manila.

The broader policies of import and exchange controls, tariff regulations, and incentives that provide subsidies to use of capital enable large firms to obtain competitive advantage over SMEs. Smaller firms in remote regions are not equipped to deal with cumbersome regulatory requirements. Capital is more difficult to raise for SMEs and come at full, unsubsidized cost to the SMEs when availed.

Various studies[1] point out the need for policy reforms that eliminate controls and subsidies and rationalize tariffs in order to reduce overall distortions in the manufacturing sector. The consequent effects of such reforms on the SMEs are broad-ranging and would reach out to the most number of SMEs. Special programs of assistance, including financing windows, are considered desirable but could only reach a small set of SME beneficiaries in view of the great number, small size and dispersal of SMEs throughout the country. A survey[2] reported that only a small portion of SMEs are aware of government assistance programs for small enterprises and that of those, only a small minority sought or received assistance. More importantly, those receiving assistance were found to be the weaker performers compared to the survey group. That study concludes that government special assistance programs appear to promote weak SMEs. This is another possible explanation for the short-term success of some government SME development efforts which could not be sustained.

There are implications of these policy constraints on the issue of financing programs for SMEs. Without further general policy reforms, there shall be residual bias against the competitiveness of SMEs compared to larger firms. The success of financing programs shall carry this constraint and only SMEs in industries where this bias is not as pronounced can financing assistance be expected to be more successful. A focus on SMEs outside Metro Manila carries a similar disadvantage. The financing institution must be allowed to select only SME borrowers which can overcome their location disadvantage and pay for the

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1 Bautista, R. M. and John H. Power and Associates, Industrial Promotion Policies in the Philippines, Philippine Institute of Development Studies, 1984.

2 Hife, Emmanuel "Survey Results on the Impact of Industrial Policies on Small Industry Development", from Bautista, Powers, et al, Industrial Promotion Policies in the Philippines.

higher transactions costs of the financing. A special financing program is constrained to reach out only to a limited set of SMEs due to funding limit relative to the large size of the sector. Another factor is the limited range of outreach of the participating financing institutions due to the dispersal of SMEs outside Metro Manila.

3.3 BRIEF ASSESSMENT OF FORMAL CREDIT INSTITUTIONS AND SME LENDING

The supply of formal credit from banking institutions follows the growth and development of commercial and industrial firms. Commercial banks and the larger thrift banks are mostly in Metro Manila because business firms are concentrated in Metro Manila and the nearby regions. These Metro Manila-based commercial and thrift banks hold the largest share of the total financial resources of the country. Under the usual commercial lending terms, banks lend to profitable and established companies to ensure the lowest risk of loan default or loss. Priority is given to larger companies and larger amounts of loans in order to reduce loan loss risks and transaction costs. Commercial banks are engaged in intense competition for the relatively few corporate accounts but provide minimal lending to SMEs, especially those outside greater Metro Manila. The funding source of these large banks is the nationwide network of branches whose primary function is to gather deposits. Various studies[3] reported that commercial banks primarily lend to large corporations in Metro Manila with funding from deposits gathered from bank branches throughout the country.

Prior studies[4] of the credit market reveal tnat the formal commercial credit market is highly segmented. Commercial banks have higher lending limits and make centralized lending policies in their Metro Manila head offices and regional units. Their portfolios do not include, in substantial numbers or value, SMEs outside Metro Manila. In comparison, private development banks and rural banks can be considered the "community bankers" because they lend to business firms in the same geographic area where they gather deposits. In the more distant regions, these loan clients are mostly SMEs. These banks are able to lend to SMEs outside Metro Manila because they know the borrowers in their area on a day-to-day basis without the need for the paperwork (transaction costs) and other formalities conducted by commercial banks. In addition, local banks know the markets served by their borrowers, allowing them to correctly assess loan default risks.

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3 For example, Lamberte, M., Comparative Bank Study: a Background Paper, Working Paper 87-04, Philippine Institute of Development Studies.

4 For example, Saldaña, Cesar G., "The Philippine Commercial Banking System: Structure, Performance and the Impact of the Capital Buildup Program of 1972. "The Philippine Reviewof Economics and Business" XX (June 1983): pp 215-232.

The commercial credit market is highly segmented, with commercial and larger thrift banks lending to large corporations in Metro Manila and the smaller thrift and rural banks lending to SMEs in the countryside.[5] It is a result of the government policies affecting the financial system and the state of industrial and commercial development of the country, particularly the concentration of business in Metro Manila. Banks are heavily regulated, particularly as to capital and lending portfolios. The difference in capital requirements across bank types account for larger asset and lending base for commercial banks compared to thrift banks. Some smaller thrift banks would not be able to lend to larger SMEs because of the Single-Borrower-Limit (SBL) constraint. Their limited size constrains their lending to the SME market. Banks are also regulated by many "mandatory" lending programs. The residual portfolio that is subject to bank management decision is then allocated to the most productive and lower risk loans. Due to the reduced amount of loanable funds, the large and more established business firms are given priority.

The implications on SME financing programs of these conditions in the financial sector are on the selection of participating financial institutions and in the management of the supply of funds for lending to SMEs. Thrift banks and rural banks serve the SME market segment and are in a better position to participate in SME financing programs. Yet as a group, these banks have limited resources and can be subject to high institutional risks to the program sponsors. Hence lending limits to pre-selected participants shall be important to the success of the financing program.

3.4 AN EVALUATION CONCEPT FOR SECP

The two main focus of the evaluation of SECP are the impact on credit delivery of the project's innovative design and whether the project benefits of expanded lending to SMEs can be sustained or replicated by IFIs beyond the project period. SECP departs from the traditional design of special lending programs. The latter are based on a diagnosis of the "financing needs" of the SMEs. On this basis, other special credit programs prescribe specific loan terms that IFIs merely administer, i.e., effectively with reduced decision making on the IFIs' part. As described in section 2.4, many of the special lending programs have subsidy features, especially on interest rates, which fund sponsors justify by "development" considerations in favor of SME beneficiaries. SECP differs from these traditional credit programs' design because it takes a market-based approach on setting loan terms and for interest rates charged to IFIs and eventually, to SME beneficiaries. It allows IFIs to structure loan terms in ways fairly consistent with those on their regular loans.

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5 The Bank of Cebu (Annex C-4) has about 10 to 15 percent of the Cebu SME loan market and observes that commercial banks are uninterested in the sector while rural and thrift banks do not have the financial capacity and staff expertise to lend SMEs.

3.4.1 An Evaluation Concept

The concept developed in the evaluation of SECP is premised on investigating the impact of the SECP project design on the SME beneficiaries working through the IFIs. Finally, the evaluation is made in the context of existing traditional financing programs and the limitations imposed by the segmented credit markets, especially outside Metro Manila.

The evaluation concept is reflected in the overall evaluation question, stated thus:

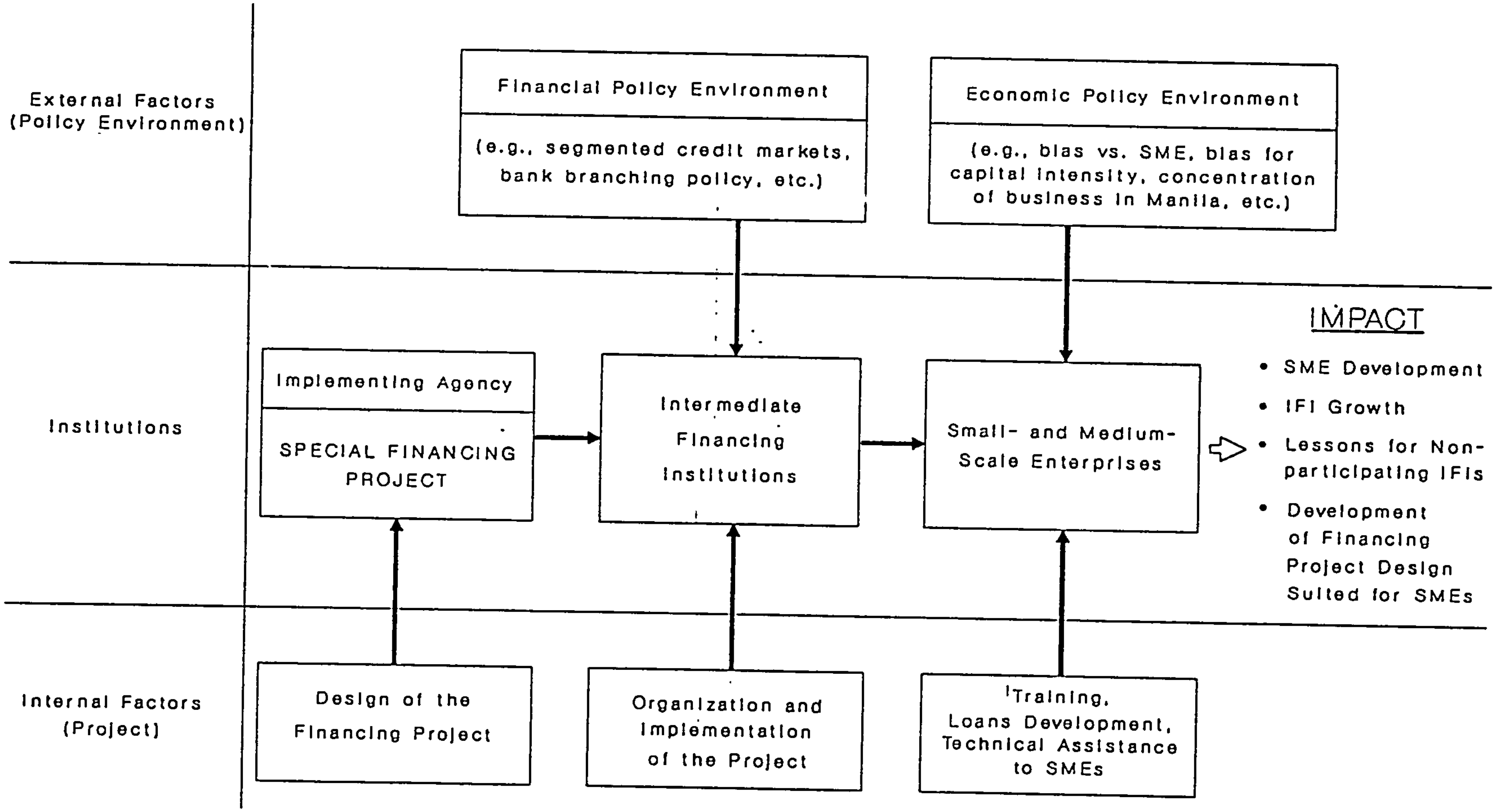
> **What is the impact on SME financing and its IFI channels of SECP, a project that is free of interest subsidies and liberalizes credit decisions in favor of IFIs, in an environment characterized by directed public credit programs and segmented private credit markets?**

There are two determinants of success in lending to SMEs, namely the design of the financing program and the other is the economic and financial environment that the IFIs and SMEs face in their respective areas. The first factor, selecting features of the financing program, is within the control of the financing program's sponsors of the executing agency for the financing. The environment variables affect the IFIs and the SMEs. These conditions can be changed only with appropriate policies of the government to promote SME development. These policies are beyond the direct control of the financing project's management or sponsors. A diagram of the controllable policy variables is shown in Figure 2.

The evaluation concept emphasizes the importance of determining the influence of the features of the credit project itself on the attainment of project objectives of assisting SMEs and stimulating SME sector growth. The ultimate beneficiaries of the credit are the SMEs. Credit delivery to SMEs depends on the IFIs' effectiveness and cost-efficiency in accessing SMEs. The project imposes conditions on the IFIs which serve to determine the degree of utilization by IFIs of the SECP facilities by the IFIs. This linkage between SECP, IFIs and the ultimate SME beneficiaries is diagrammatically shown in Figure 2.

Figure 2

Schematic Diagram of Overall Effectiveness of SME Financing Projects Depending on Project Design and the Policy Environment



As previously discussed, the local economy that SECP's IFI clients serve is partly determined by external policy variables. The policies of the monetary authorities affect the financial institutions that serve SMEs. Distortions in industrial development policy has retarded the growth of SMEs outside the Metro Manila area and contributed to the segmentation of the credit market. In particular, the SMEs have not been adequately served by the formal credit institutions. One of the objectives of the project is to create a "demonstration effect" for IFIs which successfully served SMEs and achieved profits and growth during the project period. In the process, other banks would recognize that it can be profitable to lend to SMEs under commercial, rather than subsidized, funding sources. The influence of external policies and effect of the project on non-participating IFIs are schematically noted in Figure 2. With this evaluation concept, avenues are opened for USAID and Government of the Philippines (GOP) to conduct policy dialogues based on the evaluation's results on SME development and financing issues.

3.5 KEY APPROACHES ADOPTED TO IMPLEMENT THE EVALUATION CONCEPT

It is evident from the evaluation concept that any measurement of the impact of SECP must start with a detailed survey of the IFIs' responsiveness to the project. The success of the project depends on such a favorable response from IFIs. However, the definition of the term "favorable response" is not a simple one. It is not enough that the IFIs merely utilized their allocated line of credit under the project. They must do so while pursuing their own objectives of profits and growth. At the same time, the financing should contribute to the profitability and growth of their SME clients. In short, the IFIs should help attain the project's objectives by availing of project funding to expand their SME portfolio and increase their profits and growth in assets.

The participating IFIs differ as to resources and size and diversity of the local economy they serve. An evaluation approach is developed that takes into account this difference in assets of participating IFIs and their respective local economy. Size of resources has a dominating influence on the capacity of the IFI to respond to the changes in needs of their SME clients and the opportunities offered by special financing projects like SECP.[6] In fact, the accreditation and setting of credit limits of IFIs under SECP properly recognized the range of resources among IFIs. The wide differences among IFIs in terms of resources result in differential competitiveness of these IFIs' in the credit market.

The evaluation approach involves considering all participating PDBs as one group and further classifying them in three categories on the basis of resources. The cut-

6 A "bottom line" measure of bank performance is return on investments (ROI). This study shows that statistically, for the IFIs under SECP evaluation, ROI increases with resources in a statistical regression at 99 percent confidence interval. (See footnote 20.)

off levels of resources that serve to delimit each category are based on perceived market segments of banks. The categories are as follows:

a. *Group "A" IFIs*: large PDBs with assets of ₱ 1.0 billion or more. These IFIs have Head Offices in Metro Manila and operate in the same general geographic areas as commercial banks. These IFIs can compete in the market segment of commercial banks. They are referred to in this evaluation as "large" IFIs.

b. *Group "B" IFIs*: PDBs with assets between ₱ 100 million and ₱ 1 billion. These IFIs' credit operations are entirely located outside Metro Manila. These PDBs do not generally compete with commercial banks and are referred to in this evaluation as "medium" IFIs.

c. *Group "C" IFIs*: PDBs with assets of less than ₱ 100 million. These IFIs' credit operations are mainly in their local areas. Limited resources enable them to compete only in the lower-size range in the credit markets often with rural banks. These are referred to as "small" IFIs.

Another key approach used in this evaluation is the recognition that SMEs differ as to "stages of development". Previous studies[7] have recommended that priorities in development assistance to SMEs should be given to the "progressive" SMEs, i.e., those with a clear strategy for growth and competitiveness. The financing project is intended to support SME growth and development. More insight could be derived in an evaluation approach that recognizes the differences in SMEs' stages of development. For example, financing assistance may be most crucial to SMEs only at certain specific stages of their development. It would also be interesting to determine the types of SMEs that IFIs support under the project.

The types of SMEs, by stages of development,[8] are as follows:

a. "Existence": SMEs at the start-up phase
b. "Survival": SMEs which have found a market for their products or services
c. "Success": SMEs which have established markets and are financially viable
d. "Take-off": SMEs which have established markets and are going for large-scale expansion
e. "Resource Maturity": SMEs which have become large, stable business firms

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7 Biggs, Tyler; Levy, Brian; Oppenheim, Jeremy; Schmitz, Hubert, The Small Business Policy Direction Study, Harvard Institute for International Development and Center for Research and Communication. Chap. 1, p. 7.

8 From Churchill and Lewis, "The Five Stages of Small Business Growth", Harvard Business Review, Vol. 61, No. 3.

3.6 OVERVIEW OF SCOPE OF EVALUATION

The four general areas which are to be addressed in the evaluation include: the impact of SECP in increased credit to SMEs, adequacy of PDBs and NBFI as vehicles for credit delivery and of PBSP and DBP in project administration, impact of SECP on deposit mobilization and measures to improve credit delivery to SMEs. In order to pursue the evaluation concept and process, these areas are integrated into three specific evaluation questions, as follows:

1. **How effective and efficient is SECP in achieving expansion of IFI credit delivery to SMEs?**

The evaluation would determine SECP's effectiveness in terms of a) whether there was an increase in the IFIs' SME portfolio, b) whether new SMEs were brought in to the formal credit market as a result of SECP, and c) whether the project had a significant influence on the operations of IFIs. The IFIs perception of SECP and its features would be important to the extent that they influence the attractiveness of SECP relative to other lending programs.

The efficiency of SECP would be reflected in the capacity of the IFIs to provide small loans and still cover loan processing costs. The types of SMEs served and of loans made may be related to the cost effectiveness of IFI loans under the project.

The Evaluation results on credit delivery are reported in Section 4.0.

2. **Are the credit policies and institutional lessons learned under SECP sustainable by the IFIs beyond the project period?**

The evaluation would determine the extent the liability management feature of SECP has influenced the funds and deposits generation policies of the IFI. A direct measure is whether the IFI is positioned to refinance SEC at maturity of the credit facility. There would be an investigation into the possible effects of the size of the local economy and the nature of the deposit clientele that the IFI serves on the capacity of the IFI to generate deposits.

The sustainability of the lessons learned under SECP would hinge on the adequacy and cost effectiveness of PDBs as the institutional vehicles for credit delivery to SMEs. Measurement of the financial risk and profitability of IFIs are some of the evaluation areas indicative of institutional viability.

The Evaluation results on sustainability and deposit mobilization are reported in Section 5.0.

3. **How effective and efficient is the SECP in contributing to SME growth?**

An evaluation of the ultimate SME beneficiaries would reveal how SECP financing was utilized. SME growth and sustainability are associated with fixed assets expansion and long-term financing. The question is whether IFIs took on a development finance role under SECP instead of making short-term, working capital loans associated with traditional commercial banking. Even in cases when short-term loans are made, there is a need to evaluate the types of SMEs financed and the local economy in order to ascertain whether the IFIs still perform their development financing function but are constrained by the limitations of their markets.

The Evaluation results on the impact of SECP on SME growth are reported in Section 6.0.

The discussion proceeds along these three specific evaluation areas.

The appraisal of the administrative arrangements, particularly an assessment of PBSP is conducted separately in Section 7.0.

4.0 SECP's IMPACT ON IFI CREDIT DELIVERY TO SMEs

4.1 EFFECTIVENESS OF SECP IN INCREASING SME LENDING BY IFIs

After an accreditation process that focuses on the management policies and commitment of the IFIs to lending to SMEs, the SECP accredited 16 PDBs and a non-bank financial institution to participate in the project. The selection of PDBs is appropriate because in the segmented credit market, the PDBs, along with the stronger rural banks, serve the credit needs of the local areas' SMEs. The PDBs' lending operations are geared to the search, evaluation and servicing of SME loans.

4.1.1 Overall Importance of SEC to Lending by the Development Banking Sector

Prior to evaluating credit supplied by participating IFIs under SECP, it is useful to provide an overview of the significance of SEC lending compared to the entire development financing sector.

> **OVERALL POTENTIAL IMPACT OF SECP IN DEVELOPMENT FINANCING. The project has the potential to significantly influence the supply of credit to SMEs at the regional level and only in several regions. At the national level, the credit supply it provides can lead only to a "demonstration effect" to other banks on the viability of lending to SMEs.**

A look at SEC loans outstanding for SEC relative to the total for PDBs reveals that SEC loan balances range from 2.6 percent (₱ 150 million versus ₱ 5,769 million) to 3.1 percent (₱ 179 million versus ₱ 5,867 million) of total loans in PDBs' books. Table 3 shows the regional distribution of loans granted during the project period by SEC relative to PDBs. In terms of loans granted, the proportion is lower, at around 1.2 percent in 1990 and 1991. The lower proportion is due to the long-term tenor of SEC loans. At the aggregate or national level, SEC appears to be a marginal program, supplying an amount of credit less than five percent of development finance to SMEs.

When the analysis considers the regional distribution, it becomes evident that in some regional credit markets, SEC supplied more than 10 percent of loans. From Table 3, these are in four of the 11 regions where SECP has a participating IFI using either 1990 or 1991 as basis. Clearly, the national average is influenced by NCR's loan demand. If NCR is taken out of the total loans balance, SEC loans amount to a slightly more significant three percent of the PDB sector's loans in 1991. There is a regional presence in selected regions for SECP. SECP has potential for directly influencing the real credit allocation to SMEs in these regions. At the national level (outside NCR), SECP has only the potential for creating a "demonstration effect" on the commercial banks, regarding the benefits and viability of lending to SMEs.

Loans Granted By Private Development Banks Per Region (In Millions)							
	Region	Total PDBs		SECP Loans Granted*		SECP Loans as Percentage of Total Loans*	
		1990	1991	1990	1991	1990	1991
I	Ilocos & Mt. Prov.	15.40	16.70	3.50	1.90	22.73	11.38
II	Cagayan Valley	0.00	0.00	10.00	0.70	-	-
III	Central Luzon	5,720.40	1,095.00	19.99	18.33	0.35	1.67
NCR	National Capital	3,106.70	8,625.20	0.00	1.96	0.00	0.02
IV	Southern Tagalog	1,040.40	1,264.40	47.34	46.90	4.55	3.71
V	Bicol	606.30	884.60	14.45	3.47	2.38	0.39
VI	Western Visayas	88.40	142.70	19.40	22.28	21.95	15.61
VII	Central Visayas	81.10	108.40	6.40	21.24	7.89	19.60
VIII	Eastern Visayas	0.00	0.00	0.00	4.50	-	-
IX	Western Mindanao	0.00	0.00	0.00	0.00	-	-
X	Northern Mindanao	200.60	278.00	14.63	5.99	7.29	2.16
XI	Southern Mindanano	75.10	145.60	2.80	20.12	3.73	13.82
XII	Central Mindanano	0.00	0.00	0.20	1.20	-	-
	Total	10,934.40	12,560.60	138.71	148.59	1.27	1.18
	Total w/o NCR	7,827.70	3,935.40	138.71	146.63	1.77	3.73

* With PDCP
Source: Table 3, Annex E.

4.1.2 Growth in IFI Lending to SME Due to SECP

Selection of the appropriate IFIs by itself does not guarantee attainment of the SECP's development finance goals. The important question is whether SEC made a difference to IFIs in terms of increased lending to SMEs. Another question is whether the accredited PDBs achieved growth in their SME portfolio after the introduction of the project. Sustained growth in the PDBs' loan portfolio is desirable and demonstrates the capacity of the PDBs to deliver credit to SMEs.

> **"ADDITIONALITY": SECP is being implemented through PDBs, the IFI type which serves the SME segment. These IFIs showed significant quantitative growth in credit delivery after implementation of the project. Comparatively higher loans growth was achieved by the smaller IFIs.**

Table 4 reports the annual growth in loans classified as "commercial/industrial" by PDB after implementation of SECP. The growth in the commercial/industrial loans portfolio of IFIs confirms that as a group, participating PDBs have a growing lending market. This growth was partly supported by SECP and is a broad indication of the quantitative benefits of the project in terms of credit delivery. A closer look at the IFI categories show that the smaller IFIs had the higher percentage growth, with the exception of Southern Negros Development Bank. Group B IFIs had an average annual growth in portfolio of 60 percent and Group C, 187 percent compared to Group A's 53 percent. It would appear that the Group B and C IFIs show higher growth, also called "additionality," in their loans portfolios relative to their size.

Average Annual Growth Rate in Commercial/Industrial Loans Before (1988-89) and After SECP (1990-91)

IFI Group Average	Before SECP	After SECP
Group A	31.7	52.6
Group B	50.1	60.1
Group C	77.7	187.0

Source: Table 4, Annex E.

4.1.3 Expansion of the SME Borrowers Market of the IFIs

Another indicator of "additionality" is the number of new borrower SMEs taken by IFIs under SECP. One of the objectives in rural finance development is to expand the market for formal credit institutions because it would be easier for government to influence SME development once they are in the formal sector. It should be emphasized that the risk of lending to new borrowers is generally higher compared to existing clients. The expansion by IFIs of their loans clientele under the project is a sign of their willingness to support SMEs at added risk and cost in credit evaluation of new clients.

> **QUALITY OF "ADDITIONALITY". New SME borrowers from IFIs were provided financing under SECP, a further indication of the quality of the additional loans and borrower-SMEs generated by the project. Larger IFIs provided most of the expansion in new borrower-SMEs.**

Table 5 shows that new SME borrowers outnumber old borrowers by a ratio of 1.45 to one. Across the three groups, Group A had the highest ratio in favor of new borrowers: 2.4 to one, although Group B is also close at 1.7 to one. It is interesting that the smaller IFIs tended to keep to their existing clients, taking in about one new for each existing borrower. The IFIs which had less new borrowers are in Group C - Southern Negros Development Bank and Palawan Development Bank. Smaller IFIs may be taking in less new borrowers because being small, they are already in a more risky financial position. Further, their limited resources may have prevented them from fully supporting the funding needs of existing clients. SECP allowed them to increase their support to existing clients.

Distribution of SECP Sub-loan Borrowers			
	Number of Borrowers		New/Existing
IFI Group	New	Existing	(%)
Group A	147	62	237
Group B	365	216	169
Group C	189	208	91
SNDB*	73	108	68
PDB**	55	96	57
Total	701	486	144

* SNDB - Southern Negros Development Bank; ** PDB - Palawan Development Bank
Source:Table 5, Annex E.

4.1.4 Impact on IFIs' Assets and Loans

SECP is considered by IFIs as only one of the possible sources of funding for building its loans and assets. In that sense, it is not clear that the development precepts embedded in the conditions and design of the project can significantly influence the policies of IFIs toward SMEs. Evaluation of the impact of SECP funding relative to the growth in IFIs' total assets and loans portfolio provides useful insights. If an IFI draws heavily on SECP to finance its growth, either: a) it finds the terms of SECP consistent with its orientation to SMEs; or b) it is prepared to adopt the policy of support to SME under SECP.

> **IMPACT ON RESOURCES OF IFIs. SECP had a substantial impact on IFIs because they expanded their lending to SMEs and strengthened their asset base. The more significant effects are evident among the small-to-medium size IFIs. These IFIs can be expected to be more responsive to development directions from the project.**

SECP Availments vs. Change in Assets and Change in Net Loans (in percent)		
IFI Group Weighted Average	Outstanding SECP Change in Assets	Outstanding SECP Change in Net Loans
Group A	1.15	2.0
Group B	6.30	17.1
(DCDB; BCDB; BSDB)*	(22.0;18.1;15.1)	(42.2;41.1;22.8)
Group B w/o Premiere	8.50	
Group C	46.70	68.7

* DCDB - Dumaguete City Development Bank; BCDB - Banco Cebuano - Cebu City Development Bank; BSDB - Bangko Silangan Development Bank
Source:Tables 6 & 9, Annex E.

The evaluation results indicate that SECP provided the most significant financing support to Groups B and C IFIs. Table 6 shows that SECP loans to larger IFIs in Group A constituted less than two percent of the growth in assets in 1991, excluding PDCP.[9] While the amount of funding allocation was a large component of SECP, the IFIs themselves considered SEC as a minor source of financing. In this respect, the project may have large funding allocation to an IFI group over which it has less impact as to funding and policy coordination. The resources of Group B and C IFIs are smaller and SECP provided an average of about six and 47 percent of the increase in their assets, respectively. Within Group B, Dumaguete, Banco Cebuano and Bangko Silangan's increase in assets over the project period are significantly financed by SECP. Only the presence in the group of a large PDB which is a minor user, Premiere Development Bank, resulted in a lower average.

Banks in Group B and C used SECP to expand their resources and increase their access to SMEs. Because of the importance of SECP as a source of financing, IFIs in these groups can be expected to be more responsive to the project's SME development guidelines.

SECP loans of IFIs is compared to the growth in their loans portfolio over the project period as shown in Table 6. Since SEC was available to IFIs for the two year period 1990-91, the outstanding balance of SEC loan by the IFI is considered as funding the increase in the net loans of the IFI over the same period. Data indicates that SECP expanded the lending capacities of the smaller IFIs. As of 1991, about 69 percent of Group C's increase in loans is covered by SEC. For Group B, the average ratio is 13 percent financing by SEC of loans growth. The

9 PDCP showed a decrease in total assets over the project cost of ₱ 87 million even as it had an outstanding loan of ₱ 37 million from SECP. The corresponding reduction in liabilities are in other bills payable and long-term loans over the period 1990-91.

IFIs in Group A are large users of IFIs but their loans portfolios are large and growing substantially and SEC contributes only two percent of loans growth.

There are two specific potential weaknesses related to the above overall positive evaluation results. With nearly 50 percent of growth in assets and percent in growth in loans financed by SECP, there is an evident dependence by Group C banks on the project for funding further growth in its loans portfolio. Later, Section 5.1 would evaluate the capacity of these banks to refinance future loans and assets growth with deposits. Since the SECP is taking an institutional risk with these banks, this is a particular concern related to sustainability.

Another IFI-specific finding derived from Tables 6 and 9 is the presence of decrease in assets and loans for particular banks during the project period even as these banks were accessing SEC funds. The cases in point are PDCP, Bataan Development Bank and Southern Negros Development Bank. As an example, PDCP decreased its loans portfolio by nearly ₱ 400 million from year end 1989 to 1991, while at the same time it utilized SEC facilities of about ₱ 37 million. For these banks, one may question the conclusion that fresh credit from SEC created "additionality" because these IFI's lending actually decreased.

4.1.5 The Design of SEC and Impact on Credit Delivery

It is important to relate the preceding quantitative results with the field survey findings regarding the perception and preferences of IFI management for SEC relative to other special financing programs.

> **CREDIT DELIVERY FEATURES OF SEC. The design of SEC ensured lower transaction costs and enabled IFIs to package SME loans to reduce their lending risks consistent with their management policies.**

The evaluation question raised to IFI management concerns the features of SEC that they find attractive, resulting in increased volume and quality of lending to SMEs. The responses revealed that the three main features that IFIs consider most attractive are: a) the cash advanced by SEC to IFIs prior to actual release of the sub-loan to SMEs;[10] b) the decision making allowed IFI management and c) minimal documentation requirements.

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10 Banks like Dumaguete City Development Bank (Annex C-6) agree that the SECP's cash advance enables the Bank to make timely loan releases, a key service requirement of SME borrowers. In contrast, PDCP (Annex C-10) reported that it took as long as six months to be reimbursed from the KASAPI program of SSS.

4.1.6 Overall Findings on SECP's Impact on Credit Delivery and as a Model for Rural Finance Project

Field interviews provided evidence that the SEC funds are viewed by IFIs as an ordinary commercial financing source. In reality, commercial financing is not readily available to PDBs, at any interest rate, as evidenced by IFI balance sheets which include only special lending programs as sources of borrowing. Funding from these special programs is only for short-term or matched to the tenor of the end-borrower. The availability of a commercial financing facility created by SECP is a significant contribution to rural finance development.

> **RURAL FINANCE DEVELOPMENT. The SECP has demonstrated that increasing the supply of financing at commercial interest rates contributes to expanding rural finance. There is sufficient loan demand by SMEs, making interest subsidies not essential to growth in SME lending.**

There are a few overall conclusions that tie-in the credit delivery results and the features of SEC. Recalling that the PDBs take the SME end of the market segment, one conclusion is that these IFIs do not need interest subsidies because they dominate the SME market and can find SMEs with needs that support the market-based interest cost of the funds.[11] The IFIs' need is actually for lower transaction costs in accessing the "commercial" funding source. By providing a cash advance mechanism and by setting liberal terms, SECP has effectively lowered the transaction costs to the IFI. It may be the transaction costs from the IFI to the funding source, rather than from the IFI to the sub-loan borrower, that has deterred the success of some special lending programs.

Another result is the attractiveness to IFIs of a scheme that leaves lending decisions to the IFIs themselves. In contrast, some special lending programs require IFIs to "target" small/medium-scale borrowers which have inherently high risks. By setting tight guidelines to enforce this "targeting approach", a special financing program constricts the ability of IFIs to choose loans or investments that maximize their returns and minimize their risks. In contrast, a financing program with liberal terms but with interest rates set at commercial levels enables IFIs to search for SMEs with projects whose returns can meet the commercial interest terms. These SMEs are screened to control credit risks through prudent structuring guided by internal bank management policies while keeping in line with the funding agencies' beneficiary requirements.[12]

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11 The SME market served by Southern Negros Development Bank (Annex C-13) are small SMEs in trading ("fast turnover") and so are not interest rate sensitive. The Bank's SECP sub-loan borrowers accepted interest rates ranging from 36 to 44 percent.

12 The SECP enabled the IFIs to serve the more profitable SMES in trading while allowing banks like the Bank of Cebu (Annex C-4) to lend mainly to SMEs in manufacturing as the Cebu area provided such opportunities.

4.2 EFFICIENCY OF SECP IN INCREASING LENDING BY IFIs TO SMEs

4.2.1 The Efficiency of IFIs in Small Business Lending

The efficiency of SECP in ensuring increased lending to SMEs depends on the capacity and cost-effectiveness of PDBs in servicing small loans. PDBs are capable of serving SMEs because they are the institutions that adopted to the segmented nature of the credit market. Loan requirements of these SMEs are usually of small amount. Field surveys gathered from bankers indicate that SME entrepreneurs are generally, conservative in orientation, preferring to forego business opportunities rather than take out larger loans.[13] By comparison, commercial banks have high minimum lending limits and serve larger business firms with Manila-based requirements like deposits services in multiple branch locations and foreign transactions. A third bank type, rural banks, are mostly constrained by limited capital and low SBL. Policies restricting PDB operations constrain their competitiveness with commercial banks in lending to larger businesses which require expanded banking services.

> **EFFICIENCY IN EXPANDING CREDIT DELIVERY. A greater number of SME beneficiaries was accessed because PDBs serve the SMEs market. PDBs are constrained by competition from rural banks at the lower and from commercial banks at the higher end of the SME loans market.**

The range of amount of loans under SECP indicates that the 17 IFIs operate mainly in the SME market. From Table 7, about 76 percent of SECP sub-borrowers are in the ₱ 25,000 to ₱ 500,000 range, with a median loan size of ₱ 100,000. Only 13 percent of sub-borrowers took loans of ₱ 5,000 to ₱ 25,000. Sub-borrowers with loans in excess of ₱ 500,000 constitute only 10 percent of the total. Given the segmentation of the market, Table 7 shows that loans of less than ₱ 25,000 are accessible to rural banks while those above ₱ 500,000 may already be served by commercial banks. Relatively few loans in this range of amount are made by PDBs.

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13 Both the Luzon Development Bank (Annex C-7) and Bangko Silangan Development Bank (Annex C-3) observe that the potential SME loan market in Southern Tagalog is large but not fully realized because the entrepreneurs are generally averse to assuming bank debt.

Overall Distribution of Number of Borrowers and Amount of SECP Loan by Size			
Size	Borrowers (%)	Loan (%)	Loan Type
₱ 5,000-25,000	13	1	Rural Bank
25,000-500,000	76	48	PDB
500,000 & above	10	51	Commercial
1,000,000 & above	6	37	Bank

Source: Table 7, Annex E.

4.2.2 The Efficiency of IFIs in Allocating Financing Between small and Large Business Enterprises

An objective of SECP is to provide credit to as many sub-borrower SMEs as possible. The choice of PDBs as intermediary was a correct step in guaranteeing SEC financing with access to the appropriate SME borrower market. Most of the PDBs' borrowers took out small loans and consequently, a greater number of SME beneficiaries were reached as in the cases of Southern Negros and Bicol Development Banks. To this extent, SEC was efficient in increasing the credit supply to SMEs.

> **EFFICIENCY IN ALLOCATION OF SEC FINANCING. A few large borrowers accounted for a significant percentage of SECP funds. This could have constricted the supply of funds to smaller SME borrowers. However, some of these larger loans financed SME's undergoing expansion or "graduation" to larger businesses.**

An area of concern, seen from Table 7, is that the loan size of over ₱ 1 million, has only 80 borrowers (six percent of total) but accounts for about 37 percent of the SEC loans. Total loans of over ₱ 500,000 amounted to more than 50 percent of the total SEC facility. The disproportionate amount used by a few large borrowers may have limited the capacity of IFIs to provide smaller loans to more borrowers.[14] To the extent that the allocation to larger loans limited the financing supply to smaller borrowers, this evaluation finding indicate further room for improving the efficiency in allocating credit to SMEs.

Again, the preceding quantitative evaluation results on efficiency in allocating and expanding credit should be explained by qualitative reasons. The evaluation question here is why PDBs can process smaller loans in a more cost effective way, than say, commercial bank branches in the same areas. Field surveys identified a number of reasons for the cost efficiency of PDBs, as follows: a) less

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14. All of Asiatrust's (Annex C-1) 12 SECP sub-loans amounts to ₱ 500,000 and above for a total SECP loan portfolio as of March 31, 1992 of ₱ 13.9 million.

documentation costs are incurred because loan processing is based on interviews, client visits and strong familiarity of the banker with the borrower; b) decisions are made by only a few individuals in a timely manner; and c) there is little bureaucratic costs from manuals of procedures, central office supervision and audits.[15]

4.2.3 The Economic Basis for the Competitiveness of IFIs in Lending to SMEs

As PDBs make small loans to SMEs, there is an economic basis for how these banks can cover the transactions costs associated with small loans.

> **BASIS FOR COST EFFICIENCY. The efficiency of SECP in expanding credit to SMEs is explained by: a) the cost advantage of PDBs arising from their close relationship with local SMEs; b) the resulting reduction in necessary formal loans documentation; and c) short processing time due to fewer decision makers.**

By comparison, branches of commercial banks require standard documentation designed for the "normal" large borrower. Such documentation is based on an impersonal process based on standard principles of controls. The approval process for commercial banks is highly organized into approval and review systems, often at a central location like a regional office or Manila. In recognition of the substantial costs of these systems, commercial bank branches in the rural areas have high minimum lending limits. In summary, there are cost advantages for PDBs inherent in the operations of local or "community" bankers compared to commercial banks with a nationwide outreach.

4.3 AREAS FOR IMPROVEMENT IN THE DELIVERY AND USEFULNESS OF CREDIT TO SMEs

The evaluation identified a number of issues that are related to possible improvement in the delivery and usefulness of credit to SMEs. These issues are: a) the determination of interest rates; b) the maximum term of the loan; and c) the maximum credit limit for IFIs. The evaluation findings are based on financial data of IFIs and field interviews.

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15 In Southern Negros Development Bank (Annex C-13) most of the lending decisions are done by the Bank president who also personally interviews the loan applicants. This enables the Bank to approve loans within three to five days, with minimal application documents.

4.3.1 Interest Rate Setting: Some Adverse Effects on IFIs and SMEs

DETERMINING "MARKET" INTEREST RATE: There is a weakness in using a historical basis for setting the "market" interest rate because it can result in temporary mis-pricing which either a) allows some. IFIs potential for excess profits, or b) requires SMEs to absorb above-real market costs. This evaluation result applies to all special lending programs which are based on similar pricing formulas. A study is needed to set up a pricing formula which is more responsive to market changes.

The interest rates charged to the IFIs by the project are based on a formula that uses the prevailing interest rates for the prior six months. Field interviews revealed that most IFIs are not satisfied with the resulting interest rates when these were "too high" compared to the current interest rates. This appears to happen when interest rates are going down.[16] At the same time, other IFIs preferred to access SEC versus other programs like IGLF when the interest rates for SEC are set lower than those of other programs. These evaluation results clearly reflect the deficiency of the present interest rate setting policy of SECP. There is an evident weakness in the implementation of the concept of "market" interest rate in this case.

In principle, the appropriate.interest rate schedule that SECP should adopt is the yield-to-maturity schedule, or yield curve, for three years. It is prospective in orientation, representing what the supplier of funds expects to receive for investment made today. In practice, SEC uses a formula that is based on the historical yield curve and only of a point in that curve. Only in the extreme case when the yield curve is stable and of the same slope across maturities will the forward-looking yield curve and the historical point estimate coincide. Otherwise, when the yield curve comes down, IFIs face a higher rate for SEC loans than the latest interest rate quotation in the market. Even in a segmented market where IFIs can pass on the interest rate to its sub-borrowers, the borrowers have been reported to express their dissatisfaction with the high rates.. Similarly, when the previous six months' rates were lower than the current yields, SEC funds would be priced lower than market. Examples of this case are when SEC rates were lower compared to IGLF's (which is based on previous 60 days). This is not consistent with the design of SEC because IFIs would prefer "market-based" SEC over subsidized credit programs of lower (actually, temporarily mis-priced) interest rates.

SEC should give priority to a study to revise the interest rate formula, perhaps in the context of a policy dialogue to influence the other special lending programs to SMEs. In fact, this call for revision in pricing is applicable to most special financing programs. The dysfunctional results are predictable and were observed

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16 Banco Davao (Annex C-2) noted that at one point, the SECP interest rate was much higher than the prevailing Treasury Bill rate.

in the course of the evaluation through financial analysis of IFI performance and in the field surveys. When SEC pricing is below real market IFIs can: a) repay other short-term loans, b) invest or purchase short-term investments instruments; c) simply lend and earn excess margins on loans to SMEs. Conversely, when SEC pricing is above real market, IFIs can: a) defer availment of SEC facilities; b) move out to IGLF and other-financing programs; and c) continue to lend but charge the SME the full cost of SEC funds to the SME, which could contract SME loan demand.[17] The study should explore pricing formulas that generate results which are more responsive to the market.

4.3.2 The Demand for Term Loans

> **SEC AS TERM FINANCING. Loans from SEC are positioned in the credit market as a short- to medium-term facility. Consequently, IFI management policies reflect SEC's pressure on liquidity and a bias for medium- to short-term SME projects.**

Special credit programs are attractive to IFIs because these are term financing. Survey results confirm that SEC is attractive to IFIs because it provides term finance. However, by comparison, IGLF provides a longer maximum term of fifteen years compared to SEC's three years. Given the projects of SMEs that could be financed by IFIs, SEC is positioned relative to other sources only as a "medium-term" facility.

The positioning of SEC in the loans market is a significant issue because it affects the management policies of the IFIs and the types of SME projects that shall be presented to SEC for financing. The potential effects on SMEs are covered in Section 7.1.1, mainly along a bias by IFIs for financing medium- to short-term loans. On management effects, field interviews revealed that IFIs considered SEC as a short- to medium-term funding source, especially in view of the portfolio maturity feature. Consequently, their policies on liquidity, lending and deposit generation took a shorter-term orientation. While the intent of the portfolio maturity feature is to stimulate a conscious refinancing policy for the IFI, there are other effects on other policies (especially lending) that may adversely affect credit delivery.

4.3.3 IFI Credit Limit and Lending Performance

The SEC project sets a limit on the maximum outstanding loans for each IFI. That limit is primarily based on the IFI's capital. This is a sound rule, based on the principle of the funding agency's assumption of risk of bankruptcy of IFIs (also called "institutional risk").

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17 Banks like Northern Mindanao Development Bank deferred availment of the SECP during periods when the interest rates were higher than the IGLF's rate.

CREDIT LIMIT AND IFI LENDING PERFORMANCE. The SECP faces the issue of whether to relax the credit limit for IFIs which are more effective at delivering credit to SMEs. The project's policy makers should define this trade-off between institutional risk and achievement of development finance goals.

In the actual implementation of SEC, differential lending performance emerged among IFIs. Some IFIs which are strongly capitalized did not borrow to anywhere near their credit limit. Meanwhile, there are IFIs with less capital which aggressively delivered SEC financing to SMEs but had to stop lending and relied on turnover when they reached their credit limit.[18] This raises the issue of whether the credit limit should be reviewed to consider the performance of the IFI in credit delivery to SMEs. SECP may need to consider institutional risk as well as the developmental aspects of the program in reviewing its credit limit.11

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18 The credit line drawdowns were lower for two of the biggest IFIs, Planters Bank at 88 percent (Annex C-11) and Asiatrust at 60 percent (Annex C-1). Bicol Development Bank, classified as a small banks in the evaluation of has the highest credit turnover rate of 170 percent. Southern Negros Development Bank and Palawan Development Bank have identical credit turnover rate of 150 percent.

5.0 SUSTAINABILITY OF SECP's BENEFITS BEYOND THE PROJECT PERIOD

5.1 SECP's IMPACT ON IFI DEPOSIT GENERATION POLICIES AND SUSTAINED FINANCING OF SMEs

5.1.1 Deposits Mobilization: IFI Policies and External Constraints

DEPOSIT GENERATION POLICY OF IFIs. Most IFIs have a coherent policy of increasing deposits to finance loans but their success is constrained by segmented depositor markets and limited potential for growth in some areas.

Savings deposits is the main funding source for bank loans because it carries the lowest cost. The concentration of economic activity in the Metro Manila area implies that the savings deposits potential is likewise concentrated in the same area. There is a relative concentration of savings deposits in the more progressive urban centers for the same reason.

The segmentation observed in the loans market applies to the savings deposits market as well. Commercial banks attract the larger savings deposits through various means like technology to facilitate transactions (e.g., ATMs), image of "safety of deposits," wider network of branches, etc. Commercial banks often impose minimum balances to ensure recovery of processing cost. Development and rural banks are left with the smaller depositors where transactions costs of passbook accounts are high.[19] Without minimum balance requirements, these banks find the servicing costs of these deposits too high. IFIs set their deposit policies with these constraints.

In Table 8, the average deposits to assets ratio describes the extent deposits finance the assets of IFIs. Banks in Group A located in Metro Manila have an average of 55 percent of assets financed by deposits. The comparison ratios for Groups B and C are 64 percent and 32 percent, respectively. Larger IFIs can accumulate larger deposit bases although Group A banks depend on special financing programs and borrowings to finance a large loan base. The smaller IFIs in Group C lag behind in deposits and rely on borrowing to finance their assets. This is an evidence of location and size advantage of the larger IFIs. Group A banks, the largest banks in the project, are located in Manila. Group B banks are located in urban centers while Group C banks are located in less economically endowed areas.

Table 8 presents the annual growth rate of deposits per IFI. The annual growth rates in deposits are high at 41 percent for Group A, 31 percent for Group B and 51 percent for Group C. These growth rates are indicative of a coherent policy

19 A deposit mobilization campaign of Luzon Development Bank (Annex C-7) increased the number of depositors (mainly school children), however, the deposit balances were so small that the cost of servicing the accounts was too high.

of deposit generation across all IFIs regardless of size. The difference is in the current stock of deposits among IFIs. Larger IFIs in Group A are able to sustain growth in assets due to a large balance of deposits. In contrast, smaller IFIs in Group C have small stock of deposits and are located in areas with less potential for deposit growth. For Group C banks, high deposits growth must be consistently attained, a difficult task given the limitations of their areas of operation. Unless these banks aggressively expand their capital and deposits, they would continue to rely on external financing to support growth in loans.

Deposit Performance of IFI's (1988-91)

IFI Group Ave.	Annual Growth of Deposits (%)	Deposits/Assets (%)
Group A	41.3	55.0
Group B	30.7	63.7
Group C	51.2	32.3

Source: Table 8, Annex E.

5.1.2 SEC as a Financing Source Requiring Re-Financing from Deposits

SEC significantly expanded the financing sources of Group B and C IFIs. These are banks with relatively smaller deposit bases and re-financing SEC with deposits shall be the task of their management.

Because of the liberal features of SEC, IFI management is given an assurance of an immediate funding source to meet loan demand. A substantial proportion of the increase in borrowing of banks in Group B and C came from SECP. From Table 9, SECP financing constituted only three percent of Group A IFI's total borrowing in 1991. For banks in Group B and C, it is more significant at 18 percent and 72 percent, respectively. In fact, for four of the five Group C IFIs, SEC is their only/primary source of external funding.

Larger IFIs have sufficient deposits and borrowing capacities, a condition that precludes dependence on special credit programs. In contrast, smaller IFIs have limited deposits and could not borrow funds from commercial sources. These banks depend on special financing programs for funding asset growth. Since SEC is a temporary funding source, banks in Group B and C face refinancing problems. The two ways to address this need are: a) by deposit mobilization; or b) shrinkage in lending to SMEs.

SEC borrowing provide IFI management with a target funding level that must be replaced largely by new deposits. Such targets for deposit generation are quite high especially for Group C banks given the constraints these banks face in the deposits market. For banks which could not re-finance SEC through deposits, the remaining option is to reduce loans, indicating a lack of sustainability by these banks of their part growth in loans. In this way, the institutional weaknesses of some IFIs can lead to their inability to sustain SECP's gains during the project period.

SECP Availments and IFI Borrowings, 1991

IFI Group Weighted Average	Outstanding SECP/Borrowing (%)
Group A	3.3
Group B	18.1
Group C	72.2

Source: Table 9, Annex E.

5.1.3 Capacities of IFIs for Re-Financing SEC through New Deposits

RE-FINANCING CAPACITIES OF IFIs. Larger IFIs have deposit generation capacities for re-financing their SEC-funded loans at maturity. Smaller IFIs have limited potential for re-financing SEC loan to SMEs.

The capacities of IFIs to raise deposits to re-finance SEC is evaluated by relating the increase in deposits of each IFI over the two-year period 1990-91 to its outstanding SEC balance at year-end 1991, shown in Table 10.

From Table 10, IFIs in Group A and B generated new deposits that far exceed their SECP balances. For the large IFIs, the increase in deposits is about 36 times SEC loans. For the Group B IFIs, it averages about 30 times their SEC outstanding balance. It is not likely that refinancing SEC maturities is a serious concern for these larger IFIs, with the possible exception of Dumaguete City Development Bank. However, for the smaller IFIs in Group C, deposit generation has been inadequate relative to SECP availments, with only 70 percent of SEC balance covered by deposits growth. These IFIs need to accelerate deposit growth or reduce SME lending in face of maturing SECP loans.

The increase in amount of deposits is compared to all sources of borrowing in Table 10. Banks in Group B have grown in amount of deposits that can cover an average of 3.6 times their existing borrowing. Deposits increase of Asia Trust in Group A can similarly cover 1.4 times its borrowings while Planters Development Bank could only cover 31 percent of its borrowings. the latter bank has large borrowings from special financing programs. Again, banks in Group C lag behind, with past deposits growth able to cover only about 52 percent of their total borrowing.

Ratio of Deposits Increase to Outstanding SECP and Total Borrowings Balances, 1990-91 (in percent)		
IFI Group Average	Increase in Deposit / SECP Outstanding Balance	Increase in Deposits / Total Outstanding Borrowings
Group A	3,562	86
Group B	2,963	402
Group C	70	52

Source: Table 10, Annex E.

5.1.4 The Deposit Clientele of IFIs

The issue of deposit mobilization is better understood in the context of the savings depositor market of PDBs. Outside Metro Manila and the highly urban regional centers like Cebu and Iloilo City, family income levels are much lower. In the countryside, the deposit market typically consists of SMEs, a few larger business enterprises, a number of high net worth families and the rest of the population who are the wage earners, the self-employed and students.

> **DEPOSITOR MARKET AND DEPOSIT GENERATION.- The PDBs operate as real thrift banks, serving smaller depositors and a few larger individual accounts. This market, along with high servicing costs, pose limitations for deposit mobilization efforts of PDBs.**

Commercial banks typically have the dominant position in the depositors market, taking in depositors with larger balances, particularly businesses and high-net-worth individuals. These depositors require more sophisticated bank products like trust accounts, certificates of deposits, ability to transact in Manila and other branches, and the like. PDBs could not compete with commercial banks for these types of depositors. Other depositors attracted by the facilities of commercial banks and their image of stability also become core depositors of commercial banks.

PDBs are left with the middle to lower end of the savings deposits market. Field surveys indicate that PDBs access this group in a systematic manner by organizing staff to campaign for people to open deposit accounts in the barangays, setting up youth savers clubs, approaching market vendors and school teachers and other similar activities as in the case of the Luzon Development Bank. Aside from this cost of bringing in new depositors, PDBs incur higher servicing costs. These depositors maintain smaller accounts and transact more frequently. A number of PDBs such as Bicol Development Bank, have high net worth depositors who keep their accounts with the PDBs because of personal contacts with the banks' owners. These accounts are kept as time deposits and carry competitive interest rates but can be moved out in short notice.

The structure of the depositor market outside the urban centers makes the mandate for deposit mobilization a challenging one for the smaller PDBs. There are constraints to raising deposits from small savers, especially higher transactions costs. In addition, smaller PDBs may have large deposits from a few accounts that could not be considered as core deposits to finance growth in loans.

5.2 THE ADEQUACY AND COST-EFFECTIVENESS OF PDBs AS INSTITUTIONAL VEHICLES OF CREDIT DELIVERY TO SMEs

5.2.1 Adequacy of IFI Deposit Base in Support of SME Lending

The PDBs can support growth in loans through corresponding growth in deposit liabilities. For the only non-bank IFI, PDCP, the approach is to find new financing from official development assistance and commercial sources. Since the latter alternatives are more costly than deposits, PDBs need to establish their deposit clientele, build a deposit base and ensure its growth. This is an issue that concerns the capacity of PDBs to sustain growth in lending to SMEs.

> **SUSTAINABLE CREDIT DELIVERY. The loans portfolios of most of the larger IFIs are supported by adequate levels of deposits. These IFIs offer better potential for sustaining future growth in loans to SMEs.**

Table 11 shows IFI loans as a proportion of assets and of deposits. Loans constitute on average, nearly 60 percent of assets. As PDBs lend primarily to SMEs, these assets actually represent the requirements for growth of SMEs. The extent of deposits that support loans is reflected in the loans to deposit ratio. There are differences in this ratio between Groups A and B banks on one hand and Group C banks on the other. Eight of 12 banks in Group A and B have ratios less than 100 percent, indicating that their loans are supported by deposits. The three exceptions are Planters Development Bank, North Mindanao Development Bank and Dumaguete City Development Bank whose ratios are 147, 343 and 130 percent, respectively.

The smaller PDBs in Group C lend, on average, nearly twice the level of their deposits. This loans to deposit ratio reveal these (and the three in Group A and B) PDB's dependence on external financing, rather than deposits, to finance their loans. To some extent, the special credit programs serve as appropriate financing source for loans and the L/D ratio should include such sources as "deposits." When this is done in Table 11, only Planters Development Bank's L/D became less than one, showing that its loans are covered by either deposits or special programs. Northern Mindanao Development Bank and Dumaguete City

Development Bank remained above one, indicating dependence on commercial borrowing sources.

With dependence on external funding, some disadvantages to be expected are: a) higher cost of funds; b) liquidity pressure as external financing become due or when a few large depositors withdraw their funds; and c) difficulties in sustaining lending to SMEs. The capacity of a PDB to expand its lending activities to SMEs depends on the PDB's build-up of its deposit base. The evaluation results show that larger IFIs are generally in a better position to support future expansion in SME lending while smaller IFIs need to further expand their deposit base.

Loans vs. Deposits and Assets of IFI's (Average, 1990-91)

IFI Group Average	Loans/Deposits (%)	Loans/Assets (%)
Group A	123.1	62.0
Group B	108.9	55.1
Group C	189.6	56.7
Overall Average	140.5	57.9

Source: Table 11, Annex E.

5.2.2 Profitability of IFIs

The profitability of the IFI reflects the capacity of the bank to recover its costs of operations and borrowed funds, avoid excessive bad loans and provide a return on the owners' investments. Because the size of resources is key to the revenue-generation base of a bank, one can expect the profitability of IFI to differ across the three groups under evaluation. The SECP expanded the lending base of IFIs, improving their profit potential. The evaluation should look at the impact on IFI profitability.

> **PROFITABILITY AND RELATIVE EFFICIENCY. The average profit performance of IFIs which are significant users of SEC improved after implementation of SEC. Larger IFIs show superior profit performance.**

The average returns on shareholders' equity (ROE) for each IFI in the two years before and after the project are shown in Table 12. The ROE of banks in Groups A, B and C before the project are 15 percent, 10 percent and 4.5 percent, respectively. The superior profitability of larger banks is evident. After implementation of SECP, IFIs are provided opportunities to expand their resources. ROEs increased across all IFIs especial for individual IFIs which accessed financing from SEC. The average ROEs after the project implementation are 24 percent, 15 percent and 6 percent for Groups A, B and

C, respectively. There is an improvement in ROEs across all groups during period of SEC implementation. Within this picture of improved profitability, the superiority of returns of the larger IFIs remains.[20]

Profitability is one of the criteria for accreditation under SECP because it is related to the sustainability of lending by IFIs to SMEs. The marginal profit performance of the smaller IFIs reflect their limited capacity to further incur costs of covering smaller SMEs and to gather small savings deposits. These IFIs are also more vulnerable to economic downturns that could lead to loan losses. Marginal profits limit these IFIs' capacity for internal funds generation and capital build-up. For SECP, the institutional risks are higher for the smaller and less profitable IFIs.

Comparative Returns on Shareholders' Equity of IFI's Before and After SECP (in Percent)

IFI Group Average	Before SECP (1988-89)	After SECP (1990-91)
Group A	15.2	24.2
Group B	10.5	14.9
Group C	4.5	6.4

Source: Table 12, Annex E.

5.2.3 The SME Clientele of IFIs

From the viewpoint of a lender, the SME market consists of diverse enterprises that differ as to credit risks, loan profitability and servicing costs. The types of SMEs that IFIs support under SEC can be related to the cost effectiveness of IFIs in serving the small loans needed by SMEs.

SMEs vary in stage of development and at each stage, the type of financing assistance they require varies in magnitude, type and tenor. A recent taxonomy of SMEs by stage of development needs is shown in Table 13.

> **THE TYPES OF SMEs IN THE IFIs' PORTFOLIOS. The IFIs have assumed acceptable credit risks because within the generally high risk SME market, they lend to SMEs which are successful and undergoing growth.**

The field survey revealed that IFIs evaluate their SME borrowers to determine whether they are "successful" or not in order to limit their risks. Most IFIs have

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20 An ordinary least-squares regression relating ROI with assets and dummy variable before/after SECP was done. ROI is positively related to assets (99% confidence level) and also with SECP's introduction (95% confidence level). More resources and financing that increases resources improve the profitability of IFIs.

in their portfolios the more prominent and successful SMEs in their local areas. The association of IFIs with these SMEs serve to generate more business referrals to the IFIs for other potential SME borrowers as in the case of Banco Davao. IFIs also coordinate with trade and industry associations in identifying potential borrowers as experienced by the Bank of Cebu. These organizations conduct their own screening of their members and make referrals to banks for the more successful members. In the classification in Table 13, the survey indicated that IFIs find attractive as loan client SMEs which can be called "successful" or in "take-off", i.e., growing rapidly.

The SME borrower profile of SEC classified by annual sales and number of employees is shown in Table 14. The results show that SECP addressed the financing needs of SMEs with median-size of three employees and ₱ 900,000 in median annual sales. There are differences between the three groups of IFIs. Larger IFIs have in their portfolios bigger SMEs in terms of employees (median size of 10 employees) with higher sales per year (median size of ₱ 3.5 million). By comparison, Group B IFIs have SME borrowers under SEC which are of median size of two employees and sales of ₱ 720,000 per year. The smaller IFIs in Group C have SMEs with median size of three employees and median annual sales of ₱ 471,750.

From the evaluation surveys, IFIs appear capable of financing SMEs compared to commercial banks because IFI management selects the more successful SMEs as borrowers by using business referrals and their own awareness of local business enterprises as initial screening devices. Use of local information and informants, like associations, enables IFIs to lower their costs of processing SMEs loans.

Distribution of SME's by Annual
Sales Volume and Number of Employees

IFI Group	A	B	C	TOTAL
Median Annual Sales (₱ 000's)	3,523	720	472	900
Median No. of Employees	10	2	3	3

Source: Table 14, Annex E.

6.0 IMPACT OF SECP FINANCING ON THE DEVELOPMENT AND GROWTH OF SMEs

The final beneficiaries of the SECP are the SMEs engaged in off-farm activities outside Metro Manila. In this respect, there are some qualitative benefits desirable to the project concerning SMEs. One of these benefits is the sustainable growth of SMEs. Increased production and service capacities require expansion in physical facilities of SMEs. The SECP should support the investment in fixed asset expansion of SMEs as a priority. A second desired benefit is industrial growth built upon SMEs. It is desirable to give priority to business activities related to manufacturing and service compared to trading operations. There are development benefits in the production of goods and services requiring financing support from SECP. In contrast, trading activities are relatively low risk for which commercial financing is readily available.

It is in this context that the evaluation proceeds, covering the effectiveness and the efficiency of SECP in contributing to SME development.

6.1 EFFECTIVENESS OF SECP IN CONTRIBUTING TO SME GROWTH

6.1.1 Purpose of the Loan by the IFIs to SMEs

There are two general purposes for business loans: for working capital and for fixed assets acquisition. In a working capital loan, the SME uses the loan proceeds to purchase inventory or to pay operating expenses. These loans are needed by SMEs if they do not have sufficient capital to support the existing volume of business or if there is an expansion in the volume of business on seasonal basis. Working capital loans are associated with the trading business.

> **TYPES OF SMEs SUPPORTED BY SEC. The SMEs supported by SECP are about equally distributed between trading and manufacturing or services. This reflects a balanced development financing impact on SME beneficiaries under the project.**

Most special lending programs restrict the application of funds to fixed assets, allowing for working capital only in special cases or as part of the expansion project. In principle, such restrictions focus assistance to the creation of new capacities and related employment generation. However, in practice, market opportunities for expansion are limited and subject to higher risks. Furthermore, the local SME loan market usually include many undercapitalized SMEs requiring working capital assistance. These SMEs become inaccessible to such special financing program.

In contrast to other special financing programs, SEC allows IFI management to select their credit risks within the SME sector. Without requiring fixed asset components in credit, one might expect IFIs to concentrate credit assistance to lower risk working capital financing. The evaluation results do not support this expectation.

Data on the distribution of SME beneficiaries by type of business activity is shown in Table 15. Analysis in this table indicates that about half of SECP loans was used to finance SMEs involved in trading while the remainder was allocated to SMEs in services and manufacturing. There is a balance in the overall allocation of SECP credit to SMEs in various classes of business. However, there are differences across the types of IFIs. Larger IFIs in Group A provided slightly less SECP credit allocation to trading firms at 44 percent of total compared to manufacturing and services, which together accounted for the remaining 56 percent. The smaller IFIs in Group C actually have the largest proportion of credit allocation for SMEs involved in trading, or 58 percent of their total loans. Median loan sizes for manufacturing and services are larger, implying fixed assets financing, compared to those in trading where the financing are for inventory and operating expenses.

These figures are explained by field survey results showing that smaller IFIs in Group C are located in market areas where there are fewer manufacturing activities compared to trading. Further, the accreditation process assured SECP that IFIs are committed to SME lending, resulting in a wide array and balanced allocation of uses for credit and types of SMEs served.

Distribution of SECP Loan (₱ 000's) By Purpose and IFI Type

Median Loan size	Trading	Manufacturing	Services	Total
Group A	200	225	500	250
Group B	80	150	195	96
Group C	50	155	100	70
Total IFI's	80	155	150	100

Source: Table 15, Annex E.

6.1.2 Distribution of SECP Loans: Short- and Long-Term

The actual, in contrast to the nominal, "term" of a bank loan is readily ascertained. While the nominal term in the loan agreement specifies "one year," there could be an implicit acceptance by the bank that the loan is subject to review and renewal after one year. Such loans are appropriately evaluated as "long-term." Hence an evaluation based on a review of nominal term probably overstates the actual amount of short-term loans. The evaluation of loan terms is made subject to this qualification.

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LOAN TERMS. The SEC was largely used by the IFIs as a term lending facility with a significant short-term component. This is consistent with the SME development goals of the project. SECP's design allowed IFIs to structure loan tenors suitable to the financing needs of the SME.

The SEC is a term financing facility which IFIs can access for short-term as well as long-term lending to SMEs. Banks are known to use long-term sources of funds for short-term lending. An example is the large core savings deposits of commercial banks but the predominance of short-term lending by these banks. This is the phenomenon of "reverse term transformation," a well-known development issue in the Philippine financial sector.

Some of the reasons for this practice is the lack of proper incentives for banks due to the prevailing policy distortions in the Philippine financial system. One reason is that the yield curve in market can be flat or non-existent beyond one year. That yield curve implies very little incentives for IFIs to lend long-term. Another is the differentiation of the borrower market. The segmentation makes IFIs negotiate with their borrowers on loan terms with little competitor pressure. The result is the predominance of short-term loans because renewals can be requested by borrowers on short notice while IFIs want the prerogative to terminate loans in case they face liquidity problems. Still another reason is the lack of long-term funding to banks. Consequently, banks which face large negative asset-liability gaps (maturing liabilities exceed liquid assets) keep structure mainly short-term loans.

SECP loans classified by term is shown in Table 16. The analysis reveals a bi-modal distribution of SECP loans as to tenor: one-year and 2-3 years. The amount of loans under the long-term classification (over one year) is over 60 percent of the total. The majority of the amount of loans under SECP is long-term, demonstrating that the SECP is an exception to the "reverse term transformation" behaviour observed among banks. Table 16 further shows that long-term lending is common across IFIs regardless of size. Larger IFIs actually have the most concentration of loans beyond one year. Group A successfully uses SECP as a term lending facility. Due to their wide SME markets, it is feasible for these IFIs to find SMEs and to match maturities according to the SME's needs.

Distribution of SECP Loan By Term of Loan			
	Number Per Group		
Term of Loan	A	B	C
1 - 180 days	0	32	118
271 - 360 days	0	413	152
1 - 3 days	118	174	114
TOTAL	222	642	416
Median loan term	3 years	1 year	1 year

Source: Table 16, Annex E.

The smaller IFIs in Groups B and C used SECP partly to finance the working capital needs of SMEs. These IFIs operate in narrower market locations, financing SMEs which are relatively undercapitalized. Nevertheless, these IFIs continue to access SECP for term lending. The SECP provided liberal terms with the effect that IFIs are provided the capacity to structure loan terms which are more suitable to the needs of the SMEs.[21]

Beyond SME market considerations, there are features of SECP that appear to create a bias for short-term lending to SMEs. Since interest rates of SECP are at market, currently around 32 percent for Group C IFIs, borrower SMEs could save on interest expense if they work themselves out of debt quickly. These SMEs might be inclined to request for "renewable" short-term loans to finance their medium-term needs.[22] Further, at a tenor of three years, SECP money is not perceived by the IFIs as sufficiently "long.[23]" Addressing these features would further encourage IFIs to provide SMEs with long-term financing under the program.

21 The SECP enabled the Bank of Cebu (Annex C-4) to lend to the SME export sector which the Bank would not have ventured into using internally-generated funds.

22 In Bangko Silangan Development Bank (Annex C - 3), only eleven of the Bank's 331 SECP sub-loans have a maturity of more than one year. This implies that some long-term SME financing needs may have been structured as short-term "renewable" loans.

23 PDCP (Annex C - 10) identified extending the term of the SECP loan as the single most important improvement that would significantly enhance the attractiveness of the SECP to the institution.

6.2 EFFICIENCY AND COST EFFECTIVENESS OF SECP IN CONTRIBUTING TO SME GROWTH

6.2.1 Cost Effectiveness in IFI Lending and Loan Size

The capacity of IFIs to service the smaller loan requirements of SMEs depends on their operating cost efficiency and resource constraints, primarily the SBL limitation. As an institutional segment, PDBs already serve the SME market. However, the diversity in size of IFIs and of SMEs signal the need to evaluate the possibility that IFIs select SME borrowers according to size. In fact, this is found to be the case.

> **IFIs AND AVERAGE SME LOAN SIZE. The average size of loans to SMEs is larger for larger IFIs.**

The distribution of SECP borrowers by loan size is shown in Table 17. The median loan size of Group A IFIs is ₱ 250,000, with ₱ 96,000 and ₱ 70,000 for Group B and Group C IFIs, respectively. The larger IFIs make larger loans, on average. This tendency for IFIs to take bigger loans is explained by the cost effectiveness of granting, pricing and administering larger loans compared to many small ones. The evaluation shows that it is an important factor even within the IFIs serving only the predominantly small borrowers.

Table 17 also reveals that the borrowers of SME borrowers of IFIs are predominantly in the ₱ 50,000 to ₱ 500,000 category, in terms of number of borrowers. However, in terms of amount of portfolio allocated to borrowers, the few large loans can constitute the majority of IFI loans depending on IFI size. For all IFI groups, there are substantial loans in the higher range of ₱ 1-3 million. For Group A, loans in the size range beyond ₱ 500,000 come from only 22 percent of the borrowers but account for 72 percent of the amount of SEC portfolios by these banks/NBFI. Even banks in Group C lend in this higher loan size range. Given the size of some of these banks, this raises questions about whether they do so consistent with their SBL regulations.

Distribution of Borrowers By Loan Size By IFI Group (percent to total)

IFI	A		B		C	
Loan Size	Borrowers	Loan	Borrowers	Loan	Borrowers	Loan
"Small"	0	0	13	1	20	2
"Medium"	72	28	81	66	72	55
"Large"	27	72	6	35	7	47
Median Loan Size (Pesos)	250,000		96,700		70,000	

Source: Table 17, Annex E.

These findings regarding borrower and loan size and their relationship to IFI asset size have some implications on the credit delivery of financing projects like SEC. The small to medium-size IFIs appear to serve the greater number of SME borrowers and to keep within the SME lending range. These IFIs increase the outreach of the financing project. However, this finding should be understood as due to the economics of larger loans and the SBL/resource limitations of these IFIs. If those factors are changed, one would expect the distribution of borrowers and loan sizes to change.

6.2.2 Capacity of IFIs to Finance SME Growth

IFI CAPACITY TO GROW WITH SMES. The resources of IFIs is a determining factor in its capacity to support larger financing requirements of successful SMEs. Without a plan for rapid growth in resources, some IFIs could be left with the smaller end of the SME market.

The distribution of SECP borrowers by size of assets is presented in Table 18. The results show that larger IFIs lend to larger SMEs in nearly precise mathematical progression. Group A IFIs lend to SMEs, with median asset size of less than ₱ 1 million, Group B to SMEs of ₱ 500,000 in assets and Group C to SMEs of about ₱ 250,000.

Larger IFIs can meet larger credit needs of borrowers and offer a wider range of banking services to SMEs. Due to a combination of its limited resources and the narrow market segment it serves, smaller IFIs can assist only comparatively smaller SMEs. The IFIs in Group C are themselves "the SMEs of the financial sector." They are severely constrained in extending continued assistance to faster-growing SMEs. When these more progressive SMEs outgrow the limited financing and services capabilities of the smaller IFIs, they become clients of the larger banks as experienced by Southern Negros Development Bank. This is a process of "self-selection," which in a differentiated local banking market, can lead to smaller SMEs remaining in a shrinking or high-risk end of the SME clientele. Field surveys confirm cases of this type for some smaller IFIs.

Distribution of SECP Borrowers By Size of Asset

	Group			
	A	B	C	Total
Median Asset Size	936,000	500,000	250,000	489,000

Source: Table 18

7.0 EVALUATION OF SEC PROJECT ORGANIZATION AND IMPLEMENTATION

7.1 ASSESSMENT OF SECP ORGANIZATION

7.1.1 Organization Structure

The PBSP implements the SEC Project under a grant agreement with the USAID dated September 1989. The DBP acts as Trustee Bank of the SEC funds. A Project Implementation Committee (PIC) comprised of part-time representatives from the PBSP, Development Bankers Association of the Philippines (DBAP), Department of Trade and Industry (DTI), Department of Finance (DOF) and the private sector meets regularly and provides advice on policy issues, accredits banks and decides on matters presented to it by Project Management for resolution. The USAID and the DBP participate in the PIC as non-voting members. The organization structure of the SEC Project is shown in Figure 3.

> **ORGANIZATION STRUCTURE. The SECP was implemented with minimal bureaucratic requirements under the current organization structure. However, the Project Director is responsible to two authorities for policy guidance and instructions, a deficiency in organization design.**

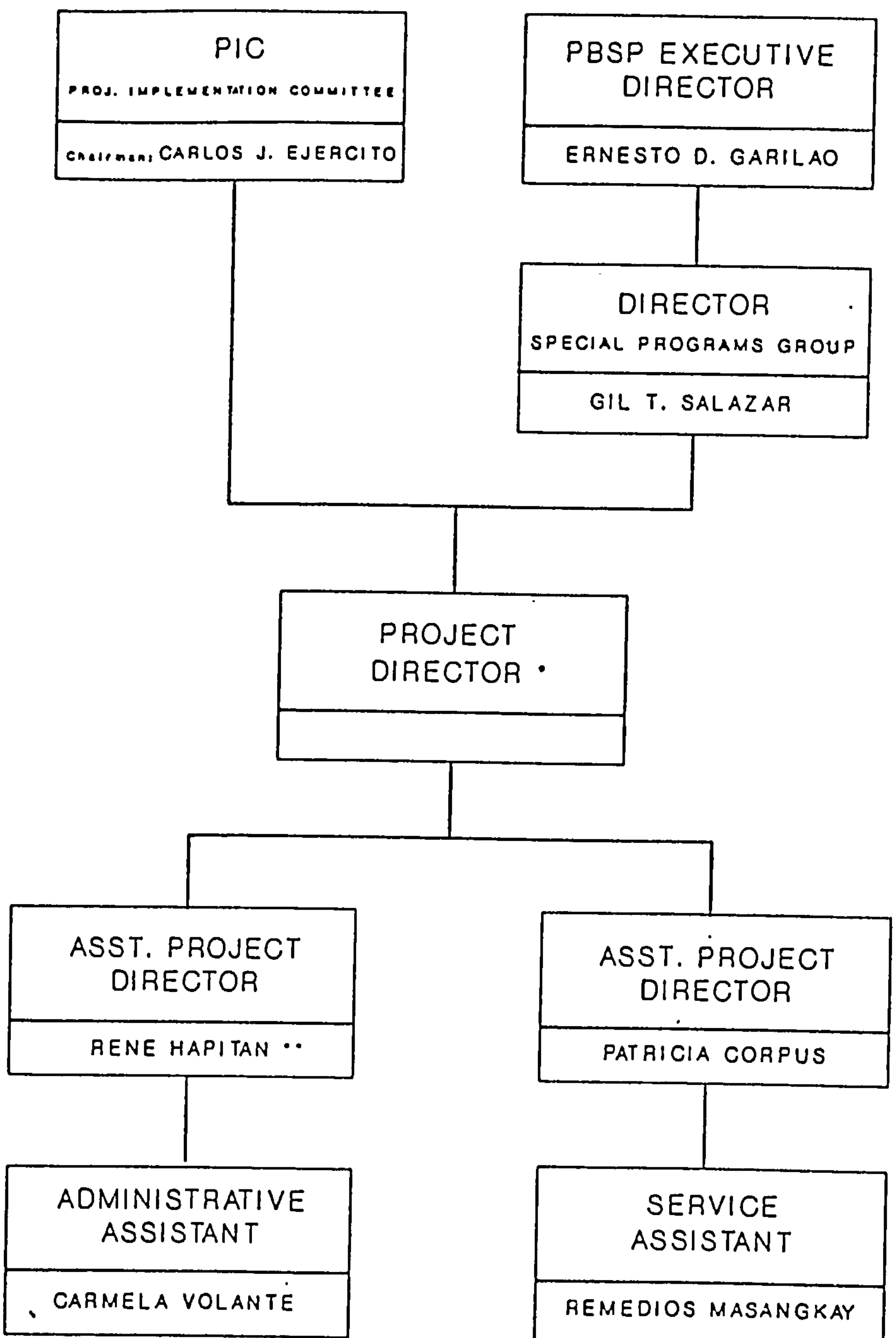
The SEC Project Management is headed by a full-time Project Director who is assisted by two Assistant Project Directors. The latter in turn supervise an administrative assistant and a service assistant. Under the present organization, the Project Director reports to two separate units: 1) the PIC itself and 2) the Office of the PBSP Executive Director through the Director of the Special Promotions Group. Operationally, he draws instructions from the PIC and provides information to the Office of the PBSP Executive Director. The PIC in turn coordinates with the Office of the Executive Director.

The current organization structure was designed to draw on the collective wisdom of a part-time PIC and still obtain oversight and guidance from a full-time Executive Director of PBSP. In practice, there were some limitations of the structure that affected project implementation. The immediate advantage from the structure seems to be the close contact of the Project Director with both the PIC and the Office of the PBSP Executive Director. The Project Director can draw from the combined experience and perspective of the different representatives in the PIC as well as from the operational insights of the PBSP Executive Director. In practice, as has been noted, the Project Director reports directly to the PIC and merely "coordinates" with the PBSP Top Management. Coordination is a loosely defined term which can mean anything from mere provision of information about SEC activities to a more substantive activity like assuring that SEC activities are consistent with the PBSP's corporate goals and vision. This may put the Project Director in an awkward situation because two lines of authority bear upon him. As per the formal organization, he reports and

Figure 3

SMALL ENTERPRISE CREDIT PROJECT

Existing Organizational Structure



Note:

* - Two Project Directors have served since October 1, 1991

Mr. Leonilo Coronel from October 1 to December 31, 1991
Mr. Ernesto D. Garilao from January 1 to July 1, 1992 and
Mrs. Aurora Tolentino, from July 1 to the present

** - Resigned May 15, 1992

File: [illegible]

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is responsible to two authorities who provide policy guidance and instructions. It may be the case that such policy guidance are not consistent. Without definite guidelines as to the real line of authority the situation is awkward and difficult from the viewpoint of all three parties, especially the Project Director. However, it is to the PMO's credit that despite the obvious limitations of the structure, it was able to implement the Project rather smoothly. The funds have been provided to the IFIs without much red tape and the field interviews revealed that the IFIs have no serious complaints about the PMO's performance.

As to staffing, the Project Management Office (PMO) appears top heavy with one Project Director and two Assistant Project Directors, each with his own assistants. The items for the Assistant Project Directors can be converted to technical positions, whose work for SMEs, field interviews point out to be needed for the effective implementation of the SECP. A gain in efficiency can be expected if the PMO is managed only by a Project Director, assisted by an Executive Assistant, and with several technical personnel as staff.

7.1.2 The PBSP

The PBSP is a non-stock, non-profit organization established in 1970 by Filipino businessmen as a concrete expression of the business sector's commitment to improve the quality of life of the Filipino poor. It receives funding from annual contributions of member companies equivalent to 20 percent of one percent of their net profits before taxes. It also receives funding from international sources as well as private individuals. Its clientele includes the landless rural workers, sustenance fisherfolk, marginal upland farmers, lowland small farmers, urban poor, cultural communities and women in development groups. It has five main programs of assistance: 1) community organizing, 2) institution building. 3) enterprise development and promotions, 4) technology management and 5) corporate involvement. Its other programs include agrarian reform, women in development, low cost housing, disaster mitigation, environment and corporate citizenship.

> **PBSP AS IMPLEMENTOR. The PBSP was an appropriate choice of institution to implement the project and has effectively performed its functions, particularly in credit delivery. However, a lack of experience in managing a credit project resulted in lower project achievements in the related components like training and policy research and in the lack of project impact monitoring.**

PBSP was registered with USAID on December 18, 1980. Since then a number of grants under the PVO Co-Financing Program has been coursed through PBSP. It is considered to have managed these funds efficiently and has maintained good working relationships both with USAID and the communities it serves. PBSP has decentralized its program administration and has regional offices in Visayas and Mindanao. The head office is responsible for Luzon.

The PBSP is currently in its fifth Five-Year Development Strategy, called the Area Resource Management Program (1991-1996). This new strategy is an improvement over the Provincial Development Strategy because it targets impact areas or contiguous clusters of three to five municipalities in 15 provinces (Pampanga, Quezon. Camarines Sur, Antique, Marinduque, Western Samar, Eastern Samar, Northern Samar; Southern Leyte, Negros Occidental, Bohol, Cebu, Davao del Sur, North Cotabato and Misamis Occidental). The PBSP decided to re-orient its development strategy early on in 1991 because the Provincial Development Strategy, in the words of Mr. A. Soriano III, PBSP Chairman, "although sound in terms of concept...with its optimistic targets and scope, strained the capacities of PBSP." Thus, the new approach which emphasizes impact areas where its resources can be concentrated and effectively utilized.

PBSP's Area Resource Management Program in the impact areas shall follow three distinct phases comprised of: 1) social preparation and institution building; 2) productivity improvement and 3) enterprise development. These activities will include environment, disaster mitigation and sustainable development, agrarian reform and women in development. In addition PBSP runs special programs, namely: 1) Samar Poverty Alleviation and Livelihood Project; 2) Cebu Hillyland Development Program; 3) Negros Productivity Improvement Program; 4) Relief and Rehabilitation; 5) Local Development Assistance Program and 6) Enterprise Development. The SECP is part of the Enterprise Development Program. Other projects under this Program are the Enterprise Resource Centers, SSS-Members Assistance for Development of Entrepreneurs (SSS-MADE) and the DA-Land Bank Integrated Rural Financing Project.

Because of its successful record in handling development projects, PBSP was selected as implementor of the SECP. Being a non-financial institution, the PBSP handled the SECP without the mindset of a bank. It viewed the SECP as a window of opportunity for the SMEs which are composed of small countryside entrepreneurs who are also PBSP's clientele. The SECP was seen by PBSP as not merely an opportunity to provide financing to SMEs but a chance to influence the thinking of bankers who have not dealt with the needs of SMEs out of too much concern for profitability and risk. This orientation is exemplified in PBSP's interpretation of "loan development activities" which are part of the Training and Loan Development Component of SECP. The PBSP interprets these terms in a broad sense to include "nurturing" activities for SMEs that may have good business prospects but do not have the skills to present an attractive loan package to the banks, "brokering" services in behalf of SMEs that do not have access to formal credit and similar "developmental" intervention for SMEs.

According to IFIs surveyed during this evaluation, the PBSP has effectively discharged its functions. In addition, IFIs credit PBSP with giving a lot of flexibility to the IFIs in the matter of loan origination and usage of the funds subject to the guidelines of the Project.[24] The main drawback of PBSP's appointment may be the fact that the PBSP is not a financial institution and has no extensive experience in managing a credit project such as the SECP. A financial institution may have a better appreciation of the nuances of SME lending, the training needs of both IFIs and SME borrowers and the monitoring of the project's performance and impact on banks and SMES.

The PBSP played a crucial function at the initial stage of the SECP. It has one of the best track records in developmental activities among PVOs/NGOs and offers an impartial structure to implement a multi-million peso grant for SME development finance. However, because of the redirection of its focus, development strategy, resources and effort, as earlier described, it may no longer be the most efficient implementor of an expanded SECP. The next generation of SECP-type approach to SME lending may call for an institution which is more aligned with and more on-track with the ultimate goal of SECP, such a goal is to institutionalize a market-oriented, flexible and development-oriented SME credit finance. A leading prospect for such an institution especially in the light of the success of PDBs as implementor IFIs of SEC,is the Development Bankers' Association of the Philippines (DBAP). As an organization of PDBs, it has the necessary orientation to the goals of SEC and familiarity with SME credit finance.

7.1.3 The Development Bankers' Association of the Philippines

In the Philippines, often individuals or groups that are engaged in similar undertaking organize themselves into associations that serve as a forum and to advocate a common cause in favor of its members. These associations may function loosely as forum to discuss and resolve common issues; they may also be more formal and aggressive in advocating a common cause for the good of all members, in which case they try to influence public thinking and policy to bring benefits to their membership. The DBAP is an association of private development banks.

> **THE DBAP. The DBAP as a project implementor has the potential to institutionalize the SECP's approach to banking for SMEs. However, DBAP needs to reorganize for the project and requires short-term technical and managerial assistance to manage the SECP.**

Appointing the DBAP as Project Implementor has the advantage of bringing the SECP and its experience closer to the ultimate goal of institutionalizing the SECP philosophy of banking with SMEs. A distinct advantage is that this will give a truly private sector initiative and support to SME lending. It can be noted that the majority, if not all, of the existing SME financing programs are heavily

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24 The SECP enabled The Bank of Cebu (Annex C - 4) to relax its loan collateral policy in lending to Cebu SME exporters. Instead of requiring traditional loan collateral requirements like real estate or chattel mortgage, the Bank accepted "purchase orders" as loan security.

affected by government intervention whether in the financial, technical and even organizational aspects. One *caveat* is in order regarding the capacity of DBAP to administer SEC, as follows.

However, while conceptually the DBAP is an appropriate implementor, it may not yet be organizationally geared up to manage the project on a full-time basis. It is still only an association of PDBs and has yet to acquire the solidarity and working organization similar to that of the Bankers' Association of the Philippines. In fact, the DBAP was only registered with the SEC last year. In contrast the BAP has a full time set of officers and personnel to carry on its identified objectives. To enable the DBAP to effectively implement the project, there is a need to provide DBAP with strong administrative and technical support.

Given the available options, DBAP may be most appropriate to administer the current or an expanded SECP. However, DBAP should organize a unit that is capable of receiving technical and managerial support in order to effectively manage the SECP. This unit shall need to pass a nurturing stage under professional consultants who will be tasked to vest upon DBAP the needed orientation and skills that will eventually enable it to handle the project.

7.2 ASSESSMENT OF PROJECT IMPLEMENTATION

7.2.1 Implementation of the Credit Component

The credit component is coursed through accredited private development banks for re-lending to SMES, particularly those with good business potential but cannot access formal credit. The DBP acts as trustee bank and the PBSP as project implementor. A Project Implementation Committee provides advice on policy issues, accredits banks and decides on pertinent project concerns. The USAID and DBP sit in the PIC as non-voting members.

> **IFI ACCREDITATION. IFIs were accredited mainly on the basis of their commitment to SME lending and capacity to expand services to SMEs.**

During the inception of the SEC Project, the PIC gave more emphasis to the policy and orientation of the IFI towards SMES. According to PBSP, the 17 IFIs that were initially accredited, were chosen on the basis of their orientation towards SME lending, future plans for sustainable SME lending and outreach capacity in the chosen areas of SEC operation.

> **LENDING TERMS AND PROCEDURES. The loan disbursements mechanism is simple and allows IFIs quick access to SECP financing. Its flexible terms enable IFIs to structure loans to SMEs to meet internal policies while lending to SMEs.**

The IFI submits to PBSP the sub-loan schedules in support of drawdowns against its approved credit line. Funding from USAID which is released through the Trustee Bank, DBP, is made available in a very short period of time. It is almost always the case that the submitted sub-loan schedules are eventually funded according to the banks that were interviewed. However, in some isolated cases, the PBSP requested the concerned banks to change particular loan requests considered to fall under activities that are not eligible for funding by the SEC Project.

With respect to the loan terms, the SEC Project compares well with the government-directed lending programs. It may even be said that because of its flexible loan terms and the minimum of red tape and requirements it is superior to the government-directed programs. The flexibility given by the SEC Project allows the IFI to design a credit package that will give SME clients access to formal credit while at the same time ensure profits for the IFI.[25] In particular, the market-orientation of the interest rates enables the bank to perform the difficult task of providing credit to the small and medium sector by varying the level of interest rate according to the relative riskiness of its borrowers. It is primarily in this way that the IFI will be able to extend SME credit on a sustainable basis, giving SMEs access to formal credit especially those with good business potential but are hampered by the lack of financing at reasonable interest rates.[26]

MARKETING SECP TO IFIs. PBSP's task of marketing SECP to IFIs is enhanced because it is not a financial institution and consequently, not seen by IFIs as able to compete with them in lending directly to SMEs.

It is important to note here that the IFI does not perceive a "conflict of interest" situation between itself and the PBSP which is not a financial institution. This "conflict of interest" perception pervades the government-directed lending programs like the Agricultural Loan Fund (now the Countryside Loan Fund) where the Land Bank wholesales agricultural credit to participating private financial institutions which in turn lend to end borrowers. The private financial institutions consider the Land Bank as a competitor in the retail loans market and this makes for the uneasiness that visited the implementation through the Land Bank of the ALF and its successor the CLF. Perhaps, the only drawback in the PBSP-IFI relationship is the IFI'S perception that the PBSP project management office lacks 1) continuity and permanency because of the rather fast turn-over of personnel assigned to the SEC Project and 2) familiarity with financial intermediation by private development banks.

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25 The flexibility of the loan term of the SECP enabled banks like Southern Negros Development Bank (Annex C - 13) to structure loans based on the payment capacity of the borrowers, e.g., working capital loans of ₱ 23,500 for three years and another of ₱ 606,000 for 180 days.

26 All Dumaguete City Development Bank's (Annex C - 6) SME SECP sub-borrowers with viable business were rejected under the IGLF because their financing need was only working capital.

ROLE OF PIC. The PIC appears to be directly involved in aspects related to management of the SECP.

It must be pointed out that the PIC has taken a direct hand in administering the Project. It was noted that the PIC handles not only policy direction and advice, but also such activities like bank accreditation, approval of credit lines and other operational matters. Its role in the Project should have been limited to direction setting, strategic thinking and planning and policy advice but excluded operational concerns where as a part-time ad hoc group, it does not have the comparative advantage of the SEC Project's full-time personnel.

MONITORING. The task of monitoring project impact has not been adequately performed under the project.

Another aspect of the project's implementation which bears some comment is the monitoring requirement of the Project. The documentation and tracking of various entries in the Transaction Report offer a good start in monitoring the Project's impact on SMEs and the participating IFIs, problems and issues arising from the implementation of the Project and related areas of concern. However, impact monitoring which is a vital component of any project, especially a development-oriented intervention such as SECP, has not been done or attempted.

There is, therefore, a need to have a formal unit in the Project which will assemble, process relevant data and analyze the impact of the Project vis-a-vis objectives and vision. This exercise will also pave the way for continuous dialogue among the SMEs, the participating IFIs and the concerned government agencies which will be necessary for SME promotion. While the accreditation and credit disbursement aspects of SECP's credit component are very much onstream there is a knowledge void on the impacts of SEC to re-direct project implementation because there is no unit given such task.

7.2.2 Implementation of the Research and Policy Analysis Component

This component is expected to produce: a) studies on policy constraints to small enterprise development, including questions of demand for and constraints to ready access to formal credit; b) seminars/conferences for the discussion of policy issues and c) a research activity that would examine entrepreneurial activity in the informal sector, especially regulatory impediments to such activity and informal/formal sector linkages.

RESEARCH AND POLICY ANALYSIS. Only one research study was completed under SECP but many of the policy issues about SME promotions and credit have not been adequately addressed.

Again, this component is a unique part of SECP. Other SME financing programs do not include this particularly significant component. There seems to be little appreciation for research and policy analysis even among Government Financial Institutions (GFIs) whose chief concern seem to be to disburse fund under the program guidelines and to collect back the loans as efficiently as possible. No effort appears to be allocated to analysis of whether the expected impact of the intervention are materializing. And if the intended impact do not readily exhibit themselves, these financing programs do not study closely what constraints derail the best of intention and effort.

The credit agreement with the USAID notes that "the research element targeting entrepreneurial activity in the informal sector is expected to identify methods to advance this group into the formal sector and up the SME ladder." Furthermore, knowledge of informal/formal linkages will yield "original thinking and models to promote entrepreneurial activity in rural non-farm employment." The research component will therefore complement past and current research and policy analysis of SMEs and development finance and will provide an information base from which to draw relevant and appropriate policy directions by the government and the banking community.

A study was commissioned in 1991 for these purpose. This is the UP-ISSI "Study on Financial Intermediation for Small and Medium Enterprises in Seven Regions of the Philippines." The consultant team was not able to review these two studies which were in varying stages of preparation/revision. A cursory review, however, of the Executive Summary of the UP-ISSI study shows that many of the issues about SME promotion policy and credit finance have not been adequately addressed. This was the same concern that was expressed during the 19th Regular Meeting of the PIC on 4 October 1991 when the PIC expressed concern whether the proposed studies would result into "actionable strategies." One member noting that too many loan programs are addressing SMEs asked whether SECP is moving in the right direction or touching base with the right industries. Another member stated that in spite of too many available funds for SMEs, these funds remain unutilized because banks wait for SMES to come to them. What is noticeable here is that the approval to commission studies on SMEs and banking seems to have been made relatively later (i.e. in October 1991) than the ideal time which may be at the first year of implementation of SECP. An early appraisal and appreciation of the problems, issues and policy concerns surrounding SMEs and banks will have been more useful to the PIC, the IFIs and other interested parties.

7.2.3 Implementation of the Training and Loan Development Component

This component has two parts: a) bank training activity and b) loan development activities. Training is "geared towards changing bankers' attitudes towards lending to the SME sector." Among other reasons, the lack of adequately-trained personnel in the IFIs especially in the areas of loan evaluation and project supervision hampers the delivery of credit to SMEs. This activity will provide training to bankers in critical areas so that their SME loan portfolios may be improved and strengthened. The training will be oriented towards increasing the operational efficiency of the banks and their technical expertise in specific areas such as, loan appraisal techniques, determination of negative environmental impact of the borrower's activity and others.

TRAINING AND LOANS DEVELOPMENT. By comparison with achievements of the credit component, the training and loans development component of SECP lags behind.

The field interviews yielded a generally positive appraisal of the workshops so far conducted by PMO. There were ten seminars and two workshops conducted as of March 1992. There were some suggestions that future seminar/workshops should be more attuned to the realities about SMEs and the local economy in which SMEs and banks operate. The training that was extended was considered by some as too "textbook-oriented and relevant to a developed economy setting."

On the other hand, the loan development activity essentially "represents SME project packaging which will result in more bankable projects for financing." This activity is intended to assist SMEs and banks to develop skills which can then be used to prepare acceptable SME project proposals. It seems that this sub-component was also not adequately implemented. As late as 8 November 1991 during the 20th Regular Meeting, the PIC was still discussing the "Concept Paper for Loan Development Project." During the 22nd Regular Meeting, the discussion centered on how best to implement this sub-component "given limited funds." The view from one member was that "with little time remaining (in the Project) it might be best to ride on existing training vehicles and not on individual IFIs" for the implementation of the loan development activities.

While training in project lending has been provided to some IFIs, there was no concrete activity related to loan development. The PBSP's interpretation of this sub-component differs from that of the USAID. The PBSP tends to interpret these terms in a broader sense to include "nurturing" activities for SMES that may have good business prospects but do not have the skills to present a financing package to the bank, "brokering" services to SMES that do not have access to formal credit and similar "developmental" interventions for SMES. The USAID sees "loan development activities" in terms of seminar/workshops for both IFIs and SMES where economies of scale and scope (of information) may be exploited.

There is a need to define the scope of activities under "loan development activities." This component of the Project should be made operational because the SMEs' lack of access to formal credit can be addressed by developing the skills of borrowers and lenders in financial evaluation and in the preparation of acceptable SME project proposals.

8.0 SUMMARY OF EVALUATION RESULTS

8.1 OVERALL ASSESSMENT OF THE SECP

8.1.1 The Policy Environment for SME Credit

The objectives of the evaluation are to assess: a) the impact of SECP on expanding credit supply to SMEs; b) whether PDBs (and an NBFI) are appropriate institutions to implement credit delivery; c) the IFIs' funds generation capability to assure sustainability; and d) the eventual benefits to SMEs financed under SECP. This Evaluation reviewed prior studies indicating that the overall success of the Project would depend on two factors: the policy environment for SME credit and the design of the Project. These two determinants of overall impact of the SECP are discussed in this section. The specific success of the project are measured along key result areas per the scope of evaluation above and are covered in Section 8.2.

There are industrial development policies that constrain the development of SMEs, like the bias in favor of capital-intensive industries, the administrative burden of regulations that favor well-staffed large firms, the concentration of support facilities in Metro Manila, among others. Many of these constraints are recognized and are being addressed by the Government. However, until moderate changes are made in such policies, there shall remain a bias against the competitiveness of SMEs relative to larger firms. Financing programs supporting SMEs shall be affected by these policy constraints. Only in industries or geographic areas where these biases are not as pronounced can the financing assistance be expected to be generally successful. Similarly, there are financial policies that are not supportive of the development financing requirements of SMEs. Some of these policies are the continued differentiation of financial institutions that serve business firms, the control of bank branching, the absence of a yield curve or pricing for long-term instruments, among others. These financial policies adversely affect SMEs in terms of restricted supply of credit, higher interest rates, high transactions costs and the unavailability of long-term financing for SME projects.

The government has been addressing these constraints to SME growth by formulating new policies and programs that support SMEs. Of key significance in this Evaluation are the various special lending programs directed at SMEs. The common characteristic of these programs is the heavy role of government oriented to "supporting" SMEs through: a) subsidized interest rates, especially for GFI-administered programs; and b) direct prescription by government of terms and "eligibility" requirements for SMEs to be implemented by IFIs. This policy and program orientation of the Government has changed little over the years. While there has been few, if any, formal evaluation of the impact of these lending programs, it seems clear that the desired development of the SMEs through financing assistance has been too slow to enable the SMEs to keep pace with industrial growth.

8.1.2 Achievements Due to SEC Project Design

The SECP takes an entirely different orientation compared to these traditional programs as to policy and in implementation. Its policy assumption is one of assisting SMEs through increased supply of term financing rather than through "cheaper" credit. In implementation, it is distinguished by the simplicity of its disbursement mechanism and the flexibility it allows the IFIs in structuring loans for SMEs. As significant is the accreditation procedure taken by the SECP which is premised on the commitment and potential of the IFIs for increased lending to SMEs.

The overall results of the project indicate that the SECP achieved success in terms of: a) increased IFI lending to SMEs; b) the high quality of such increased lending in terms of desirable development of capacities and new SME credit market; c) development of a number of IFIs into stronger institutions that shall sustain the policies of the SECP in the longer term; and d) delivering to the SMEs the financing suited to their needs.

The basis for the success of the SECP can be traced as mainly to the design of the project. It is a design that generally reflects sound credit principles as well as the realities of policy constraints to SME development.

At the bottom line, for a financing program to be successful, it must allow the financing institutions to select only the SME borrowers which can overcome their size and location disadvantage and still pay for higher transactions costs of the financing. The SECP allows IFIs the flexibility of selecting and structuring loans for their SME borrowers. In effect, the more serious the policy constraints, the greater is the general risk that the "average" SME would fail, even with directed and subsidized credit. It follows that a well-designed financing program should allow IFIs to look for SMEs that are less affected by these constraints and risks. Allowing IFIs the flexibility to structure loans is a logical design only if the IFIs are also required to absorb the risk of loan loss. This increases the incentive for the IFIs to evaluate SMEs properly and to support only those SMEs with competitive advantage in the marketplace rather than in the special financing windows of GFIs. In contrast, some special credit programs require IFIs to lend to "target" SMEs which have inherently high risks. The results for such programs have been very low success rates of SMEs and little sustainability of the financing by IFIs.

It is well-known that there is a dearth of long-term funds, especially in the countryside. SECP can be seen as a response to this condition in terms of the creation of a supply of long-term credit at commercial interest rates. Since term financing is not available to PDBs outside of directed public credit (where some do not qualify), the obvious effect of SECP is to increase the supply of financing.

One contrast between SECP and traditional special programs becomes clearer. SEC makes credit readily available through flexible terms but at commercial interest rates. In contrast, other special programs provide subsidized credit but with "eligibility" requirements that make transactions costs so high that the credit effectively becomes less available to many SMEs. The evaluation of the choice between the two is obvious. In a capital-short economy, priority should be given to increasing supply of capital. Scarce capital cannot be raised on a sustainable basis except when suppliers of capital are paid market rates.

SECP demonstrated that interest subsidies are not needed either by the IFIs or by the SMEs. The reasons are due to: a) the flexibility of the IFIs in lending allows them to choose SMEs which are successful and can pay commercial rates; and b) the segmentation of the credit market which allows IFIs to dominate the SME market and exercise their market power over SMEs in lending rates. In contrast, many subsidy schemes of special credit programs end up with the IFIs capturing the gains rather than the SMEs because of segmented credit markets. Similarly, it has been found that with subsidies, the Government ends up supporting the weaker SMEs, with adverse consequences on the long-term sustainable growth of the SME sector.

SECP showed that the greater benefits to SMEs can come from special credit programs that lower the transactions costs to IFIs and SMEs, instead of from interest subsidies. By providing a cash advance mechanism and by setting liberal terms and documentation requirements, SECP effectively lowered the transactions costs to the IFI. Since the IFI takes all the benefits of efficient credit delivery, such lower costs are either taken by the IFI, increasing their willingness to supply credit or passed on as savings to SMEs. In many special lending programs, the interest subsidy has been cited as benefits to SMEs. Often not cited are the reluctance of IFIs to increased lending which are not profitable to them and the stringent "eligibility" requirements that constitute transactions costs offsetting any subsidy.

Finally, the SECP established the importance of selecting IFIs in implementing directed credit programs. In effect, SECP's lending policy is "closed-door" except for IFIs committed to serving SMEs which are the development targets. In contrast, the approach of other special credit programs is one of "open-door", where any IFI which meets criteria other than those related to the goals of the program (like financial viability of the IFI) can be allowed to participate. There are some difficulties in implementing SECPs' approach because it requires a time-consuming qualitative assessment of the management of each IFI seeking accreditation. However, it was demonstrated in this case that the rewards in terms of achievement of the objectives of the project are substantial and likely to be more permanent. In the case of SECP, the policy constraints segmenting the credit market practically channelled the SECP into selecting the PDBs since they dominate the SMEs market. Nevertheless, as specific results indicate, appropriate screening is still necessary to select the more progressive banks from among the PDBs, where "progressive" refers to those IFIs with a clear view of how to increase the quantity and quality of their development financing to SMEs on a sustainable basis. Specific Evaluation results show that indeed, SECP sought and found a number of such progressive IFI implementors.

8.2 SUMMARY SPECIFIC EVALUATION RESULTS

8.2.1 Impact On Credit Delivery

The SEC is a relatively small special financing project when compared with other SME financing projects like IGLF and Countryside Loan Fund (CLF) and when related to the total financing requirements of the SME borrowers of the Philippine private development banks. However, the SECP is directed at SMEs outside the National Capital Region where there is a lower concentration of SMEs and financial institutions. Hence it is at the regional level where SEC has the potential to make a significant impact on increased lending to SMEs.

The SECP was implemented through PDBs which are the IFIs serving the SME segment of the credit market. The appropriate institutional vehicle for implementing an SME credit project is the "community banker." A financial institution operating in urban and rural areas which knows local conditions and which serves the local clientele is a "community banker." Such an IFI has a competitive advantage in terms of capacity to lend at the minimum transactions costs. PDBs, rural banks and lending investors are the "community bankers." In this group, PDBs generally have the resources and orientation to SMEs that make them successful implementors of the SECP. For the same reasons, selected large rural banks may have the potential to participate in the project subject to the same accreditation criteria applied on the PDBs.

A significant increase in lending to SMEs was observed after the implementation of SECP, with the most significant percentage increase among the smaller IFIs. New SME borrowers dominated the expanded credit provided under SMEs, indicating the qualitative benefits of an expanded formal credit clientele generated under the project. Overall, the result is a substantial expansion of the lending and asset base of the IFIs, particularly the small- to medium-size IFIs.

The Evaluation revealed three reasons for the availment of SEC financing by the IFIs for re-lending to SMEs.

First, SECP's design, characterized by flexibility in terms and cash advances, ensured low transactions costs from the SECP's project management office to the IFIs. Meanwhile, the transactions costs from the IFIs to the SME borrowers are also low because PDBs know their clients, have quick decision making being small organizations and require minimum documentation. The SECP's liberal design and selection of "community bankers" reduced transactions costs to ultimately benefit the SMEs probably in much the same way that a direct interest subsidy would, but certainly without the latter's distortionary effects on credit allocation.

Second, the ready availability of SEC as a source of term lending to SMEs enabled the IFIs to concentrate their efforts in marketing. The main constraint faced by IFIs remains the unavailability of long-term financing. Interest subsidies are not necessary but desirable from the viewpoint of IFIs because: a) it is easier for IFIs to market subsidized loans and b) the IFI can capture part or all of the interest subsidies.

Third, the SECP's design allows lending terms to SMEs to be decided upon by the IFIs. It enables IFIs to search for SME projects whose returns meet the commercial financing terms and whose risks are controlled through prudent loan structuring in accordance with normal bank policy. In short, SECP did not impede the IFIs' efficiency in SME lending decision process — from_search, loan structuring to collection. Because SECP does not impose any additional cost to IFIs for "developing SMEs", it is again unnecessary to provide any interest subsidies. The development of SMEs is seen by SECP as a natural consequence of supplying financing while allowing IFIs to seek out the most efficient SMEs.

Some potential weaknesses and issue were identified in the Evaluation, as follows:

a) A few borrowers accounted for a significant share of SEC financing. This may have constricted the supply to the smaller SMEs. However, some of these loans may have been to support SMEs that are "graduating" to large business.

b) SEC-sourced loans are positioned in the credit market only as short- to medium-term facility. By comparison, IGLF is considered long-term. The benefit of this design is the liquidity pressure it places on the IFI in support of the deposit generation aim of SECP. The disadvantage may be the resulting bias observed among IFIs in favor of medium- to short-term SME projects.

c) The process of setting of "market" interest rates for loans to IFIs needs improvement. The pricing basis using historical yields have limitations when there are significant changes in current yields. There are possibilities of temporary mispricing of SEC loans to IFIs in those cases, possibly resulting in either: a) higher rates to SMEs; or b) the IFIs capturing the gains from the mispricing situation. Moreover, this observation applies to all special lending programs that follow the same pricing formula.

d) There are IFIs which are more effective in delivering credit to SMEs and soon reach their maximum lending limit. However, the credit limit has been set only to control the institutional risk assumed by SECP. The question of balance between institutional risk and the need to support the liquidity needs of the more effective SMEs is a management issue facing SECP.

8.2.2 Impact on Sustainability of SECP's Development Benefits

A primary feature of the SECP is the manner it focuses IFIs management attention on the right-hand-side of the balance sheet, i.e., the refinancing of SECP loans. This presumes that the expanded loan base generated by the project shall be maintained by the IFIs — a key question of sustainability of the project's benefits.

Most IFIs were found to have coherent policies and programs for increasing deposits but their success is constrained by the segmented depositor markets and limited potential for growth in deposits in some areas. The Evaluation revealed that the main factor determining the capacity of the IFI to manage the right-hand-side of its balance sheet is the size of its resources. Larger IFIs have a clear advantage in refinancing and sustainability because they: a) have demonstrated deposit generation capacities and can refinance SEC loans; b) have loans portfolio's that are supported by adequate levels of deposits; and c) show superior profitability resulting in capital build-up and internal funds generation for lending. While there are IFI exceptions in each case, the indicators of sustainability point to the self-reliant policies being followed by the IFIs in Groups A and B: Such policies are the basis for sustainable lending to SMEs at the end of the project.

8.2.3 Impact of SECP on SME Growth

The increased lending of IFIs under SECP are generally acceptable credit risks because they selected SMEs which are successful and undergoing expansion. This policy of IFIs is consistent with sustainable future growth in lending by IFIs to the SMEs.

The SMEs supported by IFIs are about equally distributed between trading and manufacturing or services, reflecting a balanced development financing impact on SME beneficiaries due to the project. As to terms, the SECP was used by the IFIs mainly as a term lending facility with a significant short-term component. SECP's design allowed IFIs to structure tenors that are suitable to the needs of SMEs. The size of the IFI's resources was found to affect SMEs especially in the amount of lending. The size of the loans increases with the size of the IFI indicating that the economics of bank lending still favors larger loans. The SBL limitation is also a key factor in the ability of the IFI to meet the needs of the more successful SMEs. Without matching the growth of its SME borrowers, some IFIs would lose their clients to larger IFIs or to commercial banks.

8.2.4 Evaluation of Project Organization and Implementation

The present project organization is designed with two oversight units, the PIC and the Executive Director of PBSP, with the aim of drawing on the collective guidance of a multi-sector representation of PIC and the experience of PBSP. In practice, requiring the Project Director to be responsible to two separate units is not conducive to clarity in transmittal of policy and implementation guidelines to operating management. In spite of this weakness in organization design, it was found that the IFIs obtained SEC funds without delay and they have no complaints about the PMO's performance.

The choice of PBSP to implement the project at the initial stage was a sound one. The IFIs considered PBSP as effectively discharging its functions. PBSP has competently implemented the guiding policies of the SECP, particularly in giving flexibility to the IFIs in loan origination and use of funds. The main disadvantage of PBSP is its lack of experience in managing a large credit project. While PBSP competently performed the credit aspects of the project, the results in the other areas like training, policy research and project monitoring and impact assessment could stand improvement.

A key aspect of implementation that was effectively performed by the PBSP was the accreditation of IFIs based on the policy and orientation of these IFIs toward SMEs. The generally successful selection of IFIs contributed significantly to the overall success of credit delivery and provided good promise of sustainability of project results. Part of the success of the implementation of the SECP is due to the strong willingness of the IFIs to participate in the project because PBSP is not a financial institution and so is not perceived by IFIs as in a "conflict of interest" situation. A weakness in the implementation is the lack of effective monitoring of project impact on the SMEs and IFIs, and implementation problems/issues. Monitoring would have enabled the PMO and the PIC to re-direct the project and perhaps achieved increased benefits to SMEs and overall project efficiency.

The research and policy component of the SECP is a necessary one to enable the project to determine the constraints to project success and steps that should be taken to reduce these constraints. Only one study was commissioned in 1991. A summary review of this research indicated that many of the issues about SME promotion and credit policy have not been adequately addressed. Further, the commissioned studies should have been done at the initiation of the project to provide implementors an appreciation of the problems and policy concerns surrounding SMEs. Similarly, training is a useful support to the project and several were conducted to date. Field responses indicate that the training was found useful but would have been more relevant if made more relevant to an underdeveloped local economy setting. Meanwhile, PBSP was unable to undertake activities related to the loans development component of the project. The reason appears to be a difference between PBSP and USAID on the interpretation of what activities are involved in this component. PBSP refers to basic technical assistance activities to help SMEs seek financing. USAID sees this activity as the preliminary steps in the marketing process of SEC, i.e., to bring SMEs and IFIs together.

9.0 RECOMMENDATIONS

On the basis of the results of the Evaluation, certain areas for possible recommendations are identified, namely: a) measures to strengthen IFIs' delivery of credit, rural deposit mobilization and sustainability of SECP benefits; b) feasibility of involving financing institutions other than PDBs engaged in SME lending; c) suitability of increasing project funds for further IFI credit delivery; and d) choice of an implementing institution for any additional project funds. The recommendations along the above areas follow.

9.1 RECOMMENDED MEASURES TO STRENGTHEN IFIs' CREDIT DELIVERY, DEPOSIT MOBILIZATION AND SUSTAINABILITY OF BENEFITS GAINED UNDER SECP

9.1.1 Studies on Constraints to SME Development

POLICY STUDIES. Conduct policy studies on key issues affecting SME credit aimed to improve the policy environment for SMEs, as follows:

1. **Study of the SME credit market; and**

2. **Study of special SME credit programs to determine their impact on SMEs and IFI channels.**

The fundamental conditions for success and development of SMEs are determined by the policies affecting SMEs. There are a number of existing and planned legislation intended to provide credit support to SMEs but which can cause other distortions that may eventually retard the development of the SME sector. Examples are the "Magna Carta for SMEs," an existing law requiring banks to allocate a fixed amount of their portfolio for SMEs, and the "Regional Universal Bank," a pending bill requiring banks to retain funds generated in an area/region for relending in the same area/region. These policy initiatives are certainly based on sound development intentions but not necessarily on a valid assessment of the SME sector and its credit requirements. A study of the development of SME and its credit requirements shall provide the basis for anticipating and understanding the issues arising from implementation of these new policies.

The key lesson of SECP is that the success of an SME credit project is determined largely by the extent to which the project design is oriented to the characteristics of the SMEs it serves and the motivation of the IFIs channels through which credit flows. At this time, this is only a project-specific result, i.e., perhaps valid only for SECP. A broader policy question is whether the impact of the many other special SME credit programs are determined by the design features of these programs. There have been no prior studies of the impact of these credit programs on SMEs and IFIs. The perspective of program design is key to the aim of influencing future SME policy makers towards reducing the distortions that are currently experienced in the credit market.

9.1.2 Suitability of Increasing SEC Project Funds

ADDITIONAL SECP FUNDS. Increase funding assistance under SECP with emphasis in future lending to strong SME markets.

The evaluation results are unambiguous about the overall success of SECP. The Evaluation provided further insights into the segments of the market where SECP obtained the most gains. Specifically, when credit is channelled in areas with strong SME-based local economies, SECP achieved superior results. In those markets, IFIs face a deeper and more diverse lending market. Given a strong market, SECP can raise its development goals to a higher level. The IFIs, in turn, can respond to the project's development challenge because they have larger markets to draw upon to cover their costs and control lending risks. In those markets, there would be more "demonstration effect" relative to commercial banks and other IFIs of successful SMEs financed. Sustained growth of IFIs which handles SEC can also be expected. The results expected are sustained lending by participating IFIs to an expanding SME market and increased participation of commercial bank branches in SME lending even after the completion of SEC.

9.1.3 Feasibility of Involving Other Financial Institutions

INVOLVEMENT OF OTHER IFIs. Expand IFIs in SECP to involve other "community bankers" under accreditation standards as modified based on the lessons of the current SECP implementation.

A "community banker" has the orientation and track record of service to SMEs. Another key lesson of the current SECP is that a directed special lending program that uses IFIs with access to the SME market have the advantage of being already adapted to the transactions costs of this market. While the current SECP selected PDBs, this broader criteria can potentially include rural banks, savings and loan associations, branches of commercial banks, and cooperative banks. The search should be for IFIs that possess institutional strengths consistent with ensuring SME development, in particular:

a) credit marketing and processing capacities in serving a growing SME client base;
b) deposit generation policies and capabilities, supplemented by the ability to draw upon special credit programs;
c) institutional plans and strategies for developing its SME clientele and depositor market on a sustained basis.

9.1.4 Measures to Strengthen IFIs' Credit and Deposit Mobilization.

IMPROVEMENT OF SEC CREDIT DELIVERY TO IFIs. Improve effectiveness in credit delivery along areas identified in the Evaluation, as follows:

a) **Consider requiring prior evaluation and approval by the PIC of large sub-loans by the IFIs;**

Even with an increase in funding for SECP, the demand for credit by SMEs through IFIs cannot be adequately filled. Given that there is a cost advantage to IFIs in granting large loans, SECP should consider providing a further review and approval mechanism for larger loans. Large sub-loans from SMEs *per se* should not be discouraged and SECP should avoid increasing transactions costs and any delay in IFI processing for large sub-loans. In fact, SECP should continue to give large sub-loans, particularly for SMEs that "graduate" or take-off to large business. However, to the extent that other smaller loans from other SMEs are not funded or the further marketing efforts of IFIs deterred by its filled credit limit, the SECP should consider such a recommended review at the Project level.

b) **Review guidelines on credit limits of IFIs to possibly include lending performance and potential of the IFI in addition to capital.**

The main consideration applied in setting limits to IFIs' access to SEC credit is the institutional risk (of bankruptcy) that the project assumes. This is a sound principle and should remain the primary basis in setting credit limits on IFI borrowers. However, as the funding assistance to IFIs accumulate and as IFIs give priority to long-term (i.e., low turnover) sub-loans to SMEs, such credit limits shall be reached. The project would expect continuing requests from IFIs for increases in their credit limit. There is some merit to consideration of lending performance in setting credit limits on IFIs. If an extension of SECP with larger funding and a sharper developmental mandate is implemented, there may be a need to place more premium on IFI performance. For example, if one of the priorities of an extended SECP is more term finance, those IFIs which follow this mandate would attain their credit limit sooner than IFIs which lend on very short-term basis. Another example is when an area has a growing SME market but only one IFI qualifies under SECP accreditation criteria. Then that IFI would attain its credit limit sooner and further SME lending cannot be done by the IFI to the detriment of SECP's development objectives in the area.

c) **Conduct a study of the pricing of SECP loans to IFIs.**

The present pricing scheme by SECP of loans to IFIs requires further review because it is based on past history rather than on current realities of the market for funds. Evaluation results indicate that the SECP relending rates can be out of line with other currently quoted interest rates when there are rapid changes in the market conditions. The historical six-month average interest rates that SECP uses for pricing appears to be an approach used by other special lending programs. At best, use of historical interest rates helps smoothen out the fluctuations in interest rates over the previous six months.

9.2 RECOMMENDATIONS ON PROJECT IMPLEMENTATION AND ORGANIZATION

9.2.1 Proposed Project Implementing Entity for an Expanded SECP

IMPLEMENTING ENTITY: EXPANDED SECP. The lessons learned and achievements of SECP needs to be installed and made more permanent in an institution that can carry out the next phase of SECP. It is recommended that the Development Bankers' Association of the Philippines be given that role.

Because of SECP's unique contribution to the SME loan markets, there is a need to institutionalize the knowledge and skills derived from this project. It is appropriate to consider a movement in implementing institution for the project from PBSP, which has achieved its purpose of launching the project, to another institution composed of banks that serve the SME sector.

It is recommended that the implementation of SECP be passed on to the Development Bankers' Association of the Philippines.

The DBAP should assume management and implementation of the SECP because of the need to vest sustainability and a more permanent character to the project. The Project envisions a scenario where SMEs will be able to access the banking system's financial resources and services and IFIs will find this sector to be a profitable and useful sector to service. This will be made easier by assuring that the lessons gained from the initial stage of the Project are institutionalized and by promoting a permanent structure rather than by looking at the effort on a "project basis." At this time, SECP has the character of a "special project" of a prominent organization that is PBSP. Sustainability will be assured if a more formal rather than an ad-hoc character (such as what a project gives) is vested upon the project during the expansion stage. Making the DBAP the project implementor is an improvement because it brings the Project and its advantages and experience closer to its goal of institutionalization. However, there are some limitations in the current DBAP but these shall be addressed by the proposed new organization structure and roles.

9.2.2 Proposed New Organization Structure

ORGANIZATION STRUCTURE. A new organization structure should support the implementation of an expanded SECP at DBAP, using a design around the project concept with technical assistance and with capability to take on a permanence consistent with DBAP's gain in capacities by the end of the project.

The successful implementation of the next phase of SECP requires that the organizational structure of the Project be improved and strengthened. An expanded SECP requires consideration of an alternative organizational structure which can a) manage and monitor increased amounts of SME loans and b) resolve policy and operational problems with minimum cost to IFIs. Figure 4 shows the proposed organization structure which is a step to institutionalizing the knowledge and skills derived from the initial SECP. The immediate advantage of this structure is that the implementation and management of the SECP is transferred from the PBSP to the DBAP, an association which is in banking and a natural venue for advocacy for SMEs development among its membership. The main drawback of using DBAP is the absence of a strong and efficient DBAP Secretariat to serve as the Project Management Office.

This second-generation set up will ultimately give way to a situation in the future when SECP funds or similar SME funds will be managed by the individual IFIs for re-lending to SMEs on a sustainable basis. At that future time when both IFIs and SMEs will have become business partners, there will be no more need for a Project Management Office and the PIC to oversee the use of funds for SME lending.

Role of PBSP

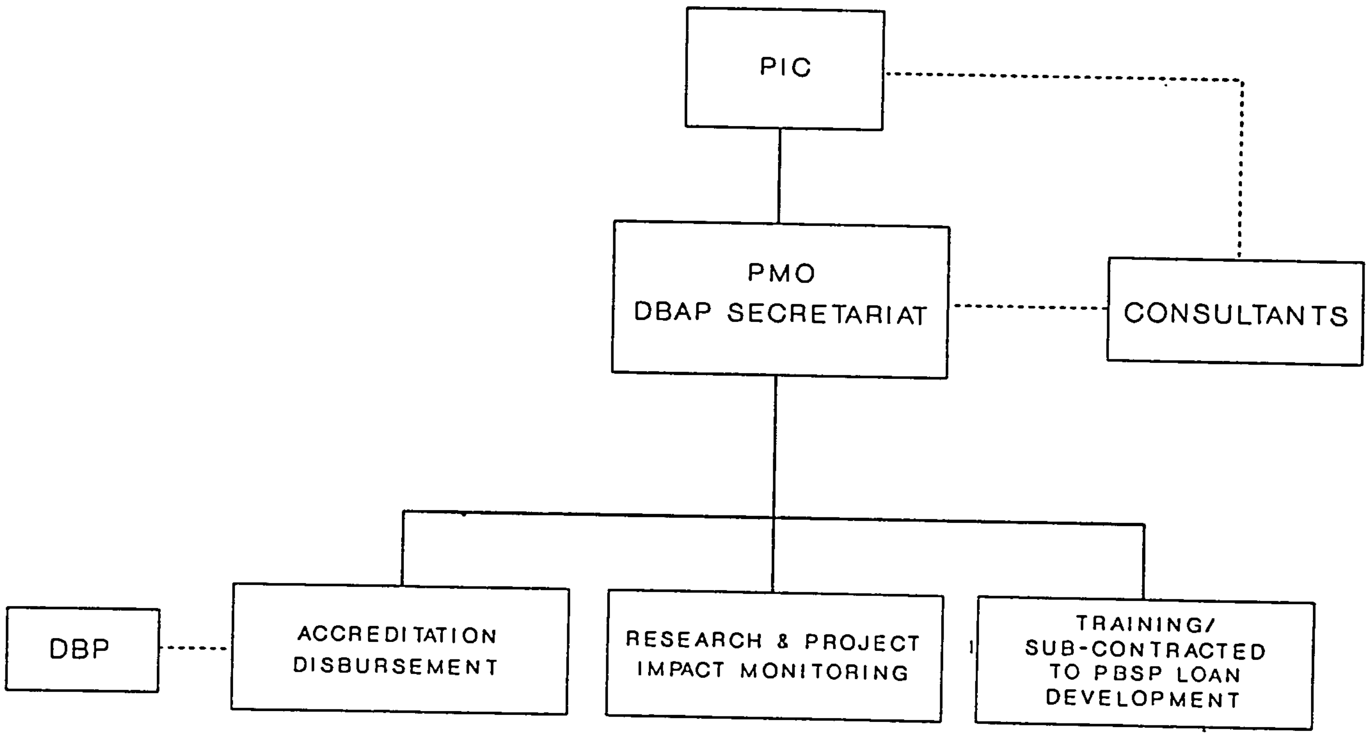
The PBSP is primarily a development-oriented NGO with an affirmed commitment to countryside development and specific focus on poverty alleviation. It has built a lot of expertise in institution building and training activities which the SECP can continue to tap.

The DBP and USAID

These two institutions continue to sit as non-voting members of the PIC. The DBP shall continue to be the Trustee Bank while the USAID shall lend advice to the PIC on policy matters.

Figure 4

Small Enterprise Credit Project
Proposed Organization Structure



9.2.3 Roles of Organizational Units and Institutions

KEY ROLES. The organization units under the proposed structure should assume key roles that are consistent with an ingredient in the success of the current SECP, namely minimum of "red tape" and transactions costs to the IFI. These key roles are:

a) The PIC: policy guidance and strategy, project performance review, and major credit allocation policies.

It is proposed that the PIC should retain its present membership but the chairman should be the DBAP President. The PIC will provide policy guidance and strategy, review the performance of the Project and make major total credit allocation decisions. It should not be involved in day-to-day administration of the Project. This function should be delegated to the PMO which is the DBAP Secretariat.

b) The PMO: administration of the project, impact monitoring, and coordinating contracted work and with

The Project Management Office (PMO) to be headed by an Executive Director will manage the Project and will be in charge of three main functions: a) IFI accreditation, loan evaluation and credit disbursement; b) research and project impact monitoring and c) training and loan development. These are functions that the SECP has, but except for (a), were not carried out effectively. There is a need for a formal unit under the PMO to provide Project impact monitoring so that the PIC and the donor agency can be regularly informed of the overall performance of the project. The training and loan development activity for SME borrowers shall be contracted to various institutions, the PBSP included, which have experience and expertise in institution building and training of beneficiaries. The training pertaining to the IFIs will be handled by the PMO which can engage professional trainors or institutions to provide the expertise.

An innovation in the structure is the use of professional consultants who will be engaged on-call basis to lend guidance and expertise to the DBAP Secretariat (PMO) so long as it is not yet prepared to assume the task of administering the SECP.

c) Consultants: technical support to PIC on policies and strategy, to PMO on key activities, and installation of a project monitoring system for the PMO.

Consultants should be engaged for a limited period of time. Their main task will be to provide expert advice and render technical support to the PMO on the three main functions of a) accreditation and disbursement; b) research and impact monitoring and c) training and loan development activities. They shall also be responsible for the formulation of a research agenda for the SECP which will be implemented during the life of the project. They shall install a project monitoring system which shall be operated by the relevant unit in the PMO. They are expected to transfer relevant expertise to the PMO. The consultants should work in close harmony with both the PIC and the PMO but shall report directly to the Executive Director.

Annex A

SCOPE OF WORK

Annex A

SCOPE OF WORK

1. Project to be Evaluated

The project to be evaluated is the Small Enterprise Credit (SEC), details of which are as follows:

Project Authorization:		September 27, 1989
Project Title	:	Small Enterprise Credit Project
Grantee	:	Phil. Business for Social Progress
Grant amount	:	$13.0 million

Project Description : The project is composed of three interrelated components: 1) an expanded intermediate financial institution (IFI) and lending component for Small and Medium Scale Enterprises (SMEs); 2) research and policy analysis to better understand the constraints facing SMEs; and 3) training and loan development courses to train bankers and entrepreneurs in SME project lending.

Project Elements:

Credit	$12,000,000
training & loan development	382,000
research & policy studies	360,000
project administration	108,000
evaluation	150,000
Total	$13,000,000

Project Assistance Completion Date (PACD): September 30, 1992

2. Purpose of the Evaluation

This mid-term evaluation of the SEC project is intended to assess the implementation of the Intermediate Financial Institution (IFI) credit mechanism after a full year in operation. While the project is viewed as a liquidity tool, it is also designed as a rural deposit mobilization tool. The evaluation should therefore measure the present project performance in both perspective.

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The project shall also be evaluated in terms of probable new lending directions it could take. Additional project funding and the inclusion of rural banks (or other thrift banks) in project lending are being considered. The evaluation should validate and justify this expanded project activity. The general concerns that the evaluation should address are the following:

a) Effectiveness and efficiency of this rural deposit mobilization and credit mechanism both in terms of its contribution to greater IFI lending to SMEs and to the SMEs themselves.

b) Adequacy and cost effectiveness of the private development banks as vehicles to deliver credit to SMEs.

c) Whether deposit mobilization was affected as a result of the banks' participation in this project.

d) Administrative, management or project implementation issues relating to the delivery or usefulness of credit to SMEs.

e) Measures that should be initiated to strengthen IFI rural deposit mobilization and the delivery of credit to SMEs

f) Possibility and desirability of expanding accreditation to include other financing institutions engaged in SME lending such as: rural banks, thrift banks, leasing and finance companies.

g) Appropriateness and usefulness of adding more funds to the IFI credit mechanism either for present institutions or for institutions identified in f), above.

h) Appropriate implementing private entity(ies) for any additional credit funds channeled through a new set of financing institutions.

3. Background

The project background and rationale are included as "Attachment A" to this Section C.

4. Evaluation Questions

This evaluation report shall address the following specific questions:

A) <u>Impact of the rural deposit mobilization and credit mechanism on the IFIs</u>

1) Is the project instrumental in introducing or encouraging greater lending to SMEs by participating IFIs?

2) How significant or. what is the extent of any additionality in the IFIs loan portfolio?

3) What portion of the IFIs SME lending portfolio were transfered to project funding?

4) Is the increased volume of SME lending by the IFIs, if any, attributable to loans for new SME borrowers or is it comprised of additional loans to existing SME borrowers?

5) What is the extent of credit fund utilization by the IFIs? How many of the accredited banks availed fully or partially and how many banks are not availing at all?

6) What accounts for availment of some banks and the non-availment by other banks?

7) How does the funds utilization in the project compare with those of other available lending programs (i.e. ALF, IGLF, etc). What are the reasons for the pattern of utilization for or against the various lending programs?

8) Does the additional liquidity to the IFIs from the project funds translate into additional lending by the IFIs, or were the funds simply placed in risk-free government securities?

9) Does the mismatched terms of the funding to the IFIs and their loans to SMEs encourage deposit mobilization? How significant is the deposit mix and increase, if any, in proportion to their total deposit level?

B) <u>Contribution of project lending to small and medium enterprises</u>

1) What are the characteristics of the borrowing SMEs? Is the project able to address the progressive SMEs engaged in non-farm activities rather than the traditional cottage and very small firms or the dominant group of large firms?

2) How have the SMEs used the credit resources provided? To finance working capital? capital purchases?

3) How many SMEs have benefitted from the credit? Does this number represent a significant percentage of total number of SMEs serviced by the participating IFI?

4) Did the micro enterprise and cottage industries benefit as well from the project funds? What percentage is this of the total number of enterprises assisted by the project?

5) How much was the actual volume of loans extended to SMEs in relation to total project lending by the participating banks?

6) In terms of sectoral coverage, is the credit able to address the needs of targeted off-farm or non-production activities? What specific sectors or activities were assisted by the project? What sectors outside those targeted were assisted?

7) Is the concentration of project lending on traditional business activities or more on growth/impact areas or those with significant value added?

8) Is credit assistance all that the SMEs need or are there other non-credit assistance requirements to strengthen their ability to absorb and repay credit?

9) Are they equipped technically to identify and prepare bankable projects?

C) <u>Constraints to Credit Delivery</u>

1) How well equipped are the IFIs in delivering credit to SMEs? What specific forms of assistance are needed by the IFIs to accelerate lending to SMEs?

2) To what extent is institutional strengthening of the participating IFIs required to help them become active participants in SME lending in the countryside.

3) What accounts for more active participation of Manila-based private development banks (PDBs) in the project lending compared to PDBs outside National Capital Region (NCR)?

4) Are the participating IFIs really practicing development lending? How prepared are they to go beyond collateral and look instead at the project's cash flow potential as the source of loan repayments?

5) Are there administrative, operational, legal or management bottlenecks affecting the flow of deposits to and credit from the servicing institutions (PBSP, DBP, the IFIs) to the SMEs? What are the usual requirements imposed by accredited banks on SME loan applicants?

6) Are the mandates of PBSP and DBP as spelled out in the agreements clear cut and supportive of the deposit mobilization and credit delivery mechanism? If not, what sort of additional roles do they have to play to become effective partners?

7) Are these institutions capable technically and administratively to run the project's credit components effectively? What training or assistance do they need to do a better job? Are there other private institutions that are better equipped?

8) What is USAID's role and contribution(s) in project implementation? Is there a need to modify or expand its role to be more effective player in future projects?

9) Are there enough viable development projects in the countryside for project funding?

10) Is there an implied need to train SMEs to prepare them better to identify business opportunities and translate them into viable projects?

11) To the extent training and technical assistance is being suggested for PBSP, DBP, IFIs, and SMEs, what are the priorities and how critically needed is such assistance?

D) New Directions of Project Lending

1) Is the present list of 17 accredited private development banks (PDBs) able to achieve geographical or nationwide presence for the project?

2) Or, should more PDBs be accredited in the regions with no project presence yet?

3) Aside from PDBs, should rural banks, thrift banks and other categories of banks or even non-banks with countryside or regional focus be considered as well to maximize the project's outreach to SMEs?

Can this be substantiated with actual indication of interest from these banks and non-banks to participate in the project's rural deposit mobilization and credit component?

4) How much additional volume of SME lendings can these banks usefully contribute to the project? This estimate will justify what additional credit funds can be added to the existing credit component.

5) Is the present project management set-up capable of taking on the project's proposed additional activity: additional funds to be channeled thru rural banks, etc.

6) How supportive are the participating IFIs in promoting the market oriented interest rate of the project funds as compared to the subsidized rate of other government lending programs?

7) Are the participating banks putting a premium on the availability of credit to new SMEs as against interest rates in their efforts to move the project funds?

8) What kind of mandate should PDBs have and what role(s) should they play for the development of SMEs? What specific banking services should they offer to SMEs?

9) What new monitoring tool(s) should be put in place to strengthen credit delivery to SMEs?

10) What specific role(s) should the Development Bankers Association of the Philippines (DBAP) play to become more responsive to SMEs?

5. Method of Evaluation

The evaluation of the project will entail the following activities:

a) Institutional assessment of PBSP (the project implementor) and DBP (the trustee).

b) Field visit to participating IFIs in their respective regions. The list of the 17 accredited banks, their location and contact address is summarized in Attachment V. Thirteen of the PDBs are operating outside the NCR Manila and will be the subject of field visits. The rest have their head office in Metro Manila.

c) Sampling of projects or economic activities assisted by the project and interview with selected project proponents.

d) Identification of other categories of banks and non-banks recommended for inclusion in project lending.

6. Team Composition

The evaluation team will be composed of individuals with appropriate professional background and work experience as follows:

An evaluation team leadersourced locally, who has academic preparation in development banking and finance and has sufficient work experience in development projects relating to rural deposit mobilization and credit programs. He/she is expected to provide leadership and direction to the team in the performance of the scope of work.

One local evaluation specialist, who has training in development finance and has sufficient technical experience in evaluating rural financial development projects.

One local evaluation assistant, who has academic preparation in accounting and liability management and experience in evaluating development projects.

7. Report Requirements

The reports will have a format as follows:

-- Executive Summary (See Attachment C to this Section)
-- Project Evaluation Summary (See Attachment D to this Section)
-- Table of Contents
-- Body of the Report
-- Appendixes

The executive summary states the development objectives of the activity evaluated; purpose of the evaluation; study method; findings, conclusions, and recommendations; and lessons learned about the design and implementation of the activity. (See Attachment C to this Section for more detailed instructions.)

The body of the report will include discussion of (1) the purpose and study questions of the evaluation; (2) the economic, political, and social context of the project; (3) team composition and study methods (one page maximum); (4) evidence/findings of the study concerning the evaluation questions; (5) conclusions drawn from the findings, stated in succinct language; and (6) recommendations based on the study findings and conclusions; stated as actions to be taken to improve project performance and must cover the following specific areas:

deposit mobilization
credit component
training component
technical assistance
policy component
implementor: PBSP,
IFI: private development banks, others.

The more detailed discussions of methodological or technical issues will be placed in appendices.

Appendices will include a copy of the evaluation scope of work, the most current Logical Framework as pertinent, a list of documents consulted, and individuals and agencies contacted. Additional appendices may include a brief discussion of study methodology and technical topics if necessary.

Annex B

STUDY METHODOLOGY

Annex B

STUDY METHODOLOGY

A detailed description of the methodology to be adopted in the evaluation of the SECP was included in PSR Consulting's proposal submitted to the USAID. A summary of the proposed evaluation methods, activities and techniques is shown in Table B-1.

The Study was undertaken using this methodology. A discussion of the actual implementation of aspects of the methodology follows.

Survey of Banks

A survey of thirteen sample participating IFIs was made. To facilitate the survey, three survey instruments were formulated, namely: an Interview Guide for IFIs, a Bank Questionnaire and a Borrower Brief. The Interview Guide asks questions on bank policies, assessment of the SME loan market and assessment of the SECP and SECP implementation. This was accomplished by the Interview Team. The Bank Questionnaire asked about basic bank statistics and lending procedures which could be prepared independently by a bank staff. The Borrower Brief was intended to validate some of the sub-borrower data already in the PBSP's file and to generate additional data needed in the SECP evaluation being conducted. This was to be prepared by the banks based on the loan folders of the SECP sub-loan borrowers. The survey instruments were designed such that data gathering can be simultaneously implemented in one bank with different respondents. This approach enabled the Field Survey Teams to gather data in the shortest possible time.

The selection of the IFIs survey was based on the following criteria:

1) Metro-Manila based IFIs
(Asiatrust, Planter's Development Bank, Private Development Corporation of the Philippines)

2) Urban areas outside Metro-Manila with perceived significant manufacturing activities
(Banco Cebuano - Cebu, Banco Davao - Davao, Bangko Silangan Development Bank - Batangas, Laguna Development Bank - Laguna, Northern Mindanao Development Bank - Cagayan de Oro, Queen City Development Bank - Iloilo and Southern Negros Development Bank - Bacolod)

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3) Urban areas outside Metro-Manila with minimal manufacturing activities (Bicol Development Bank - Bicol, Dumaguete City Development Bank - Dumaguete, and Palawan Development Bank - Palawan)

4) Branches of IFIs with head office in Manila (PDCP - Cebu, Iloilo, Davao)

In addition to the twelve IFIs and three branches, the Cebu and Davao Branches of the Northern Mindanao Development Bank were also visited to maximize the coverage of the survey since these branches are also found in the same locations as some of the sample IFIs. All in all, the survey covered a total of twelve IFI head offices and five branches.

Two field visits were conducted. The first round covered twelve IFIs. The second round was conducted to verify the initial findings and conclusions of the Study. Covered were the Visayas and Mindanao branches of the PDCP as well the IFIs in three regional growth centers, namely: Cebu, Cagayan de Oro and Davao.

The list of the banks visited is shown in Table B-2 while the list of persons interviewed is shown in Table B-3.

Survey of SECP Sub-Loan Borrowers

To acquire some understanding of the final beneficiary of the SECP, a limited survey of the sub-loan borrowers was done. For this purpose, an interview guide for SME borrowers was prepared and used during the survey. The SME borrower interviews were conducted with the following objectives: 1) to validate some loan data like actual use of the loan; 2) to develop an understanding on the business attitude and prospects of the borrowers; 3) to determine the reasons for the choice of banking with the IFI and attitude towards banking and credit access in general; and, 4) to find out the IFIs' experiences in loan application, release and repayment.

Assessment of Project Implementation

An assessment of the institutional capability of the SECP Project Management Office (PMO) of the PBSP and the DBP was undertaken. Interviews were conducted with the officers and staff of the PBSP PMO. SEC project documents and minutes of the PIC meetings were reviewed. The IFIs were also asked to make individual assessment of the PBSP and DBP during the field survey.

Review of Project Documents

The study reviewed three sets of project documents, namely: IFI sub-loan portfolio, IFI loan folders and SEC project papers and project implementation documents each described briefly below.

1. IFI sub-loan portfolio

   The IFI sub-loan portfolio is a computerized master file maintained by the PBSP. It contains the following information:

   Basic information about the loan: names of borrowers, sub-loan amount, date of loan, term, loan purpose and collateral cover percentage

   Information about the borrowers: location/address, nature of business, annual sales, asset size, number of employees

   Other information: whether borrower is a new or existing client and would the bank give a loan without SECP assistance

   These data files were developed from the Transactions Reports submitted by the IFIs for each sub-loan granted under the SECP. To a limited extent, part of the information were validated by the Study during the conduct of the field interviews.

   The Study processed and analyzed the IFI sub-loans database to observe trends in the utilization of the fund and the developmental orientation of the loans in terms of the type of SMEs financed and the extent of additionality in the IFI's portfolio.

2. IFI loan folders

   The individual loan folders of each of the seventeen SECP participating IFIs were also reviewed. In particular, analyses of the financial statements of the IFI were made.

3. SEC project papers and project implementation documents

   The SEC project papers contained the basic project concepts, objectives and operational mechanisms of the SECP. The project implementation documents consisted of minutes of meetings of the Project Implementation Committee (PIC), workshop/training reports and reports of studies commissioned by SECP. All of these documents were reviewed to develop a good perspective of the Project's concepts and objectives and how these were actually sought to be undertaken.

Review of Literature

To have a good perspective of the Philippines industrial policy structure as it affects the SME sector, the Philippine banking system and special SME financing programs, a review of relevant literature was made. The following is the list of reference materials reviewed for the Study.

1. Bautista, R.M. and John H. Power and Associates, **Industrial Promotion Policies in the Philippines**, Philippine Institute of Development Studies, 1984.

2. Hife, Emmanuel, "Survey Results on the Impact of Industrial Policies on Small Industry Development," from Bautista, Powers, et. al, **Industrial Promotion Policies in the Philippines.**

3. Lamberte, M., Comparative Bank Study: A Background Paper, Working Paper 87-04, Philippine Institute of Development Studies.

4. Saldaña, Cesar G., "The Philippine Commercial Banking System: Structure, Performance and the Impact of Capital Build-up Program of 1972," **The Philippine Review of Economics and Business** XX (June 1983): pp. 215-232.

5. Saldaña, Cesar G., "Comparative Management Structure and Institutional Performance in Rural Banking Institutions," Working Paper No. 88-16, **Research Folio Series**, November-December 1989, Philippine Institute for Development Studies.

6. Biggs, Tyler; Levy, Brian; Oppenheim, Jeremy; Schmitz, Hubert, **The Small Business Policy Direction Study**, Harvard Institute for International Development and Center for Research and Communication, Chap. 1, p.7.

7. Churchill and Lewis, "The Five Stages of Small Business Growth," **Harvard Business Review**. Volume 61 No. 3.

8. Survey of Establishments, National Census and Statistics Office, 1983.

9. Central Bank Center for Statistical Information, Department of Economic Research - Domestic, Central Bank of the Philippines.

10. Industrial Dispersal in the Philippines, Volume 1, National Economic Development Authority, 1986.

Table B-1
MID-TERM EVALUATION OF SEC PROJECT
EVALUATION METHODS, ACTIVITIES AND TECHNIQUES

EVALUATION METHODS	ACTIVITIES	TECHNIQUE
1. Institutional Assessment		
• IFI	Field Visit	Rapid Assessment
• PBSP/DBP	Visit Document Review	In-Depth Review
2. Review of SEC Loan Portfolio		
• PBSP	Visit Document Review	In-Depth Review
• IFI	Field Visit Portfolio Review	In-Depth Review
3. Review Deposit Performance Under SECP		
• Policies	Field Visit: IFI	In-Depth Review
• Performance	Field Visit: IFI	
• Growth Prospects	Market Area	Rapid Assessment
4. Evaluation of SME Lending (Market and IFIs)		
• SMEs • Other IFIs in SME Lending	Field Visit	Rapid Assessment
5. Review of SECP Design and Management		
• PBSP • USAID	Visit	In-Depth Review

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Table B-2

List of IFIs Visited

BANKS	LOCATION
Asiatrust Development Bank	Metro Manila
Bangko Silangan Development Bank	Batangas
Banco Cebuano - Cebu City Development Bank	Cebu City
Banco Davao - Davao Development Bank	Davao City
Bicol Development Bank	Legaspi City
Dumaguete City Development Bank	Dumaguete City
Luzon Development Bank	Laguna
Northern Mindanao Development Bank	Cagayan de Oro
Palawan Development Bank	Palawan
Planters Development Bank	Metro Manila
Private Development Corporation of the Philippines	Metro Manila, Cebu, Iloilo, Davao
Queen City Development Bank	Bacolod City
Southern Negros Development Bank	Bacolod City

Table B-3

List of Persons Interviewed

Philippine Business for Social Progress

Patricia Corpuz-Calilong	Assistant Project Director
Rene Hapitan	Assistant Project Director
Remedios Masangkay	Administrative Assistant
Carmela Volante	Service Assistant

Development Bank of the Philippines

Corazon Conde	Assistant Vice-President
Estrella del Cruz	Bank Executive Officer III
Feliz Lim	Bank Executive Officer III

Asiatrust Development Bank

Pedro Lucero	First Vice-President - Account Management Division

Banco Davao - Davao Development Bank

Eduardo V. Ano-os	Vice-President/General Manager
Ma. Merceditas A. Aguipo	Chief Accountant
Leon Y. Pamplona	Assistant Manager/Branch Operations Officer

Bangko Silangan Development Bank

Jessie G. Clamor	Chief Operating Officer
Maximo A. Chavez	Senior Loan Supervisor

Bicol Development Bank

Fidel L. Cu	President
Jose Eduardo A. Imperial	Loans & Administration Officer

Banco Cebuano - Cebu City Development Bank

Roland dela Torre	President
Imelda Maranan	Special Projects Officer

Dumaguete City Development Bank

Silvestre Sung	Executive Vice-President

Luzon Development Bank

Felix H. Limcaoco	Chairman/President

Northern Mindanao Development Bank

Guido Alfredo Delgado	Managing Director
Calvin Luther Genotiva	Assistant Vice-President, Business Development & Lending Services
Richard Hoasen	Branch Manager - Mandaue, Cebu
Isidro Ungab	OIC - Agdao, Davao
Jose Rolex B. Ratillla	Account Officer - Agdao, Davao

Palawan Development Bank

Eric Mondragon	President
Mariquita Pontillas	Assistant Manager - Loans & Credit Department

Planters Development Bank

Agnes Angeles	First Vice-President

Premiere Development Bank

Malou Flores	Manager - Project Evaluation Division

Private Development Corporation of the Philippines

Adolfo Ledesma	Senior Vice-President
Patricia May Siy	Assistant Vice-President - Branches
May Therese Javellana	Branch Manager - Davao City
Jima de Leon	OIC - Iloilo City

Queen City Development Bank

Rogelio M. Florete	President
Elsa L. Peregil	Vice-President - Operations
Eliezer Divinagracia	Loan Supervisor
Fred Hontanar	Loan Processor

Southern Negros Development Bank

Roberto G. Abello	President
Socorro Castellano	Acting Manager, Head Office
Teddy Filiu	Loan Officer

Annex C

CASE STUDIES OF IFIs VISITED

ASIATRUST DEVELOPMENT BANK

Asiatrust Development Bank, formerly Quezon City Development Bank, started as a development finance institution in October 1960 with an initial paid-up capital of ₱ 1.0 million. Through the years, the Bank played a major role in the growth and success of SMEs of Quezon City and in nearby areas. It has brought in a new management, increased its capital base and broadened its loan product capabilities to emphasize its developmental perspective. As of December 31, 1991, the bank had total resources of ₱ 1.6 billion and a capital base of ₱ 153.4 million. The Bank's head office is located in Quezon City. It operates ten branches located in Metro Manila (6), Rizal (2), Cavite (1), and Isabela (1). It plans to open four additional branches in Metro Manila within the year.

Uses of SECP funds

Asiatrust was accredited with the SECP in April 1990 with condition that SECP funds shall be for the exclusive use of the Bank's branches outside of Metro Manila. The Bank's initial authorized credit line was ₱ 15.0 million. This was subsequently increased to ₱ 25.0 million on of March 31, 1991.

As of March 31, 1992, total Bank drawdowns amounted to ₱ 15.0 million. This drawing represents only a 60 percent utilization of the Bank's authorized credit line. It is the lowest among the three large IFIs and compared to the seventeen participating IFIs.

The Bank has a total SECP sub-loan portfolio of ₱ 13.9 million granted to twelve borrowers. Of this amount, ₱ 11.1 million came from SECP funds. The SECP funds actually allocated for relending by the Bank translates to a low 44 percent relending efficiency rate, an SECP indicator calculated by dividing the SECP contribution to the portfolio by the amount of the total credit line.

Asiatrust had a few sub-borrowers (twelve) who were provided with relatively larger amounts of sub-loans. The average size of the SECP sub-loans is about ₱ 1.16 million, the highest among all 17 participating IFIs. Fifty percent of the sub-loans are in the ₱ 900,000 to ₱ 2.0 million loan range. In terms of amount, only four or one-third of the sub-loans account for 61 percent of the total SECP loans. The lowest sub-loan was ₱ 250,000 while the highest was ₱ 2.5 million.

The Bank used the SECP mainly to finance borrowers engaged in trading activities (67 percent). Borrowers from the manufacturing sector accounted for 17 percent of the total sub-loans. The loan purpose of two sub-loans representing 16 percent of the total of sub-loans could not be determined from the Project files.

Two or 16 percent of the sub-loans were for fixed assets acquisition while ten or 67 percent were for working capital purposes. All ten sub-loans with available information had maturities ranging from two to three years.

Four of the nine borrowers with available information (33 percent) are new while five (42 percent) are existing clients.

SME Loan Market

As a banking institution, Asiatrust management expressed its dedication to serve SMEs. The Bank considers SMEs as a market niche where it enjoys a strong competitive advantage. Asiatrust's focus on SMEs may be seen in the assignment of 22 of the Bank's 26 employees in the Loan Processing and Evaluation Unit to do the processing of SME accounts.

The Bank's main lending operation is based in Metro Manila. However, it has provided increasing support to countryside SMEs. In the case of the SECP for example, the majority of the sub-loans were granted to SME borrowers in Isabela.

During 1991, Asiatrust extended a total of ₱ 743.8 million in loans to small- and medium-scale businesses, representing 49 percent of the Bank's total loan releases. Of this total amount, ₱ 208.8 was granted to SMEs in the countryside. The Bank expects its countryside SME loan portfolio to grow as it expands its banking activities in the rural areas.

To increase its lending to SMEs, the Bank has identified the need for more training for bank personnel particularly in the following areas: (1) financial analysis; (2) appreciation of regional development trends and the status of the local economy and (3) client prospecting and identification.

Impact on the Bank's Liquidity

The SECP had a marginal impact on Asiatrust's financing source. The outstanding SECP loan balance as of December 31, 1991 accounted for less than three percent of total borrowings as of the same date. A similar marginal impact was also made on the Bank's lending operation with the SECP loan balance as of December 31, 1991 accounting for less than two percent of the change in the net loans from December 31, 1990 to December 31, 1991. The Bank's ratio of loans to deposit on December 31, 1991 was 88 percent indicating its strong capability to support Bank lending with funds generated from deposits.

Although Asiatrust is aware that it cannot always rely on special loan funds for its lending activities due to the high cost of these funds, the Bank looks at the SECP as another valuable loan facility in the Bank's inventory of loan products the variety of which, according to management, makes banking with Asiatrust attractive to its clients.

Bank Lending Policies

Asiatrust uses the following loan evaluation criteria ranked according to importance:

a. Project viability
b. Creditworthiness of the borrower
c. Track record
d. Collateral/security offered

Most of the other SECP participating IFIs placed borrower's creditworthiness as the most important criterion in the evaluation of loan applications. The high priority placed by Asiatrust on project viability indicates that the Bank uses a formal loan evaluation process.

To minimize risk, the Bank's policy is to lend only to SMEs with history of successful business operation.

Asiatrust has a relatively liberal collateral policy compared to other SECP participating IFIs. Although all loans are required to offer security, chattels like assignment of inventories or receivables are accepted. Moreover, the Bank grants loans up to as much as 100 percent of collateral value.

On average, it takes the Bank only about seven days to decide upon a loan application, which compares well with the loan processing periods of smaller SECP IFIs.

The Bank management believes that lending to SMEs requires highly-specialized skills. To improve its efficiency in handling SME accounts, the Bank trains its personnel in areas like financial analysis.

Asiatrust charges an average lending rate of 23.5 percent for SME loans. This means a 6.0 percent spread over the 17.5 percent that the Bank pays the SECP in recent transactions. The interest rate may differ depending on the client. According to management, the spread may be as low as four percent, at which rate the Bank's profit is marginal with practically no allowance for possible default.

To minimize the risk of nonpayment, the Bank adopts a system of monitoring of loan accounts by account officers who visit the borrowers at least once a month.

Deposit Mobilization and Performance

Deposit mobilization is a serious thrust of Asiatrust. Institutions and SMEs are the depositors preferred by management.

Asiatrust's deposit mobilization i ısed on generating short-term time deposits (mostly 90 days) which the Bank uses for short-term lending and investments.

Bank management believes that there it is not possible to assume that deposits are permanent or long-term because depositors can withdraw their deposits anytime to take advantage of high-yielding alternative instruments like Treasury Bills. Bank management estimates that the residual core of deposits in Asiatrust amounts to only 5 percent of total deposits. It was cited by management that due to the growing sophistication among depositors who do not lock in their money in term deposits, Asiatrust has decided to campaign mainly for 90-day placements.

The Bank has found its wide range of bank products like time deposits and trust funds and the giving of competitive interest rates effective in mobilizing deposits. Some of the other strategies used by the Bank to generate deposits are: 1) launching of an automated tellering service called the "Cash Stations," 2) creation of a Customer Satisfaction Program, 3) training of Bank personnel to provide good and personalized service, and 4) branch expansion program.

The deposit generation efforts of the Bank had very significant results. Total deposits increased at a compound annual growth rate of about 44 percent from 1988 to 1991. Moreover, there was an improvement in the Bank's deposit mix. In 1987, the Bank had a deposit mix of 55 percent savings, 39 percent time and 6 percent demand. In 1991, the composition improved to 77 percent savings, 20 percent time and 3 percent current deposits. By decreasing the share of time deposits to total deposits, the Bank was able to decrease the effective cost of funds from deposits.

Bank Assessment of the SECP

Asiatrust's corporate vision is to serve the SMEs and thus, the SECP merely complements what the bank has been doing for the past decades.

The Bank finds the following as the most favorable features of the SECP:

1. Advance funds are given based on loan projections submitted by the Bank.

2. The Bank is allowed discretion in lending.

3. The training component is helpful in improving the loan evaluation capability of the Bank personnel.

The Bank management indicates that no other financing program provides advance money to finance projects and allows bank discretion to design the sub-loan package. This was pointed out as a unique feature of the SECP which allows the bank to design a financing package to the particular needs of its SME client.

Asiatrust considers the SECP as just another source of liquidity for SMEs which the Bank will continue to serve even after the completion of the SECP. However, the important advantage that the management attributed to the SECP is its ready availability considering that bank deposits are a volatile source of loanable funds.

The management identified the market-based interest rate of the SECP as a weakness of the Program. Unlike SECP, the Land Bank-World Bank Countryside Loan Fund (CLF) offers the borrower a choice between a fixed rate or a floating rate. Asiatrust noted that to develop a special market like the SMEs, banks must be able to provide loans with interest rates that are at least one or two percentage points lower than market interest rates.

According to management, one of the disadvantages of the market-based interest of the SECP funds is that the borrowers tend to prepay their SECP loans when they are able to source cheaper funds such as from the Philippine National Bank's Pangkabuhayan Loans. Asiatrust believes that frequent loan prepayments is disadvantageous to the Bank because projected income drops with overhead expenses remaining at the same level. In addition, the paper work involved is also tedious for the Bank's Treasury Department.

Asiatrust commented on the need for some improvement in SECP's implementation. In particular, the Bank noted the rather "long reaction time from the policy decision done at the PIC level to the operational interpretation of the decision," particularly citing the SECP interest rate system issue. The Bank suggests that the PBSP should be directly responsible for training and the setting of policy guidance while the DBP should handle the trust and loan administration aspects of SECP's implementation.

BANCO DAVAO

The Davao City Development Bank, otherwise known as "Banco Davao", was established on January 25, 1965 in Davao City. It operates three branches located in Digos in Davao del Norte (opened in 1968), Tagum in Davao del Sur (opened in 1970) and Koronadal in Cotabato (opened in 1977).

Use of SECP Funds

Banco Davao was accredited with the SECP in March 1991. It has an authorized credit line of ₱ 5.0 million which has been fully drawn down. A subsequent request for an increase in the line was denied because of the failure of the Bank to reduce the equity of the Development Bank of the Philippines in Banco Davao down to 35 percent.

As of March 31, 1992, the Bank had a total SECP sub-loans portfolio of ₱ 6.56 million made out to 21 borrowers. The loan size category with the most number of sub-loans (38 percent) is the ₱ 45,000 to ₱ 100,000 loan range. However, in terms of amount, only three loans amounting to ₱ 4.2 million accounted for 64 percent of the total SECP sub-loans. The smallest loan granted was ₱ 25,000 while the biggest was ₱ 1.5 million.

The Bank used the SECP funds mainly to finance borrowers in the trading sector. About 71 percent of the sub-loans financed trading activities. Loans to the manufacturing sector was 24 percent of the total SECP sub-loans.

Most of the loans granted were short-term, with maturities of one year or less. However, a fairly significant number - 8 representing 38 percent of the sub-loans had maturities of mostly three years. This would imply that the Bank is open to giving medium to longer-term loans when justified by the financing need of the loan applicants and did not simply give out "renewable" short-term loans to finance the long-term requirements of clients.

Of the 19 SECP sub-borrowers with available information, 9 are new and 10 are existing Bank clients giving an almost one to one ratio of new to existing borrowers.

SME Loan Market

Due to its limited resources, Banco Davao considers SMEs as its natural market. Based on the SECP loan profile of the Bank, the main market of the Bank are the agri-product and fish traders. In addition, it also lends to service establishments like trucks and auto repair shops, machine and foundry shops as well as to public utility operators.

The Bank management describes the loan market in Davao as segmented according to loan size where specific types of financial institutions dominate, as follows:

₱ 25,000 and below	-	lending investors
₱ 50,000 and below	-	rural banks
₱ 50,000 to ₱ 300,000	-	development banks
₱ 150,00 and above	-	commercial banks

The Bank claims to be the leading SME lender in the ₱ 50,000 to ₱ 300,000 range loan size. Although some commercial banks in Davao already accept loan applications for at least ₱ 150,000, they do not dominate the market for this loan size. This is attributed to the long processing period of commercial banks as branches still have to refer the applications to their regional or Manila offices for approval. Banco Davao's loan processing may take as short as three days after collateral appraisal.

Banco Davao considers the good relationship among the local banking community important to the loans marketing effort of the Bank. According to management, as a result of an informal agreement among the members of the banking community in the area, it has become a practice for some commercial banks to refer to Banco Davao loan applications for amounts that fall below their minimum loan limit. The Bank in turn makes referrals to commercial banks for loan applications and/or loan inquiries beyond its single borrower's limit (SBL).

Impact on the Bank's Liquidity

SECP had a significant impact on Banco Davao's liquidity being the Bank's only source of outside financing in 1991. However, the large impact on liquidity did not translate to a major impact on Bank lending. The outstanding SECP balance as of December 31, 1991 represented only 15 percent of the increase in the net loan portfolio of the Bank from 1988 to 1991. Banco Davao has a loans to deposit ratio of 98 percent which indicate a good capacity to generate deposits to support to its lending operation.

Bank Lending Policies

The Bank cites two basic reasons for the attractiveness of lending to SMEs. First, the management finds the evaluation of the loan applications of SMEs relatively easier than those of big businesses. In particular, the Bank considers assessment of credit worthiness of small borrowers easier because a person's "gut feel", developed from exposure to the applicant's type of business and knowledge of the borrowers' reputation in the community are deemed sufficient basis.

The second reason of management is that SME entrepreneurs can easily rehabilitate its operation and start anew in case of business difficulties. This capability reduces the risk of nonpayment by SMEs.

Despite its favorable assessment of SMEs which are the Bank's main clientele, Banco Davao requires all loans except the institutional or group loans to be secured by loan default collateral. A highly conservative management attitude can be gauged from the collateral cover required. The loan value is set at a maximum of only 49 percent of the appraised value of the collateral.

According to management, the Bank's loan evaluation criteria ranked according to degree of importance are:

a. quality collateral
b. creditworthiness of borrower
c. project viability

The high importance placed on collateral is another indication of the conservative attitude of the Bank regarding loan loss recovery.

It would seem that while Banco Davao meets the SECP's desired market, its lending policies are not conducive to the attainment of the Program's objective of enhancing access to credit of viable SMEs constrained by lack of collateral.

Deposit Mobilization and Performance

The last time the Bank had a major deposit mobilization campaign was in 1988. The result was a more than 100 percent increase in deposits. Banco Davao plans to undertake another major campaign. However, it is still looking for an appropriate promotion strategy because other banks in the area are offering very attractive prizes like a house and lot package.

As its regular deposit mobilization strategy, Banco Davao offers attractive interest rates on deposits. The Bank once set the interest on savings deposits at 6 percent per annum. However, since it did not experience any marked increase in the deposit balances, Banco Davao decreased the rate to 5 percent, a rate still higher than the 4 percent at commercial banks. Time deposit rates are generally set by the Bank at one or two percentage points above the commercial banks' rates.

After the major increase in the deposit level in 1988, growth in deposits slowed down. From 1988 to 1991, total deposits grew at a compound rate of 22 percent. This increase in deposits, however, was not fully beneficial to Banco Davao because of the decline in savings deposits relative to time deposits, increasing the cost of deposit funds. From about 55 percent in 1988, savings deposits represented only 42 percent of total deposits in 1991. On the other hand, the percentage share of time deposits went up from 45 percent in 1986 to 58 percent in 1991.

Bank Assessment of the SECP

Banco Davao finds the absence of collateral requirement as the most attractive feature of the SECP. According to management, this feature makes it easy for the Bank to draw SECP funds. The second and third highest rated characteristics of the Program are: the "training component" and "advance funds." Banco Davao also finds the SECP accreditation and loan availment procedures simple and easy to comply with. According to management, the availment and monitoring requirements of the Countryside Loan Fund (formerly Agricultural Loan Fund) are more tedious to prepare compared to the requirements under the SECP.

The Bank evaluates that the SECP made a minimal impact on its lending operation because it considers the amount of its credit line to be very small.

The management also commented on the need to refine the formula for setting the interest rates on the SECP loan. It was pointed out that at one time, the interest rate charged was higher than the Treasury Bill rate.

Annex C-3

BANGKO SILANGAN DEVELOPMENT BANK

Bangko Silangan Development Bank (formerly Batangas Capitol Development Bank) was established in September 1969. In 1987, there was a change in the ownership of the Bank and an infusion of some ₱ 13 million of fresh capital. Bangko Silangan's head office is located in Batangas City. It has four branches found in Balayan, Bauan, Lemery and Nasugbu, all in the province of Batangas.

Use of SECP Funds

Bangko Silangan was accredited with the SECP in September 1990. From an initial amount of ₱ 15.0 million, the Bank's credit line was increased to ₱ 21.0 million in September 1991. Another ₱ 3.0 million increase was approved in February 1992 making the Bank's total credit line equal to ₱ 24.0. The Bank has drawn the full amount of its credit line and has even reavailed of another ₱ 7.0 million. As of March 31, 1992, the Bank's total availment has amounted to ₱ 31.0 million. In terms of funds moved, Bangko Silangan ranks first among the nine PDBs in Group B IFIs.

The Bank has granted a total of 331 SECP sub-loans amounting to ₱ 33.2 million as of March 31, 1992. About half of the loans were in amounts ranging from ₱ 45,000 to ₱ 400,000. Another major grouping accounting for about 36 percent of the SECP sub-loans were in a smaller loan category ranging from ₱ 10,000 to ₱ 40,000. The smallest loan granted was ₱ 9,000 while the biggest was ₱ 1.0 million.

The BSDB's SECP sub-loans portfolio consists primarily of SMEs in the trading sector. About 81 percent of the loans granted went to individuals and firms engaged in trading while only about 11 percent went to borrowers engaged in manufacturing. In terms of amount, those in trading accounted for about 75 percent of the SECP sub-loan portfolio.

The Bank used the SECP mainly to provide short-term financing, less preferred tenor per the Program's objectives. Majority of the sub-loans had a maturity of one year or less. Only about three percent of the total sub-loans had maturities of more than one year to three years. The short-term nature of the sub-loans granted is consistent with the general purpose of the loans which is to finance the working capital of trading companies, the majority of borrowers. The BSDB differs from the other SECP participating IFIs whose sub-loans went mostly to trade for working capital purposes but with a maturity of mostly three years.

Bangko Silangan was able to provide credit access to a substantial number of new borrowers through the SECP facility. Of the 320 sub-loan borrowers who have available information, 200 were classified as "new" and 120 as existing or a ratio of about 17 new for every one existing Bank borrower.

SME Loan Market

The Bank considers SMEs as its natural market and estimates that loans granted to SMEs constitute about 50 percent of its total loan portfolio.

Batangas, the Bank's main area of operation is essentially an agricultural province. However, there is a strong trading sector basically involving the buying and selling of agri-products and a growing number of home industries. The following is a general profile of the Bank's loan market based on the SECP loan portfolio of the Bank:

Major traded products: rice and corn, cattle and livestock, general merchandise, ready-to-wear clothes, fresh meat and fruits and vegetables.

Manufacturing industries: embroidery and garments making, bakery, handicraft manufacturing, metalcraft, food processing and stuffed toys manufacturing.

Service industries: restaurants, printing services, hospitals, recreational centers and tailoring shops.

The Bank's management believes that there is a big market for SME loans. However, the potential borrowers need to be convinced to expand their business and to finance the expansion by borrowing from banks. Management considers entrepreneurs in the area as "not aggressive" businessmen who need to be encouraged to exploit business opportunities. This observation of the Bank is consistent with the assessment of another SECP participating IFI (Luzon Development Bank) which operates in the same area as Bangko Silangan's.

It is foreseen that the SME loans market will grow as a result of the heightened economic activities that are expected to occur in the area. Growth in the economy is expected to come from investors outside of the region who will take advantage of the economic opportunities in the area.

The Bank believes that commercial banks do not generally lend in the countryside, and as such, it consideres "lending investors" as its biggest competitor. Contrary to what appears to be a common perception among the other IFIs, Bank management thinks that lending investors do not confine their lending activities to small loans. While interest rates charged by lending investors are generally higher, their main advantage is the simplicity in documenting their loans.

Impact on the Bank's Liquidity

The SECP was the only source of outside financing of the Bank. As of December 31, 1991, the Bank's outstanding SECP loan balance of ₱ 20.20 million constituted 100 percent of /total Bank borrowings. The Bank is seeking accreditation with the International Guarantee Loan Fund to augment its sources of loanable funds.

The SECP provided moderate support to Bangko Silangan's lending operation. As of December 31, 1991, the outstanding SECP net balance represented about 23 percent of the change in the Bank's total loan portfolio. This may be explained by the BSDB's low loans to deposit ratio of 76 percent which is indicative of the Bank's strong capability to generate deposits to support its lending activities.

Bank Lending Policies

As a general rule, the Bank tries to minimize risk by financing projects that have business track records although no minimum years of operation is required. However, depending on the borrower's background, the Bank may consider "start up" projects if the owner/manager has had previous experience in the business (e.g., production or sales manager).

It is Bangko Silangan's policy to lend on the basis of the prospects of the business and never not on the strength of. As an example, the management cited the case of a jeepney operator who, due to his special relationship with a landowner, has been given the exclusive and shorter right-of-way to a destination passing through the landowner's property. The shorter route substantially reduced the duration of the trip which enabled the jeepneys to make additional trips.

The Bank looks at the business as the main source of loan repayment. As such, the management claimed that the Bank is open to granting clean loans to viable businesses. However, there appears some discrepancy in the application of this policy in the case of the SECP sub-loans which are more than fully-secured, either by a real estate or chattel mortgage. The amount of the sub-loans, in general, represented about 60 percent of the collateral values.

The management claims to provide full financing support to the borrower by designing the amount and term of the loan around the financing needs of the project. A longer loan maturity of between three and five years is considered if warranted by the project. On the basis of this policy, it appears that the Bank utilized the SECP facility properly. A significant majority of the loans had a maturity of one year while the SECP is meant to provide medium to long term financing. The Bank appeared to have few qualified borrowers for long-term financing among its loan applicants.

The Bank's lending practice appears to be flexible such that it is able to exploit even higher risk loan opportunities. This can be seen in the case cited by management involving a loan applicant whose business was assessed to be basically viable. The Bank determined that the financial difficulties of the applicant were due to the company's weak financial management capability. The Bank approved the loan application of the borrower, however, in order to minimize the risk of nonpayment, it placed a condition that the Bank will be allowed to put a Bank-seconded treasurer in the company.

Bangko Silangan exhibits development-oriented lending practices by engaging in activities which are meant to develop potential borrowers. The Bank is involved in organizing a marketing arm for a group of local handicraft manufacturers who refuse to export directly because of their lack of knowledge of export procedures and lack of financing. The assistance is intended to improve the profitability of the manufacturers while the Bank expects to benefit from the expanded banking services of these growing businesses.

The Bank's organization is geared towards aggressive loans marketing. On top of the branch managers are loan product managers at head office who are responsible for loan marketing and monitoring (e.g., there is a product manager for the USAID SECP). They cut across the geographic areas of responsibility of the branch managers. According to the Bank's management, this organizational set up has been successful as evidenced by the increase in loan applications received by the Bank.

The Bank believes in the institution of a formal credit process and in the training of staff. Its professional management team is headed by a former officer of a multinational bank who brought into Bangko Silangan a new kind of thinking and technology on banking, in general, and on credit and loans marketing, in particular.

Deposit Mobilization

Bangko Silangan's deposit mobilization effort has significantly increased the Bank's deposit level. Total Bank deposits increased at an annual compound growth rate of 55 percent from 1988 to 1991. However, the increase has been mainly in time deposits, as reflected in the deterioration of the Bank's deposit mix at the end of 1991. The share of savings deposits declined from 37 percent in 1988 to 28 percent in 1991. Correspondingly, the share of time deposits increased from 63 percent in 1986 to 72 percent in 1991.

Bank Assessment of the SECP

The Bank's management found the "no collateral requirement," "training component" and "advance fund" as the three most attractive characteristics of the SECP. The Bank management found the flexibility of not requiring collaterals advantageous. However, it appeared to have failed to take advantage of this flexibility when the Bank uniformly applied its collateral policy even on the SECP sub-loans.

The management believes in staff training and always participated in the training programs sponsored by the SECP. According to the Bank, the availability of loanable funds in advance enabled it to be aggressive in loans marketing.

It is the opinion of Bank management that the three-year maximum term of the SECP loan is not long enough. The term should be lengthened to five years to make a more significant impact. Considering that the Bank's SECP loan portfolio are mainly short-term in nature, it would appear that the Bank is thinking of a prospective rather than a current financing need for their SMEs.

Annex C-4

BANCO CEBUANO

Banco Cebuano (formerly known as Cebu City Development Bank) was established in December 1961. During the past thirty years, the Bank has undergone several changes in both ownership and management. A new group of stockholders took over the ownership of the Bank and a new management team was put in place in 1988. Its head office is located in Juan Luna, Cebu City. It operates a network of five branches in the following locations: Lapulapu, Tabunok, Mactan Export Processing Zone, Mandaue and Consolacion.

Use of SECP Funds

Banco Cebuano was accredited with the SECP in September 1991 and was approved an initial credit line of ₱ 5.0 million. In February 1992, the Bank's credit line was increased to ₱ 15.0 million due to the approval of an additional line of ₱ 10.0 million. The Bank has fully drawn the initial ₱ 5.0 million line as of December 31, 1992. By March 31, 1992, it has drawn the entire ₱ 15.0 million line.

As of March 31, 1992, the Bank has given a total of 32 sub-loans amounting to ₱ 4.3 million. A significant portion of the loan (63 percent) went to borrowers engaged in manufacturing. The balance of about 37 percent were equally shared by borrowers in the trading and service categories.

Majority (about 75 percent) of the Bank's sub-loans were in the PDB loan size from more than ₱ 45,000 to ₱ 200,000. The lowest amount of sub-loan granted was ₱ 15,000; the highest was ₱ 500,000.

The SECP sub-loans were mostly short-term. Of the 32 loans granted, 26 or 81 percent had a loan term of one year or less. The remaining 6 loans (19 percent) had loan term ranging from more than one year to three years.

Most of the SECP sub-borrowers (about 84 perecent) are new borrowers of the Bank. The ratio of new to existing borrowers is about 14 to one, reflecting efforts by the Bank to expand its client base with SECP.

The SECP borrowers of Banco Cebuano can be considered SME's both in terms of the number of employees and asset sizes. There are not more than 10 employees in most of the enterprises whose loan amounts vary directly with their asset base.

SME Loan Market

The SME borrowers of Banco Cebuano manufacture a variety of products showing the widening manufacturing base enjoyed by the Cebu province compared to other SECP project areas. Some of these products are fashion accessories, stonecrafts, soap, fertilizers, shoes, hats, metalwork and other metal fabrications, bakery products, automobile sunshields, furniture and public utility jeepneys.

The Bank's target market consists of both individuals and companies in the SME sector, 90 percent of which are in manufacturing.

The Bank has about 10 to 15 percent share of the SME loan market which the Bank management believes is currently dominated by the Northern Mindanao Development Bank (NMDB). Commercial banks appear to be uninterested in the SME sector while the rural and thrift banks do not have the financial capacity and expertise to handle SME loans.

The Bank management foresees an improvement in the economy especially in Cebu, substantial part of which is expected to come from the growth in the SME sector. It was pointed out that the SME sector has grown very fast in recent years and that one of its unique advantage is its flexibility. Management cites the experience of local rattan craft manufacturers which, after the decline in the rattan-related business, shifted nimbly to the manufacture of fashion accessories.

Impact on the Bank's Liquidity

The SECP was the Bank's only source of outside financing in 1991. The Bank's outstanding SECP loan as of December 31, 1991 of ₱ 5.00 million represented 100 percent of its total borrowings.

The SECP was a substantial source of support for the Bank's lending operation. The ₱ 5.0 million outstanding balance of the SECP loan as of December 31, 1991 constituted about 41 percent of of the change in Banco Cebuano's net loan portfolio.

Bank Lending Policies

Management expressed the following policies relative to its SME lending:

1. SMEs are more risky and requires more attention compared to the traditional trading and commercial companies. Specially trained staff are needed to efficiently handle SME accounts.

2. Borrowers should have been engaged in business for at least five years.

3. SECP sub-loans, which are mainly to new borrowers for the Bank, are charged an average interest rate of 30 percent. This reflects the kind of risk that the Bank perceives among new borrowers who perhaps do not have the credit track record among banks that can be the basis for a more accurate risk management. The more important result is that due to SECP, financing was made available even to marginal SME borrowers.

4. All loans are collateralized. However, the Bank has not relied on traditional real estate mortgages to secure the SECP loans and has accepted less secure collaterals like chattel mortgage and purchase orders. Purchase orders financing are commonly used by export-oriented firms.

5. The Bank consciously seeks out SMEs engaged in manufacturing. The Bank management regularly consults with the Department of Trade and Industry (Cebu) and the Cebu Chamber of Commerce to determine the industries that these offices will promote in the area. In addition, the management also gives guidelines on priority industries to support. For example, the shoe industry in Carcar, which has not been growing as much as expected has been identified for financing support by the Bank.

Deposit Mobilization and Performance

Banco Cebuano considers deposits to be a good source of loanable funds because these are relatively low cost. However, Bank management perceives deposits to be a volatile source noting that at any given time on average, only 50 percent of total deposits remain as "core" deposits of the Bank. In which case, the management thinks that the SECP loan, while relatively costlier than deposits, is a better source of loanable funds because it is available over a fixed term. The Bank plans to mobilize funds in the rural areas where it had better experience in retention of deposits (in the bank) compared to the urban areas of Cebu province.

The Bank employs two schemes to mobilize deposits, namely:

1. promotional campaigns
2. competitive interest rates

The promotional scheme consists of offering a combination of an interest rate which is 2 percent higher than those offered by other banks and a life insurance policy for the depositors for minimum deposits of ₱ 10,000. The bank offers 8 to 10 percent on savings deposits, Banco Cebuano's interest rate is one percent higher than those of other banks.

Bank management believes that its deposit mobilization has been strengthened by the establishment of four additional branches, spread over strategic locations in the province of Cebu, in the last two years. The impact of this move started to be felt in 1991 when total deposits increased by 51 percent over its 1990 level.

Over the four-year period, 1988 to 1991, the Bank's total deposit increased at a compound annual growth rate of 14 percent. Although the rate of growth in deposits was rather slow, the Bank was able to achieve a significant improvement in its deposit mix. The ratio of savings to total deposits increased from 26 percent in 1987 to 52 percent in 1991. On the other hand, time deposits decreased from 74 percent in 1987 to 48 percent in 1991.

Bank Assessment of the SECP

The Bank finds the cash advance arrangement as the most attractive feature of the SECP. The second and third highest ranked SECP features are "no collateral requirement" and "flexible policy to determine loan terms," respectively. These features are valued by the Bank respondents and reflect the simple administrative procedures and flexibility of terms on the SECP terms to IFI.

The Bank management commented that the SECP-sponsored training that had been implemented were more attuned to commercial bank lending and not oriented towards countryside development and development financing. Management also expressed a need for a training program for bank personnel.

Management considers the SECP interest rates high and calls for a reduction to promote "SME borrowings". The Bank management further proposes that the "large spread enjoyed by DBP" should be eliminated so that the interest on SECP funds can be lowered, which is indicative of the Bank's inadequate understanding of the role of DBP in SECP.

Bank management would like to explore SECP assistance in building an appropriate database on SMEs so that client prospecting can be facilitated. In particular, the management bilieves that there is a need to systematize the gathering of information on various SMEs and the industries where they operate.

Annex C-5

BICOL DEVELOPMENT BANK

Bicol Development Bank is the first development bank in the Bicol region. Subsequently, it encountered financial difficulties. In November 1989, the Development Bank of the Philippines approved the total buy out of the controlling stocks of the Bank. The new owners are headed by Mr. Fidel Cu who also owns the Rural Bank of Nabua, Inc. (RBNI). RBNI was the seventh largest rural bank in the country in 1989 in terms of resources.

The new management immediately put in place programs of action to rehabilitate the Bank, namely:

1) updating past due accounts
2) increasing savings deposits
3) expanding credit facilities
4) project development

The fourth program aims to create a new image of the Bank. Management sought to instill in the community a message that the "new" bank is a bank with a social conscience. This means that the Bank will be more active in community development.

The Bank's capital in 1989 was ₱ 3.2 million and total resources was ₱ 12.7 million. By 1991, the new owners increased capital stock to ₱ 8.75 million and total resources grew to ₱ 37.1 million. The shares of the Land Bank of the Philippines were already bought back by the owners and the buy back of the Development Bank of the Philippines shares were being finalized last June 1992. By July, the Bank would be 100 percent privately owned.

Uses of SECP Funds

The Bank was accredited in 1990 with a credit line of ₱ 5 million. One month later, the credit line was increased to ₱ 10 million. As of March 1992, the Bank had the highest credit turnover in SECP at 1.7 times its credit line. Management fully utilized the Bank's ₱ 10 million credit line and reavailed another ₱ 7 million. During the same period, the Bank submitted portfolios with a total value of ₱ 18 million. The SECP financed 80 percent or about ₱ 14.4 million. As a result, the Bank used 96 percent of the ₱ 15 million it withdrew from the SECP.

As of May 1992, the Bank has submitted the largest number of accounts (1,611). The amount of this portfolio is ₱ 18.9 million for an average size of ₱ 11,700.

About 95 percent or 1,536 of the portfolio had loan amounts of less than ₱ 5,000. These loans amounted to ₱ 5.4 million or 28 percent of the portfolio. Another three percent or 52 projects had loan amounts of less than or equal to ₱ 25,000. This group's loan amount of ₱ 359,000 is only about two percent of the portfolio. The rest of the loans have values of more than ₱ 25,000, with the largest loan amounting to ₱ 700,000. These loans, amounting to ₱ 13.1 million, comprised 69 percent of the portfolio. However, they accounted for only 23 percent of the total number of borrowers.

All loans except nine accounts went to businesses classified as those engaged in manufacturing. However, the average size of these loans is only ₱ 8,950. This indicates that small borrowers are engaged in cottage and micro enterprises. On the other hand, three of the loans went to traders with a combined loan amount of ₱ 4.6 million for an average loan size of ₱ 1.5 million.

A total of 1,532 borrowers were new borrowers of the Bank. These borrowers accounted for ₱ 18.2 million in loans or about 96 percent of the SECP portfolio.

SME Loan Market

There are few small-scale or medium-scale enterprises in the Bicol region. While there are manufacturing enterprises in the area, these are mostly cottage-scale and micro-scale enterprises. In the Tabaco area, there are steel fabricators manufacturing blades or in some firms, farm implements. Narra furniture makers can also be found in the area. Daraga and Oas have abaca handicrafts. Food processing, such as pili nut processing, can be found in Camarin, Guinobatan and Sto. Domingo. Construction materials, like hollow blocks, are manufactured all over the area because of the abundance of quality "Albay sand." There is a tire retreading plant in Legaspi but a commercial bank already handles its credit needs.

Small-scale enterprises are usually involved in trading of commodities such as rice.

In terms of target markets, the Bank looks at major industries in the area. Examples are metalcrafts in Tabaco and pili nut processing in Camarin. The Bank is studying the opportunities for financing of subcontractors doing piecemeal work in the area to convert the subcontractors' project-based operations to a continuous operation.

The Bank designed an innovative lending program using the IBM-DECS. Public school teachers can avail of small unsecured loans under this program. These loans are usually processed and released on the same day of application as the use of credit tools are minimal. Collection of payments is done through a salary deduction scheme in coordination with the IBM-DECS.

This arrangement explains the large number of loan accounts of the Bank, borrowers working as teachers but own small livelihood projects operated by family members at home.

Impact on the Bank's Liquidity

In 1991, the outstanding balance of the SECP was ₱ 9.63 million. This is 26 percent of the its total resources of ₱ 37.1 million making it a major source of fund. The high loans-to-deposit ratio of the Bank (4.13 in 1990 and 1.73 in 1991) show that it requires external financing to cover the gap between deposits and loans created.

The Bank considers the SECP as a major source of liquidity and that its loans will decrease when SECP terminates. Without the SECP, management would require a more selective lending policy due to funding limitations.

Bank Lending Policies

Since the new management took over in the later part of 1989, all available funds were put to maximum use. No investments were made and minimum cash balances were maintained. Instead, most funds were used for loans, with focus on micro-scale enterprises with small loan requirements. Although management seems aggressive in asset generation, it has a conservative lending policy. Management requires a loan-to-equity ratio of 1:1 and a loan-to-collateral ratio of 1:2. The Bank accepts applications for loans sizes as small as ₱ 3,000. However, its large loans has been as large as of ₱ 3.6 million.

The Bank defends its conservative policy in loan evaluation by pointing to its funding constraint. By going after small loans, bank management believes that it would not be adversely affected by loan defaults by a few borrowers. The Bank also focuses on collecting past due accounts taken over from previous owners of the Bank.

The Bank's minimum lending limit is now set at ₱ 50,000. It still targets small businesses or individuals as it is still building its deposit base. Past loans show that most loans went to firms with assets between ₱ 50,000 and ₱ 100,000 or cottage-scale enterprises. The ₱ 50,000 minimum loan amount indicates a move towards small-scale enterprises. It was a result of the audit findings of the Project Management Office (PMO) of the SECP. The PMO called the attention of the Bank on the small amount of the loans (₱ 3,000-₱ 5,000) submitted for SECP financing.

The primary criteria for evaluating loan applications are: 1) creditworthiness of the borrower, 2) project viability, 3) collateral, and 4) capacity to pay. These criteria are used in all loan evaluations regardless of the size of the borrower's enterprise.

The Bank has a staff of four in its loan processing and evaluation unit. Assignments are regularly rotated within the Bank to transfer skills and to ensure continuity of operations in the absence of key personnel.

Deposit Mobilization Strategies and Performance

Deposits grew by 383 percent from 1989 to 1991, an increase from ₱ 648,000 to ₱ 15.1 million. In 1991, savings deposits accounted for ₱ 8.7 million and time deposits accounted for ₱ 6.4 million. Almost all accounts are held by individuals.

The new management has been aggressively mobilizing deposits since it took over operations in 1990. Bank personnel actively campaign for deposits because of incentive system programmed by the Bank. Management and staff prefer to take primarily individual rather than corporate depositors.

In January, the Bank made a deposit campaign among market vendors which generated ₱ 1.0 million in deposits over three months. It has also started a Kiddie Savers Club to encourage savings among children. Special prizes are given to new depositors of the Kiddie Savers Club depending on the opening amount. All these is supported by radio ads. There is a plan to conduct another raffle, with jeepney operators as preferred depositors. The bank president personally campaigns among community members for large balances in of time deposits.

Clients of the Bank can also avail of the services of the five branches of the Rural Bank of Nabua, Inc. and Rural Bank of Milaor, Inc. aside from the Bank's extension office at Tabaco, Albay.

Bank Assessment of the SECP

The advance funds feature of the SECP was ranked first followed by absence of a collateral. Surprisingly, management was not aware of the advance funds feature. Loans were already released to the end borrowers before the Bank asked for a reimbursement from the SECP.

The market-based interest rate was ranked last. Management pointed out that a historical basis for interest rate setting would not reflect current market prices.

Management agrees that SECP contributed to increased lending to SMEs and to the Bank's loan profitability. However, it points out that the SECP also affects their liquidity position because of the 20 percent counterpart contribution required of IFIs.

DUMAGUETE CITY DEVELOPMENT BANK

The Dumaguete City Development Bank (DCDB) was established in July 1980 in Dumaguete City, Negros Oriental with an initial capital of ₱ 4.0 million. As of December 31, 1991 or about eleven years later, shareholders' equity has increased to ₱ 24.1 million and total resources amounted to ₱ 104.8 million. DCDB has a branch in Valencia, Bukidnon.

Uses of SECP Funds

The Bank was accredited with the SECP on July 20, 1990. As of March 31, 1992, DCDB has availed of ₱ 12.0 million or only 80 percent of its total credit line of ₱ 15.0 million.

Together with its counterpart contribution, the Bank was able to grant loans amounting to ₱ 17.55 million to 24 SECP sub-loan borrowers all in the trading and service business. There was no sub-loan to the manufacturing sector because the local economy is in agriculture and trading. There is virtually no manufacturing base in Dumaguete City and nearby areas.

The sizes of the sub-loans granted by the Bank were relatively high compared to the other SECP participating IFIs. Majority (62 percent) of the Bank's SECP sub-loans were in the ₱ 100,000 to ₱ 500,000 loan category. Another significant (25 percent) grouping of sub-loans was in the ₱ 1.0 million to ₱ 3.0 million category. The smallest SECP sub-loan granted was ₱ 50,000 and the biggest was ₱ 3.0 million.

Majority of the Bank's SECP sub-loan borrowers have a track record of successful business operation. For the 15 borrowers with available information, 10 have been in business for six to forty years; 5 for two to five years.

While the nature of the financing need is basically for working capital and therefore generally short-term, nearly 80 percent of the Bank's SECP sub-loans have a maturity ranging from two to three years. Since most of the sub-loan borrowers have been in business for at least five years, this may indicate that part of the "working capital" loans may have actually been used to acquire fixed assets to support business expansion, while some might be as permanent capital of the business.

SME Loan Market

The local economy is basically agriculture based. Trading, particularly of agri-products, is also a major activity. There is virtually no manufacturing base in Dumaguete City and nearby areas. As a result, the Bank's clientele are mostly from the agriculture and trading sectors. Some examples of commodities/ goods covered by the trading activities financed by the Bank are: agri-products/livestock (rice, corn, copra, cattle and fish), dry good/general merchandise, restaurant/bakery products, medical supplies and construction materials.

Amidst this background, the DCDB targets a mixed market of individuals and companies, fifty percent of which can be considered as medium-scale enterprises mostly in trading.

The Bank perceives the potential SME loan market in the area to be large and growing (average of about 30 percent over the next two years because of the expected improvement in political stability and availability of power). The growth is expected to continue to come from the non-manufacturing sectors. While the SMEs engaged in manufacturing may also be expected to grow, the Bank sees that the effective SME loan demand will still come mainly from the viable SMEs in trading and commercial/service activities.

The DCDB is the only private development bank in Dumaguete City. Management considers the Bank as the leading lender to SMEs in the area. Lending investors rather than the commercial banks and rural banks are viewed as the Bank's main competitors in the SME loan market. However, lending investors have the disadvantages of charging higher interest rates and requiring high collateral cover from SME borrowers.

Impact on the Bank's Liquidity

The Bank's outstanding SECP loan balance as of December 31, 1991 stood at ₱ 11.25 million. This represented about 31 percent of the Bank's total borrowings and about 43 percent of the change in net loan portfolio.

A two-year comparison of the DCDB's loan portfolio is shown in the table below.

DCDB Loan Portfolio December 31, 1989, 1991 (million Pesos)					
LOAN CLASSIFICATION	1991		1989		% INCREASE (DECREASE)
	AMOUNT	% TO TOTAL	AMOUNT	% TO TOTAL	
AGRICULTURAL	27.9	44	14.0	37	99
REAL ESTATE	11.1	17	10.7	29	4
COMMERCIAL	10.3	16	6.3	17	63
INDUSTRIAL	10.0	16	4.7	12	113
CONSUMPTION, OTHERS, RESTRUCTURED, PAST DUE AND ITEMS IN LITIGATION	4.4	7	1.8	5	144
TOTAL	63.7	100	37.5	100	70

As can be seen from the table, agriculture continued to be the dominant sector financed by the Bank. Agricultural loans about doubled in amount and as a percentage of the loan portfolio, its relative share increased from 37 percent in 1989 to 44 percent in 1991. The commercial and industrial loans also increased quite significantly in amount with the industrial loans accounting for the bigger increase (113 percent). Relative to total portfolio, however, there was only a minor improvement (3 percent increase) for both the commercial and industrial loans.

The combined increase in commercial and industrial loans (85 percent), where SME loans under SECP are classified, was much higher compared to the increase in the total loan portfolio (70 percent). This increase in the C-I loans has been largely attributed by management to its availment of the SECP loan facility as an indication of the substantial impact on the Banks's liquidity position of the Program. Moreover, the Bank also acknowledged that the liquidity the SECP provided enabled it to expand its lending to SMEs.

Bank Lending Policies

The Bank employs the same set of criteria and requires the same sets of documents to evaluate SME loan applications as those used for other loan applications. The criteria consist of project viability, creditworthiness of the borrower, collateral/security and social impact of the project. The documents include: the application form, feasibility study (when applicable), financial statements, Transfer Certificates of Titles, business permits. license permits and similar documents. Loan processing takes about 15 days from date of submission.

The minimum acceptable loan size is ₱ 50,000.

The Bank appears to lend only to lower risk and "tested" clients as may be indicated by its collateral requirement and apparent preference for long-time bank clients (either depositors or borrowers). The usual types of collateral required are real estate, chattel mortgages and deposit holdouts. However, in some cases, the Bank accepted assignment of inventory as collateral.

The borrowers do not belong to new or start-up business category but have a track record of successful business operation. It was noted that from 16 borrowers with available information, the minimum number of years in operation is two years while the maximum is forty years.

While the DCDB would like to increase its exposure to SMEs, it does not particularly seek out SMEs for its lending operation. Management follows a lending policy that, in the words of Mr. Sung, EVP " loans help business to grow and business in turn helps banks to grow; no matter the size of the business, no matter the classification (i. e., whether SMEs or non-SMEs), all the bank sees are lending opportunities." Moreover, the management is aware of the need for specially trained personnel to handle SME accounts and recognizes that its capability to handle an increased volume of SME lending will be constrained by the present inadequacy of trained personnel in the Bank.

Deposit Mobilization Strategies and Performance

With its conscious deposit mobilization strategy, the DCDB appears to have put a lot of effort in deposit mobilization which has brought positive results in terms of the number of deposit accounts as well as the amounts mobilized.

There was a doubling in the number of deposit accounts serviced by DCDB as of December 31, 1991. From 4,183 in 1989, the deposit accounts increased to 8,614 in 1991. The biggest increase was realized in individual compared to institutional accounts which increased by 107 percent (4,137 in 1989 to 8,546 in 1991).

In terms of the amount mobilized, total deposits increased at a compound annual growth rate of around 40 percent from 1988 to 1991. The increase in total deposits has not been fully beneficial to the Bank because of the 7 percentage points deterioration in the relative share of savings deposit (59 percent in 1988, 52 percent in 1991). Time deposits, the more costly source of loanable funds, increased from 41 percent in 1988 to 48 percent in 1991.

Management claims that the Bank seeks all types of depositors, whether individuals and institutions. Its deposit mobilization approaches include personal campaigns and appeal by Bank personnel and the offering of competitive interest rates on savings and time deposits. In addition, the DCDB also taps its network of friends and business associates whose trust and confidence it has managed to gain over the years through its services and good image.

Deposits generation is conducted regardless of the level of availment of relatively costlier funds like SECP. The DCDB recognizes that deposits is a low-cost source of loanable funds. The management's strategy is to source both low-cost funds, such as deposits (which is an unstable source), and relatively higher cost special financing, such as the SECP (which is an available and steady source), to have a mix of loanable funds which the Bank can offer to its clients. The importance of SECP to DCDB lies less from its ability to make DCDB look for cheaper sources of loanable funds, but in its immediate availability to potential borrowers and the fact that it is a non-reservable fund source.

Bank Assessment of SECP

The Bank finds the feature of the SECP involving cash advance to the IFI as one of the most attractive characteristics of the Program. Management finds the availability of loanable funds as advantageous to both the Bank and its clientele because a loan may be extended when the business requires the financing. The timeliness of loan release is a key service requirement of business borrowers.

Another key characteristic which the Bank appears to also find attractive is the flexibility of the terms and conditions of the SECP loan making it available to borrowers who do not qualify under other special financing programs for SMEs. The SECP funds were used to finance sixteen sub-borrowers who did not qualify under the IGLF because they are engaged in purely trading activities.

The Bank finds the market-oriented interest rate policy of the SECP as a disadvantage and proposes the lowering of the rate to make the fund more affordable to SMEs.

LUZON DEVELOPMENT BANK

Luzon Development Bank (LDB) was established in May 1961 as Laguna Development Bank. In 1976, it changed its name to Luzon Development Bank. Among the medium-sized IFIs, the Bank has one of the biggest branch networks. LDB operates a total of twelve branches, located in Laguna (8), Batangas (3) and Cavite (1) in the Southern Tagalog area. Another branch is located in another region, Nueva Ecija in Central Luzon, intended to develop a new market area for the Bank.

Use of SECP Funds

The LDB became a participant of the SECP in March 1990. It was initially approved a credit line of ₱ 15.0 million which was subsequently increased to ₱ 20.0 million in June of the same year. The Bank has drawn the full amount of its credit line.

As of March 31, 1991, the Bank has given a total of 104 SECP sub-loans amounting to ₱ 24.8 million. Based on available information on 89 or about 86 percent of the total sub-borrowers, a relatively large portion of the loans went to borrowers engaged in trade (38 percent) while about 27 percent went to manufacturing and another 21 percent went to services.

The Bank supported mainly small businesses as indicated by the size of the sub-loans granted. Majority (73 percent) of the sub-loans were in amounts that ranged from ₱ 50,000 to ₱ 300,000. The smallest loan granted was ₱ 37,000 while the biggest was ₱ 2.0 million.

The LDB used the SECP as a medium-term lending facility for SMEs. The Bank appeared to have granted sub-loans with matched terms because a significant majority (80 percent) had a maturity of three years which coincides with the term of the SECP loan to the Bank. None of the 89 sub-loans with available information had a term longer than three years.

Based on 89 sub-borrowers with available information, the Bank achieved a ratio of about 15 to 1 new to existing borrowers. This indicates that the LDB was able to effectively use the SECP loan to give credit access to many new borrowers.

The Bank estimates that about 80 percent of every 100 Bank borrowers can be considered as existing borrowers. Of this, about 5 to 10 percent can be considered to have "graduated" to become larger enterprises.

SME Loan Market

The management considers SMEs as its target market and, the Cavite-Laguna-Batangas areas as its natural market.

Basically agricultural areas, Cavite, Laguna and Batangas are also characterized by a growing number of both SMEs and large industries. Cavite and Laguna are beneficiaries of the government's drive for industries to locate outside of Metro Manila. As such, it is where the manufacturing facilities of many large companies with head offices in Metro Manila are located. However, the financing requirements of these large establishments are handled by their Manila offices and are sourced from there. Bank management sees that the loan market opportunities for the Bank come from the local small- and medium-size manufacturing, trading and service industries. Based on the SECP loans portfolio, the industries/business financed by the Bank include:

Manufacturing:	embroidery and garments, footwear, metal/ironcraft, furniture, hollowblocks, handicraft
Trading:	rice and corn, dry goods/general merchandise, meat/food and vegetables, chemical/fuel supplies, animal feeds
Services:	restaurants, machine shops, freight services

The Bank management estimates the size of the SME loan market to be fairly substantial. However, the Bank believes that this market's loan potential cannot be fully realized by banks because as entrepreneurs, the Tagalogs appear to be generally "risk averse." As such, management thinks that SMEs would tend to be more conservative and to ignore economic opportunities that require them to go into debt. It is interesting to note that the management of another SECP participating IFI operating in LDB'S market area (the Bangko Silangan Development Bank) shared the same observation about Tagalog businessmen.

The management forecasts that the market for loans shall expand due to the expected increase in the economic activities in the area. The Cavite, Laguna and Batangas provinces are part of the four-province industrial zone designated by the government for development. The growth is expected to be in the export and service industries.

Impact on the Bank's Liquidity

SECP had a significant impact on LDB's financing sources. It was the most important source of financing for the Bank with the outstanding SECP loan balance as of December 31, 1991 of ₱ 13.15 million accounting for about 78 percent of the Bank's total borrowings for the same period. However, the major liquidity impact did not translate to a significant support for the Bank's lending operation. The loan balance as of December 31, 1991 represented about 14 percent of the change in net loan portfolio of ₱ 96.15 million. This is indicative of the Bank's strong capability to support its lending activities mainly from deposits and is partly explained by its relatively low loans to deposits ratio of 72 percent.

Bank Lending Policies

The Bank's lending policies highlight the competitive strength of a "community banker." This refers to the ability of the Bank to base key lending decisions on highly personal information about the borrower gathered from informal sources and/or developed from familiarity with the general business condition in the community being served. These factors probably reduce the transaction cost of lending which in turn enables the Bank to service the small loan requirements of SMEs.

The Bank considers the reputation and paying record of the borrower as the most important criteria in approving loan applications. According to management, the assessment of reputation covers both the applicant's public image as a person and as a businessman. In particular, it was stated that the Bank tries to answer the question, "Is the borrower a good guy?" As a businessman, the Bank is interested to find out about the borrower's knowledge of business and any record of business growth or failure. When assessing the applicant's paying record, the management claimed that it looks at the pattern of delayed payments and any loan foreclosures involving the applicant. These information are gathered mainly from informal sources like industry associations and the banking community, and from interviews of the applicant.

After satisfying itself about the reputation and paying record criteria, the Bank assesses the applicant's paying capacity. According to management, this is based on the cash flow of the business to be financed. The Bank did not elaborate on how the assessment is done but simply described the process "as an art because of the lack of formal business records." This implies that the Bank may be using an internally-developed cash flow evaluation system and considers it part of its own trade tools and techniques.

Another loan evaluation criteria identified by the Bank is that the borrower must have a stake in the business although the management did not specify any minimum owners' capital ratio to the total project cost. Management bewailed its frequent receipt of loan applications from some young entrepreneurs ("eager business school graduates") who have "promising ideas" but no capital.

A final Bank criterion is the borrower's collateral. All loans are required to be secured by a real estate and/or chattel mortgage. The SECP does not impose on IFIs any collateral on their sub-borrowers, the Bank nevertheless uniformly applies this loan collateral policy.

According to management, due to the high transaction cost of servicing small loans, the Bank prefers loan sizes of at least ₱ 1.0 million. However, for the SECP, the Bank serviced smaller loan applications with the smallest being ₱ 37,000. This may be explained by the apparent low transaction cost in availing SECP funds (due to the simplicity of procedures and advance fund features) which in turn enabled the LDB to lend to the smaller SMEs.

Deposit Mobilization

The Bank has external and internal approaches for mobilizing deposits. The LDB'S external strategies include: a) circulation of a "community letter" to promote awareness of the Bank and its services, (b) sponsorship of civic activities like art contests and choralfests during December and other special occasions and (c) distribution of give-aways during December. The internal approach is a staff incentive plan which involves distribution of cash incentives to the employees of the Bank who are able to bring in new depositors or in the case of existing depositors, increase the average daily balance of savings account depositors or increase the amount of placements of time depositors.

In an attempt to expand its deposit base, the LDB had launched a campaign in the past to promote savings consciousness among school children. While this increased the number of depositors, the deposit balances maintained were so small that it became more costly for the Bank to service the accounts.

The involvement of the entire bank staff in deposit generation has been found effective compared to the other Bank promotions implemented in the past.

LDB gives the same interest on savings accounts as those offered by commercial banks in the area. The Bank management does not believe that increasing the interest rate will substantially increase the savings deposit balances because most of the Bank's depositors are small vendors and small household savers who have a limited capacity to increase the amount of their savings.

The LDB's deposit mobilization effort is reflected in a 21 percent compound annual growth of total deposits during the period 1988 to 1991. There was also an improvement in the mix of the Bank's total deposits. The percentage share of savings deposits increased from 47 percent in 1986 to 55 percent in 1991. Correspondingly, the share of time deposits decreased from 53 percent in 1986 to 45 percent in 1991.

Bank Assessment of the SECP

The Bank's management finds "very little red tape in gaining access to funds" as the most important feature of the SECP. The training programs sponsored by the project were also rated highly.

The Bank's management proposes that additional training should be conducted in the areas of loans marketing and monitoring. Preferably, these should be conducted in the IFIs' offices since the Bank has only a few personnel and it cannot afford to send out its people on training.

A negative factor seen in project implementation is the use of the floating interest rate. The Bank experiences difficulty in implementing the flexible interest rate system because of its long practice of using fixed interest rates. The Bank's management is apprehensive because its old borrowers are unable to understand the periodic adjustments in the amount of the loan amortizations due to the changes in interest rate. Moreover, the administrative cost of changing the amortization schedule every quarter could be prohibitive especially for the smaller loan accounts. The management proposes that instead of a floating interest rate scheme, the SECP should charge the IFIs a fixed interest rate and specify a fixed on-lending spread to the sub-borrowers.

Annex C-8

NORTHERN MINDANAO DEVELOPMENT BANK

Northern Mindanao Development Bank (NMDB) was established in March 1982 as a joint undertaking of Mindanao and Metro Manila business leaders. Conceived under the leadership of the Private Development Corporation of the Philippines (PDCP), a major nonbank financial institution also involved in development financing, NMDB was meant to be a response to the government's goals to develop the countryside by encouraging the establishment and growth of SMEs.

Consistent with the rationale for its establishment, the Bank has developed to become a major SME lender in Northern Mindanao. As of December 31, 1991, NMDB's portfolio of SME loans amounted to ₱ 283.2 million compared to ₱ 169.4 million as of December 31, 1989 or an impressive 67 percent growth. The SME loans as of December 31, 1991 are distributed as follows: (a) industrial loans (which are SME manufacturing enterprises): ₱ 125.4 million or 44.3 percent of total loans; (b) agricultural production loans: ₱ 88 million or 31.1 percent; (c) commercial and services: ₱ 68.9 million or 24.3 percent and (d) real estate and housing: ₱ 1.0 million or 0.3 percent. In contrast, as of December 31, 1989 the bulk of NMDB loans was devoted to (a) agricultural production - ₱ 83.0 million or 49 percent; (b) industrial - ₱ 54.5 million or 32.2 percent; (c) commercial and services - ₱ 27.8 million or 16.4 percent and (d) real estate and housing - ₱ 4.0 million or 2.4 percent. This seems to indicate a significant shift to industrial borrowers as the local economy's industrial and manufacturing base expands. While agricultural production loan continues to hold a large share of total loans, the NMDB seems to devote more resources to the SMEs.

The Bank operates seven branches in strategic locations in Northern and Southern Mindanao and in the province of Cebu. The seven branches and their specific locations are as follows: Toril and Agdao (Davao), Valencia (Bukidnon), Malungon (South Cotabato), Lapasan and Velez (Cagayan de Oro City) and Mandaue City (Cebu). The Lapasan branch serves as the Bank's head office.

Among the branches, as of April 30, 1990, the Davao branches accounted for the largest share (40 percent) of the agriculture loan portfolio. In the case of the industrial sector, the Head Office (Cagayan de Oro) had the largest share at 44 percent with the Cebu branch providing the other significant contribution of 35 percent.

Use of SECP Funds

Northern Mindânao Development Bank was accredited with the SECP in March 1990. It has total credit line of ₱ 25.0 million which have been fully drawn. The Bank has not reavailed on its credit line even as repayments have already amounted to about ₱ 20.0 as of March 31, 1992.

Together with the Bank's counterpart contribution, NMDB was able to finance thirty-nine SECP sub-loans amounting to ₱ 27.5 million. The Bank is focused toward the service sector which accounted for about fifty percent of the sub-borrowers. Borrowers from the manufacturing sector accounted for 28 percent while those in trading made up about 23 percent.

The SECP was used by the Bank mainly to grant medium-term financing. A significant majority of the loans granted had a maturity of 1.5 to 3 years. Only about 5 percent of the loans had a term of one year or less. None of the SECP sub-loans had a term longer than three years.

NMDB basically serves the "medium-to-large" end of small-size enterprises. About 70 percent of the SECP sub-borrowers had assets ranging from ₱ 1.0 million to ₱ 5.0 million. This is also reflected in the Bank's relatively high average SECP sub-loan size of ₱ 705,000. The loan size with the biggest number of borrowers was the ₱ 400,000 to ₱ 500,000 category. About 31 percent of the total SECP sub-loans were in this category. The smallest loan granted was ₱ 100,000 while the largest was ₱ 3.2 million.

About 50 percent of the SECP sub-borrowers were new while about 36 percent were existing Bank borrowers. The status of about 14 percent of the borrowers could not be determined from the Project records.

SME Loan Market

The bank's target market consists of a mix of companies and individuals engaged in small- and medium-scale businesses, mostly in the agriculture and manufacturing sectors.

Some examples of the types of businesses that have been served by the Bank include: (a) agri-products production/processing: prawn farming, rice milling and food processing; (b) manufacturing/industrial: farm machinery fabrication, machine shop, furniture manufacturing and bakery; and (c) services: printing press, trucking/hauling/forwarding services, bus transportation, dipping treatment, hardware/construction, food restaurant, commercial store and empty sacks trading.

As of December 31, 1991, the NMDB serves a total clientele of about 2,368 borrowers with an average loan size of approximately ₱ 120,000 compared to 1,311 borrowers with an average loan size of approximately the same amount (₱ 129,000) in December 1989.

According to management, about 80% of the Bank's SME clients can be considered "progressive", i. e. those with definite plans for expansion in the future. The Bank also identified the following as major factors that will enable the SMEs to "graduate" to large enterprises: (a) technology; (b) access to market and (c) determination to grow. It was the management's opinion that to a large extent, financing makes it possible for the SMEs to harness these three major factors.

NMDB considers itself as the leading SME lender in the area. Close competitors are the Metro Bank and Trust Company, which grants "clean loans" (i.e. non-collateralized) mostly to local merchants, and about fifty lending investors in the area. The management also mentioned Planters Development Bank which is setting up a branch in the city as a potential competitor. Management thinks that rural banks do not lend to SMEs but to other types of borrowers.

Impact on the Bank's Liquidity

As of December 31, 1991, the outstanding balances of NMDB's borrowings amounted to ₱ 133.7 million compared to ₱ 263.2 million in the previous year. The following is the breakdown of these borrowings by major sources:

SOURCE	1989 (Million Pesos)	1991* (Million Pesos)
IGLF AND ALF	81.3	128.9
FMO**	50.0	50.0
KASAPI	-	29.5
USAID-SECP	-	10.3
OTHERS	2.4	44.5
Total	133.7	263.2

* Reconstructed from the December 31, 1991 NMDB report to the Central Bank.
** Netherlands Development Finance Company

From the table, the IGLF and ALF continued to provide a sizeable portion of NMDB's loan funds (60 percent in 1989 and 50 percent in 1991). Another important source is the KASAPI funds which are funds sourced from the Social Security System for relending at interest rates below the market rates.

In order to attract clients, the NMDB first informs borrowers of the SSS-Kasapi loan which is offered at 16% per annum. The Bank was able to lend out ₱ 30 million from the Kasapi facility. It appears that the NMDB has already taken full utilization of the KASAPI money and now offers both the SECP and the IGLF to its clients. This shows that the Bank first uses its subsidized financing facilities before availing of the "market interest-based" special financing programs like the IGLF and the SECP.

Between the IGLF and SECP, it was found during the interview that since the IGLF does not allow financing for purely trading activities, most of the SECP funds went to finance trading activities in the Mindanao area. The IGLF, on the other hand, was used to finance the industrial loans granted largely by both the Head Office and the Cebu branch.

The SECP provided only about 4 percent of the Bank's total borrowings as of December 31, 1991. It was also a minor support for NMDB's lending activities accounting for only less than ten percent of the change in the change in the Bank's net loan portfolio. However, despite its apparent insignificance, the SECP is considered by the Bank as an important financing source for bridging the liquidity gap that arise because of the huge loan demand of SMEs in the area.

Bank Lending Policies

NMDB applies the same set of screening and lending criteria to all SME loan applications, regardless of the funding source. This means that the same criteria are used for applications to IGLF, ALF, KASAPI, etc. financing. The most critical criterion is the borrower's creditworthiness; next in importance is the project's viability followed by the collateral/security offered by the borrower.

Loan applications are either approved or disapproved within 15 days from date of submission.

The most critical reasons for loan disapproval, according to their importance, are as follows: (a) lack of creditworthiness of the borrower; (b) project is not feasible; (c) insufficient collateral; (d) amount applied for is too big and (e) amount applied for is too small. The last two criteria seem to indicate that NMDB has a certain loan size that it considers to be the appropriate amount for SMEs and therefore, within its lending criteria.

While NMDB has developed the expertise in SME lending, it still has to be encouraged to minimize its requirement for collateral. Data show that the Bank required collaterals like real estate mortgage and in some cases, a chattel mortgage in addition to real estate mortgage, from its SME borrowers who have been in the business for a number of years and can be considered good credit risks. This orientation towards security may hamper its plan to have a more aggressive posture in the SME loan market. The NMDB is aware of the potential competition that Planters Development Bank and the Metro Bank can make. The Bank will need to review of its lending policies if it were to make a definite headway in the SME loan market.

The average interest rate charged was 25.5 percent.

Deposit Mobilization Strategies and Performance

The Bank has a conscious deposit mobilization strategy wherein high networth individuals are targeted primarily for the deposit campaign. Among the instruments used to mobilize deposits are the following: (a) advertising through the media; (b) personal campaigns and appeal by the Bank's president; (c) promotional schemes like raffles and (d) involvement by the Bank in community undertakings. Late 1991, the Bank started a major deposit mobilization promotion culminating on August 1, 1992. Minor and major prizes were raffled weekly and quarterly to bank depositors. The grand prize was a KIA Pride car.

Due to its conscious deposit mobilization policy and several instruments for raising deposits, the Bank experienced a considerable growth in deposits. Total deposits increased at a compound growth rate of 68 percent from 1988 to 1991. Aside from these factors, a strong local economy was responsible for the huge turnout of depositors in favor of NMDB. The Bank also gave credit to the effort of its personnel in deposit mobilization.

There has been a dramatic increase in the number of depositors of the Bank. As of December 31, 1991, the Bank's deposit clientele consisted of 13,365 depositors of which 13,207 are individuals and 158 are institutional depositors. This compares with 7,594 depositors of which 7,524 are individuals and 70 are institutional depositors as of December 31, 1989. This increase in the number of individual depositors can be seen as a significant step towards the development of a stable source of cheap loanable funds for an expanded number of borrowers in recent years.

There was a deterioration in the deposit mix of the Bank from 1986 to 1991. Savings deposits decreased from about 67 percent in 1986 to only about 36 percent in 1991. The decrease in savings deposits was partly due to the conversion of some savings deposit accounts to Negotiable Order of Withdrawal or "NOW" accounts in 1991. "NOW" deposits represented about 13 percent of total deposits. Thus, in 1991, the total low cost component of bank deposits was effectively 49 percent of total deposits. From 33 percent in 1986, time deposits went up to about 51 percent of total deposits in 1991.

Bank Assessment of the SECP

Several key features which characterize the SECP's unique design are seen by the Bank as major advantages. They are ranked by NMDB according to importance as follows: (a) liquidity provided through advance funding; (b) flexible policy to determine loan terms; (c) market-based interest rates; and (d) absence of any collateral requirement.

Although the term of the SECP loan is also found to be attractive, the Bank proposed that it should be made even longer to be able to effectively serve the need for long-term financing of the manufacturing/industrial sector of SMEs.

The Bank identifies the interest rate as a major consideration in the use of the SECP because of its floating nature. It was emphasized by the Bank that the IGLF has an advantage over the SECP because it offers longer term loans (i.e., 5-7 years) and a choice between a fixed or variable interest rate.

The SECP is considered by the Bank as just one among many sources of financing for SMEs of NMDB. Because of the sheer size of available funds, the major sources are IGLF and ALF. While these sources impose market-oriented interest rates, the SSS KASAPI loans are priced below existing market rates. Like the IGLF and ALF, the SECP also has a market-oriented interest rate. Moreover, it has the additional advantage of giving the financial institution a flexibility in designing loan packages. The Bank is of the opinion that the use of the special SME financing programs with market-based interest rates like the SECP is constrained by the distortionary impact of the SSS KASAPI loans in the credit markets in Northern Mindanao.

Although a minor source of outside financing, the Bank nevertheless viewed the SECP as a strategic fall back source of funds due to the relative ease in its availment. With a growing clientele, the NMDB finds the need to be able to commit to clients applying for loans and to draw loanable funds fast enough to satisfy the commitment.

The Bank gave a satisfactory rating to PBSP as a project implementor and a very satisfactory rating to DBP as trustee bank. Some weaknesses of the PBSP pointed out by the Bank are the fast turnover of personnel who handle the SECP and the "inability of PBSP to provide assistance in the banking area." What the latter comment presumably means is that the PBSP is not equipped to handle banking and finance matters and to lend guidance and/or expertise in SME lending. On the other hand, the DBP disburses the funds fast enough and is seen as a competent trustee bank.

PALAWAN DEVELOPMENT BANK

Palawan Development Bank (PDB) was incorporated in October 1984 with an authorized capital stock of ₱ 40.0 million. At present, its paid-up capital is ₱ 10.0 million. Its head office is located in Puerto Princesa City, Palawan. It has two branches in Palawan, one in Narra and the other in Brooke's Point.

Uses of SECP Funds

The Bank was accredited into the program in April 1990 with a credit line of ₱ 10.0 million. It has utilized the entire credit line and has reavailed of another ₱ 5.0 million of its credit line for a turnover of 1.5 times. It ranks second in terms of credit turnover.

Management has submitted a total portfolio of ₱ 30.18 million to the SECP as of March 1992. The ₱ 15.0 million drawdown was used to finance 50 percent of the portfolio. The Bank has the distinction of submitting the largest portfolio among non-Metro Manila based banks.

Although the Bank had loans with maturities over three years, most of the loans mature in one year or less. About 78 sub-loans with a value of ₱ 4.4 million mature between three and six months. Fifty-two sub-loans with a value of ₱ 20.0 million have maturities ranging from nine to 12 months. Together, these two groups account for 85 percent of the total number of SECP loans and 81 percent of its value. The short-term nature of its SECP loans is surprising considering the growth of time deposits in the Bank.

Most of the borrowers are engaged in trading. Of the 153 sub-loans submitted to SECP, 111 (72.5 percent) accounts with a total amount of ₱ 22.2 million went to trading. Thirty-three accounts (21.6 percent) with a total loan amount of ₱ 6.6 million went to services. Only seven (4.6 percent) accounts with a total amount of ₱ 1.3 million went to manufacturing.

The SECP portfolio also reflects the Bank's thrust on existing borrowers. Ninety-six of the 153 accounts were existing clients of the Bank.

Almost half of the SECP portfolio belong to cottage-scale enterprises with asset sizes between ₱ 50,000 and ₱ 500,000. This group accounted for ₱ 10.3 million or about 34 percent of the total portfolio. About 20 percent of the total number of sub-borrowers have asset sizes below ₱ 50,000 with total loans of ₱ 1.1 million or about four percent of the total portfolio. Another 36 percent of the total sub-borrowers have assets of more than ₱ 500,000. These sub-borrowers accounted for ₱ 18.8 million or 62 percent of the total portfolio.

The Palawan province also exhibited the segmentation of loan market observed during the evaluation. About 74 percent of the 153 sub-loans had loan amounts between ₱ 25,000 and ₱ 500,000. The total loans granted to this group, which is considered a market of private development banks, amounted to ₱ 18.6 million or about 62 percent of the total SECP portfolio. Twenty-nine or 19 percent of the borrowers had loan sizes below ₱ 25,000. The rest of the loans had sizes above ₱ 500,000.

SME Loan Market

The increase in agricultural loans reflects the predominant sector in the area. Agricultural loans increased from ₱ 330,000 in 1986 to ₱ 13.3 million in 1991 for a compounded growth rate of 109 percent. Commercial and industrial loans also increased from ₱ 4.6 million to ₱ 14.6 million during the same period achieving a growth rate of 26 percent. The three-digit growth of agricultural loans is reflected in the agricultural loans' 37 percent share of total loans in 1991, up from only five percent in 1986. Commercial and industrial loans, on the other hand, dropped from 73 percent to 40 percent of total loans.

Past due loans increased from ₱ 32,129 to ₱ 4.2 million increasing its share of the total loan from less than one percent to 11 percent.

Impact on the Bank's Liquidity

The Bank's outstanding SECP loan as of December 1991 stands at ₱ 9.33 million. This is 16 percent of its total resources making SECP a major source of funds. Aside from the SECP, the Bank taps the Palawan Integrated Area Development Project (PIADP) as another source. Outstanding PIADP loans amounted to ₱ 7.9 million in 1991.

Bank Lending Policies

The Bank has targeted small- and medium-scale enterprises even before the SECP because of the sector's profitability. Specifically, it targets sole proprietors involved in trading or agriculture.

Management has a policy of concentrating on the Bank's large existing accounts. New borrowers are only considered by the Bank if the request is for a minimum amount between ₱ 100,000 and ₱ 150,000. This minimum amount may be lower for the branches. The current focus of management is on the value of the loan and not on the number of loans. This emphasis on existing borrowers could be the effect of the high past due rate the Bank has been experiencing over the past three years.

Loan processing and evaluation are centralized at head office. It takes the Bank about a month to process loans. However, the Bank is now offering credit lines to borrowers to effect quicker loan releases.

Deposit Mobilization Strategies and Performance

The Bank mobilizes deposits through personal campaigns of its employees. Employees are given incentives when certain levels of deposit are met. To complement this effort, the Bank makes sure its interest rates are competitive. As of May 1992, the interest rate for savings was six percent and 13-17 percent for time deposits. The Bank also has plans to open two more branches in Palawan.

Total deposits increased from ₱ 3.1 million in 1986 to ₱ 35.8 million in 1991 for a compounded growth rate of 63 percent. A major portion of the increase came from time deposits. Starting at ₱ 0.25 million in 1986, it grew to ₱ 20.2 million in 1991 for a 140 percent growth rate. Subsequently, its share increased from eight percent to 56 percent. The increase in time deposits provides the Bank with costlier funds for long-term loans. All of these accounts are individual accounts.

The average loans-to-deposit ratio of Group C banks (banks with resources of less than ₱ 100 million) is about 190 percent. Palawan Development Bank has the lowest ratio in the group with 109 percent average ratio, both in 1990 and 1991.

Bank Assessment of the SECP

Among the features of the SECP, the Bank lists the term of the loan and the role of DBP as trustee as the most attractive. The three-year maximum term of the SECP loan allows the Bank to offer similar terms to its clients. Other features cited are: flexible policy to determine the loan terms, advance funds given to the bank and PBSP as the implementing agency.

Despite a high turnover of credit at 1.5 times its credit line, management still observes that PBSP requires too much paperwork to process the loan applications. Also, management has a misconception that the DBP sets the interest rates passed on to the IFIs. Specifically, the high interest rates passed on by the DBP were noted by management.

PRIVATE DEVELOPMENT CORPORATION OF THE PHILIPPINES

The Private Development Corporation of the Philippines (PDCP) is a privately-owned development finance institution established in 1963. PDCP operates on a nationwide basis through six branches located in the cities of Dagupan, Legaspi, Cebu, Iloilo, Bacolod and Davao.

Use of SECP Funds

PDCP was accredited with the SECP in June 1990. As of March 1992, it has an authorized credit line of ₱ 40 million. The PDCP has fully drawn from its credit line and has made a reavailment of ₱ 7 million more. With its total funds availment of ₱ 47 million, PDCP has one of the highest rates of credit line utilization among the 17 participating IFIs at 117 percent.

The Corporation has a total SECP sub-loans portfolio of about ₱ 59.4 million of which about ₱ 47 million was financed out of the SECP funds. This would mean that the PDCP achieved a rate 100 percent efficiency in moving the SECP funds down to the sub-borrowers.

PDCP's SECP loan portfolio consists of 163 accounts. Of this, trading accounts represents about 49 percent of total sub-borrowers. Manufacturing is next with 26 percent, followed by the services sector with 24 percent. The purpose of the remaining 1 percent of total loans could not be determined from the Project records.

Three major groupings in the distribution of the SECP sub-loans granted by the PDCP were noted. These are as follows: 74 percent - ₱ 45,000 to ₱ 300,000 range; 11 percent - ₱ 400,000 to ₱ 500,000 range and 7 percent - ₱ 1.0 to ₱ 2.0 million range. This loan-size profile would indicate that the PDCP used the SECP funds mainly to finance small businesses.

All of the 163 sub-loans of the Corporation have a maturity of three years which coincides with the term of the SECP loan. Being a non-bank financial institution, it could be expected of PDCP to simply match loans granted to sub-borrowers with the features of the main loan or grant from the SECP.

Of the Corporation's 163 SECP sub-borrowers, 118 are new and 41 are existing borrowers. The high 2.87 to one ratio of new to existing borrowers is indicative of the significant "additionality" impact that the SECP was able to achieve through the PDCP.

SME Loan Market

PDCP as an institution serves both large-scale and small and medium-scale enterprises. Management indicated that the allocation of loanable funds depends on the financing lines that are available. In the case of the SECP, for example, the target clients are the SMEs. One branch which has dealt with SMEs quite extensively is the Iloilo branch. The following is a description of PDCP Iloilo's loan market.

PDCP Iloilo has been lending to SMEs since its establishment in 1979. The Branch intends to continue servicing SMEs which dominate the business in Iloilo. The annual SME market is estimated to be about ₱ 100 million, and the Branch aims to seize a good share of about 10 percent.

The Iloilo Branch management believes that competitor banks have the advantage in SME lending because they can use hold-outs on deposits as security for loans. The management considers that PDCP Iloilo assumes greater risks because it does not have deposits to secure loans. However, it is expected that once PDCP operates as a bank, the Branch would be competitive in the SME loan market.

As of March 1991, PDCP Iloilo has a total loan portfolio of ₱ 6 million in SECP funds. It targets to lend ₱ 18 million in 1992 and another ₱ 20 million in 1993. These are company wide targets and reflect the Branch's large absorptive capacity. The establishment of the agro-industrial center in Pavia under the Philippine Assistance Program (PAP) in 1990 is seen as instrumental in generating interest on investments in local agro-industries.

The Iloilo Branch hopes to exploit the growth prospects by actively identifying potential SME clients particularly those engaged in trading, manufacture of fertilizer and chemicals, and machine shops.

Impact on the Bank's Liquidity

The SECP had a sizable impact on PDCP's financing sources. Its outstanding SECP loan balance as of December 31, 1991 of ₱ 37 million accounted for about 18 percent of the institution's total borrowings as of the same date. There was a decline in PDCP's net loans from 1990 to 1991. Using the year-end balance of the total loan portfolio on a company wide basis, the SECP provided minimal support to PDCP's lending activities. The outstanding loan balance as of December 31, 1991 represented only a small 5 percent of total loans. However, a significant impact on some branches could be noted as in the case of the Iloilo branch.

Since 1990, the Branch has increasingly used SECP funds, improving the liquidity position of the Branch and enabling it to service new clients. Of the 21 SECP sub-borrowers, only 2 are existing clients. Nineteen or about 93 percent of total SECP accounts are new borrowers of the Bank. The management projects that with the SECP funds, the Iloilo branch will be able to increase its loan exposure to SMEs by more than 20 percent.

The Branch considers lending under the SECP as profitable to PDCP. The period 1991 to 1992 has a repayment rate of over 90 percent. Of 25 accounts as of July 1992, only three are classified as past due: one has sufficient collateral while the other two were unsecured loans.

It is to be noted, however, that the branch intends to continue lending to SMEs even with the eventual termination of the SECP. There will be other funds to tap and the mobilized deposits to use in view of the growth prospects of trading and off-farm business activities in the area.

Bank Lending Policies

PDCP selects its clients carefully, requiring that they be in profitable operation for at least one year. They should also be duly registered by government licensing offices to establish their legal capacity to enter into loan contracts.

The branches of PDCP only have limited loan approval authority. Loan approvals for amounts up to ₱ 200,000 are done at Cebu. Loan approvals for higher amounts are made at the head office in Makati. The branches originate and screen the loans. Those that qualify in the initial assessment by the branches are documented and sent to Manila for further processing.

The branches are equipped with trained staff to process loan applications. At PDCP, loan processing includes preparing studies for the applicant to assess the viability of his business. Based on experience, the management has noted that the clients find this service valuable because they do not have to do the studies themselves. On the part of the institution, it helps to shorten loan processing as well as minimize credit risk because the studies are done in accordance with PDCP's quality standards.

PDCP has a relatively liberal loan collateral policy. Less secure collaterals like assignment of receivables and purchase orders or no collateral at all is required for loans of less than ₱ 200,000. These "clean" loans are granted to SMEs with good business record. The length of experience in the business is also taken into consideration.

Deposit Mobilization

PDCP has been granted a license to operate as a bank and it expects to start as one in August 1992. The Branch is gearing up to this new organizational set-up and hopes to mobilize sizeable amounts of deposits. PDCP hopes that its almost twenty-nine years of operation and good reputation as a development financial institution will be a major factor in mobilizing deposits. The planned change in PDCP's organization is partly based on the need to source cheaper money from deposits to meet the increasing need for development funds.

Bank Assessment of the SECP

According to management, the three most attractive features of the SECP are: (1) the flexible policy to determine loan terms, (2) funds are given in advance, not on a reimbursement basis, and (3) no collateral is required.

According to management, the flexibility given to the IFIs to determine the loan terms, enables the PDCP to design credit packages according to the needs of their clients. The availability of funds enables PDCP to assure prospective clients that funds are available for release once loans are approved. PDCP also finds that by not requiring collateral, the SECP imposes less "administrative complications." The case of IGLF-financed loans was cited whereby all the documents pertaining to the collateral have to be sent to the Development Bank of the Philippines. Retrieving these documents when the borrower prepays entail complications because of some administrative policies covering the IGLF.

The management identified that a change in the SECP loan period would make the greatest impact on PDCP's use of the facility. In particular, it was cited that three years is not long enough and that the maturity should at least be five years. Moreover, a grace period especially for acquisition of fixed assets loans would also be important.

PDCP also noted that the SECP interest rate should be a "fast responsive rate". The interest rates were cited to be out of line with current market rates.

For the institution, the limit on the asset size of first time SECP borrowers of ₱ 5.0 million is too small and increasing it to ₱ 10.0 million would be more flexible.

PLANTERS DEVELOPMENT BANK

Planters Development Bank (PDB) was originally incorporated in March 1961 as Bulacan Development Bank and operated primarily in the province of Bulacan. In December 1972, a new management took over the Bank and ushered a series of organizational changes in order to accelerate growth. Between 1975 and 1986, the Bank merged with and acquired other development banks in Bulacan, Pampanga, Zambales and Manila. Its acquisition of the Investors Savings and Loan Association, Inc. in 1977 enabled the Bank to transfer its head office to Makati, the country's financial center.

The new name Planters Development Bank was assumed in 1976.

As of March 1990, PDB operated a wide banking network consisting of a head office in Makati and twenty-seven branches. It has a strong presence in Central Luzon where the Bank operates nineteen branches. There are five additional branches in the capital and other key cities in Southern Luzon and one in Metro Manila.

Uses of SECP Funds

The PDB became a participant of the SECP in March 1990. Its initial credit line of ₱ 20.0 million has been increased a number of times since it was accredited and amounted to ₱ 80.0 million as of March 31, 1992. It accounts for about 25 percent of the total SECP IFI approved credit lines, the highest amount of credit line granted to a single IFI. Funds availment has amounted to ₱ 70.0 as of the same date accounting for an 88 percent utilization of the approved credit line.

As of March 31, 1992, the Bank has granted sub-loans amounting to ₱ 48.2 million. Of this, the SECP provided about ₱ 38.5 million and the Bank put up a 20 percent counterpart contribution of about ₱ 9.6 million. This accounts for only about a 50 percent efficiency of moving the SECP funds to the final borrower computed by dividing the SECP funds actually loaned out by the total credit line. This performance does not compare favorably with those of medium-size IFIs like the Northern Mindanao Development Bank (81 percent) and Luzon Development Bank (94 percent).

The Bank granted a total of 47 SECP sub-loans as of March 31, 1992. The average size of the loans amounted to about ₱ 1.0 million, the highest among the seventeen SECP participating IFIs. About half of the loan accounts were in the ₱ 900,000 to ₱ 2.0 million category. In terms of amount, the loans in this category accounted for about 64 percent of the SECP loans portfolio of the Bank. The smallest loan granted was ₱ 100,000 and the highest was ₱ 2.5 million.

About 47 percent of the PDB's SECP loans supported trading activities. Loans to the manufacturing/industrial sector had the smallest share at 21 percent.

All of the 45 sub-loans with available information had a maturity of three years which coincides with the maturity of the Bank's SECP loan. This would imply that the Bank simply matched maturities of sub-loans to SMEs with its loans from the SECP. It was also noted that while the sub-loans were long-term, 85 percent of these sub-loans were mainly used for working capital. Only about 15 percent of the sub-loans financed fixed asset acquisition.

Majority of the SECP sub-borrowers were new clients of the Bank. Of the 41 sub-borrowers who have available information, 25 are new and 16 are existing Bank borrowers accounting for a 1.56 to one ratio of new to existing borrowers.

SME Loan Market

Planters Development Bank's target market is the SMEs. The Bank pointed out that this focus towards SMEs is reflected in its loan portfolio. On December 31, 1991, commercial and industrial loans constituted about 60 percent of the total portfolio. Only about 22 percent was accounted for by agricultural loans and the remaining 18 percent represented consumption and other loans as well as restructured, past due and items in litigation. It was estimated by management that about 80 percent of the C-I loans are SME accounts.

Moreover, the clear policy and directed efforts of the Bank in serving the SME loan market can be seen in the relative increase in resources placed in C-I loans compared to other types of loans. The C-I loans increased by an impressive 128 percent from 1989 to 1991 compared to the less significant increase in agricultural loans of 51 percent.

PDB sees a vast and potentially profitable SME loan market in its areas of operation. The PDB has twenty-seven branches of which 19 are located in Central Luzon, 5 in Southern Tagalog, one in Pangasinan, and two in the National Capital Region. Based on the concentration of its branches, the Bank's main area of operation is in the province of Bulacan (9 branches).

Both Central Luzon and Southern Tagalog have a large agriculture sector but with a fast-growing industrial base. These areas are major producers of rice, coconut and coffee and trading of these agricultural products is a major economic activity in the area. On the other hand, Bulacan and Pampanga in the north and Laguna and Cavite in the south have been major beneficiaries of the government's industrial dispersal program to promote the relocation of industries to places outside Metro Manila. In addition, the presence of export processing centers in Pampanga and Cavite and industrial estates in Laguna are expected to boost the manufacturing and support services industries in these areas. SMEs participate in these economic activities as subcontractors (garments), providers of support services (trucking/hauling services, public utility transport operators, freight forwarders, repair shops and motor works, hotels and restaurants) and traders (auto supply and spare parts, lumber and hardware). In addition, SMEs are also involved in local industries like processed food, furniture making, textile and metalcraft. To support the growing population in Metro Manila, poultry and livestock raising has also become a major industry in the area.

The PDB has expertise in SME lending and considers itself one of the leading SME lenders. The management estimates that it has about 50 percent of the SME loan market in its area of operation. The Bank considers "lending investors" which have proliferated in major urban centers as its major competitor in the SME market. The management has also noted the growing interest among commercial banks to penetrate the SME market.

The management conceded that commercial banks have well-trained personnel and enjoy a wider branch network. Due to their bigger deposit base, they could afford to offer lower interest rates and provide bigger loans to SMEs. To offset these advantages and meet competition, the PDB plans to intensify the training of its personnel and to use its information and experience base in dealing with SMEs that it has developed over the years.

The management also expressed some concern over some government banks like the Land Bank of the Philippines (LBP) as a growing competitor. The Land Bank offers subsidized credit to cooperatives and other countryside borrowers despite the announced market-oriented credit policy of the government.

The following factors were identified by the Bank management as required policies, actions, and conditions in order to further increase its lending to SMEs:

(1) a vigorous campaign for deposit mobilization so that the Bank will have a cheaper source of loanable funds for SMEs;

(2) lower interest rates to SMEs;

(3) more training for bank personnel on SME lending;

(4) acceptable collateral from SMEs; and

(5) credit guarantee for SME loans. (According to management, a preferential rediscounting facility for SMEs will help lower the Bank's lending rates.)

Impact on the Bank's Liquidity

The SECP had a minimal impact on Planters Development Bank's sources of funds as well as on its lending activities. The outstanding SECP balance of ₱ 29.49 million as of December 31, 1991 represented only about 2 percent of the Bank's total borrowings as of the same date. As a percentage of the change in net loan, the outstanding SECP loan accounted only for slightly more than 2 percent of the increase in the loan portfolio of the Bank from December 31, 1990 to December 31, 1991.

Management considers SECP as an insignificant source of funds in amount relative to its total borrowings and loan portfolio. The SECP is considered by management as just another source of liquidity.

The Bank clarified that the decision to lend to SMEs was not motivated or influenced by the SECP but by its corporate mission "to serve SMEs." Management said that it will continue pursuing its corporate mission even after the completion of the SECP.

Bank Lending Policies

The Bank ranks creditworthiness of the borrower as first criterion for evaluating loan applications. The other factors considered according to their degree of importance to the Bank are: project viability, collateral/security, condition of the industry and other sources of income.

The Bank requires the same set of documents for SECP and non-SECP loan applications. These include the usual application form, authorization to borrow (in the case of corporations or cooperatives), financial statements, income tax returns and documents for the collateral being offered.

It takes the PDB an average of one-and-a-half months to a maximum of two months to evaluate and approve/disapprove loan applications. This compares poorly with the loan evaluation periods of the other IFIs which on average takes from one to two weeks from the date of submission of the loan application.

The Bank has installed a formal loan monitoring system to assure itself that the loans are utilized for their declared purposes.

The management recognizes the need for the PDB to offer better interest rates in order for the Bank to be competitive in the SME loan market. Their strategy has been to open more branches in order to enlarge the client outreach and to be able to mobilize more deposits as a source of lower cost loans.

The PDB's average lending rate for SMEs is 24 percent per annum. According to management, the rate can be brought down if the client brings in "compensating business to PDB, such as deposits." However, since deposits are withdrawable anytime, it was emphasized that this is not a sure way of bringing down interest rates. The Bank specified that the size of the loan and whether the loan applicant is a prime client or not, are the other key factors considered in interest rate setting. Inasmuch as SMEs are generally not considered prime clients, this interest setting policy must be applicable to the bigger clients of the Bank.

The Bank selectively avails of the government-run credit guarantee program under the GFSME because the guarantee fee only increases the cost of money to SMEs. For example, it was pointed out that due to the market-orientation of SECP interest rates, the Bank does not avail of the guarantee program because management believes that the guarantee fee shall make the SECP loan unaffordable and will drive away SME clients. However, the GFSME is used for other types of loans especially those that involve higher risks.

The PDB has 27 branches located in strategic places in Central and Southern Luzon. These branches originate and evaluate SME loan applications. However, loan approval is mostly made at the head office because the credit authority of branches covers only loans to market retailers in amounts not exceeding ₱ 30,000. Once approved, the loans are monitored by the branches which are also in charge of collection. The highly centralized approval process of the Bank is the major factor accounting for the relatively longer approval period of loan applications. In addition, this may also be a reason for the relatively poor performance of the Bank in moving SECP funds down to the final borrower.

The management believes that the Bank has enough trained personnel in the Head Office to handle SME loan accounts. However, there is still a need to strengthen the branches with more trained personnel. It was also noted by the Bank that continuous upgrading of personnel skills shall be required in order for the PDB to stay competitive in the SME loan market. In particular, the management identified financial analysis and evaluation of feasibility studies as the two areas where training is needed.

Deposit Mobilization Strategies and Performance

Planters Development Bank is committed to SME lending, mobilizing all types of resources to meet this goal. The Bank seeks all types of depositors and employs various schemes to mobilize deposits. In particular, management cited the following four schemes: (1) providing depositors quality service; (2) motivating employees through an incentive system to campaign for deposits; (3) offering competitive interest rates; and (4) involving the individual branches in community civic projects. The last scheme depends on the discretion of the individual branch managers and is not a bank-wide strategy. According to management, its deposit mobilization strategies helped develop depositor confidence which is important in maintaining the stability of deposits.

The Bank's deposit generation efforts resulted in a 29 percent compound annual growth rate of deposits from 1988 to 1991. This increase in the amount of deposits was accompanied by an improvement in the deposit mix in favor of savings deposits, the cheaper source of funds. From about 59 percent in 1988, the relative share of demand and savings deposits to total deposits increased to 69 percent. On the other hand, the relative share of time deposits decreased from 41 percent in 1988 to 31 percent in 1991.

Bank Assessment of the SECP

The flexible policy allowing the Bank to determine SME relending terms and the training component are considered to be the advantages of the SECP. The management, however, feels that the three-year maturity is not long enough. In addition, the market-based interest rate of SECP is seen as a drawback.

QUEEN CITY DEVELOPMENT BANK

Queen City Development Bank started operations in July 1981 with a paid-up capital of ₱ 4.0 million. The Bank, a single branch bank, is located in Iloilo City. Total resources in 1991 was ₱130.88 million from ₱ 47.58 million in 1986 and capital funds was ₱ 64.54 million in 1991 from ₱ 12.22 million in 1986.

Uses of SECP Funds

The Bank was accredited into the SECP program in April 1990 with a line of ₱ 15.0 million. It submitted a portfolio of ₱ 2.7 million in 1990 of which ₱ 2.0 million was financed by SECP.

The Bank's portfolio consisted of 10 accounts. Half of these went to businesses involved in trading with a total loan amount of ₱ 330,000. Almost 80 percent of the loan amount (₱ 2.1 million) went to four enterprises involved in services. The remaining sub-loan went to a manufacturer with a loan value of ₱ 280,000.

Nine of the ten loans had maturities of one year with the remaining loan maturing in two years. The two-year loan had a value of only ₱ 40,000.

In terms of asset size, five of the ten borrowers are cottage-scale enterprises (asset size of ₱ 50,000 to ₱ 500,000). Four firms have asset sizes of between ₱ 1.0 million and ₱ 5.0 million which puts them under the small-scale category. One borrower can be considered as a large enterprise since it has assets of ₱ 35.0 million.

The Bank's SECP portfolio reveals that five of the 10 loans have amounts between ₱ 25,000 and ₱ 500,000. This range was observed to be the market niche of PDBs during the evaluation. The value of the loans (₱ 620,000) is about 23 percent of the portfolio. Two of the loans are considered commercial loans with amounts of more than ₱ 500,000. The combined value of the two loans (₱ 2,050,000) accounts for 75 percent of the portfolio. Four of the ten borrowers had prior loans with the Bank.

SME loan market

Bank management has identified several industries where SMEs may be financed under SECP. These are furniture and woodcraft, concrete products and food processing.

Impact on the Bank's Liquidity

The Bank has a very liquid position. Its loans-to-deposit ratio for 1991 is only 69 percent from 39 percent in 1986. Because of its liquidity, it has rarely used external funds to finance its loans. For example, the Bank drew from its SECP credit line only in 1990 and did not find the need to draw again from the line after that. The only external financing availed in 1991 was a ₱ 500,000 SSS Kasapi loan which is only about one percent of the Bank's total loan portfolio of ₱ 40.5 million. The Bank does not foresee the need for SECP funds in the next two years.

Bank's Lending Policies

The major accounts in the Bank's portfolio are: commercial and industrial loans (C-I), real estate and agriculture. From 1986 to 1991, total loans increased from ₱ 11.4 million in 1986 to ₱ 40.5 million in 1991 for an annual compounded growth rate of 29 percent.

Commercial and industrial loans continued to dominate the bank's portfolio with a 52 percent share in 1991. From ₱ 5.5 million in 1986, its value increased to ₱ 26.2 million in 1991 for an annual compounded growth rate of 37 percent. Agricultural loans declined from 33 percent of total loans in 1986 to 7 percent in 1991. Its value decreased from ₱ 3.7 million to ₱ 2.9 million. Real estate loans increased its share from 16 to 18 percent with an increase in value from ₱ 1.8 million to ₱ 7.4 million (or a compound growth rate of 32 percent).

The bank management has set the minimum loan size at ₱ 50,000. However, the size of the loan applications currently being processed average from ₱ 100,000 to ₱ 200,000. The objective of bank management is to eventually reach a minimum loan size of ₱ 1 million. The Bank targets institutions or firms and reports a very conservative position towards agricultural loans because of the CARP. It is currently lending to small-scale enterprises but is preparing to service medium-scale enterprises. While the bank's loans are mostly made to enterprises in Iloilo City, management has plans to expand to areas outside the city. In fact, management has plans of acquiring private development banks in Bacolod City and Iloilo City. A branch in Cebu is also being planned.

The Bank looks for potential accounts by conducting credit investigations. Services of the Bank are offered to the credit worthy institutions or individuals.

The collateral offered by a borrower is a major criterion of the loan evaluation. Usually, real estate mortgages are required. The Bank rarely accepts chattel mortgages.

Loan terms are usually set at one year. The Bank wants the flexibility to get out of a loan commitment should it find the need to do so. These short-term loans can be renewed annually as long as the collateral and paying capacity can still cover the project.

The Bank's loans department is currently staffed by one loan supervisor, two credit investigators, one loan processor and one clerk. An addition of two more credit investigators is necessary because of the projected increase in workload. During the second quarter of 1992, about 40 loan applications were received monthly. Aside from this, there is a strong pressure from management to create loans because of the excess funds of the Bank.

Deposit Mobilization Strategies and Performance

Deposits increased from ₱ 40.8 million in 1989 to ₱ 58.9 million in 1991 for a compound growth rate of 7.6 percent per annum. Savings deposits were ₱ 30.1 million in 1989 and ₱ 34.3 million in 1991 for a compound growth rate of 4.4 percent. Time deposits posted a 32 percent growth rate with deposits of ₱ 10.7 million in 1989 and ₱ 24.6 million in 1991. There were 4,485 accounts in 1991. Almost all (4,794) are individual accounts. About 95 percent are deposited in savings accounts and the rest to time deposits. The average size of deposits is ₱ 7,500 for savings and ₱ 91,000 for time deposits.

The Bank employs a very aggressive deposit mobilization campaign because of management's plans to operate as a commercial bank. As a result, management wants to project itself as a large bank and not a bank for small borrowers and depositors. One of the steps management has taken is to increase the Bank's deposit level. Among the strategies management has employed to generate deposits are:

1) a raffle offering a 1600cc car and appliances
2) extended banking hours (8:30 am - 5:00 pm)
3) pick-up tellers for large accounts
4) savings deposit interest rate of 6.5 percent
5) requiring the Bank's VISA cardholders to open a savings account
6) advertising through radio

Management has applied with the Central Bank to offer services such as a demand deposit and an FCDU. To further boost the Bank's deposits mobilization campaign, it has plans of opening another branch and acquiring two more banks.

BANK ASSESSMENT OF SECP

The Bank's liquid position makes the SECP, with its market-oriented interest rates, an unattractive funding source. The SECP is seen by bank's management as a reserve source of financing for the bank's future expansion.

SOUTHERN NEGROS DEVELOPMENT BANK

Southern Negros Development Bank (SNDB) was established in 1976 with an initial capital of ₱ 2.86 million. On December 31, 1991, shareholders' equity increased to ₱ 10.59 million or about four times the initial capital and total assets were at ₱ 78.65 million. SNDB's head office is located in Bacolod City, Negros Occidental. It operates a total of four branches in the province.

Use of SECP funds

SNDB was accredited with the SECP in March 1990 and was approved an initial credit line of ₱ 5.0 million. This was subsequently increased by another ₱ 5.0 million making the total credit line equal to ₱ 10.0 million. As of March 31, 1992, the Bank has drawndown the full amount of its credit line and has even reavailed of another ₱ 5.0 million. Based on SNDB's total loan availment of ₱ 15.0 million and total credit line of ₱ 10.0 million, the Bank's efficiency in moving the SECP funds down to the final borrowers is an impressive 150 percent. This is the highest among the 17 SECP participating IFIs.

The Bank was able to relend a total of 577 SECP sub-loans amounting to ₱ 17.3 million. About half of the sub-loans are small with loans of ₱ 5,000 or less. Up to about 75 percent of the sub-loans had amounts of ₱ 25,000 and below. The bigger loans (₱ 45,000 to ₱ 200,000) constituted only about 17 percent of the SECP loan portfolio. The biggest loan granted was ₱ 1.2 million while the smallest was ₱ 1,600.

The Bank is highly focused on financing of trading activities. This is shown by the significant share (84) of loans to individuals and firms engaged in trading compared to the four percent share of the loans to those in the manufacturing sector.

About half of the SECP sub-loans had a maturity of one year or less. The other half had maturities of more than one year to five years. Only one loan had a term longer than five years. This relatively high percentage of medium-term loans to the total SECP loan portfolio is consistent with the "long-term loan specialist" image being promoted by the Bank.

Majority of the SECP sub-borrowers are existing clients of the Bank. Of the 577 sub-borrowers, only about 17 percent represented new borrowers.

SME Loan Market

The Bank's target market consists mainly of the "smaller" segment of the SMEs in Negros Occidental. In particularly these are the market vendors, sari-sari storeowners, bakers, utility vehicle operators and artisans.

These small loan accounts were observed by the management to keep their business with the Bank. In contrast, big business borrowers do not use the Bank's deposit facilities and transfer their accounts easily to commercial banks when they are offered better interest rates. Moreover, due to the "fast turnover" nature of the SME business, the management also commented that they do not tend to be sensitive to interest rates, making them a profitable sector to serve. However, the SNDB finds that lending to SMEs require personal attention even from the top officers of the Bank. In addition, loan evaluation requires special procedures and knowledge since there are generally no business records to use. In the case of the Bank, these include personal interviews by the Bank president and familiarity with the personal background and business of the loan applicant.

The Bank rated the majority of its borrowers to be "progressive" because most have grown bigger as evidenced in the increase in the amounts of their subsequent borrowings.

SNDB considered itself as the leading SME lender in the area. Next to it, the Bank identified rural banks and financing companies. The third group was stated to consist of the lending investors.

The SME loan market is foreseen to grow because of the economic recovery that is expected to come with the installation of a new set of government leaders. The Bank expects that most of its clients will continue to be mainly individuals engaged in trading and services because of the limited manufacturing activities in the area.

Impact on the Bank's Liquidity

The SECP significantly expanded the Bank's financing sources. As of December 31, 1991, about half of SNDB's borrowings was sourced from SECP. The Program also provided major support to the Bank's lending activities. The outstanding SECP loan represented about 23 percent of SNDB's total loans and discounts. The importance of this support is further highlighted by the Bank's average ratio of total loans to total deposit in 1991 of 168 percent. This is indicative of SNDB's inability to generate adequate deposits to support its lending activities and its dependence on borrowed money as a source of loan funds.

Bank Lending Policies

The Bank's management appeared to have a very good understanding of SMEs, sharing the following insights about SMEs:

1. SMEs are good credit risks. SME entrepreneurs are able to easily recover from business failures and have the capacity to start up on another venture. Past experience has shown that the Bank incurred lower levels of delinquency in its commercial and industrial loan accounts where most borrowers are SMEs.

2. SMEs are profitable loan accounts. The high transaction cost of processing small loans can be recovered by charging a higher rate of interest. Due to the "fast turnover" nature of their business, SMEs can absorb high interest rates.

3. Personal relationship is important in lending to SMEs. Due to their lack of banking experience, SME entrepreneurs easily get overwhelmed and discouraged by the formal atmosphere and credit process of commercial banks. Service should be personalized and should allow SMEs to relate directly with the Bank's top officers to discuss their financing needs and problems.

The following are some of SNDB's lending policies:

1. Businesses to be financed should have been in operation for at least five years. The management explained that this requirement is intended to minimize credit risk because entrepreneurs of firms with track records are already familiar with the business which increases the chance of success.

2. Loan applications (of specified amounts) are approved or disapproved based on the result of interviews conducted by the Bank president with the loan applicants. The president's personal involvement in the loan evaluation process is intended to strengthen the screening of loan applications in order to identify possible problem accounts at the beginning of the lending process. The Bank finds this critical in view of its awareness that it cannot efficiently monitor the loans once approved because of SNDB's numerous loan accounts (577 under the SECP alone).

3. The management identified the applicant's knowledge of the business and his entrepreneurial attitude as the main criteria for approving or disapproving loan applications. These are the two most important factors that are evaluated during the Bank president's interview of the loan applicant. The management explained that since there are hardly any business records, knowledge of business is gauged by the applicant's ability to explain his operation fairly quickly ("five minutes").

4. The term of the loan was said to be based on the paying capacity of the borrower. The Bank may approve a longer payment period depending on the amount of the loan amortization that the borrower says he can afford. For example, SNDB structured a working capital loan of ₱ 23,500 for three years and another working capital loan of ₱ 606,000 for 180 days. The maximum term for SME loans is five years.

5. All loans are secured by either a real estate or a chattel mortgage on fixed assets. A real estate mortgage is required for loan amounts of at least ₱ 200,000.

6. In order to generate as much loan volume as possible, the Bank has set the minimum loan size at relatively small amount of ₱ 1,000.

Deposit Mobilization

The Bank sets an annual target for new deposit levels and is engaged in deposit generation activities throughout the year to achieve this target. The Bank uses mainly two strategies: distribution of printed promotional materials and offering of competitive interest rate.

The printed materials consist of flyers, which are inserted in Sunday newspapers, and posters that are put up in the Bank's premises and in major establishments. The Bank has been preparing flyers for two years.

SNDB is aware of its handicap in competing with commerial banks for deposits from individual depositors. In the case of institutional accounts, it is constrained by the limited banking services that the Bank is authorized to offer. Working within these limitations, in 1991, the Bank decided to utilize interest rates as a means of competing for deposits with commercial banks.

The Bank's interest rates on savings deposit are higher than that of commercial banks. Interest rates range from 6 percent.to 12 percent on savings deposits with average daily balances (ADB) of ₱ 100 to less than ₱ 60,000, and those with ADB higher than ₱ 200,000, respectively.

Interest on time deposit is competitive with that of commercial banks. In particular, the rates are set at the same level as those of Treasury Bills adjusted weekly. The rate offered on placements of ₱ 200,000 is the same as the commercial bank rate for ₱ 1.0 million.

To encourage borrowers to maintain savings accounts with the Bank, lower interest rates are charged on loans of depositor-borrowers. Non-depositors are charged interest rates which are as much as 12 percent higher than the rate for depositor-borrowers. Monthly interest rebates to depositor-borrowers are determined based on the ADBs.

The deposit generation strategies of the Bank have resulted in a 17 percent compound annual growth in the Bank's total deposits from 1988 to 1991. Moreover, the profile of the Bank's deposit liabilities changed in favor of savings over time. In 1986, deposit liabilities consisted of 30 percent savings deposits and 70 percent time deposits. In 1991, the composition improved to 45 percent savings deposits and 45 percent time deposits. Deposits of other banks in SNDB accounted for an additional ten percent.

Bank Assessment of the SECP

The three SECP features which SNDB finds most attractive are:

a. very little red tape, simple procedure
b. advance funds
c. no collateral requirement

Citing the difficulties encountered by the Bank in satisfying the re-accreditation requirements of the IGLF and CLF, the Bank's management finds the simplicity of the accreditation and fund availment procedures as well as the quick release of funds as the most beneficial aspects of the SECP.

Benefits of being able to increase loans to small borrowers and from attendance to the training programs sponsored by SECP were also cited.

Annex D

PROFILE OF MAJOR FINANCING PROGRAMS

Annex D

PROFILE OF MAJOR SME FINANCING PROGRAMS

SME financing programs can be divided into two broad categories: a) those which provide loans to SMES and b) those that provide only credit guarantees. The first category can be further sub-divided into i) financing provided through banks/financial institutions; ii) financing provided through government agencies and iii) financing provided through Private Voluntary Organizations/Non-Governmental Organizations. Under the second category are i) the credit guarantee provided through the Guarantee Fund for Small and Medium Enterprises (GFSME) and ii) the USAID guarantee program.

The credit guarantee schemes are intended to encourage more lending to SMEs by absorbing most of the attendant loan default risks. GFSME has been at the forefront of these schemes. Credit guarantee can induce banks to lend to progressive and promising SMEs and it may therefore be an important feature of any SME financing program. However, there is a need to assess whether the credit guarantees only give banks additional protection at substantial costs on the part of the SMEs which shoulder the guarantee fees. The question of additionality in lending seems to persist because of the opinion that banks continue to lend only to tried and tested SMEs (old clients) and use the guarantee to simply buy more protection against loan defaults. However, this report concentrates only on the direct lending schemes for SMEs notwithstanding the importance of assessing the utility of guarantee schemes.

SME Financing through Banks/Financial Institutions

The following financing programs belong to this category:

(a) Small and Medium Industry Loan Program (SMILP)- a Land Bank-SSS Partnership
(b) Social Security System (SSS) *Kasapi* Loans
(c) PNB *Pangkabuhayan* Loans
(d) Industrial Guarantee and Loan Fund (IGLF)
(e) Countryside Loan Fund (CLF)
(f) Bankers' Association of the Phils. Credit Guaranty Loans

Table D-1 shows the key features of each of these financing programs that use banks/financial institutions as lending channels. Except for the BAP Credit Guaranty Loans, these financing programs are all government-directed or inspired. Under this approach the government institution concerned provides the lending channels, usually the private financial institutions, with the funds which will be lent to target beneficiaries. A set of accreditation criteria is used to screen the participating PFIs. These retail outlets in turn earn from the spread which is the difference between the cost of the funds from the government institution and the lending rate to the end-user or target client.

The financing programs are intended to finance short-term and permanent working capital, acquisition of capital assets, and various forms of building construction. The eligible activities range from productive agricultural activities, food and agro-processing, manufacturing, particularly labor-intensive and export-oriented SMEs.

Because of the financial reforms, the interest rate charged against the final borrower is usually aligned with the market rates. This is the case for the currently two biggest sources of SME financing, the CLF and the IGLF. On the other hand, the SSS provides low cost funds to the private financial institutions which they will lend at a spread of not more than 3 percent in the case of Metro Manila non-export-oriented projects and at a spread of not more than 4 percent in the case of non-Metro Manila /export-oriented projects. PNB and Land Bank charge fixed rates. PNB charges fixed rates of from 17 percent to 19 percent based on the loan maturity; the Land Bank SMILP also charges a fixed rate of 20 percent for a five year loan. The private sector-initiated BAP Credit Guaranty Loans are slightly below the prevailing commercial rate for working capital loans and for fixed assets, the rate is the BAP rate plus 2 percent.

In the financing programs using government banks, the PNB and the LBP use their own network of branches and local offices to lend to SMEs. For example, under the Land Bank-SSS partnership, instead of wholesaling the SSS funds intended for small and medium industry, the Land Bank itself retails the loans to SMEs. The PNB, on the other hand, using its own funds, directly lends the *"pangkabuhayan"* loans to SMEs. These financial institutions provide loans at lower than market rates to SMEs. In contrast, those financing programs which use private financial institution as lending channels rely on the private banking network to lend to SMEs at generally market-oriented rates, such as those provided under the IGLF and the CLF.

A recent addition to the different SME financing programs is the BAP Credit Guaranty Loan. This is implemented by the BAP Credit Guarantee Corporation which was created and capitalized in 1991 by the universal and commercial banks to address what they perceive to be a financing gap for SMES. The program provides the credit requirements of SMES which are not serviced by the banks because of their relatively small asset base and financing need, or lack of track record or collateral. According to the BAP the BCGC will bridge the gap between the SME sector and the banks and will nurture the SMES until they have sufficiently grown in size and developed a credit record with the BCGC. When these objectives shall have been attained, the banks take over the financing of the mature SMES.

The BCGC offers both short-term working capital loans and fixed asset loans at interest rates which are generally much lower than prevailing commercial rates. The BAP Credit Guaranty Loan also requires collaterals but aside from the traditional real estate and chattel mortgages it also asks for the joint and several signatures of borrowers and co-makers and post-dated checks. Total loans granted to SMES amounted to ₱ 36 million as of April 1992 after less than a year in operation of which about ₱ 18 million have been collected. There were only 51 borrowers under this financing program.

All of the SME loans coursed through formal financial institutions require some form of collateral or security against the loan. The most common forms of security consist of the traditional collaterals like deed of real estate mortgage, deed of chattel mortgage, government bonds and securities, and hold-out deposits. The maturity differs by type of project financed and purpose of the loan. Thus, loans for permanent working capital may have longer maturities than those for export packing credit and production credit.

These financing programs cover the entire nation and do not disqualify projects based on geographic location. The IGLF provides maximum loan ceilings while the CLF has a minimum loan size of ₱ 100,000 and a maximum loan size equivalent to 5 percent of Land Bank's equity. Quedan financing distinguishes between a working capital loan (maximum size is ₱ 50,000) and fixed assets (maximum size is ₱ 100,000). The Land Bank-SSS SMILP imposes a loan ceiling of ₱ 20 million per project while the PNB *Pangkabuhayan* Loan has a maximum loan amount of ₱ 1 million per borrower. The BAP has a ceiling of ₱ 2 million.

Direct Lending by a Government Agency

The Technology and Livelihood Resource Center, a government agency under the Office of the President lends to SMES directly. It has two SME Direct Lending Programs, namely, a) the Agro-Industrial Technology Transfer Program (AITTP) and the Export Industry Modernization Project II (EIMP). The OECF provided the loanable funds to these two financing programs. The AITTP started in 1983 while the EIMP was implemented in 1988.

Table D-2 shows the key features as well as the status of these financing programs. Both provide loans for working capital and the acquisition of fixed assets at highly subsidized rates. Eligible borrowers for AITTP are producers and processors of agri- or aqua-based projects while those for EIMP are new or starting small and medium enterprises. Both have a nationwide coverage. Under this approach it is the TLRC which lends to the eligible borrowers using funds borrowed from multilateral sources. The interest rate to the end-user is highly concessional perhaps because the OECF of Japan usually requires the Philippine government to re-lend the funds, which it borrowed from the OECF at a low interest rate, also at highly concessional rates. The interest rate policy as well as the use of a government agency to do direct lending seem contrary to the established market-orientation of credit policy and the encouragement of more private sector participation, and conversely, less government involvement in direct lending activities.

With respect to the AITTP, the TLRC reports loans granted amounting to ₱ 545.2 million of which ₱ 380.2 million remain outstanding. The repayment rate of 63 percent is rather low while the past due ratio of 26 percent is on the high side, considering that the Central Bank allows only a maximum past due ratio of 25 percent for financial institutions. It was only able to reach 100 borrowers.

SME Lending through PVOs/NGOs

An innovative approach taken by some of the SME credit programs is the use of PVOS/NGOS as conduits of SME loans. The government provides these institutions with funds at subsidized rates which are then re-lent to the target beneficiaries at rates determined by the government agency in the case of the NLSF financing programs and at prevailing commercial rates in the case of the DTI *Tulong sa Tao* Program. The approach has some distinct advantages: the target SMES are reached because of the lower transaction costs and the information on borrowers enjoyed by these institutions. The collateral requirements are not as strict and substantial as those demanded by the traditional lenders like banks and the maturity schedule is adjusted to suit the project cash flow (but not to exceed 5 years) in the NLSF-run programs (Table D-3).

The reported repayment rates seem to be high but the question of continuing efficiency and the ability to meet increasing loan demands over the long pull may be raised. Once loan demands increase and the client base expands, the PVO/NGO may lose its comparative advantage over formal financial institutions which may have economies of scale and scope to handle ever increasing loan volumes and clientele.

Impact on the SME Sector and PFIs

Among the direct lending programs for SMES, the IGLF and the CLF seem to have the largest coverage. This may be due to the wide branch network of the participating private financial institutions and the large funding made available both to the wholesale banks (the DBP and LBP, respectively). The approach uses the private sector network which has a wider reach and depth than that of the government.

Total availments under the IGLF amount to ₱ 5.071 billion as of June 26, 1992. Aside from the large funding available from this source, PFIs continue to access IGLF because of several reasons: 1) the loan can be a 100% working capital loan subject to presence of excess plant capacity; 2) the loan can be advanced by DBP; 3) absence of an environmental clearance certificate, another requirement usually imposed by external sources of financing and 4) familiarity by the PFIs with the requirements of the program. Borrowers can approach any accredited bank to borrow from the IGLF.

On the other hand, the Land Bank's CLF is a $150 million credit facility from the World Bank that uses a network of commercial banks, rural banks, thrift banks and NBFIs as credit channels. The CLF requires compliance with all laws and regulations of the Philippines related to environmental protection. A monitoring system has been devised by the Land Bank to track the PFI's post release compliance of the submission of the environmental clearance certificate issued by the Environmental Management Bureau of the DENR. The Land Bank reports 30 accredited rural banks and thrift banks; 24 commercial banks; 2 NBFIs and 2 government specialized banks as participating FIs. As of March 1992, total loan releases amount to ₱ 89.3 million which were provided to 28 projects. Of these, 3 are in manufacturing (hollow blocks, industrial oxygen and paints); one in service (transportation); 6 are in food processing (ice plant, rice milling, coconut oil milling, bakeshop) and the rest are in agriculture production (piggery, poultry, cattle fattening, cut flower, citrus and duck egg).

There has been no systematic evaluation of the impact on SMES and the PFIs of these various financing programs. The cost to government and the GFIs of running these financing facilities has not been studied despite the proliferation of these programs and the tendency of Congress to create similar programs. Evaluation is necessary for consistency and effectiveness of these approaches especially because of the continuing problem of lack of access by SMES to formal finance.

There is no readily available information on the impact of most of these programs, including those implemented through government agencies and the PVOs/NGOs, much less on the administrative and management costs of running these credit programs. Two things, however, are important when evaluating these programs and how they have been designed. The first is whether or not the target beneficiaries, i.e. the SMES have been reached as claimed by these financing programs and second, the sustainability of these programs.

A quick gauge of the latter consists of the a) repayment rate and b) past due ratios. Some financing programs report these indicators while the recently-established programs have yet to have the experience in SME lending. Although the repayment rate looks high for some programs, the reported past due ratios are a cause for concern.

The NBFIs like the TLRC and the BAP Credit Corp. are located in the National Capital Region and definitely have a smaller outreach. The government and private financial institutions have the advantage of both Metro Manila and countryside presence because of their widespread branch and office network. However, despite claims by the different financing programs that they have a wide coverage and reach, a recent study by Lamberte et al.,(1989)[1] pointed out that the special credit programs' presence in the provinces is hardly felt by the target market. What is evident in the field interviews is that there is a large SME loan market that is waiting to be tapped by the more enterprising PFIs but this does not materialize because of any or a combination of the following reasons: 1) the lack of flexibility of financing program ; 2) collateral orientation of the financing programs; 3) the risks in SME lending that is exacerbated by the lack of information on projects and the character of SME borrowers; 4) the failure to tie deposit mobilization with term credit for SMES.

With respect to the mobility to raise deposits, all the financing programs seek to provide funds which the PFIs lend at maturities that match their own loan obligations with the GFI or with the government. There is therefore a strict and straightforward matching of maturities between the PFI loan from the GFI/government and its own loan to the end-borrower. On the other hand, the lack of flexibility refers to the fact that the lending criteria and requirements of these financing programs are dictated by the need

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1 Lamberte, Mario. PIDS Working Paper # 90-20. "MCSME Promotion Policy and Legislative Agenda: Focus on Monetary Policy, Finance and Credit Programs." July 1990.

of the funding agency (whether foreign or local) to recover loan exposure and less by the situational need of the target SMEs. In short, the PFI has very little room to design a financing package that will suit the particular requirements of concerned SMEs. A case in point is the IGLF which simply follows the route of traditional SME financing packages and operates the program as a reimbursement scheme in order to minimize its risks. There is in fact no margin for loss both for DBP and the PFIs because of this approach and the fact that the loans are heavily collateralized.

The redeeming factor of these financing programs seems to lie in the market-orientation of the interest rates with the exception of those approaches which continue to provide highly concessional but unsustainable and distortionary rates. There is the view that the main difficulty is not really the cost of credit but the lack of access to it which the different programs intend to cure. However, there seems to be some mismatch between the heavy reliance on commercial banks to deliver the credit and the intended clients, the SMEs which are clearly outside the sphere of commercial bank clientele. This Evaluation gives indication that in all likelihood the SMEs are not effectively reached by most special SME lending programs and the loans that have been disbursed mainly through the commercial banks were given to big borrowers and the not the intended SME targets.

The initiative by the banks to address the financing problems of the SME, through the BAP Credit Guarantee Corporation, is worth noting because it was done without any pressure or encouragement from the government. The other view is that the private sector saw the failure of the traditional financing packages to effectively reach the SMEs. It seems that the banks saw the potential business and profits they can get from the SME sector and created an instrument to handle the particular nuances of SME lending.

Table D - 1

KEY FEATURES OF GOVERNMENT SME FINANCING THROUGH BANKS/FINANCIAL INSTITUTIONS

GOVERNMENT LENDING PROGRAMS	LENDING CHANNELS	LOAN PURPOSE	LOCATION OF ELIGIBLE BORROWERS	ELIGIBLE BUSINESS ACTIVITIES	COLLATERAL REQUIREMENT	MAXIMUM LOAN SIZE (P)	LOAN TERM	INTEREST RATE (to lending channel)	INTEREST RATE (to final borrower)
Countryside Loan Fund	Commercial Banks, Unibanks, Rural Banks, Thrift Banks, and nonbank financial institutions	medium- and long-term credit for capital assets	Nationwide especially countryside	productive agricultural activities, food and agro-processing and export oriented manufacturing and service SMEs	REM, CHM, bonds or securities guaranteed by RP, deposit holdout	5% of Land Bank's Equity	1 to over 8 years	FloatR - WAIR (quarterly) Fixed - WAR (fixed) = prem	As negotiated by PFIs and borrowers
Industrial Guarantee and Loan Fund	Commercial Banks, Thrift Banks, Rural Banks	permanent working capital, factory site for projects, buildings construction, capital assets & installation costs	Nationwide	manufacturing and manufacturing-support service industries	any collateral acceptable to PFI	Accredited Scheme: .4 - 16 million Sponsorship Scheme: 500,000	working capital - 7 yrs w/ 2 yrs grace export packing credit - 180 days production credit - 1 yr fixed assets - 12 yrs w/ 3 yrs grace	Fixed or Variable Market rate at IFI's	- market based but moral suasion is used to dissuade large spreads
Small and Medium Industry Loan Program (SMILP)	Branches of the Land Bank of the Philippines	acquisition of projects, warehouse sites & capital assets, factory building/warehouse construction (expansion)	Nationwide	agribusiness, manufacturing, transportation, communication, commercial production, utilities, export related activities	REM, CHM, other acceptable collateral	0.5 million - 20 million per project	Maximum of 7 years with 2-year grace period	16 %	20 %
SSS Kasapi Loan	Private Financial Institutions (PFI)	acqsit'n of machn'ry and equipment, working capital, constrc'n/improv't of factory buildings, warehouse & other civil works, increase capacity utilization	Nationwide	agribusiness, manufacturing, utilities, transport'n/commc'n, commercial and for export production	any collateral acceptable to PFI, preferably REM	10 million	5 years w/ 1 yr grace	MetroManila: - 14% Outside MetroManila - 12%	MetroManila: - 17 % Outside MetroManila: - 16 %
PNB Pangkabuhayan Loan	Philippines National Bank	working capital, fixed asset acquisition and capital expenditure	Nationwide	production, processing, manufacturing, palay drying/milling & storage/ cold storage activities	REM, CHM, savings and time deposits	1.0 million/borrower	working capital - 1 yr fixed asset - 5 yrs w/ 1 yr grace		1 year: 17% 3 years: 18% more than 3 years: 19%
BAP Credit Guarantee Loan	BAP Credit Guarantee Corp.	start-up & shortterm working capital & fixed assets	Nationwide	labor intensive, export oriented activities, import-substituting industries	REM, CHM, PDC, LC/PD	2.0 million	fixed asset - 4 years		Fixed Asset BCGC quarterly rate plus 2 percentage pt. Working Capital: commercial rate minus 2 percentage pt.

Table D - 2

KEY FEATURES AND STATUS OF DIRECT LENDING PROGRAMS
OF A GOVERNMENT AGENCY

	AGRO-INDUSTRIAL TECHNOLOGY TRANSFER PROGRAM (AITTP)	EXPORT INDUSTRY MODERNIZATION PROJECT II
LENDING CHANNEL	Direct re-lending of funds by TLRC-AITTP	Direct re-lending of funds by TLRC
LOAN PURPOSE	Acquisition of fixed assets and provision for working capital.	Building, machinery, working capital
LOCATION OF ELIGIBLE BORROWERS	Nationwide	Nationwide
ELIGIBLE BUSINESS ACTIVITIES	Producers/processors of agri- or aqua-based projects	New or existing small and medium enterprise
COLLATERAL REQUIREMENT	Land; land improvements; buildings; and chattels	100% coverage with hard assets from the projects, such as land, building machines
MAXIMUM LOAN SIZE	21 million	5 million
LOAN TERM	5 to 15 years inclusive of 1 to 5 years grace period	
INTEREST RATE	8.75% p.a.	10% p.a.
LOAN STATUS	As of December 31, 1991 Loans Granted (PM) : 545.189 Loans Matured (PM) : 263.32 Loans Collected (PM) : 164.974 Loans Outstanding (PM) : 380.215 Loans Past Due (PM) : 98.346 Repayment Rate (%) : 63 Past Due Ratio (%) : 26 Number of Borrowers : 100	

Table D - 3

KEY FEATURES OF SME LENDING THROUGH PVOs/NGOs

	TULONG SA TAO PROGRAM	NATIONAL LIVELIHOOD SUPPORT FUND-LIVELIHOOD DEVELOPMENT PROJECT
LENDING CHANNEL	Private Voluntary Organizations (PVOs)	Non-government organizations
LOAN PURPOSE	Assistance to labor intensive micro, cottage, small and medium-scale businesses.	Livelihood/Income-Generating
LOCATION OF ELIGIBLE BORROWERS	Nationwide	Nationwide, especially in depressed areas
ELIGIBLE BUSINESS ACTIVITIES	Micro-business and livelihood projects	Livelihood projects
COLLATERAL REQUIREMENT		None
MAXIMUM LOAN SIZE	1 million to PVOs; P25,000 to Beneficiaries	P300,000
LOAN TERM	1 year	5 years
INTEREST RATE	7% p.a. to PVOs; Commercial rate to beneficiaries	6 % to NGO; Maximum of 15 % to beneficiaries
LOAN STATUS	Approved Funding Commitment - 60 million	As of December 3, 1989 Approved Funding Commitment - 388,779,000 No. of Approved Programs - 47 Funds Released to SDOs - 62,764,450 No. of SDOs used as Fund Conduits - 27 No. of Proj. funded by Programs - 3,043 No. of Direct Beneficiaries - 9,729

Annex E

TABLE REFERENCES

Table 2. REGIONAL DISTRIBUTION OF FIRMS BY NUMBER OF EMPLOYEES
(Percentage Distribution Across Regions)

NUMBER OF EMPLOYEES	METRO MANILA		II & IV		Other Regions		TOTAL (PHILIPPINES)
	NO. OF FIRMS	% SHARE*	NO. OF FIRMS	% SHARE*	NO. OF FIRMS	% SHARE*	
Less than 10	8,066	35.4	5,592	24.5	9,144	40.1	22,802
10-19	1,351	49.1	462	16.8	939	34.1	2,752
20-49	1,134	54.2	345	16.5	615	29.4	2,094
Total (less than 50)	10,551	38.2	6,399	23.1	10,698	38.7	27,648
More than 50	1,438	62.3	364	15.8	505	21.9	2,307
Total All Sizes	11,989	40.0	6,763	22.6	11,203	37.4	29,955

* Number of Firms Over Total Number of Firms in the Philippines
Source: NCSO, Survey of Establishments, 1983
Industrial Dispersal in the Philippines, Vol.1, NEDA

FILE.TABL81

Table 3. LOANS GRANTED BY PRIVATE DEVELOPMENT BANKS (PDBs) PER REGION

(in millions)

REGION		TOTAL LOANS GRANTED BY PDBs		SECP LOANS GRANTED				SECP LOANS AS A PERCENTAGE OF TOTAL LOANS			
				WITH PDCP		WITHOUT PDCP		WITH PDCP		WITHOUT PDCP	
		1990	1991	1990	1991	1990	1991	1990	1991	1990	1991
I	ILOCOS & MT. PROV.	15.40	16.70	3.50	1.90	0.00	0.00	22.73	11.38	0.00	0.00
II	CAGAYAN VALLEY	0.00	0.00	10.00	0.70	10.00	0.70				
III	CENTRAL LUZON	5,720.40	1,095.00	19.99	18.33	19.36	16.78	0.35	1.67	0.34	1.53
NCR	NATIONAL CAPITAL REGION	3,106.70	8,625.20	0.00	1.96	0.00	1.96	0.00	0.02	0.00	0.02
IV	SOUTHERN TAGALOG	1,040.40	1,264.40	47.34	46.90	46.84	46.90	4.55	3.71	4.50	3.71
V	BIÇOL	606.30	884.60	14.45	3.47	14.45	3.47	2.38	0.39	2.38	0.39
VI	WESTERN VISAYAS	88.40	142.70	19.40	22.28	12.97	7.94	21.95	15.61	14.68	5.56
VII	CENTRAL VISAYAS	81.10	108.40	6.40	21.24	0.15	18.89	7.89	19.60	0.18	17.43
VIII	EASTERN VISAYAS	0.00	0.00	0.00	4.50	0.00	4.50				
IX	WESTERN MINDANAO	0.00	0.00	0.00	0.00	0.00	0.00				
X	NORTHERN MINDANAO	200.60	278.00	14.63	5.99	14.63	5.99	7.29	2.16	7.29	2.16
XI	SOUTHERN MINDANAO	75.10	145.60	2.80	20.12	2.10	11.93	3.73	13.82	2.80	8.19
XII	CENTRAL MINDANAO	0.00	0.00	0.20	1.20	0.00	1.20				
	TOTAL	10,934.40	12,560.60	138.71	148.59	120.51	120.26	1.27	1.18	1.10	0.96
	TOTAL w/o NCR	7,827.70	3,935.40	138.71	146.63	120.51	118.30	1.77	3.73	1.54	3.01

Source: Central Bank Center for Statistical Information, Department of Economic Research - Domestic
Central Bank of the Philippines

FILE TABLES

Table 4. AVERAGE ANNUAL GROWTH IN COMMERCIAL/INDUSTRIAL LOANS BEFORE (1988-89) AND AFTER (1990-91) SECP

BANK	Before SECP 1988-89	After SECP 1990-91
GROUP A		
PLANTERS DEV'T BANK	33.54	51.08
PRIVATE DEV'T CORP. OF THE PHILIPPINES	(22.0)*	---
ASIATRUST DEV'T BANK	83.69	54.22
AVERAGE	31.74	52.65
GROUP B		
PREMIERE DEV'T BANK	63.34	17.60
LUZON DEV'T BANK	3.068	16.53
NORTHERN MINDANAO DEV'T BANK	174.2	55.07
BANGKO SILANGAN DEV'T BANK	152.1	42.02
BATAAN DEV'T BANK	-11.4	20.30
QUEEN CITY DEV'T BANK	16.32	58.25
BANCO DAVAO-DAVAO DEV'T BANK	65.01	66.12
DUMAGUETE DEV'T BANK	17.87	133.32
BANCO CEBUANO-CEBU CITY DEV'T BANK	(29.4)	131.79
AVERAGE	50.14	60.11
GROUP C		
SOUTHERN NEGROS DEV'T BANK	2.019	(25.57)
PALAWAN DEV'T BANK	41.08	41.72
TARLAC DEV'T BANK	(25.3)	544.77
ISLAND DEV'T BANK	292.8	---
AVERAGE	77.67	186.97

* Consists of loans in Manufacturing, Transportation & Communication, Mining and Construction.

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Table 5. DISTRIBUTION OF SECP SUB-LOAN BORROWERS: EXISTING VERSUS NEW

BANK	BORROWERS		NEW / EXISTING (%)
	NEW	EXISTING	
GROUP A			
ASIATRUST DEVELOPMENT BANK	4	5	80
PLANTERS DEVELOPMENT BANK	25	16	156
PRIVATE DEV'T CORP. OF THE PHIL.	118	41	288
SUB-TOTAL	147	62	237 *
GROUP B			
BATAAN DEVELOPMENT BANK	8	23	35
BANGKO SILANGAN DEVELOPMENT BANK	200	120	167
BANCO CEBUANO	27	2	1,350
BANCO DAVAO	26	14	186
DUMAGUETE CITY DEVELOPMENT BANK	22	2	1,100
LUZON DEVELOPMENT BANK	53	36	147
NORTHERN MINDANAO DEV'T BANK	20	14	143
PREMIERE DEVELOPMENT BANK	4	1	400
QUEEN CITY DEVELOPMENT BANK	5	4	125
SUB-TOTAL	365	216	169 *
GROUP C			
BICOL DEVELOPMENT BANK	18	0	NR
ISLAND DEVELOPMENT BANK	36	3	1,200
PALAWAN DEVELOPMENT BANK	55	96	57
SOUTHERN NEGROS DEVELOPMENT BANK	73	108	68
TARLAC DEVELOPMENT BANK	7	1	700
SUB-TOTAL	189	208	91 *
TOTAL	701	486	144 *

* Derived by Dividing Total Number of New Borrowers by Total Number of Existing Borrowers
Note: Data Does not Include Loans of Bicol Development Bank and Southern Negros Development Bank With Amounts Less Than 10,000 Pesos It Also Includes Loan Accounts of Unkown Borrower Status

FILETABLE5

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Table 6. SECP AVAILMENTS AND IFI RESOURCES
(in Millions, As of December 31, 1991)

BANK	OUTSTANDING SECP LOAN	CHANGE IN ASSETS (1990-91)	OUTSTANDING SECP LOAN / CHANGE IN ASSETS (%)
GROUP A			
PLANTERS DEVT BANK	29.49	2,182.59	1.35
PRIVATE DEVT CORP. OF THE PHILIPPINES	36.98	(87.33)	(42.35)
ASIATRUST DEVT BANK	7.03	990.50	0.71
WEIGHTED AVERAGE			1.15
GROUP B			
PREMIERE DEVT BANK	0.87	294.56	0.30
LUZON DEVT BANK	13.15	170.10	7.73
NORTHERN MINDANAO DEVT BANK	10.23	276.07	3.71
BANGKO SILANGAN DEVT BANK	20.20	133.49	15.13
BATAAN DEVT BANK	3.00	42.90	6.99
QUEEN CITY DEVT BANK	1.26	63.49	1.98
BANCO DAVAO - DAVAO DEVT BANK	4.48	43.47	10.31
DUMAGUETE CITY DEVT BANK	11.25	51.22	21.96
BANCO CEBUANO - CEBU CITY DEVT BANK	5.00	26.67	18.75
WEIGHTED AVERAGE			6.30
WEIGHTED AVERAGE w/o Premiere			8.49
GROUP C			
SOUTHERN NEGROS DEVT BANK	10.00	16.87	59.28
PALAWAN DEVT BANK	9.33	20.74	44.99
BICOL DEVT BANK	9.63	24.40	39.47
TARLAC DEVT BANK	2.63	4.18	62.92
ISLAND DEVT BANK	4.55	11.22	40.55
WEIGHTED AVERAGE			46.69

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Table 7. OVERALL DISTRIBUTION OF NUMBER OF BORROWERS AND AMOUNT OF SECP LOANS BY SIZE

SIZE OF LOAN	BORROWERS		LOAN		
	NUMBER	% TO TOTAL*	AMOUNT	% TO TOTAL*	
UNKNOWN	13		0		
5,001 - 10,000	16		144,000		RURAL BANK LOAN SIZE
10,001 - 15,000	46		658,000		
15,001 - 20,000	62		1,205,400		
20,001 - 25,000	43	13%	1,058,686	1%	
25,001 - 30,000	49		1,458,300		PDB LOAN SIZE
30,001 - 35,000	27		935,900		
35,001 - 40,000	49		1,949,500		
40,001 - 45,000	15		667,000		
45,001 - 50,000	130		6,495,000		
50,001 - 100,000	269		22,869,460		
100,001 - 200,000	213		34,936,797		
200,001 - 300,000	100		27,184,878		
300,001 - 400,000	49		18,258,281		
400,001 - 500,000	76	76%	37,344,444	48%	
500,001 - 600,000	8		4,768,000		COMMERCIAL BANK LOAN SIZE
600,001 - 700,000	10		6,731,000		
700,001 - 800,000	20		15,282,706		
800,001 - 900,000	5		4,417,450		
900,001 - 1,000,000	15		14,807,340		
1,000,001 - 2,000,000	49		76,102,777		
2,000,001 - 3,000,000	14		35,630,000		
3,000,001 - 4,000,000	2	10%	6,300,000	51%	
TOTAL	1,280	100%	319,204,919	100%	
MEDIAN LOAN SIZE			100,000		

° Number of borrowers or Amount in the Range Over Total Borrowers or Total Amount
Note: Data Does not Include Loans of Bicol Development Bank and
Southern Negros Development Bank With Amounts Less Than 10,000 Pesos.

FILE:TABLE7

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Table 8. DEPOSIT PERFORMANCE OF IFIs (1988-1991)

BANKS	ANNUAL GROWTH OF DEPOSITS (%)	AVERAGE DEPOSITS/ASSETS (%)
GROUP A		
PLANTERS DEV'T BANK	28.7	46.9
PRIVATE DEV'T CORP. OF THE PHILIPPINES	---	---
ASIATRUST BANK	53.9	63.0
AVERAGE	41.3	55.0
GROUP B		
PREMIERE DEV'T BANK	28.6	62.3
LUZON DEV'T BANK	20.8	77.1
NORTH. MINDANAO DEV'T BANK	67.7	19.1
BANGKO SILANGAN DEV'T BANK	54.8	80.2
BATAAN DEV'T BANK	17.7	75.6
QUEEN CITY DEV'T BANK	11.3	57.4
BANCO DAVAO-DAVAO DEV'T BANK	22.3	84.9
DUMAGUETE CITY DEV'T BANK	39.5	46.4
BANCO CEBUANO-CEBU CITY DEV'T BANK	13.5	70.3
AVERAGE	30.7	63.7
GROUP C		
SOUTHERN NEGROS DEV'T BANK	17.0	36.8
PALAWAN DEV'T BANK	43.6	56.2
TARLAC DEV'T BANK	70.6	14.7
ISLAND DEV'T BANK	73.3	21.6
AVERAGE	51.2	32.3

FILE: TABLE8

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Table 9. SECP AVAILMENTS AND IFI BORROWINGS
(in Millions, As of December 31, 1991)

BANK	OUTSTANDING SECP LOAN	BORROWINGS*	CHANGE IN NET LOAN (%)	OUTSTANDING SECP LOAN / BORROWINGS (%)	OUTSTANDING SECP LOAN / CHANGE IN NET LOAN (%)
GROUP A					
PLANTERS DEV'T BANK	29.49	1,691.00	1,333.32	1.7	2.2
PRIVATE DEV'T CORP. OF THE PHILIPPINES	36.98	206.67	(393.46)**	17.9	N.R.
ASIATRUST DEV'T BANK	7.03	297.54	505.91	2.4	1.4
WEIGHTED AVERAGE				3.3	2.0
GROUP B					
PREMIERE DEV'T BANK	0.87	29.23	132.26	3.0	0.7
LUZON DEV'T BANK	13.15	16.81	96.15	78.2	13.7
NORTHERN MINDANAO DEV'T BANK	10.23	263.22	111.55	3.9	9.2
BANGKO SILANGAN DEV'T BANK	20.20	20.20	88.45	100.0	22.8
BATAAN DEV'T BANK	3.00	3.01	(0.97)	99.7	N.R.
QUEEN CITY DEV'T BANK	1.26	5.00	19.61	25.2	6.4
BANCO DAVAO - DAVAO DEV'T BANK	4.48	4.48	29.29	100.0	15.3
DUMAGUETE CITY DEV'T BANK	11.25	36.28	26.36	31.0	42.7
BANCO CEBUANO - CEBU CITY DEV'T BANK	5.00	5.00	12.18	100.0	41.1
WEIGHTED AVERAGE				18.1	12.9
GROUP C					
SOUTHERN NEGROS DEV'T BANK	10.00	21.31	(4.74)	46.9	N.R.
PALAWAN DEV'T BANK	9.33	9.33	11.69	100.0	79.8
BICOL DEV'T BANK	9.63	9.63	16.08	100.0	59.9
TARLAC DEV'T BANK	2.63	4.33	2.89	60.8	90.9
ISLAND DEV'T BANK	4.55	5.43	7.39	83.8	61.6
WEIGHTED AVERAGE				72.2	68.7

NR Ratio Not Relevant

* Borrowings include: short-term bills payables, long-term loans payables, time deposits-special financing...

** Total amount of allowance for probable losses was deducted from loans receivable.

Table 10. RATIO OF DEPOSITS INCREASE TO OUTSTANDING SECP AND TOTAL BORROWINGS BALANCES, 1990 - 1991

(in Percent)

BANK	INCREASE IN DEPOSIT (in Thousand)	AS PERCENT OF SECP OUTSTANDING BALANCE (12-31-91)	AS PERCENT OF TOTAL OUTSTANDING BORROWINGS (12-31-91)
GROUP A			
PLANTERS DEV'T BANK	512,684	1,738.5	30.3
PRIVATE DEV'T CORP. OF THE PHILIPPINES	---	---	---
ASIATRUST DEV'T BANK	378,563	5,385.0	127.2
AVERAGE		3,561.8	78.8
GROUP B			
PREMIERE DEV'T BANK	174,758	20,087.1	597.9
LUZON DEV'T BANK	74,093	563.4	440.8
NORTHERN MINDANAO DEV'T BANK	45,429	444.1	17.3
BANGKO SILANGAN DEV'T BANK	60,869	301.3	301.3
BATAAN DEV'T BANK	20,058	669.0	666.4
QUEEN CITY DEV'T BANK	7,507	594.0	150.1
BANCO DAVAO-DAVAO DEV'T BANK	25,116	560.6	560.6
DUMAGUETE CITY DEV'T BANK	(236)	NR	NR
BANCO CEBUANO - CEBU CITY DEV'T BANK	24,197	484.0	484.0
AVERAGE		2,962.9	402.3
GROUP C			
SOUTHERN NEGROS DEV'T BANK	12,425	124.2	58.3
PALAWAN DEV'T BANK	2,752	29.5	29.4
BICOL DEV'T BANK	9,712	101.0	101.0
TARLAC DEV'T BANK	885	34.0	20.4
ISLAND DEV'T BANK	2,865	63.0	52.8
AVERAGE		70.3	52.4

NR - Ratio Not Relevant

FILE:TABLEK

Table 11. LOANS VS. DEPOSITS AND ASSETS OF IFIs
(Average, SECP Period 1990 and 1991, in Percent)

BANKS	LOANS / DEPOSITS	LOANS / DEPOSITS*	LOANS / ASSETS
GROUP A			
PLANTERS DEV'T BANK	94.0	146.7	64.0
PRIVATE DEV'T CORP. OF THE PHILIPPINES	---	---	60.3
ASIATRUST BANK	86.0	99.4	61.8
AVERAGE	90.0	123.1	62.0
GROUP B			
PREMIERE DEV'T BANK	78.0	82.2	54.2
LUZON DEV'T BANK	72.0	72.0	55.0
NORTH. MINDANAO DEV'T BANK	266.5	343.2	67.3
BANGKO SILANGAN DEV'T BANK	75.9	75.9	60.0
BATAAN DEV'T BANK	53.0	53.0	40.0
QUEEN CITY DEV'T BANK	65.5	65.5	33.5
BANCO DAVAO - DAVAO DEV'T BANK	92.0	92.0	76.0
DUMAGUETE CITY DEV'T BANK	120.0	130.0	63.0
BANCO CEBUANO - CEBU CITY DEV'T BANK	66.0	66.0	46.5
AVERAGE	98.8	108.9	55.1
GROUP C			
SOUTHERN NEGROS DEV'T BANK	168.5	168.5	60.5
PALAWAN DEV'T BANK	109.0	109.0	69.0
BICOL DEV'T BANK **	291.0	291.0	71.3
TARLAC DEV'T BANK	249.0	249.0	47.4
ISLAND DEV'T BANK	130.5	130.5	35.3
AVERAGE	189.6	189.6	56.7
OVERALL AVERAGE	126.1	140.5	57.9

* Without Time Deposits - Special Financing
** Under new ownership in 1989.

FILE:TABLE11

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Table 12. COMPARATIVE RETURNS ON SHAREHOLDERS' EQUITY OF IFI's BEFORE AND AFTER SECP
(In Percent)

BANKS	Before SECP 1988-1989	After SECP 1990-1991
GROUP A		
PLANTERS DEV'T BANK	17.0	28.8
PRIVATE DEV'T CORP. OF THE PHIL.	9.5	22.4
ASIATRUST BANK	19.2	21.4
AVERAGE	$\boxed{15.2}$	$\boxed{24.2}$
GROUP B		
PREMIERE DEV'T BANK	20.5	18.1
LUZON DEV'T BANK	13.3	21.7
NORTHERN MINDANAO DEV'T BANK	9.0	8.0
BANGKO SILANGAN DEV'T BANK	(12.8)	7.1
BATAAN DEV'T BANK	16.2	19.7
QUEEN CITY DEV'T BANK	18.3	14.9
BANCO DAVAO-DAVAO DEV'T BANK	13.8	21.0
DUMAGUETE CITY DEV'T BANK	11.0	14.6
BANCO CEBUANO-CEBU CITY DEV'T BANK	5.2	9.2
AVERAGE	$\boxed{10.5}$	$\boxed{14.9}$
GROUP C		
SOUTHERN NEGROS DEV'T BANK	6.9	12.5
PALAWAN DEV'T BANK	(0.6)	0.4
BICOL DEV'T BANK	1.0	1.6
TARLAC DEV'T BANK	12.9	14.2
ISLAND DEV'T BANK	2.5	3.1
AVERAGE	$\boxed{4.5}$	$\boxed{6.4}$

FILE.TABLE12

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Table 13. STAGES OF SME DEVELOPMENT

STAGE	MANAGEMENT FACTORS	
	STATUS	FINANCIAL NEED
EXISTENCE	- penetrate market	- start-up working capital
SURVIVAL	- small market base	- how to generate cash to recover cost to breakeven
SUCCESS-DISENGAGEMENT	- established market	- for financial stability
SUCCESS-GROWTH	- growing market - business profitable	- finance expansion
TAKE-OFF	- rapid growth	- finance growth/expansion
RESOURCE MATURITY	- large enterprise	- replacement/rehabilitation of major capital assets

Source: Churchill and Lewis, "The Five Stages of Small Business Growth," Harvard Business Review. Volume 61, Number 3.

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Table 14. DISTRIBUTION OF SMEs BY ANNUAL SALES VOLUME AND NUMBER OF EMPLOYEES

	NUMBER OF BORROWERS			
	A	B	C	TOTAL
A. BY ANNUAL SALES				
UNKNOWN	10	390	55	455
1 - 250,000	13	68	105	186
250,001 - 500,000	11	38	82	131
500,001 - 1,000,000	18	44	65	127
1,000,001 - 2,000,000	37	35	44	116
2,000,001 - 3,000,000	16	22	18	56
3,000,001 - 4,000,000	22	22	6	50
4,000,001 - 5,000,000	17	6	11	34
5,000,001 - 10,000,000	42	10	19	71
10,000,001 - 25,000,000	31	6	11	48
25,000,001 - 50,000,000	5	1	0	6
TOTAL	222	642	416	1,280
MEDIAN ANNUAL SALES	3,522,900	720,000	471,750	900,000
B. BY NUMBER OF EMPLOYEES				
UNKNOWN	1	5	7	13
OWNER-OPERATED	26	142	87	255
1 - 5	56	345	231	632
6 - 10	31	65	55	151
11 - 20	55	59	27	141
21 - 30	22	18	5	45
31 - 40	8	8	1	17
41 - 50	7	0	3	10
51 - 200	16	0	0	16
TOTAL	222	642	416	1,280
MEDIAN NUMBER OF EMPLOYEES	10	2	3	3

Note: Data Does Not Include Loans of Bicol Development Bank and Southern Negros Development Bank with Amount Less Than 10,000 Pesos.

FILE TABLE14

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Table 15. DISTRIBUTION OF SECP LOAN BY PURPOSE AND IFI TYPE

	TRADING	MANUFACTURING	SERVICES	TOTAL
GROUP A				
TOTAL AMOUNT	53,410,000	28,200,000	37,070,000	121,480,000
MEDIAN LOAN SIZE	200,000	225,000	500,000	250,000
GROUP B				
TOTAL AMOUNT	55,635,364	25,737,344	27,539,473	112,076,181
MEDIAN LOAN SIZE	80,000	150,000	194,775	96,000
GROUP C				
TOTAL AMOUNT	50,026,168	12,110,041	23,198,529	85,648,738
MEDIAN LOAN SIZE	50,000	155,100	100,000	70,000
TOTAL IFIs				
TOTAL AMOUNT	159,071,532	66,047,385	87,808,002	319,204,919
MEDIAN LOAN SIZE	80,000	155,100	150,000	100,000

Note: Data Does not Include Loans of Bicol Development Bank and Southern Negros Development With Amounts Less Than 10,000 Pesos.

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Table 16. DISTRIBUTION OF SECP LOAN BY TERM OF LOAN

TERMS OF LOAN	GROUP						TOTAL	
	A		B		C			
	NUMBER	AMOUNT	NUMBER	AMOUNT	NUMBER	AMOUNT	NUMBER	AMOUNT
UNKNOWN	103	34,215,000	17	1,780,000	12	747,500	132	36,742,500
1 - 90 DAYS	0	0	10	1,785,000	24	951,500	34	2,736,500
91 - 180 DAYS	0	0	22	2,569,000	94	5,425,729	116	7,994,729
181 - 270 DAYS	0	0	0	0	1	350,000	1	350,000
271 - 360 DAYS	0	0	413	43,176,886	152	31,343,480	565	74,520,366
1 - 2 YEARS	3	1,550,000	31	8,613,518	65	9,560,248	99	19,723,766
2 - 3 YEARS	115	84,715,000	143	69,637,777	49	15,347,600	307	169,700,377
3 - 4 YEARS	0	0	0	0	12	1,964,281	12	1,964,281
4 - 5 YEARS	1	1,000,000	5	1,474,000	6	2,073,400	12	4,547,400
OVER 5 YEARS	0	0	1	590,000	1	335,000	2	925,000
TOTAL	222	121,480,000	642	129,626,181	416	68,098,738	1,280	319,204,919
MEDIAN LOAN TERM	3 YEARS		1 YEAR		1 YEAR		1 YEAR	

Note: Data Does not Include Loans of Bicol Development Bank and Southern Development Bank With Amounts Less Than 10,000 Pesos.

FILE:HLONTRM

Table 17. DISTRIBUTION OF BORROWERS BY LOAN SIZE BY IFI GROUP

SIZE OF LOAN	A				B				C				
	BORROWERS		LOAN		BORROWERS		LOAN		BORROWERS		LOAN		
	NUMBER	% TO TOTAL*	AMOUNT	% TO TOTAL*	NUMBER	% TO TOTAL*	AMOUNT	% TO TOTAL*	NUMBER	% TO TOTAL*	AMOUNT	% TO TOTAL*	
UNKNOWN	1		0		5		0		7		0		
5,001 - 10,000	0		0		6		59,000		10		85,000		RURAL BANK LOAN SIZE
10,001 - 15,000	0		0		21		312,000		25		346,000		
15,00[illegible] - [illegible],000	0		0		30		588,000		32		617,400		
20,001 - 25,000	1	0%	25,000	0%	21	13%	516,686	1%	21	20%	517,000	2%	
25,001 - 30,000	0		0		28		834,800		21		623,500		PDB LOAN SIZE
30,001 - 35,000	0		0		15		520,000		12		415,900		
35,001 - 40,000	0		0		29		1,152,000		20		797,500		
40,001 - 45,000	0		0		10		444,000		5		223,000		
45,001 - 50,000	28		1,400,000		61		3,045,000		41		2,050,000		
50,001 - 100,000	39		3,730,000		149		12,664,500		81		6,474,960		
100,001 - 200,000	40		7,300,000		104		16,797,897		69		10,838,900		
200,001 - 300,000	18		5,095,000		50		13,614,849		32		8,475,029		
300,001 - 400,000	8		3,140,000		27		10,007,500		14		5,110,781		
400,001 - 500,000	27	72%	13,400,000	28%	28	81%	13,624,444	65%	21	72%	10,320,000	53%	
500,001 - 600,000	4		2,380,000		3		1,788,000		1		600,000		COMMERCIAL BANK LOAN SIZE
600,001 - 700,000	3		2,050,000		4		2,675,000		3		2,006,000		
700,001 - 800,000	5		3,860,000		10		7,605,278		5		3,817,428		
800,001 - 900,000	0		0		2		1,749,450		3		2,668,000		
900,001 - 1,000,000	11		10,870,000		2		2,000,000		2		1,937,340		
1,000,001 - 2,000,000	29		48,200,000		10		14,277,777		10		13,625,000		
2,000,001 - 3,000,000	8		20,030,000		2		4,600,000		4		11,000,000		
3,000,001 - 4,000,000	0	27%	0	72%	1	6%	3,200,000	34%	1	7%	3,100,000	45%	
TOTAL	222	100%	121,480,000	100%	618	100%	112,076,181	100%	440	100%	85,648,738	100%	
MEDIAN LOAN SIZE	250,000				96,000				70,000				

* No. of Borrowers or Loan Amount In The Range Over Total Borrowers or Total Amount
Note: Data Does Not Include Loans of Bicol Development Bank and Southern Negros Development Bank With Amounts Less Than 10,000 Pesos.

Table 18. DISTRIBUTION OF SECP BORROWERS BY SIZE OF ASSET

SIZE OF ASSET	GROUP A		GROUP B		GROUP C		TOTAL	
	NUMBER	LOAN AMOUNT	NUMBER	LOAN AMOUNT	NUMBER	LOAN AMOUNT	NUMBER	LOAN AMOUNT
UNKNOWN	16	13,200,000	136	14,925,900	60	3,800,400	212	31,926,300
1 - 50,000	8	2,100,000	26	4,290,000	45	1,870,000	79	8,260,000
50,001 - 100,000	4	1,100,000	31	3,604,000	65	3,034,000	100	7,738,000
100,001 - 200,000	12	4,300,000	56	7,478,500	48	4,273,840	116	16,052,340
200,001 - 300,000	13	2,300,000	55	5,690,586	39	5,470,381	107	13,460,967
300,001 - 400,000	13	2,790,000	54	7,779,000	22	3,423,400	89	13,992,400
400,001 - 500,000	14	2,250,000	57	6,748,222	17	2,674,400	88	11,672,622
500,001 - 1,000,000	45	12,455,000	87	13,684,400	47	8,802,569	179	34,941,969
1,000,001 - 2,000,000	28	13,815,000	72	21,179,832	39	14,352,500	139	49,347,332
2,000,001 - 3,000,000	33	31,560,000	27	15,483,053	18	6,494,248	78	53,537,301
3,000,001 - 4,000,000	24	22,260,000	13	11,157,221	8	5,353,000	45	38,770,221
4,000,001 - 5,000,000	8	4,850,000	22	13,055,467	6	4,650,000	36	22,555,467
5,000,001 - 10,000,000	4	8,500,000	2	1,300,000	2	3,900,000	8	13,700,000
10,000,001 - 50,000,000	0	0	4	3,250,000	0	0	4	3,250,000
TOTAL	222	121,480,000	642	129,626,181	416	68,098,738	1,280	319,204,919
MEDIAN ASSET SIZE	936,000		500,000		250,000		489,000	

Note: Data Does not Include Loans of Bicol Development Bank and Southern Negros Development Bank With Amounts Less Than 10,000 Pesos.

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Table 19. OVERALL PROFILE OF IFIS BY GROUP, 1991

COMMON SIZE STATEMENT OF CONDITION

LEGEND:

- A = Assets
- L = Liabilities
- S/E = Shareholders' Equity

	GROUP A: A	GROUP A: L + S/E	GROUP B: A	GROUP B: L + S/E	GROUP C: A	GROUP C: L + S/E
	LOANS 58.04%	DEPOSITS 53.9%	LOANS 53.62%	DEPOSITS 61.77%	LOANS 58.68%	DEPOSITS 39.26%
	OTHERS 41.96%	OTHERS 35.1%	OTHERS 46.38%	SECP 4.02%	OTHERS 41.32%	SECP 19.67%
		S/E 10.07%		oth. 13.66%		oth. 13.94%
				S/E 20.55%		S/E 27.13%

KEY RATIOS/FIGURES

KEY RATIOS/FIGURES	GROUP A	GROUP B	GROUP C
TOTAL LOANS/DEPOSITS	105.46%	104.55%	167.32%
INCOME/SHAREHOLDERS' EQUITY	22.39%	13.97%	4.54%
SECP OUTSTANDING/CHANGE IN NET LOANS	2.00%	12.90%	68.70%
SECP OUTSTANDING/CHANGE IN ASSETS	1.15%	6.30%	46.69%
INTEREST INCOME/TOTAL LOANS	22.27%	20.62%	17.41%
COMMERCIAL-INDUSTRIAL LOANS/TOTAL LOANS	59.50%*	39.69%	36.65%**
COMPOUND ANNUAL DEPOSIT GROWTH, 1988-91	41.30%	30.70%	51.20%*
DEPOSITS / ASSETS, (Average 1988-1991)	54.95%*	63.71%	32.32%
LOANS / DEPOSITS, (Average 1988-1991)	121.57%*	116.22%	218.59%
SHAREHOLDERS' EQUITY/ASSETS	10.07	20.55%	27.13%
ESTIMATED SBL (P mm)	43.67	7.67	1.34
MEDIAN SECP LOAN SIZE (P), 1988-92	250,000	96,000	70,000

Group A: * Does not include PDCP

Group C: * Does not include Bicol; ** Does not include Bicol and Island