2 Progress toward Microfinance Commercialization

This chapter focuses on the progress of Indonesian MFIs toward commercialization as a whole and by institutional type. A historical overview of the establishment and development of the various types of MFIs in Indonesia is provided and their current collective and individual performance is summarized in terms of outreach, financial self-sufficiency, and efficiency.

HISTORICAL OVERVIEW

The Indonesian microfinance industry is exceptionally old and is one of the most commercialized in the world in terms of its provision of sustainable microfinance with large scale and sustainability of outreach. The industry is very heterogeneous but the biggest players are predominantly formal (regulated by BI) and savings based. One of the best known, because of its status as the largest MFI in the world, is the Bank Rakyat Indonesia's (BRI) Micro Business Division (referred to as BRI Units). Also important is Bank Dagang Bali (BDB) as one of the first, if not the first commercial bank established primarily to serve low-income and poor clients.

The BRI Units were established in the early 1970s as outlets under the *Bimbingan Massal* (BIMAS, or Mass Guidance) program of directed credit for rice intensification. The BIMAS credit program had essentially accomplished its goal of making Indonesia self-sufficient in rice production in the mid-1970s. By the early 1980s, however, the program was becoming increasingly unsustainable, due to subsidized interest rates, poor loan repayment, and employee incentives directed toward disbursing credit rather than generating profits.

In 1983, declining budgetary revenues resulting from lower oil prices, together with increasing expenses under BIMAS due to deteriorating loan collections, led the Indonesian Government to radically transform the BRI Units–with technical support from the World Bank, United States Agency for International Development (USAID), and Harvard Institute for International Development (HIID)–into a self-sustainable microfinance operation within BRI. With a relatively small initial subsidy in 1983, and the launching of a simple, but appropriately designed and priced microcredit product in 1984 called the *Kupedes* (general rural credit), the Unit system became profitable within just 18 months. Three years later, deposit services, including the extremely successful *Simpedes* savings product, were added to the BRI Units' microfinance product mix. Although BRI remains a 100% state-owned limited liability company (state bank), its Unit system operates in a commercial manner with a financially self-sufficient network of 4,063 outlets that served around 27.0 million savers and 2.8 million borrowers at end-2001.[43]

BDB is one of the oldest private commercial banks offering microfinance on a commercial basis in the world. It was established in 1970 by a husband and wife team of professional moneylenders to serve better the Balinese community of local traders and produce merchants.[44] Although BDB is a relatively small bank, it is important because it has remained dedicated to microfinance and small business lending. While commercially structured, the bank has retained a social objective over the last 30 years by opting to make only moderate profit margins in order to concentrate on prudently increasing its depth of outreach (i.e., reaching lower-income clients).

Numerous other commercially-oriented MFIs exist and many of them have a long history of operation. For example, some of the 4,500 village-owned village credit organizations (*Badan Kredit Desas*, or BKDs) have been providing microfinance at the local level, particularly in rural Java, for more than 100 years. Only slightly younger, the system of more than 2,500 locally-owned BPRs also has a long history of providing commercial microfinance. Indonesian NGOs, unlike their counterparts in most other countries, play a relatively minor role in the microfinance industry, partly because of their repression under the Soeharto regime and because most of them have concentrated on social rather than financial intermediation.

Government and/or donor-supported microcredit or microfinance programs have had a mixed record in supporting the commercialization of microfinance. Since the 1970s, expanding access of the poor to credit has been a major part of the Government's strategy to promote equitable growth and reduce poverty.[45] While a few interventions have facilitated the commercialization of microfinance by following the new "financial systems approach," many microcredit programs based on the old paradigm of subsidized, directed credit have been harmful to the expansion of commercial microfinance.

The most positive interventions have focused on institutional strengthening and/or savings mobilization as a useful service for the poor and a large and stable source of funds for MFIs with clear legal status. A few particularly market-friendly government and/or donor-sponsored programs have been, in chronological order, the Rural Income Generation Project (RIGP) supported by the Indonesian Government, ADB, and International Fund for Agricultural Development, and implemented by the Ministry of Agriculture and BRI, as part of the *Proyek Peningkatan Pendapatan Petani-Nelayan Kecil* (P4K) program, in various forms since 1979; the transformation begun in 1983 of the BRI Units into a self-sustainable microfinance operation within BRI with technical support from the World Bank, USAID, and HIID; the Microcredit Project implemented by BI with ADB-funded technical assistance since 1996; and the Promotion of Small Financial Institutions (ProFI) project also implemented by BI but with technical assistance support from GTZ from 1999.

Examples of subsidized, directed credit programs that inhibit commercial microlending are unfortunately plentiful. Perhaps the largest of a number of high-cost, unsustainable microcredit programs was the 1993 Presidential Instruction on Backward Villages (*Inpres Desa Tertinggal*, or IDT) program coordinated by the National Development Planning Agency, BAPPENAS. Until it ended in 1997, the IDT program injected a total of about Rp1.3 trillion (more than $550 million) into infrastructure development and poverty reduction, including substantial funds for unsustainable microcredit components. In addition, the Family Welfare Income Generation Project (*Usaha Peningkatan Pendapatan Keluarga Sejahtera*, or UPPKS) disbursed around Rp1.4 trillion (approximately $200 million) in highly concessional loans, with 6% effective annual interest rates and less than a 20% cumulative repayment rate.

There was a move by the Government to give up the subsidized credit approach as ineffectual and wasteful in 1990, when 30 of the 34 major programs were scrapped.[46] However, experiences like the above show that government policy has been highly inconsistent. Worse, it appears that policy reversion to the old paradigm is an increasing danger in light of recent decentralization of government budgets and the regional drive to use a portion of those funds to create new MFIs; increase fund injections, such as the fuel subsidy program (the Cash Subsidy for Gasoline Program; BMM [*Program Dana Tunai Subsidi Bantuan Bakar Minyak*]); and use cheap credit as a tool to attract votes in the 2004 elections.

Unlike other commercial microfinance industries, an individual lending approach has been more prevalent than group lending in Indonesia. The success enjoyed by BRI, as an early market leader, with its individual loan product *Kupedes*, influenced later microcredit product development by other MFIs. The

traditional group lending methodologies usually employed by microfinance NGOs had little relative influence on the market, in line with the unusually small role NGOs have played in Indonesia's microfinance industry. The long-standing focus on individual lending has kept attention on project viability, income streams, and debt capacities, but these have not come at the cost of microfinance service provision to lower-income clientele (e.g., individual lending is employed by most MFIs, serving a wide range of clients including the very poor).

EVIDENCE OF UNMET DEMAND

Demand for microfinance varies between and within regions. Existing demand is arguably only partly met by MFIs and there exists an opportunity to expand outreach. Despite the remarkable outreach that the BRI Units and other highly commercial MFIs have achieved in extending savings and credit services throughout Indonesia, most Indonesians still do not make use of formal banking services. Evidence supporting this is provided by two recent surveys.

As part of an ADB-supported project preparatory technical assistance concluded in 2003, participatory rural appraisals were carried out in 10 selected villages across 5 provinces to assess the demand for financial services. The methodology included focus-group discussions, surveys of 120 rural households (representing an approximately equal mix of nonpoor, poor, and extremely poor) and in-depth interviews with 34 poor, rural households that had microenterprises. Although these surveys were limited to only a few households, they provide at least indicative results concerning access to financial services as well as constraints and opportunities to expand outreach. Almost half of the sampled households did not have a savings account and more than 60% of the respondents had no access to credit from any semiformal or formal financial institution.

An earlier, more comprehensive survey conducted by BRI jointly with Harvard University advisors in late 2000 produced similar results. The BRI survey had wider household coverage, with 1,426 respondents throughout Indonesia. The design parameters and the sampling process were structured in a way that allowed results from selected respondents to be used to make assumptions about the general population. The results showed that, despite all efforts of financial deepening over the past 3 decades, the majority of villagers still do not have access to formal or semiformal financial services. Some 62% of surveyed households without a viable enterprise did not have savings accounts and 68% did not have credit from any financial institution.[47] In households with a viable enterprise, 52% did not have a savings account and 58% did not have a loan from a financial institution.

However, it is important to recognize that "lack of access to credit" is not necessarily equivalent to "unmet demand for credit."[48] Findings from both surveys were that it is often the villager's own decision not to borrow, for good reasons. During the in-depth interviews conducted as part of the ADB survey, respondents voiced doubts about their own repayment capacity and their resulting unwillingness to pledge any collateral for fear of losing it, especially those involved in agricultural production and subject to substantial price and yield risks. Similarly, in the BRI survey, two thirds of the 68% who did not have credit from any financial institution said that they did not want to have debt. It appears that demand for microsavings is high, while demand for microcredit is considerably lower than commonly assumed.

Ample evidence has shown that low-income households primarily need savings instruments that enable them to manage their liquidity effectively and finance special expenditures. Repeated surveys through the 1980s and 1990s have consistently shown that the rural poor in Indonesia valued safety, liquidity, and convenience more than returns.[49] This is supported by the 2003 ADB survey findings, which indicate that there appears to be a considerable demand for safe, convenient, and easily accessible savings facilities that are geared

to the savings capacity and needs of the poor. Women, in particular, show a considerable demand for these type of services because they often try to build up reserves for school expenses, family health care, or children's wedding expenses, and often hide them from their husbands.

Microcredit demand based on the two surveys is considerably lower and varies much more than demand for microsavings by location and client type. Clients range from "tiny family businesses characterized by subsistence orientation, low productivity, and high volatility to fast-growing businesses with high potential to graduate to the small enterprise sector."[50] Microcredit demand is primarily for the expansion of existing businesses and for a variety of off-farm activities. Required loan sizes are Rp1 million–3 million ($112–336, based on end-2002 exchange rates). Comparing these indicative figures with the cash-flow patterns and level of indebtedness of the interviewed sample, there seems to be sufficient repayment capacity to sustain this loan demand. None of the households interviewed in the 2003 ADB survey indicated an interest in borrowing from commercial sources for farming activities. In general, agricultural production was considered to be too risky to be financed from borrowings. Households claimed that to obtain agricultural inputs they preferred to rely on savings from previous harvests, supplemented by income from other economic activities.

TOTAL SUPPLY

The microfinance sector is currently comprised of a large variety of public and private institutions as well as government and donor-sponsored programs (Table 2.1). This section highlights the various institutions and programs in order of the formality of their structure.

Formal MFIs

The largest and most significant players in Indonesia's microfinance market are formal MFIs that employ a commercial approach to microfinance. These include commercial banks and the system of BPRs, regulated by BI; and

Table 2.1: Supply of Microfinance by Formality of Provider Type

Least Formal → Most Formal

Informal Microfinance Providers (predominant level of service)	Semiformal MFIs (predominant level of service)	Formal MFIs (predominant level of service)
Microfinance NGOs (village)	Rural credit fund institutions (LDKPs) (subdistrict and village)	Primary commercial banks (district and subdistrict)
Moneylenders (village)	Village credit institutions (BKDs) (village)	- State-owned BRI Units - BDB
Traders (village)	Microfinance cooperatives (district and subdistrict)	Secondary banks (subdistrict)
Savings and credit associations (village)	- Savings and credit cooperatives (KSP)	- BPRs
	- Savings and credit units of cooperatives (USP)	State-owned pawnshops (district and subdistrict)
Friends and family (village)	- Savings and credit service points (TPSP) (village)	

Sources: Adapted from Sukarno 1999, p. 6-7; and Holloh 2001, p. 32.

the outlets of a state-owned pawning company (*Perum Pegadaian, or* PP), regulated by the Ministry of State-owned Enterprises. Many banks are involved in the microfinance sector by acting as channels for government credit programs and by cooperating with small financial institutions and cooperatives; however, only a few commercial banks have their own units dedicated to providing microfinance.[51] The only microfinance window of the banking sector with national coverage is the BRI Unit system, although BDB has regional significance.

Semiformal MFIs

The main semiformal MFIs include a variety of NBFIs, cooperatives, and credit unions that operate at the subdistrict or village level. The two major NBFIs are the BKDs and the Rural Credit Fund Institutions or *Lembaga Dana Kredit Pedesaan* (LDKPs), which have been established on the initiative of provincial governments since the 1970s and are licensed, regulated, and supervised by the provincial governments. Licensed cooperatives and credit unions are regulated by the Ministry of Cooperatives. The dearth of documentation concerning cooperatives, however, allows only information on the microfinance operations of the LDKPs and BKDs to be used here (see Table 2.2).

Informal Providers

The main informal suppliers are local organizations, such as microfinance NGOs, which are licensed by the Ministry of Justice and Human Rights[52] but not actively regulated or supervised; savings and credit associations

Table 2.2: Total Microfinance Supply

MFI Name/Type	Units	O/S Loans		O/S Loans		Total Deposits		Total Deposits	
	No.	No.	%	Rp billion	%	No.	%	Rp billion	%
BDB	31	9,311	0.1	57	0.3	242,146	0.7	190	0.6
Formal MFIs									
BRI Units	4,063	2,790,000	23.2	9,841	43.5	27,040,000	77.5	21,991	74.2
BPRs	2,143	1,900,000	15.8	6,420	28.4	5,200,000	14.9	5,597	18.9
Perum Pegadaian	714	5,230,743	43.4	1,355	6.0	–	0.0	–	0.0
LDKPs	1,603	500,000	4.2	337	1.5	871,000	2.5	342	1.2
Semiformal MFIs									
BKDs	4,518	658,871	5.5	198	0.9	571,744	1.6	38	0.1
Cooperatives									
KSPs	1,097	655,000	5.4	531	2.3	655,000	1.9	85	0.3
USPs	35,218	–	0.0	3,629	16.0	–	0.0	1,157	3.9
Credit Unions	1,071	296,000	2.5	272	1.2	296,000	0.8	249	0.8
Total	**50,458**	**12,039,925**	**100.0**	**22,640**	**100.0**	**34,875,890**	**100.0**	**29,648**	**100.0**

BDB = *Bank Dagang Bali*; BKD = *Badan Kredit Desa*; BPR = *Bank Perkreditan Rakyat*; LDKP = *Lembaga Dana Kredit Pedesaan*; KSP = *Koperasi Simpan Pinjam*; USP = *Unit Simpan Pinjam.*

BDB: All figures reflect self-reported data as of end-2001. **BRI Units**: data are as of end-2001and from BRI (2001, p. 44); units include BRI Units (3,823) and Village Service Posts (PPDs) (240). **BPRs**: data are as at 30 September 2002 from BI (2003). ***Perum Pegadaian***: data are as of end-2001; units refer to number of branches (BI 2001, p. 147); the total number of outstanding loans is based on 15.7 million customers served in 2001 (with an average loan maturity of 4 months); the total outstanding loan amount is from ADB (2003). **LDKPs**: estimates are for 30 June 2000 for 7 of 8 types of LDKPs as included in Holloh (2001, p. 34). **BKDs**: data are as of 31 July 2002, provided by the BRI Head Office; the number of units equals the active number of BKDs. **Cooperatives**: data are as of 30 April 1999 based on estimates presented in BI 2003 and ADB 2003. **Credit Unions**: data are as of end-2001, from ADB (2003).

(*Koperasi Kredit*); rotating savings and credit clubs (*Arisans*); moneylenders; traders; and friends and family. Due to the lack of information on these informal microcredit or microfinance providers, only the microfinance NGOs are included in this assessment of total microfinance supply.

Program Microfinance

In addition to the various types of institutional and informal sources of microfinance, several large government and donor-funded microfinance programs exist. These include, among others, the Rural Income Generation Project (RIGP/P4K) of the Ministry of Agriculture and BRI, with funding from the Indonesian Government, ADB, and International Fund for Agricultural Development; the Family Welfare Income Generation Project (UPPKS) implemented by the National Planning Coordination Board (BKKBN), funded mainly out of a revolving fund set up by former President Soeharto; the Subdistrict Development Program (PKK) implemented by BAPPENAS, supported by the Government and World Bank ($200 million); and the Urban Poverty Alleviation Project (P2KP), also implemented by BAPPENAS and funded in part by the World Bank ($100 million). Detailed discussion of the major programs, however, appears in Chapters 3 or 5, depending on whether or not they are conducive to increased microfinance commercialization.

Relative Market Shares of Major Microfinance Suppliers

Table 2.2 shows clearly that formal MFIs dominate the microfinance market in terms of their share of the total outstanding loans and deposits by number and by amount. Interestingly, the market leader in terms of number of microloans is the state-owned pawning company, with 43% of the total outreach. However, the BRI Units enjoy more than 40% of the microcredit market by amount of outstanding loans. More than 90% of the total loans disbursed by the BRI Units in 2001 were less than Rp10 million ($974) and 75% were less than Rp5 million ($487). The BRI Units have successfully funded their microcredit outreach by mobilizing over 70% of the total deposits by number and amount. BPRs have about 30% of the market outreach by number of microloans and about 16% by amount outstanding. BPRs also are the second largest mobilizers of deposits to fund their microcredit outreach.

The low market shares of semiformal MFIs reflect the much smaller, localized nature of their operations and the fact that they do not engage significantly in deposit mobilization. Unfortunately, lack of reliable data on the microfinance operations of cooperatives and credit unions prevents a full comparison of their relative market positions.

MAJOR MICROFINANCE INSTITUTIONS

Private Commercial Banks

The banking sector is still recovering from the crises of the 1990s; most private commercial banks maintain a conservative lending policy and keep away from microenterprises and poor households, which are generally perceived as higher credit risks than wealthier clients with larger businesses. While a few private commercial banks have begun offering microcredit products in recent years, largely because of the demonstration effect of BRI Units profitability, most of these operations remain small. Many private commercial banks still require traditional forms of collateral, and most microentrepreneurs and poor households, especially the rural poor and women, generally do not have collateral in their name. BDB, however, has overcome these constraints to achieve regional significance in the microfinance market.

By virtue of its private ownership and formal status as a commercial bank, BDB may be considered the most commercial MFI operating in Indonesia. Despite this, the bank has not lost sight of its original mission of serving poor and low-income clients. BDB was established by a husband and wife engaged in microenterprise and moneylending. As their moneylending businesses grew, it became apparent that creating a formal

bank offered the couple the best opportunity to continue to expand their microfinance activities. Over the last 30 years, BDB has accumulated significant expertise in serving microenterprises and small-scale businesses while turning a profit, which amounted to Rp46 billion ($4.4 million) in 2001.[53]

BDB classifies 70% of its outstanding loan portfolio as microcredit, which is mostly disbursed to rural and urban retailers and small traders on the island of Bali. However, BDB also has had healthy growth in its relatively small microfinance operations in Surabaya and Jakarta. The average outstanding microloan amount is around Rp6 million ($577), but this represents a wide range of better-off clients borrowing amounts of more than Rp10 million ($962) mixed with poorer clients who borrow smaller amounts (about 10% of BDB's clients borrow amounts less than Rp4.5 million [$433]). Around 90% of the bank's clients are repeat customers, indicating strong client loyalty, and about 25% of the borrowers are women. BDB reports a 92.7% on-time loan repayment rate for its total portfolio and a 100% on-time loan collection for its microcredit portfolio. To ensure high loan repayment, BDB requires personal marketable asset collateral or cosigners on the loan. BDB charges a 30–36% annual interest rate (based on a declining balance) on its loans.

Due in large part to BDB's formal status, commercialized operations, and good performance, mobilized deposits fund most of the bank's microlending. The bank's deposit-to-loan ratio exceeds 300% because the current savers far exceed active borrowers. BDB management recognizes that access to safe and liquid savings provides a useful service for their clientele. The average amount saved, nearly Rp800,000 (around $77), is much lower than the average outstanding loan. In addition to mobilizing deposits as a source of funds, BDB has accessed international financial markets, at least in terms of social investors. For example, the bank signed an agreement in late 2001 to finance microenterprises and small businesses in Indonesia with the Dexia Micro Credit Fund and the Netherlands Development Financial Company (FMO). BDB's excess liquidity is split about evenly between placements with other banks (interbank call money and certificates of deposits) and holdings of marketable securities. The bank's surplus of funds may largely be due to its regional focus (as opposed to national coverage) and its virtual saturation of the local market of creditworthy potential borrowers who are willing and able to pledge collateral in order to access microloans. Recent tapping of social investors by BDB may be an effort to cover at least some the costs of the bank's expected future expansion beyond the limited areas it currently serves.

BRI Units

BRI houses the world's largest microfinance network in its Micro Business Division, which caters to micro and small-scale entrepreneurs and operates on a commercial basis, despite its public ownership. There are currently 3,823 BRI Units (96% of which are profitable) and 240 village service points, in addition to BRI branches. The Micro Business Division functions as an independent profit center within BRI, and each unit is a profit center within the division. The BRI Units have an extremely efficient management information system that allows management to assess the performance of each unit and apply a sophisticated employee incentive system, which encourages profitability, loan recovery, and savings mobilization. The Micro Business Division freely sets its own loan terms, although transfer prices (discussed below) are set by the parent company. The commercial approach applied by the BRI Units is reflected in their application of cost-recovery lending interest rates and maintenance of an interest rate spread sufficient to cover the high costs of servicing small loans and deposits. The original interest rate was and remains a flat 1.5% per month (although it briefly rose to 2.2% during the 1997–98 Asian financial crisis). The average annual yield obtained on loans has oscillated around 32% in recent years while average annual financial costs have been about 10%, yielding a large margin of 22%.

Kupedes loans are provided for working capital or investment purposes to individuals having a productive enterprise or with regular incomes, such as civil servants and employees of local enterprises. Typical borrowers are government employees or pensioners, small traders, and entrepreneurs.[54] Loan amounts are Rp25,000–25 million ($3–2,683, based on 2002 average exchange rates), but loan applications of less than Rp500,000 ($54) are now rare. As long as the maximum ceiling is not reached, a borrower can take both working capital and investment loans in parallel. *Kupedes* terms are 3–36 months, with repayment schedules adjusted to match the cash flows of the borrower's enterprise. All loans are monthly installment loans with grace periods of 3–6 months.

With an average disbursed loan size of Rp5.6 million ($538) and an average outstanding loan size of Rp3.5 million ($337) as of end-2001, it appears that the BRI Units lend to better-off poor and nonpoor households. As of June 2000, the arrears ratio for all loans one day or more past due was only 3.9%.[55] To minimize default risk, BRI requires individual borrowers to put up collateral, a policy that excludes the poorest borrowers. The collateral required is equivalent to the value of the loan principal and interest to be paid. Loans larger than Rp5 million ($559, based on end-2002 exchange rate) require a land certificate as collateral. Loans are usually secured with land certificates, motor vehicle ownership certificates, or a pledging of salary or pension. Deposits may be pledged as partial collateral. The client has to sign an acknowledgment of his debt, an authorization for the bank to execute the collateral pledged, and his wife/her husband has to sign a guaranty.[56] The loan principle and interest are secured by life insurance and the 0.75% premium is paid by BRI. Staff have discretion to increase the loan size for reliable borrowers who may not be able to fully collateralize their loans. Loan officers typically start clients off with small loans and condition future larger loans on good repayment.

A special feature of the *Kupedes* loans is the incentive system to promote timely repayments. A refund of 25% of the interest paid is made when installments are not delayed for six consecutive months. *Kupedes* borrowers have paid back more than 97% of all loans that ever have fallen due.[57] According to BRI, the Units' 12-month loss ratio at the end of 2001 was only 1.5%.

Surveys since 1982 have pointed to extensive rural demand for reliable and liquid deposit facilities.[58] Four savings instruments, with interest rates that vary by account size and liquidity, were made available at the BRI Units starting in 1986, as part of their new rural savings program. The instruments were designed to be appropriate for the target market and BRI Unit deposit growth has been quite rapid. Deposits have exceeded the outstanding loan portfolio since 1989 and the deposit-to-loan ratio has increased every year since. At end-2001, this ratio was 223% of the loan portfolio.[59]

As a profit center, the BRI Units have immediate value for their excess liquidity (total deposits minus total loans and cash required to support saving and loan transactions) by moving excess funds to BRI and benefiting from a transfer price that aims to compensate the BRI Units' financial and operational costs of mobilizing deposits. The transfer price is adjusted periodically according to BRI's overall liquidity position. The transfer price is usually set slightly higher than the top savings rate offered at the Units so that those with a surplus of funds can at least cover their interest costs, and are not discouraged from mobilizing savings.[60] BRI's maintenance of a transfer price higher then the interest rate paid by the Units on savings has prompted them to mobilize deposits actively and this has largely contributed to the phenomenal amount of mostly small deposits mobilized by the Unit system. Prior to the Asian financial crisis, the BRI Unit system reinvested close to 60% of deposits mobilized in their loan portfolios. This ratio has dwindled to about a third since the crisis. This drain of funds out of the Unit system to BRI indicates that the many small savings mobilized by the BRI Units (average size was Rp700,000 or $67 at end-2001) have been converted into larger loans provided to an urban and more affluent clientele of the bank, rather than to the rural poor.

The BRI Units are not subsidized and have been highly profitable since the mid-1980s. During 1996–1999, the Unit system made profits amounting to Rp2.9 trillion ($525 million).[61] Prior to the financial crisis, the Units contributed about one quarter of BRI assets and produced annual profits larger than the bank's total retained profits, thus maintaining positive returns.[62] Despite the high profitability of the BRI Units, their status as a profit center within a state-owned bank puts the system's profits at risk of being diverted to unprofitable investments and at no time was this made clearer than during the 1997–1998 Asian financial crisis. However, when BRI was affected by the crisis, 56% of its mainly large loan portfolio had to be written off resulting in a loss of $3.3 billion against a capital base of only $215 million, leaving the bank technically insolvent. The Government had to step in to recapitalize BRI and the nonperforming loans were transferred to IBRA.

BPRs

The system of BPRs has a long history and includes a variety of MFIs with different historical backgrounds. The first institutions that would become recognized as BPRs, with a 1988 deregulation package and the 1992 Banking Act, had their start in the early 1900s. Some historical highlights are presented below.[63] The focus here is on the BPR system at present, its level of commercialization, and recent performance.

The BPR industry in general is providing microfinance on a commercial basis through the formal financial system, having predominantly local, private ownership, and funding the provision of microcredit almost wholly from deposits. The system of BPRs is extremely diverse in terms of governance, management, outreach, and financial performance.[64] Nevertheless, the system as a whole has achieved significant outreach, reaching clients in some regions that had no access to banking services before the 1988 banking reforms. At the end of September 2002, there were 2,143 licensed BPRs.[65] With changes in the law and classification of BPRs over time, BPRs are allowed to take several legal forms. At the end of 2002, 62% were registered as limited liability companies, 35% as regional government enterprises, 3% as cooperatives, and less than 1% as other legal forms.

As of March 2000, about 5% of Indonesian households had loans provided by BPRs and the average BPR had 905 loan accounts, with an average outstanding amount of Rp1.2 million ($141) each.[66] The average outstanding loan size was Rp3.1 million ($333) as of June 2002.[67] BPR credit products vary with regard to interest rates and terms. The average annual effective interest rates are 31–44%, which are undoubtedly commercial. Loan maturities averaged 9–26 months. The average annual effective interest paid on the main savings products was 12%, allowing a margin of 19–32%.

Unlike commercial banks, no ownership of BPRs by foreign parties is permitted. This limits the ability of BPRs to attract foreign capital as a source of funds. However, most BPRs have access to mobilized deposits as a source of funds. As of March 2000, the average BPR had 1,882 savings accounts and assuming one account per household, an outreach to about 10% of all households.[68] The average BPR industry savings deposit was Rp0.9 million ($97) as of June 2002, when total deposits contributed approximately 86% of the total outstanding loan portfolio, although there were significant regional differences between BPRs. In addition to mobilizing deposits as a source of commercial funds, increased disclosure and transparency of BPRs promoted by BI's BPR Supervision Department is leading to increasing access of BPRs to loans from commercial banks (Box 2.1). An estimated one third of BPRs now have established borrower relationships with commercial banks. For loans in excess of Rp500 million ($55,928), however, physical collateral is still generally required by commercial banks. The BPR system as a whole has substantial liquidity, but much of this is needed to offset the high, 2:1, ratio of term deposits to savings deposits, to provide a cushion for increased lending, and to offset the lack of an effective inter-BPR funds transfer mechanism.[69]

Several indicators of loan portfolio quality signal that the BPRs generally have fairly

Box 2.1

Increased Access of BPRs to Loans from Commercial Banks

Bank Indonesia's BPR Supervision Department has been facilitating linkages between commercial banks and BPRs over the last few years to enhance BPR eligibility to take up commercial bank loans as a source of funds. To be eligible, BPRs must specify as part of their business plan the loan amount desired and how the funds will be utilized. Once this has been submitted, along with usual financial disclosure and reporting, BI ranks the BPR as sound, fair, or unsound according to CAMEL (Capital, Asset, Management, Equity, and Liquidity) criteria. BI may informally recommend to the 15 commercial banks currently participating that the BPR is financially healthy and represents a good credit risk. BI also provides interested commercial bankers with 2-week training courses on how to evaluate BPRs as prospective borrowers. When a match is made, loans of up to Rp500 million ($55,928) are lent by the commercial banks without collateral for 1 year rollovers at an annual interest rate around the current prime of 18–20% (declining basis) and re-lent by the BPR at annual interest rates of 24–30%.

Source: Interview with Mr. Santoso Wibowo, Manager of Research and Regulation of BPRs, Bank Supervision Department, BI.

high-risk operations with relatively poor portfolio quality, thereby placing client deposits at some risk. The overall loan portfolio-at-risk ratio[70] was 21% for loans over 90 days past due. BI classified 4% of the industry's total loan portfolio as substandard, 6% as doubtful, and 11% as lost. However, its loan classification system provides high tolerances, i.e., monthly installment loans in arrears for less than 3 months are classified as standard. These loans have to be classified as lost only after 27 months.[71] One third of the BPRs lack clear policies for lending to related parties. General lending limits applied do not prevent concentrating large parts of the loan portfolio in a few hands.[72] More adjustments will be needed to ensure that BPR performance improves to enable them to play a significant role in the expansion of commercial microfinance.

Pawnshops

Pawnshops are an important part of the microfinance sector in Indonesia and have been major providers of commercial microcredit for some time. The first pawnshops were established in the beginning of the 20th century. For many years, pawning was a monopoly of the Government and from 1990 it was organized in the form of a profit-oriented state enterprise, PP. The company has grown in professionalism and developed into a service-oriented institution that provides low-income households, who hold their savings in movable assets, with an important source of liquidity.[73] While regulated and supervised for many years by the Ministry of Finance, the company is now regulated and supervised by the Ministry of State-owned Enterprises.

The Government liberalized the pawning business in 2002, ending PP's monopoly and allowing banks or private firms to act as pawnbrokers. Already, two major commercial banks—Mandiri and BRI—have set up their own pawn operations based on the Sharia model.[74] A number of private companies have also set up shop in major Indonesian cities, focusing on attracting middle- and upper-class clients. However, these newer operations remain quite small relative to PP's pawning business.

Between 1990 and 2001,[75] PP's offices increased in number from 505 to 714 and are now in every district capital and increasingly in subdistrict capitals. PP offers efficient services: they are open 6 days each week, provide simple and fast transactions—usually 15 minutes or less—and allow customers to turn their valuables (gold, jewelry, household items, electronic goods, motor vehicles, and recently even unhulled paddy, valuable fabrics, and hand-woven cloth) into cash without having to sell them. Borrower transaction costs are minimal. Administrative expenses on average loans outstanding are about 20.75%.[76] Loans can range from Rp5,000 ($0.56) to more than Rp20 million ($2,237). Smaller loans

carry lower interest rates, a flat 1.25% per month for loans up to Rp150,000 ($17) to 1.75% per month for loans in excess of Rp500,000 ($56). Standard maturity is 120 days. Additionally, the company charges insurance costs and a deposit fee on all loans.

The decline in financial intermediation by banks because of the Asian financial crisis contributed to the sharp growth of PP. Between the end of 1996 and the end of 1999, the company's assets increased from Rp647 billion ($88.2 million) to Rp1,151 billion ($162.1 million), its amount of loans outstanding from Rp414 billion ($56.5 million) to Rp705 billion ($99.3 million), and its net profit from Rp34 billion ($4.6 million) to Rp61 billion ($8.6 million).[77]

In 2001, the company provided 22.2 million loans to 15.7 million borrowers. Its loans are small in size. As Table 2.3 shows, about 88% of PP loans in 2001 were less than Rp500,000 (roughly less than $60).[78] Also, the items accepted/pawned indicate that PP indeed serves microcredit clients ranging from very poor to low-income. Box 2.2 describes a typical low-income borrower. About 35% of PP clients are farmers, fishers, and small-scale entrepreneurs. During 2001, it disbursed Rp5,970 billion (about $702 million) and at the end of 2001 had an outstanding loan portfolio of Rp1,355 billion ($159 million). Its loan recovery rates are high. Collateral is sold when borrowers default, although it has only had to auction 0.5% of all pawned goods to date. Its return on assets and return on equity in 2001 were 4.5% and 17.0%, respectively. Together these indicators all point to a successful, commercial enterprise, despite its public ownership.

PP's sources of funding are mixed between commercial and subsidized sources. To raise working capital, PP issues bonds and notes, a favorite on the corporate bond market and one of the most highly traded on the local secondary market. However, during the Asian financial crisis, it also resorted to borrowing from the Government as well as taking BI liquidity credits to meet the greatly increased public demand for loans. PP recently received new soft loans from

Table 2.3: Distribution of *Perum Pegadaian* Loans by Size, 2001

Loan Size ($ Equivalent)	Number of Loans (million)	%
1.1 - 4.5	8.6	39
4.5 - 16.7	5.4	24
16.7 - 55.5	5.6	25
>55.5	2.6	12
Total	**22.2**	**100**

Notes: Data are as of end-2001; the total number of outstanding loans is based on 15.7 million customers served in 2001 (with an average loan maturity of 4 months; note that 5.2 million loans were outstanding at the end of the year, shown in Table 2.2); the total outstanding loan amount is from ADB (2003).

Source: Fernando 2003, p. 4.

Box 2.2

Expanding Access to Microcredit through Pawning

When Ms. Sumarni, a maid working in Jakarta, needed Rp300,000 ($34) to help her brother fix his motorcycle last year, she went to a pawnshop, and took out a short-term loan using an FM radio set and some gold jewelry as collateral.

She had 4 months in which to pay back the loan plus 3% monthly interest, and to redeem her items, but she spent most of her next salary to do so.

"The pawnshop suited my purpose. Borrowing from my employer was possible, but I didn't want to do that. A private moneylender would have charged higher interests, while banks would have been too complicated and taken too long.

I paid quickly to avoid the interest charges and to make sure my collateral didn't get auctioned off by accident," Ms. Sumarni explained.

Source: Go 2002.

the Government in order to expand its operations. Dedy Kusdedi, President Director of PP, told Reuters in an interview on 5 February 2003 that the firm had recently secured Rp1.5 trillion ($167.8 million) in soft loans from the Government. While PP will obviously use the cheaper funds as long as they are available, it has grander intentions of listing in the stock market to attain additional financing and expand its operations.

LDKPs

The LPD (*Lembana Perkreditan Desa*) system of LDKPs is the most successful and the only viable system of village-level financial institutions in Indonesia. LDKP is a general term used to describe a variety of regional nonbank MFIs established by provincial and district governments, mainly during the 1970s–1990s. In 1992, the LDKPs were mandated to upgrade to BPR status by October 1997 (by the Banking Act of 1992 and Government Decree No. 71 of 1992). Since the 1997 deadline, the remaining LDKPs have not been allowed to mobilize deposits. According to the monthly financial statistics of BI, the total number of LDKPs stayed essentially the same between the late 1980s (1,936) and the end of 1996 (1,978) and then decreased to 1,603 by June 2000 because of the conversion of about one quarter of them to BPRs.[79] Currently, the Balinese LPDs make up more than half of the remaining active institutions and they operate with 77% of the system's total assets and 85% of the total deposits. The second largest system of LDKPs is the Subdistrict Credit Boards (BKKs) with 14% of the system's total assets.[80]

Although LDKPs are licensed, regulated, and supervised by the provincial governments, technical assistance and supervision are usually delegated to the regional development banks (BPDs), which are also owned by the provincial governments.[81] Although the BPDs can require reporting by LDKPs, such reports are not forwarded to BI and BI has no jurisdiction to require such reporting. The BPDs also deliver technical guidance to LDKPs, but the quality of this assistance and supervision is reported to vary greatly from province to province, just as the quality of BPDs varies. Because there is no system providing reliable LDKP data at the national level, the focus here is on the remaining LDKPs in Bali (the LPDs), which account for most of the LDKP operations. They are the most commercially-oriented LDKPs and have the most reliable data on their solid performance.

LPDs began in Bali in 1985 and their numbers had grown to 912 by June 2000. There has been high and sustained government commitment to establish an enabling framework for the development of self-reliant and sustainable financial institutions under the ownership of the Balinese *Desa Adat*.[82] The Government of Bali is responsible for regulating and supervising the LPD industry within the framework of national regulations. National banking regulations have been requiring LDKPs to convert to BPRs, but the Balinese Government has been resisting such conversion and continues to demand a national regulatory framework that provides greater flexibility for nonbank MFIs.

BI allows LPDs to mobilize funds from members of the *Desa Adat* provided the LPDs refrain from using banking terminology. This compromise provided LPDs with flexibility to accept deposits, but did not resolve the issue of their legal status in the financial sector. LPDs offer savings deposits, time deposits, and credit services with varying terms. The LPDs have had great success, in part because of their ownership by individual, leading community members and the trust they inspire. The entire loan portfolio and more than three quarters of the total assets of the LPD industry are financed through voluntary savings. The majority of LPDs collect compulsory savings as a percentage of the loan amount disbursed. However, these compulsory savings seldom contribute more than 10% of total funds mobilized.[83] The proficiency of the LPDs at mobilizing deposits also enables them to have large outreach. LPDs provide microfinance in two thirds of the *Desa Adat* and to one third of all Balinese households.

Most loans are provided by LDPs for productive purposes, based on character and membership. Most loans have monthly installments but have a high variance with regard to both terms (10–36 months) and interest rates (2% declining to 3% flat per month). As of March 2000, savings deposits made up 44% of the total liabilities and equity of the LPD industry and they presently offer annual effective interest rates of 10–12%, commensurate with those offered by commercial banks. The average outstanding loan size is around Rp860,000 ($89) and the average savings account is Rp200,000 ($21).

According to the ratios and calculation methods applied by the LPD supervision system, the LPD industry is highly profitable. However, a ProFI survey showed that average return on assets (1999) decreased from 8.6% to about 4% for a sample of 81 LPDs (of 912 total) when full loan loss provision costs were included in adjusted income statements (not including adjustments for inflation). Without taking into account full loan provision and inflation costs, the LPD industry had a return on assets of only 2.4% (based on aggregated data) in the first quarter of 2000.[84]

BKDs

The *Badan Kredit Desa* (BKDs) operate in Java and are village-level financial institutions with historical roots dating back to colonial times. The evolution of banking laws and regulations has resulted in a contradictory situation in which BKDs were acknowledged as BPRs by the letter of the law but are neither regulated nor supervised as secondary banks in practice. BKDs are tiny institutions, often described as profitable and sustainable, providing demand-oriented financial services with a significant outreach to low-income groups.[85] However, several statistics show that while a few individual institutions might perform well and play a significant role in the village economy, BKDs as a whole are far from commercial in their approach to microfinance and their general performance is poor.

According to BRI statistics, there were 4,566 operational BKDs as of June 2000. They currently reach less than 3% of the total number of households in Java. BKDs are usually described as village-owned financial institutions. However, there is a distinction between village-level institutions owned and controlled by the village community and those owned and controlled by the village government.[86] The LPDs in Bali are examples of the first type while BKDs fall into the second category in that they are managed and controlled by the village bureaucracy. Weak ownership and governance combined with poor banking skills and lack of effective internal control have contributed to low levels of outreach and financial sustainability. Based on unadjusted financial statements, profits made during the first half of 2000 were equivalent to 39% of total income and almost 4% of average assets during the period. However, taking loan portfolio quality and full loan loss provisions into account there are negative net margins,[87] ranging from -6% in East Java to -22% in West Java, with an average of -8.5% for the entire BKD industry.

By virtue of being registered with the Ministry of Finance, BKDs are subject to regulation/supervision by BI, but historically they have been under the field supervision of BRI officers. BRI continues to supervise the BKDs on behalf of BI and is reimbursed for this service. The supervision system applied by BRI to the BKDs is stricter, at least in terms of measuring loan portfolio quality, than the CAMEL standards applied by BI to banks.[88] Loans without late payment of installment, interest, and compulsory savings are classified as "standard." Loans with late payments that have fallen due for up to 6 months are classified as "doubtful." Loans with late payments that have fallen due for longer than 6 months are classified as "lost." However, BRI is constrained in its role as delegated supervisor because it has no enforcement powers. In addition, the stricter loan classifications are not used in determining credit risk exposure and loan loss provisions. This practice is highly problematic because most BKDs avoid writing off loans and do not fully account for loan loss provision costs in their income statements.[89]

As of June 2000, BKDs were suffering from extremely poor loan portfolio quality. Only 39%

of all loans outstanding and 59% of the total value of the loan portfolio were classified as standard; 37% of all loans and 20% of the loan portfolio were classified as lost. Even if the BI standards were used, with a classified-to-performing-assets ratio of more than 19% on average, the BKD industry would be rated unsound. In addition, with an overall loan loss reserve ratio of only 8% on average, the BKD industry reflects unprudential banking practices.[90]

BKDs are open for business only on certain days, depending on demand and operating capacity issues. While some may be open twice a week, others are open twice a month, and a few are open only once a month. Loan sizes are Rp100,000–1 million ($11–112) and disbursements are usually made no more than a week or two after application. Interest rate charges to clients are 2–6% flat monthly and the most common interest rate applied is 3% flat per month.[91]

Although the high interest rates charged by BKDs can be considered commercial, BKDs lack sufficient business orientation and commercial operational efficiency to expand in any significant way, despite their provision of microfinance only on a part-time basis. Average loan size has remained stable in recent years at Rp300,000–400,000 ($34–45); large loans are usually required by farmers for seasonal loans while petty traders with a fast turnover borrow small amounts with weekly installments. These amounts are generally lower than those of other small financial institutions and of some poverty-oriented microfinance programs. However, the low average loan sizes may reflect low levels of capitalization and savings mobilization that restrict the ability of BKDs to meet their customers' credit demand rather than a focus on particularly poor clients.[92] BKDs are not legally authorized to mobilize voluntary savings and most BKDs concern themselves solely with accepting compulsory deposits as prerequisites to loan funds. As of June 2000, total savings made up only 10% of total assets and 87% of these savings were compulsory, collected as a percentage (10%) of the loan disbursed.

Cooperatives and Credit Unions

The cooperative sector has been characterized by the dualism of semiformal cooperatives and a variety of informal organizations that work according to cooperative principles but have refrained from adopting the legal status of cooperatives. Microfinance cooperatives here are defined as cooperatives that provide microfinance services and are licensed, regulated, and supervised by the Ministry of Cooperatives. Cooperatives specializing in financial services are known as *Koperasi Simpan Pinjam* (KSPs) or savings and credit cooperatives. Multipurpose cooperatives[93] are allowed to provide microfinance if they operate an organizationally differentiated savings and credit unit or *Unit Simpan Pinjam* (USP).

Government intervention in the development of cooperatives was legitimized by Article 33 of the 1945 constitution, which stipulated that the economy has to be organized according to cooperative and family principles.[94] During the "guided economy" (1957–1966) era, cooperatives were used for channeling inputs and credit to farms. Despite the widespread corruption and high losses incurred by subsidized credit programs that continued to be channeled through the cooperatives during the 1980s and 1990s, the cooperative sector has been exempt from the series of market-oriented reforms implemented since the late 1980s. Even while financial sector reforms during this time reduced existing distortions, new ones were added by reinforcing the protection and subsidization of cooperatives.

The cooperative sector is presently regulated by Government Regulation No. 9 of 1995 and Ministerial Decree No. 351 of 1998.[94] The regulation stipulates that savings and credit activities may only be carried out by KSPs and USPs that are separated from other business units of primary or secondary multipurpose cooperatives.[96] It also provides for the Ministry of Cooperatives to provide "guidance" rather than supervision to KSPs/USPs; carry out inspections; and provide advice regarding capitalization, changes of management, and

liquidation when problems cannot be resolved. The Ministerial Decree was aimed at motivating the establishment of new KSPs/USPs and improving the performance of the industry. The establishment of new KSPs/USPs and branches requires a paid-up capital of Rp15 million ($1,678) for primary cooperatives and Rp50 million ($5,593) for secondary cooperatives, although the decree also states that KSPs/USPs that have not yet fulfilled the capital requirements will nevertheless be legalized, but must limit financial services to members.[97] Fully capitalized cooperatives may provide financial services to members, member candidates, and other cooperatives and their members.

More detailed provisions on the contents of required finance reports as well as the functions and organization of supervision followed in more recent decrees in 1998 and 1999. However, lack of enforcement by the Ministry of Cooperatives has rendered regulation and supervision ineffective. Lack of supervision and unreliable reporting are fundamental weaknesses of the system and no dependable data exist on the licensed cooperative sector as a whole. The reporting system of the Ministry does not allow identification of cooperatives that provide financial services let alone data on their financial operations.

Almost daily news of mismanagement and corruption plague the cooperative sector and the resulting lack of trust has made deposit mobilization virtually impossible. Cooperatives remain extremely dependent on outside funds and many are involved with channeling subsidized credit. Nevertheless, there is a range of member-owned cooperatives that have independently grown in a "grassroots" manner, through strong participation by their members and reliance on their own resources. One example, from West Nusa Tenggara, is *Koperasi Karya Terpadu*, highlighted in Box 2.3. Another is the credit union movement discussed below. There is also a successful microfinance cooperation model called *Swamitra*, discussed in Chapter 3 on institutions and programs that are enabling the expansion of commercial microfinance.

Box 2.3

Development of the *Koperasi Karya Terpadu* Cooperative

Located in East Lombok, this cooperative emerged from 13 womens' groups participating in the P4K Rural Income Generation Project, a microfinance and poverty alleviation project implemented by the Ministry of Agriculture and BRI. It is part of a multipurpose cooperative (*Koperasi Serba Usaha*) that focuses on financial services as its main business but also runs a small shop with basic goods, and provides social funds for medical purposes and in the cases of birth, marriage, and death. As of June 2000, the cooperative had organized 42 small groups with 501 members. Its assets, amounting to Rp51 million, were larger than those of many cooperatives with wealthier members and subsidized by government funds.

With its private ownership, reliance on own resources, and businesslike approach to providing microfinance, this cooperative is one example of a successful commercially-oriented MFI, created out of the RIGP/P4K project and continuing to be well managed.

Source: Adapted from Holloh 2001, p. 169.

Credit unions or *Koperasi Kredit* do not differ in terms of organization and operations from savings and credit cooperatives. Until recently, however, they usually operated as informal savings and credit groups because of the heavy government involvement in the cooperative system. Since the liberalization of cooperative regulations, an increasing number of credit unions and their secondary structures have adopted the legal status of savings and credit cooperatives.[98]

Credit unions have been promoted by a national NGO established in 1970, now called the Credit Union Coordination Board of Indonesia (*Badan Koordinasi Koperasi Kredit Indonesia*, BK3I). BK3I established in 1998 a national secondary cooperative for its registered savings and credit cooperatives after having been prevented from doing so for many years.

Presently, the movement has 28 regional chapters of which 16 have already adopted the status of secondary cooperatives. At the primary level, there are 1,105 credit unions.

Despite the financial crisis, the credit unions' total savings and credit grew by about 35% in both 1998 and 1999. Contrary to the vast majority of other types of cooperatives, credit unions have been emphasizing deposit mobilization and reliance on their own resources.[99] Deposits overall represent about 63% of their total liabilities and equity. With reserves and profits equivalent to 16% of total assets, the credit unions appear to be generally sound. Return on assets decreased from 13% in 1998 to 10% in 1999, but remained at a remarkably high level.

NGOs

Contrary to the situation in other countries, NGOs have not played a leading role in microfinance in Indonesia. NGOs have traditionally been involved with providing training and other social services–social intermediation rather than financial intermediation. NGOs have mostly concentrated their efforts on promotion of self-help groups and many NGOs have focused on the development of savings and credit groups. However, early efforts on the part of a few NGOs to formalize their microfinance operations deserve note because they may be among the world's earliest experiences in the establishment by NGOs of formal financial intermediaries. Although Indonesian NGOs are forbidden to mobilize savings of members unless these are deposited in a regulated financial institution, a few NGOs set up their own BPRs to overcome this constraint.

As one of the oldest and largest NGOs in Indonesia, *Bina Swadaya* is perhaps the most prominent NGO to have established a licensed bank to carry out its microfinance activities. In total, the NGO has established four BPRs over the last decade. The latter have a mission that balances a social orientation with a commercial approach and commercialized operations (Box 2.4). Because of the 1995 Company Law No. 1, which states that limited liability companies (the most popular form of BPRs) need to be established by at least two parties, all BPRs established by *Bina Swadaya* have equity shares split between the NGO and its staff association with ratios ranging from 90:10 to 50:50.

In one case, an NGO (*Yayasan Purba Danarta*, located in Semarang, Central Java) even managed to establish in 1990 a locally-operated commercial bank–*Bank Purba Danarta*. Another NGO (*Lembaga Penelitian dan Pengembangan Sumber Daya*, LP2SD, in East Lombok, West Nusa Tenggara) established its own credit cooperative, providing an umbrella for its savings and credit groups. LP2SD aims to develop financial self-help groups into formal savings and credit cooperatives and sees the development of independent secondary structures (associations or cooperatives) of these groups as a crucial element in sustaining financial services to low-income groups. However, apart from the few NGOs that have established semiformal or formal MFIs, the vast majority of microfinance NGOs consists of small and unsustainable organizations, dependent on recurrent injections of donor funds to survive.

Box 2.4

Mission Statement of the *Bina Swadaya* BPRs

"The mission is to develop loving and bankable people, to give appropriate profit to stakeholders, to improve performance-based remuneration to its workers, to develop regional autonomy, and to develop self-reliance and sustainability."

Source: Bina Swadaya.