

**Speech by
President Haruhiko Kuroda
Asian Development Bank**

**at the
Japan Microfinance Symposium**

**10 May 2007
Asian Development Bank Institute
Tokyo, Japan**

I. Introduction

Good morning, and thank you for the opportunity to address you today.

As an institution whose vision is a poverty-free Asia and Pacific region, the Asian Development Bank takes a keen interest in the subject of modern microfinance. ADB considers microfinance to be an important tool for reducing poverty. However, microfinance is still at an early stage of development in the financial world and it has a long way to go in fully meeting the demand for financial services among the poor and low-income households and their microenterprises.

Thus, I am pleased to offer a perspective today on the achievements in modern microfinance, and the challenges that it faces in harnessing its full potential for the benefit of the millions of poor and low-income households who are still underserved and unserved. Let me commend the organizers of the symposium for their initiative to share the knowledge of microfinance widely within Japan.

II. History of Microfinance

Modern microfinance emerged in the form of small-scale micro-credit facilities for poor households in Bangladesh. Professor Muhammad Yunus pioneered these efforts. The impressive results that he and his team achieved led to the establishment of the now well-known Grameen Bank which provides financial services on a national scale. I may mention here that honoring Professor Yunus with the Nobel Peace Prize in 2006 for his pioneering work in the area of microfinance also signifies the importance of microfinance in promoting peace and prosperity around the world.

III. Achievements

Today, modern microfinance can claim many achievements. In my view, the most profound achievement is the launch of an irreversible process of financial democratization. Early successes shattered the deep-rooted myth that poor people have neither willingness nor capability to repay loans. Later on, another myth about the poor was dispelled: that poor people have neither capacity nor willingness to save. Today, the recognition that poor people's demand for financial services goes well beyond microcredit and deposit services is further democratizing financial services.

According to some estimates, over 100 million poor people in the Asia and Pacific region now have access to micro-credit from institutional sources. In addition, millions of poor people have gained better access to deposit facilities and other financial

services of semi-formal or formal institutions. This outreach in itself is an achievement given the massive financial exclusion of the poor that existed about two decades ago. Its significance is even greater because majority of the microfinance clients are poor women – undoubtedly the most vulnerable group in most societies.

The second remarkable achievement of modern microfinance is the impetus it provided to commercialize the provision of financial services to the poor and low-income households. It took more than a decade to generate this momentum. Modern microfinance has shown that there is potential for profit at the bottom of the market pyramid – that institutions can do well while doing good. It is for this reason that we see today an increasingly diverse range of market-oriented institutions in the once barren landscape of formal financial services for the poor.

These institutions include conventional domestic banking institutions and global giants that previously shunned the poor for a variety of reasons. In addition, we see many different types of social investors and private investment funds providing debt and equity investments for retail microfinance institutions in many countries.

These diverse institutions bring a range of innovations to expand the depth and breadth of financial services to the poor. The growth of cellphone-based financial services, other emerging forms of branchless banking, and microinsurance services in countries such as the Philippines and India provide a glimpse of the future of financial services that will benefit the poor.

Today's fertile landscape illustrates not only the achievements of modern microfinance, but also its bright future. However, this does not mean there are no challenges ahead.

IV. Challenges

One of the biggest challenges is to further improve the enabling policy environment. For example, interest rate caps on small loans by banks remain a major issue in a number of countries, including India and the People's Republic of China, where the unserved and underserved market for financial services for the poor is still massive. Many countries also continue to operate highly subsidized government microcredit programs through state-owned financial and non-financial institutions. These programs fail to adequately deliver financial services to the poor and undermine growth in commercial microfinance. Some countries have shown a tendency to introduce interest rate ceilings for microcredit, thus increasing policy risks and making the investment climate less attractive. Hence, while complex, the issues related to policy environment must be addressed.

The second biggest challenge is building adequate retail capacity to provide a broad range of services in demand among the poor. This is particularly true in countries such as India and the People's Republic of China where the unserved and underserved markets continue to be still very large. In China, massive efforts are necessary to

establish retail institutions, reform the existing rural credit cooperatives and build the capacity of domestic banks to become dynamic players in the microfinance industry. In India, the capacity of poorly performing self-help-groups and many other retail institutions which continue to struggle to achieve efficiency and scale needs to be developed systematically. The current retail capacity limitations in many states of India are putting tremendous pressure on a small group of core microfinance institutions to overstretch geographically. Many relatively smaller countries also have to address the issue of inadequate retail capacity.

Another challenge is the need for microfinance institutions to significantly reduce the transaction costs of providing a broad range of services. Some poor people are unable to access formal financial services due to high costs. If the industry is to deepen its services to reach the poorer potential clients and those in remote locations that it has not been able to reach on a significant scale to-date, transaction cost reduction is essential. Transaction costs result in a wedge between the prices clients pay and the returns that service providers receive. Reducing transaction costs will therefore have a positive impact on both the supply and the demand for services, creating a win-win situation for all. My prediction is that the next revolution in modern microfinance will be brought about by a series of process innovations that will significantly reduce transaction costs and significantly expand the currently limited scope of services.

V. Conclusion

Ladies and gentlemen, as the region's development partner, ADB has been a long-standing supporter of the microfinance industry as a means to pursue inclusive, socially sustainable economic development in Asia and the Pacific. As the industry has changed, so has our focus – from support for narrowly defined microcredit programs to support for the development of comprehensive financial systems for the poor. We have worked with a number of our developing member countries to build the policy environment, financial infrastructure, viable institutions, and other elements necessary for the growth of the industry. Microfinance provides a great opportunity to ensure that the benefits of accelerated economic growth are shared by the poor, thus helping them to escape from poverty.

Let me close by reiterating ADB's strong commitment to build inclusive financial systems in the region, and wishing you all the best in your deliberations.

Thank you.