

**MICROFINANCE INDUSTRIES IN EMERGING  
ECONOMIES: A COMPARATIVE INVESTIGATION INTO  
EFFECTIVENESS AS A TOOL FOR POVERTY  
ALLEVIATION**

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Key Words: microfinance, poverty alleviation, rural finance, regulatory framework, emerging economies, Philippines, Cambodia

JEL Classification(s): G2, O1, O2

**Abstract**

*The inspiring growth of the microfinance industry, not least in Asia, has been seen to emerge as a major force supporting poverty alleviation. This paper analyzes the microfinance industry in two developing Asian countries, from the viewpoint that problems creating the gap between supply and demand in providing the necessary sources of finance impeded the establishment of an effective microfinance framework in the two countries, and attempts to uncover and explain the underlying reasons. The comparative analysis is based on several elements which are economic and poverty indicators as well as market size, existence of non-bank financial institutions providing microfinance services and products, supervision of microfinance institutions by a financial regulators, experience with transformation of microfinance institutions into regulated non-bank financial institutions (NBFIs), maturity of a supervisor in performing its role*

*and innovation and diversification in products. The paper concluded that the microfinance industry in both countries, facing similar problems, could be made more effective by creating specialized microfinance channels, inducing greater governmental commitment, and making necessary changes to the regulatory and supervisory framework.*

## **INTRODUCTION**

Microfinance is an emerging important financial sub-sector in transition countries. This sub-sector is largely dominated by banking systems that play a limited role in financial intermediation. In most cases, these banks cater limited number of clients, and mainly provide short-term credit. Hence access to finance has been identified by most developing countries, where Cambodia and Philippines are no exception, as one of the main impediments to private and public sector development.

This paper attempts to give a comparative analysis of microfinance sector in Cambodia and Philippines. It focuses on exploring the Microfinance Regulatory Framework of these countries, their current situation and the policies adopted. The comparative analysis is based on several elements such as: 1) Economic and Poverty indicators as well as market size, 2) Existence of non-bank financial institutions providing microfinance services and products, 3) Supervision of microfinance institutions by a financial regulator, 4) Experience with transformation of microfinance institutions into regulated non-bank financial institutions (NBFIs), 5) Maturity of a supervisor in performing its role and 6) Innovation and diversification in products.

Hossain (2004) describes microfinance as “the practice of offering small, collateral free loans to members of cooperatives who otherwise would not have access to the capital necessary to begin a small business or other income generating activities.” This view is too narrow, since it not only excludes such services as saving accounts and insurances (Robinson, 2001), but also ignores

the possibility of collateral demanding MFIs. Although it is true that many MFIs do not take collateral, especially if they are focusing on the poorest, who normally do not possess any collateral; several MFIs in fact do require some form of collateral. According to Ali (2011), the collateral in microfinance works based on the concept of joint liability where the risk is getting shared among members of small groups and thus, if any member defaults the group is responsible for repayment.

Roth and Steinwand (2004) gave a more general definition, and described 'microfinance' as "the provision of banking and financial services, primarily lending and savings products, to economically active poor clients who are generally unable to access services offered by formal financial institutions". A number of Alternative Financial Institutions (AFIs), including state-owned development banks, postal, agricultural, and savings banks, as well as smaller entities like savings and loan cooperatives, provide a mix of basic financial services to their clients (Littlefield and Rosenberg, 2004), all of which can be described as microfinance.

Microfinance rates high on the public agenda after the UN Year of Microcredit of 2005 and the awarding of the Nobel Peace Prize to Mohammad Yunus and the Grameen Bank in 2006. There is much literature to suggest that microfinance is an effective tool for fighting poverty. Development of microfinance can be seen as a tool to fight against poverty, especially in a country where micro and small enterprises play a substantial role in economic life (Baradei and Mahdy, 2006) and eradicate poverty (Al-Mamun et.al, 2012, Noruwa and Emeka, 2012). Woodworth and Woller (1999) define the term microfinance as "arguably the most innovative strategy to address the problems of global poverty". Further, microfinance activities have several positive environmental effects when they use sustainable inputs and follow energy efficient and environment friendly methods of production (Archer and Jones-Christensen, 2011).

The success of microfinance has challenged commonly held assumptions regarding lending to the poor, demonstrating that it is indeed possible to collect loans and cover the costs associated with

lending to poor clients. Many established microfinance institutions have achieved long-term sustainability and extensive outreach. Indeed, by the end of 2003, microcredit institutions throughout the world had reached a total of 80.9 million clients, according to the Microcredit Summit Campaign. Of these, 54.8 million microfinance clients were within the poorest economic strata when they took their first loan (Harris, 2004).

Nevertheless, microfinance still reaches only a fraction of the world's poor (Robinson, 2001, Christen et al. 2004). Helms (2006) and the Consultative Group to Assist the Poor (C-GAP, 2004 and C-GAP, 2006) consider the lack of strong MFIs to be a major constraint in the further development of the microfinance industry, and CSFI (2008) identifies governance as a major obstacle to the growth of Micro Finance Institutions (MFIs). Studies by Asian Development Bank (2012) indicate that combining access to financial services with livelihood programs, food aid, skills training and asset transfers that help people in extreme move into sustainable livelihoods through commercial microfinance.

### **Research Question**

The dynamic growth of the microfinance industry has been promoted not only by market forces but also by conscious actions of National Governments, Non-Governmental Organizations (NGOs) and the donors who view microfinance as an effective tool for eradicating poverty (Shastri, 2009). Considering that the shape of existing financial systems and the degree of institutional development quite differ from country to country, questions arise: What are the current impediments in the microfinance sector in Cambodia and Philippines that caused a huge gap between the supply and demand side in providing finance and derive policies to develop a well-established microfinance framework in these countries? This paper tries to answer the relevant sub-questions such as: What is the structure of microfinance market and how it has developed in Cambodia and Philippines and what are the development indicators? Are there laws regulating microfinance in

these two countries and what are their implications on the development of MFIs? What are the successful practices in this regard? What are the main factors that can lead us to a more effective microfinance sector?

The importance and justification of this research strives from several reasons such as the ability of the microfinance sector to act as stimulating vehicle to the developing economies and the need to capitalize on opportunities in this sector.

### **GENERAL INFORMATION ON THE INDUSTRY**

Microfinance started in the Philippines twenty years ago when the market appeared as a simple credit and savings market, with MFIs staffed with socially conscious individuals. The microfinance market in the Philippines offers savings, housing, leasing, fixed asset, micro insurance and other products and services to the working poor. The drastic change the market was due to the number of transforming MFIs and the entrance of new commercial players. On the other hand, since the nineties, microfinance in Cambodia was mostly led by NGOs established by international organizations. NGOs activities in microfinance (MF) were mainly focused on credits and some saving services.

There are currently three categories of MFIs in Cambodia supervised by National Bank: Deposit-Taking MFIs, Licensed MFIs and Registered MFIs. There are also unregistered NGOs that offer microcredit on a small scale (less than 1000 active clients), in addition to MF programs offered by banks. In contrast to this, MFIs in Philippines are categorized as: banks, cooperatives and NGOs. Banks are categorized as universal, commercial, thrift, rural and specialized banks. Around 224 banks – largely dominated by rural banks – offer micro-loans to almost 900,000 active clients with an outstanding portfolio of around \$128 million, in addition to a total of \$38 million of deposits as of September 2007. Yet, 36.5 percent of the municipalities – mainly rural low-income areas – do not have bank offices. Around 500 NGOs and 4,500 Savings and Credit Cooperatives (SCCs) offer MF services in the Philippines,

of which approximately 20 NGOs and 300 SCCs have a sustainable number of clients.

The prevailing microfinance products in the Philippines are micro-credit (business, agricultural and housing), micro-savings, remittance and micro insurance. Micro-savings are considered – not only a service for the clients – but also a cheap source of funds for the MFIs. Micro-savings are mostly offered by rural banks and the interest rate charged on deposits is relatively low (1.5% – 2%). In addition, the Philippines is recognized as a leader of successful mobile-banking services. Remittances are among the most widespread services offered due to the successful implementation of mobile-banking (\$16 billion per year). MFIs also act as agents to insurance companies by offering micro-insurance products.

However, in the case of Cambodia, the prevailing products are microloans and micro-savings. Micro-savings are offered by banks (namely ACLEDA Bank), while MFIs offer compulsory savings. MFIs lack the capacity to offer micro-saving on a large scale, namely lack of institutional systems and large network of branches accessible by the public, and of financial resources which offer credit and provision for savings. In addition, the public confidence in the formal financial system has not yet been restored due to their bad experience with the collapse of the formal financial sector in the early nineties.

Philippines has a comparatively wide range of formal, semi-formal and informal institutions providing microfinance services to the urban and rural poor and underserved sectors of the economy (Gallardo, 2001).

### **Policy and Regulatory Framework**

In Philippines, Bangko Sentral ng Pilipinas (BSP) which is the central bank act as the regulator and supervisor of MF services offered by banks, as well as micro-savings offered by NGOs beyond compulsory savings (i.e. beyond the compensating balance). While in Cambodia, three entities, namely The Ministry of Economy and Finance (MEF), the National Bank of Cambodia (NBC) and the Cambodian Microfinance Association (CMA),

implemented the Financial Sector Development Plan (FSDP) 2001-2010 with particular focus on expanding the financial services to the rural people in order to help them improve their living conditions.

The regulatory framework of MFIs in Cambodia allows for the gradual transformation of NGOs into full-fledged banks depending on their operations and ability to comply with the regulations and supervision requirements. But in Philippines, BSP is committed towards the development of a microfinance-friendly policy and regulatory environment. To that end, BSP conducts periodic meetings with industry stakeholders to discuss industry trends, issues and needs. In addition, BSP encourages banks to launch MF programs in under-served areas, and offers incentives to commercial banks, which provide wholesale finance to rural banks.

### **Transformation**

The banking law and MF-related decrees allow for the transformation of NGOs into formal financial institutions as well as the gradual shift from one tier of institutions to a higher tier. The reasons for transformation as stated by stakeholders in Cambodia were access to commercial capital, product diversification, expansion of outreach and achievement of self-sustainability and profitability. The transformation requirements, in addition to the regulatory ones, are building the capacity of the staff, improving the internal control and risk management systems, enhancing MIS, finding shareholders with common vision, and addressing the ownership issue.

On the other hand, in Philippines, the prominent reasons for transformation are diversification of products and services, access to different sources of financing, mobilization of savings from the public, affordability of the capital requirement and the ease of compliance with the regulations and reporting requirements.

**Table 1- Statistical Comparison of Cambodia and Philippines**

Criteria	Cambodia	Philippines
Country context	<p>The population of Cambodia is 14 million inhabitants, of which 77.7 percent live below \$2 per day, and 11 percent are unemployed.</p> <p>Number of active clients exceeds 800,000 (as of December 31, 2008), versus more than 560,000 in December 2006.</p> <p>The number of served clients has been steadily growing since the enactment of the microfinance regulations, which gives a good opportunity to learn how the implementation of regulations can grow the microfinance market.</p>	<p>The Philippines' population is 84.6 million and economic / poverty indicators are comparable with that of Cambodia.</p> <p>Number of active microfinance clients in the Philippines are 2,025,402. Just a few years ago, it had only one million active clients.</p>

<p>Existence of several types of formal financial institutions providing microfinance services and products</p>	<p>The MFIs in Cambodia are divided into (3) tiers:</p> <ul style="list-style-type: none"> <li>- Commercial Banks</li> <li>- Specialized Banks - Licensed MFIs (savings of \$25,000 or 1,000 depositors, outstanding loan portfolio of \$250,000 or 10,000 borrowers)</li> <li>- MFIs (NGOs or companies) - Registered MFIs (savings of \$250,000 or 100 depositors, outstanding portfolio of \$25,000 or more)</li> <li>- Un-registered MFIs (less than above ceilings)</li> </ul>	<p>MFIs in the Philippines vary between thrift and rural banks, credit unions, credit NGOs, and informal suppliers (traders, money lenders, etc.), which will explore various types of MFIs with a diverse product range.</p>
<p>Supervision of microfinance institutions by financial regulator</p> <p>Maturity of the supervisor in performing its role</p>	<p>Microfinance institutions are supervised and regulated by the National Bank of Cambodia (Central Bank), under the provisions of the Banking Law of 1999 and a set of microfinance regulations issued since 2000. A special unit of the Supervision Department is responsible for off-site and on-site supervision of MFIs.</p> <p>The law on banks and financial institutions covers both banks and NGOs.</p> <p>Larger MFIs must be licensed by the Central Bank, smaller ones are registered.</p> <p>Licensed MFIs must comply with prudential ratios:</p> <ul style="list-style-type: none"> <li>- Minimum Capital (\$62,000)</li> <li>- CAR (Capital at Risk) 20%</li> <li>- Liquidity 25%</li> <li>- Risk concentration</li> <li>- Loan classification and provisions</li> <li>- Regular reporting for off-site supervision and occasional on-site examinations.</li> </ul> <p>Registered MFIs submitted to less demanding regulations and reporting.</p>	<p>The Philippines' Central Bank (BSP) is the supervisory authority of the microfinance banks, as per Circular No. 272 since 2001. Other types of MFIs report to the Central Bank, although not under its direct supervision.</p> <p>BSP has been supervising microfinance operations for almost seven years, which provides a unique opportunity to study a regulator with recent and rich experience as well as lessons learned regarding the microfinance unit establishment, supervision of the microfinance sector, and its unique features.</p>

<p>Experience with transformation of microfinance institutions into regulated formal financial institutions</p>	<p>ACLEDA, the Association of Local Economic Development Agencies, was the first NGO specialized in microfinance. Registered in 1992, it became a specialized microfinance bank in 2000 and a full commercial bank in 2003. Ten MFIs are now licensed by the Central Bank, nine former NGOs and one originally set up as a private company.</p>	<p>Microfinance started in the Philippines twenty years ago; a simple credit and savings market, with MFIs staffed mainly with socially-conscious individuals. The drastic change the market experienced was due to the number of transforming MFIs and entrance of new commercial players.</p> <p>Moreover, competition has sparked innovation, improved client service, raised industry standards, and increased access to commercial sources of funds.</p> <p>MFIs are increasingly developing aggressive growth plans to achieve scale, boosting their profitability by innovating low cost distribution channels, expanding savings services, and developing new and improved loan instruments.</p> <p>An example of the progress being achieved is the recent first mobile microfinance bank of the Philippines being established as well as the credit information act being signed into law for financial institutions.</p>
<p>Diversification in products</p>	<p>Credit, savings, microinsurance (health)</p>	<p>The microfinance market in the Philippines is one of the world's most sophisticated microfinance markets offering savings, housing, leasing, fixed asset, micro insurance and other products and services to the working poor.</p>

Source: Prepared by Researcher based on Human Development Report UNDP/  
World Development Indicators database 2008/ The World fact book

**Table 2- Comparative Review for the Microfinance Market in Philippines and Cambodia**

Criteria	Philippines	Cambodia
Information Last Updated	2008	2008
Human Poverty Rank	54	87
Population (Millions)	90.35	14.7
Population below \$1 per day (%)	14.8 (2005)	34.1 (2005)
Population below \$2 per day (%)	43 (2007)	78 (2007)
Population living below the national poverty line (%)	31 (2007)	5 (2007)
GNI per capita (US\$)	3900	1820
GDP per capita (US\$)	1886.1	602.7
Total Unemployment (% of labor force)	7.4% [2008]	3.5 [2008]
Employment in Agriculture (% of total employment)	35%	75%
Exchange rate (as of October 14, 2008 - XE.com)	1 USD : 47.596 PHP	1 USD : 4180.95 Riel
Number of active clients (only MFIs reporting to Mix Market as of December 2007)	2,025,402	802,329
Sources of Microfinance	Thrift and rural banks	Commercial and

and Regulators	<p>(Central Bank of the Philippines)</p> <p>Credit unions (Cooperative Development Authority)</p> <p>Credit NGOs (Reporting to Central Bank)</p> <p>Informal suppliers (traders, money lenders, RoSCAs and ASCAs)</p>	<p>specialized banks (National Bank of Cambodia)</p> <p>Microfinance Institutions (National Bank of Cambodia)</p> <p>NGOs</p>
NGO microfinance provider formalization or transformation issues	Existing microfinance organizations have legal authority to apply to become microfinance thrifts or rural banks, provided capitalization requirements are met with and the geographical area is not fully served by a rural bank.	The National Bank of Cambodia issued a sub-decree to license large deposit-taking institutions and to register the smaller ones.
Applicable Laws	<p>Rural Banks Act 1992</p> <p>Law on Corporations</p> <p>Thrift Banks Act Law on Corporations See also Circular Nos. 272 (Jan 2001), 273 (Feb 2001), 282 (April 2001)</p> <p>Cooperatives Code (Act No.6939) 1990</p> <p>Law on Trusts and Non-Profit Foundations</p>	<p>Laws on banking and financial institutions.</p> <p>A 'Prakas' (i.e. government decree), on microfinance regulation was enacted in 2000, and implemented by the National Bank of Cambodia</p>

Source: Prepared by Researcher based on Human Development Report UNDP/ World Development Indicators database 2008/ The World fact book

## **Analysis of findings**

### **1. National Framework for Poverty Alleviation**

In both the Philippines and Cambodia, the MF regulatory framework stemmed from a national strategy aiming at poverty alleviation using MF as one of the main tools for improving the living conditions of the poor. The existence of a national framework for poverty alleviation comprehended by all stakeholders – both regulators and practitioners – led to the development of rather inclusive regulations of MF. In addition, the national framework in both countries was designed to increase access of MF services to the poor through different channels and types of institutions. It is noted that the national reform plan in Cambodia had a specified timeframe and clear objectives to monitor the impact of MFIs on poverty reduction in the country.

### **2. Regulatory and Supervisory Framework**

In both countries, the MF regulations had a positive impact on the expansion of outreach to the poor, product diversification, access to commercial sources of funds, and improved operations and performance of MFIs. In both countries, an open dialogue was maintained between the regulator and the MFIs, which helped improving the policy and regulatory environment governing the MFIs. Furthermore, the regulators were quite flexible in the first-time implementation phase of the regulations, allowing time for the MFIs to upgrade their systems to be in full compliance with the regulatory requirements. The flexibility was maintained afterwards in terms of continually enhancing the regulatory framework, listening, and responding to the industry needs.

3. In Cambodia, the approval of new products is done on MFI-basis; therefore, each MFI receives a license for offering a new product. While in the Philippines the approval of a new product is done on the industry level, and thus all MFIs can offer it.

4. Although the MF-related regulations in both countries are considered to be good practices of regulations, there were some shortcomings discovered in each country. In the Philippines, there is a loan ceiling for microcredit programs, which is considered to be relatively low. In addition, the definition of microfinance in the banking law is limited to income generation loans only, which prevents the introduction of a diversified range of loans. In Cambodia, NBC's approval of the CEO of an MFI is found to be unnecessary as it creates the risk of nepotism in hiring CEOs. In addition, the influential shareholder rule – which requires the shareholder owning 20 percent of the capital to be the one primarily in charge of increasing the capital in case the capital requirement is increased by the regulator - is considered to be a disincentive for equity investors. Furthermore, the absence of credit bureaus in both countries increases the risk of over-indebtedness of clients.

In this regard, the key characteristics of the regulatory framework in both countries are:

- The regulator is flexible, knowledgeable of MF good practices, and acts in partnership with MFIs;
- Regular and efficient communication between the MFIs and the regulator is maintained to address the industry needs;
- The advocacy effort exerted by the practitioners is a key reason for introducing and amending regulations;
- The prudential norms of the industry were included in rules rather than laws to ensure flexibility and easiness of amendment as needed;
- The rules and regulations are mostly in line with international best practices of MF and aimed at standardizing the performance of MFIs
- The articles in the rules and regulations are attractive to investors and do not include too restrictive clauses that would be difficult to implement
- The regulator designs incentives for MFIs to open in underserved areas and ensures a level playing field among

MFIs to create healthy competition leading to less expensive and more diversified products meeting clients' needs.

5. In both countries, the reporting requirements are focused on the financial performance of the MFIs and are mostly adapted to good practices of MF. As for the on-site inspection, MFIs are notified several days prior to the inspection date in order to have all documents and staff needed ready. In both countries, draft inspection reports are submitted to the MFIs for review and comment before finalization of the report. In addition, recommendation or warning letters are sent to the MFIs for corrective actions following the inspection. In case of serious findings during the inspection, a follow-up visit is conducted without prior notice to verify whether remedy actions are implemented. Fines are charged for late submission of reports. Repeated non-compliance with the regulations or warnings issued by the regulator result in license revocation.

In this regard, some of the key characteristics of the supervisory framework in both countries are:

- The off-site supervision is focused on the financial report and performance of MFIs;
- The reports frequency, quantity and content differ based on the services offered (voluntary savings versus credit only / compulsory savings);
- The on-site inspection is conducted on yearly basis with a short notice on the date of the inspection and examines not only the financial performance of the MFIs but also covers the existing systems, manuals, branch performance and visits to clients;
- The MFIs receive a copy of the draft inspection report and are allowed to respond to comments/findings;
- Warning / Follow up letters/emails are sent to the MFIs after the completion of the inspection with recommendation for corrective actions occasionally. In some cases,

inspections are conducted with no prior notification to ensure corrective actions are implemented by MFIs.

- MFIs should receive a copy of the final inspection reports
- The sanctions are limited to fines of various amounts for under-compliance or delays in and/or incomplete submission of reports; the revocation of the license is kept as a sanction for serious cases of fraud/ material non-compliance with regulations.
- Staff at the regulatory authority received extensive and lengthy training on inspection, which made them very professional and competent.

#### **6. Microfinance Unit**

At the Central Bank of the Philippines, there is not specialized unit for supervision and licensing of MFIs, but rather a functional model is adopted. Yet, all MF activities in the different departments are reported to a MF Committee chaired by the deputy governor. The functional model requires very good communication among the different departments and clear lines of authority to ensure the appropriate flow of information. In addition, all staff employed in the unit should be well-trained in MF in order to fulfill the supervisory responsibilities. In each of the functional departments, three staff members are appointed to carry out the responsibilities of the department. The inspection department's staff conducts the MFIs' inspection on rotational basis.

While at the National Bank of Cambodia, a different model is adopted. There is a specialized unit for MF established at NBC in charge of licensing and supervising MFIs. This model is characterized by the high speed and good communication whether it is responding efficiently to external needs and requests or internal flow of information based on the industry performance, lessons learned through implementation of supervisory responsibilities, and/or transfer of know-how among the staff. The MF unit consists of three members in addition to the management, each one of them is assigned one category of MFIs.

It was noted that the model of unit – whether single unit or functional unit – should ensure the following:

- Good communication and flow of information,
- Clear lines of authority,
- Transparent criteria for decision making to avoid risk of corruption,
- Continuous exchange of lessons learned and know-how among staff,
- Good knowledge of MF special nature and how different it is from other financial instruments,
- Existence of one focal point (person or committee) which ensures efficient internal and external communication, and
- Quick and efficient response to industry needs.

#### **7. Transformation**

Transformation models were different in both countries. In the Philippines, practices reflect a partial transformation where an NGO establishes a bank and transforms some of the branches of the bank based on the degree of compliance of the branch with the banking regulations. In Cambodia, a phased/tiered approach of transformation is applied where the legal status of the MFI is determined by its outreach level.

It is noted that in both countries the reason for transforming is to gain access to commercial capital, product diversification, and expansion of outreach. MFIs had to address several challenges in order to undergo the transformation process including staff capacity building, improvement of existing systems, enhancement of MIS and resolving the NGO ownership issue. It was noticed that the MFIs applying best practices of MF were faster and more capable of undergoing a rather smooth transformation process. In addition, the transformation process was possible due to the willingness of the regulator to supervise and regulate transforming NGOs, which were compliant with the regulations requirements.

It is noted that existing MFIs applying good practices were the first to undergo the transformation process. The transformation model differed in both countries (NGO owning shares in a formal

financial institution versus NGO changing its legal structure), yet the common factor was the willingness and endorsement of the regulator to the transformation process. The transformation cost and timeframe differed from one MFI to the other depending on its governance, internal systems especially MIS, application of good practices and capacity building of staff. In general, in countries where the NGOs received donors' grants, there was a consensus by the donors to transfer the grants to the transformed MFI. It was also noted that the regulator allowed sufficient time and showed needed flexibility regarding the transformation process in order to allow smooth and gradual approaches (e.g. allowing time for NGOs to upgrade and improve their systems to be fully compliant, a starting minimum level of compliance was required by the transforming NGO).

### **Conclusions & Recommendations**

The existence of specialized MFIs such as banks, microfinance banks, and commercial credit-only institutions add greatly to the availability and outreach of a broad range of services and such microfinance institutions would improve outreach and catalyze microcredit markets.

When regulatory change allows for the creation of non-bank commercial MFIs, successful NGOs may begin to consider revising their legal status to transform into formal financial institutions. This transformation option could appeal to NGO-MFIs that wish to offer a greater variety of microfinance services, thereby maximizing their outreach. Such transformations could significantly contribute to increased outreach and competition in the microfinance market.

The present situation in the microfinance industry in both the countries could be improved by focusing on the development of a legal and institutional framework overseeing the microfinance activity, integrating different stakeholders in the development process and giving donors guidance in their efforts to move the microfinance sector forward into a more dynamic phase of its development. To achieve its full potential, microfinance must

become a fully integrated part of a developing country's mainstream financial system.

The microfinance sector in these countries would greatly benefit from the implementation of a new policy framework that would grant legal recognition and legitimacy to microfinance institutions and institute a regulatory and supervisory framework under the authority of a "financial ministry."

The ideal scenario would be to appoint "financial ministry" as MFIs' supervisor and regulator, overseeing the activity and champion for the cause of microfinance. But the ministry may not be ready to assume these responsibilities, for a number of reasons: It needs more information about the microfinance sector, views it as marginal compared to the banking sector, and considers some of its activities (e.g., group loans) as social or charitable rather than financial. In this regards, the study concludes and recommends that it would be preferable to adopt a gradual approach for the implementation of the new policy framework for microfinance in these countries.

Financial ministries might have their own reservations about assuming that responsibility. These could be overcome if donor agencies were prepared to offer a package of financial and technical assistance to give support to set up a specialized MFI Unit within their organization, and if it was understood that the policy framework would be implemented gradually, so that both the supervisor and the MFIs have time to adjust.

This study has a number of limitations; first, data collection related to the topic was fragmented and collected from various unpublished reports from international sources such as web sites and reports issued by donors. Second, due to time constraint, interviews with related stakeholders operating in the microfinance could not be arranged which could be helpful to determine the level of success or otherwise of the industry.

In this paper, microfinance has been investigated from legislative perspectives, based on good practices in Philippines and Cambodia. Further analytical research done on a bigger scale with

large sample size could shed light on how microfinance activities affect the average living standard of poor people.

For future researchers in the field of financial sustainability, it might be useful to investigate the sustainability of MFIs from the perspective of the organization that receives support. It would have been interesting to investigate the role of the donors' agencies in their sustainability.

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