

**Republic of the Union of Myanmar**

**Data Selection Survey on SME  
Finance in Myanmar**

**Final Report**

**August 2017**

**Japan International Cooperation Agency (JICA)**

**Daiwa Institute of Research Ltd.**

**Japan Economic Research Institute Inc.**

## Table of Contents

CHAPTER 1. CURRENT STATUS OF SME FINANCING IN MYANMAR .....	1
1-1 CONCERNING LAWS, REGULATIONS AND TRANSACTION PRACTICES .....	1
1-1-1 Financial Institutions Law, regulations and others .....	1
1-1-2 Restrictions on financial institutions .....	2
1-1-3 Recent Deregulations .....	5
1-2 SUPERVISORY FRAMEWORK OF BANKS BY CBM .....	5
1-3 PRACTICE OF NOTIFICATION, INSPECTION AND ADMINISTRATIVE DIRECTION BY CBM .....	6
1-4 DEVELOPMENT OF THE CREDIT BUREAU .....	6
1-5 LIBERALIZATION OF INTEREST RATES AND ACCESS TO FINANCE IN OTHER COUNTRIES AND THEIR IMPLICATIONS TO MYANMAR.....	7
1-6 ROLE OF BANKS AND MICROFINANCE INSTITUTIONS (MFI) IN SME FINANCING IN MYANMAR: CURRENT SITUATION AND PROSPECTS.....	11
1-7 DEPOSIT INSURANCE.....	12
1-8 GOVERNMENT POLICY ON SME DEVELOPMENT .....	12
1-9 SUPPORTS BY INTERNATIONAL ORGANIZATIONS, SUCH AS WORLD BANK, ON SME FINANCIAL SYSTEM...	15
CHAPTER 2. LESSONS LEARNED FROM “JICA SME TWO-STEP-LOAN” .....	19
2-1 OVERVIEWS OF END-BORROWERS AND USE OF LOAN FUNDS.....	19
2-1-1 Overviews of end-borrowers and studies on their use of funds .....	19
2-1-2 Survey of all end-borrowers by questionnaire .....	21
2-2 EFFECTS OF JICA SME TWO-STEP-LOAN .....	21
2-2-1 Result of interview survey .....	21
2-2-2 Result of survey by questionnaire .....	21
2-2-3 Issues recognized through interviews .....	24
2-2-4 Other points confirmed through survey.....	24
2-2-5 Relationship between end-borrowers and Japanese companies .....	24
2-3 ISSUES AND POSSIBLE IMPROVEMENTS IN ODA LOAN PROJECTS IN SME FINANCIAL FUNCTION ENHANCEMENT PROJECT BASED ON 2-2.....	26
2-3-1 Enhancement of understanding of the concept, frameworks, and requirements of TSL .....	26
2-3-2 Strengthening of monitoring of fund use .....	26
2-3-3 Execution of loans proportional to each company’s creditworthiness .....	26
2-3-4 Promoting competition among PFIs .....	26
2-4 POSSIBLE IMPROVEMENTS ON LOAN CRITERIA AND DOCUMENTS USED IN TSL BASED ON THE SUGGESTIONS IN 2-3 .....	27
2-4-1 Preparation of a guidelines for reviewing the use of funds.....	27

CHAPTER 3. CREDIT GUARANTEE SYSTEM IN MYANMAR.....	28
3-1 PREEXISTING POLICIES AND SCHEMES RELATED TO CREDIT GUARANTEES IN MYANMAR.....	28
3-1-1 Overview of Credit Guarantee Insurance (CGI), provided by Myanmar Insurance (MI).....	28
3-1-2 Guarantee Scheme of CGI.....	28
3-1-3 Utilization of CGI.....	30
3-2 OVERVIEW OF MYANMAR INSURANCE.....	30
3-2-1 History.....	30
3-2-2 Supervision and Governing Law.....	30
3-2-3 Organizational Structure.....	31
3-2-4 Business Overview.....	31
3-2-5 Financial Situation.....	32
3-3 CURRENT SITUATION OF CGI(LLEGAL SYSTEM AND INTERNAL PROCEDURES WITHIN MI).....	32
3-3-1 Governing Laws and implementation regulations of CGI.....	32
3-3-2 Internal Procedures regarding to CGI within MI.....	32
3-4 ATTITUDE TOWARD CGI OF MYANMAR GOVERNMENT AGENCIES AND COMMERCIAL BANKS.....	33
3-4-1 Attitude of Government Agencies.....	33
3-4-2 Attitude of Commercial Banks.....	33
3-5 ESTABLISHMENT BACKGROUND OF CREDIT GUARANTEE SYSTEMS AND THEIR UTILIZATIONS IN JAPAN AND NEIGHBORING COUNTRIES.....	34
3-6 DEMANDS FOR CREDIT GUARANTEE SYSTEM.....	39
3-6-1 Demands from SMEs.....	39
3-6-2 Demands from Commercial Banks.....	40
3-7 CHALLENGES IN INTRODUCING A CREDIT GUARANTEE SYSTEM.....	40
3-7-1 Challenges of current CGI.....	40
3-7-2 Overview of new credit guarantee system.....	41
3-7-3 Challenges in introducing new credit guarantee system.....	43
3-8 SUPPORT BY INTERNATIONAL ORGANIZATIONS OR FOREIGN AGENCIES FOR CREDIT GUARANTEE SYSTEM.....	50
CHAPTER 4. IMPLEMENTATION STRUCTURE OF SME LOANS BY FINANCIAL INSTITUTION IN MYANMAR.....	51
4-1 OVERVIEW OF PRIVATE FINANCIAL INSTITUTIONS.....	51
4-2 FUNDING METHODS BY PRIVATE FINANCIAL INSTITUTIONS.....	51
4-3 LOAN APPRAISALS AT PRIVATE FINANCIAL INSTITUTIONS.....	51
4-3-1 Loan appraisal, approval and decision making.....	51
4-3-2 Analysis on financial statements upon loan appraisals at banks.....	51
4-3-3 Loan approval criteria.....	52
4-4 COLLATERALS AND CREDIT GUARANTEES.....	52

4-5	CREDIT RISK MANAGEMENT .....	53
4-6	LOAN ASSET MANAGEMENT AT FINANCIAL INSTITUTIONS .....	53
4-6-1	Internal credit rating at financial institutions .....	53
4-6-2	Loan management after disbursements.....	53
4-6-3	ALM (Asset liability management) .....	53
4-6-4	Asset quality review and provisioning.....	54
4-7	MARKETING METHODS BY PRIVATE FINANCIAL INSTITUTIONS .....	54
4-8	LOAN APPRAISAL CAPACITIES OF PRIVATE FINANCIAL INSTITUTIONS IN NEIGHBORING COUNTRIES.....	55
	<b>CHAPTER 5. POLICY RECOMMENDATIONS TOWARD IMPROVEMENT OF SME FINANCE SYSTEM .....</b>	<b>57</b>
5-1	OUTLINE OF POLICY RECOMMENDATIONS AND ITS PRIORITY.....	57
5-1-1	Summary: Multiple and cross-interactive policies are necessary .....	57
5-1-2	Demand-supply gap of fund.....	57
5-1-3	Biased lending to large company .....	59
5-1-4	Insufficient long-term lending.....	60
5-2	NECESSITY AND FEASIBILITY OF CREDIT GUARANTEE SYSTEM AND MEASURES TO ESTABLISH IT .....	61
5-2-1	Necessity of Credit Guarantee System .....	61
5-2-2	Strengthening CGI by Myanmar Insurance (Short-term measure).....	61
5-2-3	Establishing new credit guarantee system (Long-term measure) .....	61
5-2-4	Introduction of re-insurance system (long-term measure) .....	62
5-2-5	Other policies (long-term measure).....	62
5-3	PROPOSAL FOR CREDIT APPRAISAL CAPACITY BUILDING OF BANKS .....	62
5-3-1	Encouraging breakaway from credit appraisal biased to collateral .....	62
5-3-2	Directly capacity building.....	62
5-4	PROPOSAL TOWARD ENHANCING TWO-STEP LOAN FOR SME .....	63
5-4-1	Problem and issues of existing Two-Step Loan for SME .....	63
5-4-2	Proposal for 2nd phase of Two-Step Loan for SME.....	64
5-4-3	Decrease of PFI interest margin (Proposal 1) .....	65
5-4-4	Mechanism to breakout from collateral biased lending (Proposal 2).....	65
5-4-5	Measure to encourage competition between PFIs: “M-League” (Proposal 3).....	66
5-4-6	Measure to select end-borrowers by PMU (Proposal 4).....	67
5-4-7	Promoting trading with Japanese related company (Proposal 5).....	68
5-4-8	Requirement for company registration (Proposal 6).....	68
5-4-9	Requirement for SME card (Proposal 7) .....	68
5-5	PROPOSAL FOR OTHER JICA AIDS (GRANT AND TA) IN SME FINANCE SECTOR .....	68
5-5-1	Capacity building of CBM.....	68

5-5-2 Technical assistance for PFI.....69

## FIGURES

FIG 1: FINANCIAL INSTITUTIONS LAW (25 JANUARY 2016).....	1
FIG 2: MINIMUM DEPOSIT RATE AND MAXIMUM LENDING RATE (AS OF 22 JUNE 2017) .....	3
FIG 3: DEPOSIT RATES AND LENDING RATES BY MAJOR BANKS (AS OF 22 JUNE 2017) .....	3
FIG 5: ORGANIZATION CHART OF CENTRAL BANK OF MYANMAR .....	6
FIG 6: NUMBER OF MICROFINANCE INSTITUTIONS (OCTOBER 2016) .....	12
FIG 7: DEFINITION OF SMALL COMPANIES .....	13
FIG 8: DEFINITION OF MEDIUM COMPANIES .....	14
FIG 9. SME LOANS VIA SMIDB.....	14
FIG 10: TOP TEN DONORS OF GROSS ODA FOR MYANMAR, 2014-2015 AVERAGE .....	15
FIG 11: STATUS OF SUPPORTS BY DONORS .....	17
FIG 19: INTERACTION CHART OF CREDIT GUARANTEE UNDER THE CGI SCHEME .....	28
FIG 20: SME MEMBER CARD .....	29
FIG 21: GUARANTEE FEE RATE (% OF LOAN AMOUNT).....	32
FIG 22 : CREDIT GUARANTEE SCHEMES IN ASEAN COUNTRIES .....	34
FIG 23: OVERVIEW OF THE CREDIT GUARANTEE SYSTEM IN JAPAN.....	35
FIG 24: OVERVIEW OF KUR .....	38
FIG 25: CHALLENGES OF CGI USE .....	41
FIG 26: REFORM FLOW OF CREDIT GUARANTEE REFORM .....	42
FIG 27: DRAFT OF CREDIT GUARANTEE SYSTEM.....	43
(MODEL 1).....	43
FIG 28: CHOICES OF REFORM.....	44
FIG 29 : PROVISION BASED ON OVERDUE PERIOD .....	54
FIG 30 : COMPARISONS OF DOMESTIC CREDIT / GDP AMONG NEIGHBORING COUNTRIES.....	55
FIG 31 : COVERAGE OF BORROWERS BY PUBLIC AND PRIVATE CREDIT INFORMATION INSTITUTIONS (UNIT: %).....	56
FIG 32: ISSUES AND POLICY RECOMMENDATIONS FOR SME FINANCE SYSTEM .....	58
FIG 33: DEPOSIT AND LENDING INTEREST RATE AS OF 22 JUNE, 2017 (SAME AS FIGURE 3) .....	64
FIG 34: PROPOSAL FOR EASED COLLATERAL LENDING.....	66
FIG 35: OUTLINE OF M-LEAGUE.....	66
FIG 36: PMU’S SCREENING FLOW IMAGE.....	67

## Abbreviation

ALM	Asset Liability Management
CBM	Central Bank of Myanmar
CGI	Credit Guarantee Insurance
FRD	Financial Regulatory Department
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
IBRD	Insurance Business Regulation Board
MBA	Myanmar Bank Association
MFI	Microfinance Institution
MI	Myanmar Insurance
MMSE	Myanmar Microfinance Supervisory Enterprise
MoPF	Ministry of Planning and Finance
PFI	Participating Financial Institute
PMU	Project Management Unit
SME	Small and Medium-sized enterprise

"Dollar (USD)" in this report refers to the US dollar unless otherwise stated.

## Chapter 1. Current status of SME financing in Myanmar

### 1–1 Concerning laws, regulations and transaction practices

#### 1–1–1 Financial Institutions Law, regulations and others

In Myanmar, banks are regulated by the Central Bank of Myanmar Law, the Financial Institutions Law, regulations and rules under those laws, and instructions by the Central Bank of Myanmar (CBM). Those laws, regulations, rules, and instructions impose banks restriction on liquidity, interest rate, capital requirement and so on.

New Financial Institutions Law was implemented in January 2016 after 26 years from the Financial Institutions of Myanmar Law 1990. Contents of the Financial Institutions Law are as follows;

Fig 1: Financial Institutions Law (25 January 2016)

Chapter 1	TITLE AND DEFINITION
Chapter 2	OBJECTIVES
Chapter 3	ESTABLISHMENT
Chapter 4	GENERAL POWERS AND DUTIES OF THE CENTRAL BANK OF MYANMAR IN RELATION TO FINANCIAL INSTITUTIONS
Chapter 5	LICENSE
Chapter 6	Non-BANK FINANCIAL INSTITUTIONS (NBFI) and FOREIGN BANK REPRESENTATIVE OFFICE
Chapter 7	RESTRICTIONS RELATING TO ACCEPTANCE AND SOLICITATION OF DEPOSITS
Chapter 8	CAPITAL, RESERVES AND SIGNIFICANT OWNERSHIP
Chapter 9	PERMITTED ACTIVITIES
Chapter 10	BOARD OF DIRECTORS, CHIEF EXECUTIVE
Chapter 11	ACCOUNTING, AUDITING AND FINANCIAL STATEMENTS
Chapter 12	REGULATION, INSPECTION AND SUPERVISION
Chapter 13	CORRECTIVE ACTION AND BANK RESOLUTION MEASURES
Chapter 14	ADMINISTRATORSHIP
Chapter 15	REHABILITATION OF BANK
Chapter 16	REHABILITATION OF NBFI AND SCHEDULED INSTITUTION
Chapter 17	LIQUIDATION OF BANKS, PRIOR APPROVAL NEEDED FOR VOLUNTARY WINDING-UP AND LIQUIDATION OF A BANK
Chapter 18	E-MONEY, E-BANKING AND MOBILE BANKING
Chapter 19	OVERSIGHT OF PAYMENT AND SETTLEMENT SYSTEM
Chapter 20	CREDIT INFORMATION
Chapter 21	POWER TO EXEMPT, RECOVERY OF FEES, BANK HOLIDAYS AND JUDICIAL REVIEW
Chapter 22	ELECTRONIC EVIDENCE
Chapter 23	PARTICULARS OF UNCLAIMED MONEYS OR DORMANT ACCOUNTS
Chapter 24	ADMINISTRATIVE PENALTIES
Chapter 25	PROHIBITIONS
Chapter 26	OFFENCES AND PUNISHMENT
Chapter 27	GENERAL

Source: Financial Institutions Law



## 1-1-2 Restrictions on financial institutions

### (1) Capital Adequacy Requirement

CBM Notification (No. (16/2017)) dated 7 July 2017 stipulates that the regulatory capital adequacy ratio is 8%, and that the minimum Tier 1 capital<sup>1</sup> adequacy ratio is 4%.

### (2) Minimum Reserve Requirement

Banks have to hold more than 10% of total deposit as reserve. 75% of this reserve has to be held in the current account in CBM without interest, and remaining 25% has to be held in cash.

If the amount of reserve becomes insufficient, a bank has to pay to CBM interest of 0.2% of the amount of the shortage per day. A bank has to fill up shortage in 30 days. Interests have to be paid in a week after the end of the week, in which shortage appears.

### (3) Non-performing Loan Ratio

CBM Notification (No. (17/2017)) dated 7 July 2017 stipulates that banks have to classify loans as follows;

Standard	30 days or less
Sub-Standard	31- 60 days
Doubtful	61 - 90 days
Loss	180 days or more

### (4) Liquidity Ratio Requirement

CBM Notification (No. (19/2017)) dated 7 July 2017 stipulates that banks have to maintain liquidity ratio (liquid assets to eligible liabilities) at least 20%. Every bank have to calculate daily liquidity ratio position and report CBM weekly average at the beginning of following week.

### (5) Loan Loss Provision

Banks have to allocate maximum 2% of total loan balance as general provision. Other than general provision, banks have to build up special provision according to loan classification set by CBM regulation.

Standard	0%
Watch	5%
Sub-standard	25%
Doubtful	50%
Loss	100%

---

<sup>1</sup> "Tier 1 (Core) Capital" = "Total Equity Capital" – ("Profit & Loss of Current Year if negative" + "Intangible Assets" + "Net Deferred Tax Assets" + "Pre-operating Expenses" + "Related Party Lending")

## (6) Interest Rate

CBM regulates the minimum deposit rate and the maximum lending rate of banks by the instruction dated 27 December 2011. Central Bank rate has been set at 10%. Minimum deposit rate is 2% points less than Central Bank rate (=8%), and the maximum lending rate is 3% points more than Central Bank rate (=13%). These rates (Central Bank rate: 10%, minimum deposit rate: 8%, maximum lending rate: 13%) are effective as at 22 June 2017.

Fig 2: Minimum Deposit Rate and Maximum Lending Rate (as of 22 June 2017)

Interest Rate(%)	
Central Bank Rate	10% pa
Minimum Bank Deposit Rate	8%pa
Maximum Bank Lending Rate	13%pa

Source: Website of the Central Bank of Myanmar

<http://www.cbm.gov.mm/>

Formerly, banks had set deposit rate at the minimum deposit rate and set lending rate at the maximum lending rate. As of 22 June 2017, banks offer the same interest rates on time deposits of 3 months to 12 months. On the other hand, deposit rates on savings accounts differ among banks from 8.25% to 8.6%, reflecting policy of each bank and conditions (possible number of withdrawal in a month, and so on) on account. Lending rates also differ 12% and 13%. Competition among banks generated difference in interest rates between banks.

Fig 3: Deposit Rates and Lending Rates by Major Banks (as of 22 June 2017)

	Deposit Rate (%)						Lending Rate
	Savings Deposit	Time Deposit (# of months)					
		1	3	6	9	12	
KBZ	8.25	9.00	9.25	9.50	9.75	10.00	13.00
CB	8.25	9.00	9.25	9.50	9.75	10.00	13.00
Yoma	8.25	9.00	9.25	9.50	9.75	10.00	13.00
APEX	8.50	8.50	9.25	9.50	9.75	10.00	12.00
AGD	8.60	9.00	9.25	9.50	9.75	10.00	12.00
AYA	8.25	9.00	9.25	9.50	9.75	10.00	n.a.
SMIDB	8.50	9.00	9.25	9.50	9.75	10.00	12.00
GTB	8.50	-	9.25	9.50	9.75	10.00	12.00

Source: Websites of banks

## (7) Collateral

CBM instruction dated 26 May 2005 stipulates that banks have to secure “strong collateral” on lendings, consequent to banking crisis in February 2003. This instruction does not refer to what “strong collateral” means specifically. As it is stated in the same instruction, however, that banks have to check immovable price changes of their collateral in a consistent basis, and additional collateral should be taken at the time of declining immovable prices, “strong collateral” has been interpreted as immovable (land and buildings).

Afterward, collateral expanded gradually through financial reforms. At present gold, gold products, deposit, treasury bonds, machinery, crops and farm machines are recognized as collateral.

Fig 4: Collaterals and CBM Instruction

Date of Issue	Instruction	Collateral
25 May 2005	Instruction No. (1/2005)	“Strong Collateral”
8 September 2011	Instruction No. (22)	Gold, Accessories made of gold
27 December 2011	Instruction No. (24)	Bank deposits
25 January 2012	Instruction No. (25)	Machines, Goods, Crops
8 June 2012	Instruction No. (27)	Government treasury bonds

Source: Instructions of CBM

The setting of collateral is achieved by signing the registered document of the mortgage holder and two or more witnesses, and must be registered in accordance with Registration Law. In the case of a company, the Company Law also requires the registration of collateral and imposes an obligation to place a copy of the document on collateral in the registration office.

There are two ways of selling collateral.

### (a) Selling collateral through courts

The collateral owner may request the court to order the collateral to be sold, unless the repayment is made or a foreclosure decree is issued for the receivable loan. If the obligee's claim is accepted, the court will determine the amount of remaining obligation at that time. The sale of the collateral is carried out in accordance with the provisions of the court, and the amount deducted from the sale is paid to the court and it is allocated to the amount of the obligation.

### (b) Arbitrary sale by the collateral owner

Arbitrary sale of collateral is prescribed in certain cases in Property Transfer Law. In cases that both parties are not a certain religion, race or tribe, or in cases that the collateral owner is the government and it is described in the certificate that the collateral owner have right to sell collaterals. In such cases, if a notice of repayment has been sent but not repayed for more than 3 months, arbitrary sale of collateral is permitted.

## (8) Loan-to-Deposit Ratio

Loan-to-Deposit ratio is regulated to be maximum 80%. Due to limitation of financing method by

banks to deposit, loan-to-deposit ratio requirement limits increase of loan lendings by banks. As a result, it consists limiting factor of financial access by SMEs.

### (9) Large Exposures Regulation

Banks shall not take on financial exposure in respect of a person or a single counterparty or group of connected counterparties which constitutes in the aggregate a liability amounting to more than 20% of the core capital of the bank (CBM Notification (No. (18/2017)) dated 7 July 2017

Non-state-owned banks are subject to all of the above requirement and restriction, but state-owned banks are subject to only minimum reserve requirement and liquidity ratio requirement.

### 1-1-3 Recent Deregulations

As noted above, CBM allowed treasury bonds, gold and gold products, machinery, crops, and farm machines as collateral other than land and buildings. In some banks' website, it is stated that they accept crops and others as collateral. However, in general banks take immovable as collateral in practice, loan lending with other collateral does not common yet.

By the instruction by CBM (May 2015), lending period has been restricted to be less than 1 year, because banks could finance through gathering deposit maximum 1 year. By CBM instruction (August 2013), banks can offer deposit with period more than 1 year, and accordingly, banks can offer loans with more than 1 year period. However, due to limitation on lending rate (13%), banks cannot add interest rate according to risk on long term lending. As a result, long term lending is not spread in actual.

According to Financial Institution Supervision Department of CBM, CBM has ongoing discussion on lifting ban on unsecured loan to SME. That aims to promote SME development, and to take loans, SME may have to prepare financial statements compliant with IFRS. Time schedule has not been made yet as of 8 June 2017, it is unclear when it will be determined and implemented.

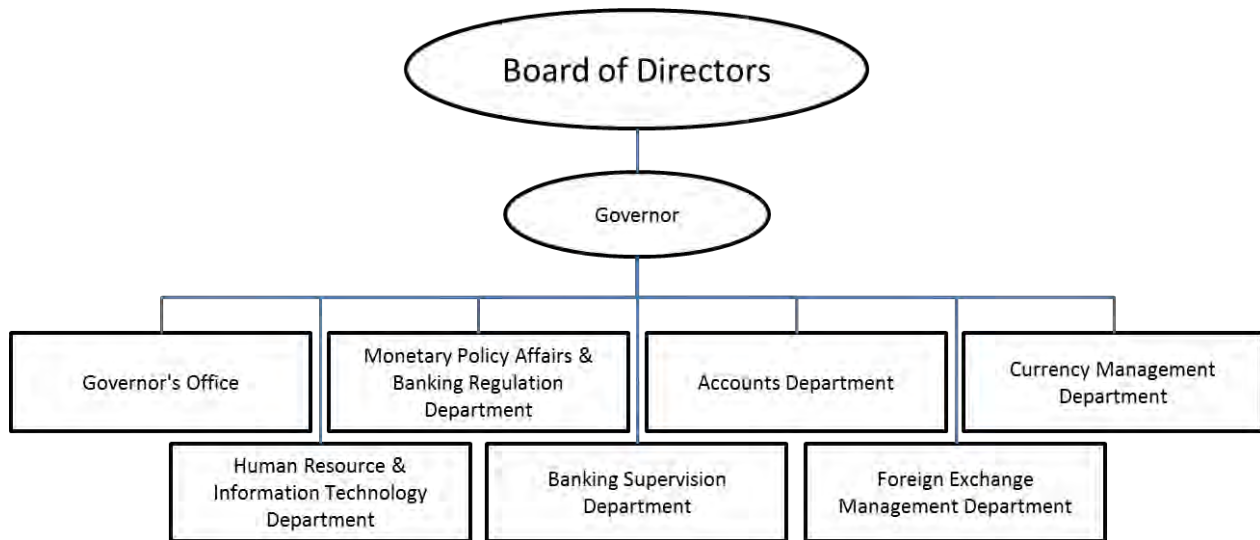
In the instruction of CBM issued in April 2017, it is stated that each bank shall prepare and submit risk management policy to CBM. CBM shall review risk management policies prepared by banks and approve, if there are no problem. Financial Institution Supervision Department is in charge of reviewing banks' risk management policies. According to that department, if banks set up adequate risk management method, unsecured loans to SME can be approved. However, it is not clear what the "adequate risk management method" is, whether the department can correctly judge the appropriateness. After submission of risk management policies by banks to CBM, concrete requirements for unsecured loans will be decided through discussions with between CBM and banks.

### 1-2 Supervisory framework of banks by CBM

Central Bank of Myanmar regulates and supervises banks in Myanmar. CBM issues and withdraws banking license, conducts on-sight/off-sight monitoring of banks, and others to maintain sustainability of financial system in Myanmar.

Organizational structure of CBM has been changed in 2017, but new structure is not publicly announced as at 21 June 2017. Following figure shows organization chart based on information from CBM.

Fig 5: Organization Chart of Central Bank of Myanmar



Source: Information from CBM

“Monetary Policy Affair & Banking Regulation Department” and “Banking Supervision Department” are the major supervising bodies of private banks. Number of staff of “Monetary Policy Affair & Banking Regulation Department” is about 200. Under the department, “Financial Institutions Regulations & Anti-Money Laundering Department” engages in making CBM regulations, rules and instructions. “Banking Supervision Department” engages in inspection and supervision of banks, including on-sight/off-sight monitoring of private banks. Monetary Policy Affair & Banking Regulation Department” has 65 staff.

### 1–3 Practice of notification, inspection and administrative direction by CBM

Banking Supervision Department of CBM supervises banks and financial companies in Myanmar. The department is divided in 4 sections, and each section takes responsibility of supervision of banks (finance companies) in charge. Off-sight monitoring is implemented once a quarter on each bank. On-sight monitoring is stipulated in the Financial Institutions Law to be implemented once in two years for a bank (a finance company). But according to interview with banks, on-sight monitoring is implemented once a year actually.

Monitoring by CBM is conducted based on collateral at present. CBM plans to shift to risk-based monitoring in the future.

### 1–4 Development of the Credit Bureau

The Central Bank of Myanmar Law stipulate in article 75 about establishment of the credit bureau as follows;

“The Central Bank may establish or allow the establishment of a credit bureau to collect, in a manner and to such extent, as it thinks fit, credit information or any other information relevant in the assessment of the creditworthiness of the customers and to inform of these information to financial institutions.”

The Financial Institutions Law also stipulates in the “Chapter XX” (section 142) as follows;

- (a) In addition to section 75 of the Central Bank of Myanmar Law, the provisions of this Chapter shall apply to matters relating to credit information.
- (b) The Central Bank may establish or authorize the establishment of a credit bureau designed to collect and provide information on the payment record of the clients of all bank, NBFIs and other financial institutions in Myanmar.
- (c) The Central Bank may require any credit institution and any other entities engaged in the extension of credit to report any information required by the credit reference system.
- (d) Banks, NBFIs and other institutions shall ensure the veracity of the credit information of its clients submitted to the system.

The Credit Bureau will be established by Myanmar Bank Association (MBA) and NSP Holding, a Singaporean company, as a joint venture. CBM issued a regulation regarding credit information system in March 2017, and is preparing legal backdrop for the credit bureau. CBM will issue 5 more regulations regarding the Credit Bureau.

#### 1–5 Liberalization of interest rates and access to finance in other countries and their implications to Myanmar

The interest rates in Myanmar are regulated by the central bank, and banks are not allowed to set deposit rates lower than 8% and loan interest rates higher than 13%. Based on this, many banks set deposit rates and loan interest rates at 8% and 13% respectively, although they tend to make deposit rates higher than 8% and loan interest rates lower than 13%<sup>2</sup>, due to recent severe competitions among banks.

Although deposit rates and loan interest rates were fixed by the regulation, it was pointed out that the real interest rates (nominal interest rates – inflation rates) have fluctuated and sometimes became negative, due to the fluctuations of inflation rates. It was also pointed out that residents in Myanmar maintain their financial assets in foreign currencies and look for opportunities for speculations<sup>3</sup>.

In this background, according to a research study by Deutsche Gesellschaft für Internationale Zusammenarbeit (German Federal Enterprise for International Cooperation, GIZ), most banks wish for the liberalization of interest rates, based on the following reasons;

- Competitions on deposits (especially on time deposits) are getting more severe and depositors are putting more pressures on the increase in deposit rates. Therefore, deposits at banks are getting less attractive.
- On the other hand, as loan margins for banks are shrinking, the transaction costs of the loans to smaller borrowers are increasing. As a result, banks are more reluctant to provide loans to such borrowers.

Regulated interest rates tend to be smaller than the interest rates determined in the market. The negative aspects for such artificial low interest rates are pointed as follows;<sup>4</sup>

---

<sup>2</sup> Daiwa Institute of Research, 2017, Increasingly competitive banking sector in Myanmar, Available at <[http://www.dir.co.jp/consulting/asian\\_insight/20170327\\_011849.html](http://www.dir.co.jp/consulting/asian_insight/20170327_011849.html)> [Accessed 31 May 2017].

<sup>3</sup> Daiwa Institute of Research, 2017, Issues in macro economic policy reforms in Myanmar, Available at <[http://www.dir.co.jp/research/report/overseas/asean/20170515\\_011974.html](http://www.dir.co.jp/research/report/overseas/asean/20170515_011974.html)> [Accessed 31 May 2017].

<sup>4</sup> Tsuji, S., 1995, Financial depressions and liberalization in developing countries [pdf], Available at <

- Gross savings are hampered by low deposit rates.
- Investors prefer non-productive investments (e.g. commodity inventories and gold) to bank deposits and thus funds for loans available in the market will be limited.
- Due to the caps on interest rates, banks cannot secure risk premiums, and thus banks avoid profitable but risky investments.
- As a result, economic growth in the country is hampered.

China, which has regulated interest rates, started liberalization of interests in 2012. The liberalization of interest rates in China was completed by the abolishment of loan interest floors in July 2013 and the abolishment of deposit rate caps in August 2015, which was followed by the introduction of deposit insurance in May 2015<sup>5</sup>.

One of the negative aspects of such interest regulations in China was that banks avoided providing loans to high risk borrowers, such as small and medium enterprises and newly established companies, and focused more on large state owned enterprises<sup>6</sup>, because loan margins for banks were limited. Therefore, after the liberalization of interest rates, banks can determine interest margins according to the sizes of credit risks of borrowers. At the same time, small and medium enterprises, which had problems in having banks loans, would have better accesses to bank loans.

However, it has been also pointed out that cautions reactions would be needed when liberalizing interest regulations, as sudden liberalization on interest rates might lead to instability of financial system in the country.

Liberalization of interest rates is one of the approaches of financial liberalizations. The actions taken for financial liberalizations in 1980s and 1990s based on “McKinnon-Shaw Approaches” are as follows<sup>7</sup>;

- Liberalization of interest rates
- Liberalization of loan limits
- Liberalization of entrance barriers

In some counties, the privatization of state-owned financial institution is included in such financial liberalization approaches<sup>8</sup>.

Possible sequences of financial liberalization, based on “McKinnon-Shaw Approaches” mentioned above is (i) Stability in Macro economy (reduction in fiscal deficit and reduction in inflation rates), (ii)

---

[http://ci.nii.ac.jp/els/contentscinii\\_20170702213000.pdf?id=ART0000407201](http://ci.nii.ac.jp/els/contentscinii_20170702213000.pdf?id=ART0000407201)>, [Accessed 31 May 2017].

<sup>5</sup> Jingu, K., 2016, How far did the financial liberalization in China progress, Toyo Keizai [online] 15 September 2016, Available at < <http://toyokeizai.net/articles/-/133944> >, [Accessed 31 May 2017].

<sup>6</sup> Okoshi, T., (2013), China abandons floors to bank lending rate, Nikkei [Online] 19 July 2013, Available at <[http://www.nikkei.com/article/DGXNASGM1904H\\_Z10C13A7MM8000/](http://www.nikkei.com/article/DGXNASGM1904H_Z10C13A7MM8000/)> , [Accessed 31 May 2017].

<sup>7</sup> Komatsu, M., 2001, Experiences in financial liberalization in Indonesia, Basic study for policy support type cooperation in financial sector (JICA) [pdf], Available at <[https://www.jica.go.jp/jica-ri/IFIC\\_and\\_JBICI-Studies/jica-ri/publication/archives/jica/field/pdf/2001\\_02b.pdf](https://www.jica.go.jp/jica-ri/IFIC_and_JBICI-Studies/jica-ri/publication/archives/jica/field/pdf/2001_02b.pdf)> , [Accessed 31 May 2017].

<sup>8</sup> Tsuji, S., 1995, Financial depressions and liberalization in developing countries [pdf], Available at < [http://ci.nii.ac.jp/els/contentscinii\\_20170702213000.pdf?id=ART0000407201](http://ci.nii.ac.jp/els/contentscinii_20170702213000.pdf?id=ART0000407201)>, [Accessed 31 May 2017].

Liberalization of domestic finance (Liberalization of loan and deposit rates, liberalization of the regulations on new establishment of banks and branches, and liberalization of foreign direct investments) and (iii) Liberalization of foreign capital transactions<sup>9</sup>.

One of the examples of financial liberalization is the case of Indonesia. Indonesia had been regarded as one of the successful cases of financial liberalization in 1980s, but its financial system became seriously instable as a result of non-performing loans triggered by Asian Financial Crisis in 1997.

The financial liberalization in Indonesia is summarized as follows;

First Phase of Financial Liberalization (June, 1983)	Second Phase of Financial Liberalization (October, 1998)
<ul style="list-style-type: none"> <li>➤ Liberalization of interest rates (at state-owned banks)</li> <li>➤ Liberalization of regulations on loan limits</li> </ul>	<ul style="list-style-type: none"> <li>➤ Liberalization of the establishment of banks by banks</li> <li>➤ Liberalization on the establishment of private financial institution and others.</li> </ul>

The real interest rate in Indonesia, which was negative before the financial liberalization, became positive after First Phase of Financial Liberalization. As a result, the amounts of time deposits at banks significantly increased. At the same time, the ratio of money supply to GDP (M2 / GDP), which shows the depth of financial market, increased from 17.7% in 1982 to 46.4% in 1992<sup>10</sup>. Through the Second Phase of Financial Liberalization, many domestic banks and new branches were established very rapidly, and the number of banks increased from 118 in 1982 to 208 in 1992.

Because of these achievements, Indonesia had been regarded as one of the successful cases of financial liberalizations. However, after Asian Currency Crisis in 1997, it was turned out that banks had huge amounts of non-performing loans and the processes of financial liberalizations in Indonesia contained potential problems.

The underlying reasons of the significant increase in non-performing loans in Indonesia, pointed out by several critics, are as follows;

- Because foreign exchange regulations were lifted in 1970s, foreign capital started flowing into Indonesia following the financial liberalization in 1980s.
- Receiving foreign capital inflows, banks in Indonesia started quantitative expansions (increased loan balances). Banks expanded loans to real estates and also to the businesses in the same enterprise groups (Due to the lack of loan appraisal capacity, banks expanded loans to businesses in same groups in order to avoid transaction costs for loan appraisals and loan monitoring).
- Banks could provide loans only to unpromising businesses, as promising businesses (borrowers) took loans at Singapore in order to avoid high interest rates in Indonesia.

Before Asian Currency Crisis, financial regulations, such as regulations on capital adequacy, regulations on foreign currency positions, regulations on liquidity ratio, regulations on loan to deposit ratio and regulations on single borrowers limit, were in place and active. Based on the regulations on single borrower's limit, the loan balances for one borrower and one business group was regulated not to

<sup>9</sup> Takeda, M., 2000, Sequences in financial liberalization and vulnerability issues [pdf], Available at < <http://www.ide.go.jp/Japanese/Publish/Books/Sousho/501.html> >

<sup>10</sup> Tsuji, S., 1995, Financial depressions and liberalization in developing countries [pdf], Available at < [http://ci.nii.ac.jp/els/contentscinii\\_20170702213000.pdf?id=ART0000407201](http://ci.nii.ac.jp/els/contentscinii_20170702213000.pdf?id=ART0000407201)>, [Accessed 31 May 2017].



exceed 20% and 50% respectively of the total asset of the bank. However, at some banks, the loan balance for one business group turned out to have reached up to 70 to 90%. Therefore, such financial regulations were not necessarily functioning well<sup>11</sup>.

If the regulations on interest rates are liberalized in Myanmar, there would be some positive effects such as increase in deposit amounts following the increases in deposit rates. Then loan balances would also increase following the increase in deposits. Nevertheless, as the increase in deposits and loans might lead to the instability in financial system, cautious approaches should be considered before liberalization.

Such cautious approaches would include;

- The banking supervision function of CBM is enhanced
- Capacity of financial institution on credit risk assessment and management is enhanced, and
- Financial institutions secure sufficient capital adequacy (even after sufficient amount of provisions are accounted as a result of credit risk assessments)

Liberalization of interest rates should be implemented considering the progresses of these actions. In addition, a deposit insurance system should be established or enhanced, as the major funding sources of loans by financial institutions are deposit.

International organizations, such as the World Bank, Asian Development Bank (ADB) and International Monetary Fund (IMF) have suggesting the government of Myanmar to take cautious and gradual approaches upon liberalizing interest rates. Their opinions are summarized as follows;

World Bank <sup>12</sup>	<ul style="list-style-type: none"> <li>- There is also the concern that financial stability may be affected if interest rate restrictions were lifted too soon.</li> <li>- Nonetheless, interest rate caps tend to shift lending to lower risk activities, to the detriment of micro, small and medium enterprises (MSMEs).</li> <li>- The authorities could consider a phased relaxation of interest caps. This could be partial to encourage medium- and long-term deposits that will form the appropriate funding base for longer-term commercial loans.</li> <li>- In the near term however, implementation of the new Financial Institutions Law (2016) through issuance of prudential regulations could be critical for financial sector stability.</li> </ul>
ADB <sup>13</sup>	<ul style="list-style-type: none"> <li>- The fixed interest rate structure has meant that real interest rates have been very volatile, given the variance in inflation rates</li> <li>- CBM should adjust this structure (fixed interest rate) from time to time to reflect</li> </ul>

<sup>11</sup> Takeda, M., 2000, Sequences in financial liberalization and vulnerability issues [pdf], Available at < <http://www.ide.go.jp/Japanese/Publish/Books/Sousho/501.html> > [Accessed 31 May 2017]

<sup>12</sup> World Bank, 2016, Myanmar Economic Monitor: Anchoring Economic Expectations [pdf], Available at < <https://openknowledge.worldbank.org/handle/10986/25972>>, [Accessed 31 May 2017]

<sup>13</sup> Asian Development Bank, 2015, Developing Myanmar's financing sector to support rapid, inclusive, and sustainable economic growth [pdf], Available at < <https://www.econstor.eu/bitstream/10419/128548/1/ewp-430.pdf>>, [Accessed 31 May 2017]

	<p>macroeconomic conditions and monetary policy objectives</p> <ul style="list-style-type: none"> <li>- Liberalizing interest rates too early in the absence of a strong financial infrastructure and supervision and risk management system can lead to risky bank behavior and exacerbate systemic risks.</li> <li>- The appropriate sequence should be, i) stick to the CBM establishing the interest rate structure as it is doing now, but ensure that depositors earn positive real returns on deposits and banks have an adequate intermediation margin, ii) after some years and the development of CBM capacity and suitably strong financial infrastructure, the central bank could consider replacing the fixed interest rate structure with a floor for lending rates and a ceiling for interest rates, and iii) after what could be more than a decade or two of strong finance sector development, the government could consider liberalizing lending rates first, and later liberalizing deposit rates.</li> </ul>
IMF <sup>14</sup>	<ul style="list-style-type: none"> <li>- In cases where the macroeconomic situation was unstable and interest rates were liberalized, high real interest rates sometimes developed, leading to corporate and banking problems.</li> <li>- The next steps towards financial liberalization need to be taken carefully and be built upon sound monetary and fiscal financing policies and further strengthened supervision capacity and oversight of the financial system.</li> </ul>

#### 1–6 Role of Banks and Microfinance Institutions (MFI) in SME Financing in Myanmar: Current Situation and Prospects

Microfinance Institutions in Myanmar are governed by the Microfinance Business Law, enacted on 30 November 2011. Microfinance Business Law stipulates to establish “Microfinance Supervisory Committee” as the supervisory body of microfinance institutions in Myanmar. In this law, Microfinance Supervisory Committee is stipulated to develop policies and supervise MFIs in Myanmar. Under Microfinance Supervisory Committee, Myanmar Microfinance Supervisory Enterprise (MMSE) is stipulated to implement inspection and supervision of MFIs. In September 2014, MMSE had been reorganized to be Financial Regulatory Department (FRD) in the Ministry of Planning and Finance.

Before enactment of Microfinance Business Law in 2011, already existed microfinance institutions in Myanmar. Those MFIs were mainly international NGOs, established based on the Memorandum of Understandings between Myanmar government and international NGOs.

As at 2009, there were only 6 MFIs in Myanmar, but through improvement of legal framework, number of MFIs has increased significantly. Following table shows number of MFIs at October 2016.

---

<sup>14</sup> International Monetary Fund, 2016, Myanmar: Selected issues [pdf], Available at <<http://www.imf.org/en/Publications/CR/Issues/2017/02/02/Myanmar-Selected-Issues-44613>>, [Accessed 31 May 2017]

Fig 6: Number of Microfinance Institutions (October 2016)

Organization	#
International NGO	5
NGO	24
Myanmar Company	107
Foreign Company	28
Partnership	4
Total	168

Source: FRD website

<http://www.mof.gov.mm/en/content/myanma-small-loans-enterprise?q=en/node/270>

Based on the Microfinance Business Law, MMSE (current FRD) issued a procedure. In this procedure stipulated maximum interest rate of 2.5% per month (30% per annum). Due to the setting of maximum interest rate, it is pointed out that it is difficult to cover the cost required for frequent follow-up in the remote rural areas, and flexible product design such as interest rate setting according to risk.

At present, the interest rate of loans provided by banks is about 13% per year around ceiling interest rate, and microfinance institutions are stuck at 30% of the maximum interest rate. Lending of interest rates between 13% and 30% is not provided, and a service that fills this is required.

According to interview with CBM, CBM considers that the provider of this non-existing service should be banks, not nonbanks. In other words, it seems that the idea that banks should take risks through liberalization of lending rates is mainstream.

### 1-7 Deposit Insurance

Myanma Insurance (MI) provides “Deposit Insurance” as one of insurance products from 2012 according to direction by CBM. This deposit insurance covers low-volume accounts up to 1 million MMK. Depositors of those low-volume accounts are guaranteed up to 1 million MMK. Policyholders are banks, and the premium rate is 0.12% of the account balance. At the time of implementation, all banks (23 banks at the time of introduction) contracted, but now only 8 banks have the contracts, others canceled the contracts. In June 2017, number of accounts covered by deposit insurance was 38,691 accounts, and total balance was 105 million MMK.

Banks are supposed to confirm the account balance once a month and update the deposit insurance contracts, but it is the situation in which banks renew the contract once a year. According to MI, MI does not ask banks for purchase of deposit insurance. There have been no track records of insurance payment.

As mentioned above, all banks introduced deposit insurance initially, but it is virtually voluntary at the moment. Because banks renew contract once a year, it is considered that accounts that are not covered by the guarantee will be generated due to the timing of the opening of the account, if a bank actually collapses. Supposed that guaranteed amount as small as 1 million MMK should be one reason that banks are reluctant to use deposit insurance.

### 1-8 Government Policy on SME Development

On 9 April 2015, enacted the Small and Medium Enterprises Development Law. Objectives of the law are as follows;

- (a) to enable to accept the information related to business, technical assistance and financial aids for the small and medium enterprises;
- (b) to reach local and international markets and enhance the competitiveness of small and medium enterprises;
- (c) to have new employment opportunities and increase income of the people through the development of small and medium enterprises;
- (d) to reduce the difficulties and obstacles in business operations of small and medium enterprises

Under this law, the Central Committee of Small and Medium Enterprises was established, and this Central Committee is responsible for drawing up policies for developing small and medium enterprises and providing SMEs guidance for obtaining technical and financial support through domestic and foreign organizations.

This law defines the small and medium enterprises as follows;

Fig 7: Definition of Small Companies

sector	# of employees	capital	turnover
Manufacturing	up to 50	up to 500 million MMK	
Labor Intensive	up to 300	up to 500 million MMK	
Wholesale	up to 30		up to 100 million MMK
Retail	up to 30		up to 50 million MMK
Service	up to 30		up to 100 million MMK
Others	up to 30		up to 50 million MMK

Source: Small and Medium Enterprises Development Law

Fig 8: Definition of Medium Companies

sector	# of employees	capital	turnover
Manufacturing	more than 50 & up to 600	more than 500 million MMK & up to 1 billion MMK	
Labor Intensive	more than 300 & up to 600	more than 500 million MMK & up to 1 billion MMK	
Wholesale	more than 30 & up to 60		more than 100 million MMK & up to 300 million MMK
Retail	more than 30 & up to 60		more than 50 million MMK & up to 100 million MMK
Service	more than 30 & up to 100		more than 100 million MMK & up to 200 million MMK
Others	more than 30 & up to 60		more than 50 million MMK & up to 100 million MMK

Source: Small and Medium Enterprises Development Law

The SME Development Policy has been drawn up in 2015. “Vision” of this policy is as follows;

“Creation of regionally innovative and competitive SMEs across all sectors that enhance income generation and contribute to the social-economic development.”

The policy points out “difficulties in access to finance” as one of the obstacles SME faces, and it is supposed to provide supports on “financial resource” in addition to “human resource”, “technology development and innovation”, and others. As financial support measures supposed low-interest loans, development of insurance, establishment of venture capital, and others.

Myanmar government had provided SME low-interest loans (8.5%) through Small & Medium Industrial Development Bank (SMIDB) in 2012-2014. However, this low-interest loan did not broadly accepted, due to disrepute among SMEs, because it took long time for proceeding. In 2014, total amount of loans SMEs had received was 6.0 billion kyat out of 20 billion kyat budget. For SMIDB it was not so good deal due to slim margin.

Fig 9. SME loans via SMIDB

	# of companies	Total loan amount	Average loan amount
2012	37	5	0.14
2013	62	10	0.16
2014	237	6.9	0.03

Unit: billion kyat

Source: Press materials

In June 2014, Myanmar Insurance started providing Credit Guarantee Insurance (CGI) to SMEs, which do not have collateral such as land and buildings. Using CGI, SMEs can take loans without collateral (see “Chapter 3. Credit Guarantee System in Myanmar”).

As mentioned in “1 – 1 – 3 Recent Deregulations”, CBM discusses possibility of providing unsecured loans to SMEs. However, there are uncertainties whether the central bank can properly evaluate banks’ risk management policies. There is the possibility that SMEs may have to prepare IFRS compliant financial statements. If so, SME may face high hurdle in preparing necessary documents.

#### 1 – 9 Supports by international organizations, such as World Bank, on SME financial system

International organizations such as the World Bank (WB) and developed countries such as Germany and Japan provide funds and technical assistances for Myanmar as official development assistance (ODA). According to the statistics of the Organization for Economic Cooperation and Development (OECD), the annual ODA grant from 2014 to 2015 amounts to about 1.7 billion dollars. From the view of the proportion of countries, Germany accounts for the largest number of 530 million dollars, followed by Japan (\$ 280 million) and the UK (150 million dollars).

Fig 10: Top Ten Donors of Gross ODA for Myanmar, 2014-2015 average

No	Country / Organization	Amount	% of total
1	Germany	531	31.5%
2	Japan	283	16.8%
3	United Kingdom	147	8.7%
4	United States	99	5.9%
5	EU Institutions	95	5.6%
6	Australia	72	4.3%
7	Global Fund	60	3.6%
8	Austria	54	3.2%
9	International Development Association	51	3.0%
10	Switzerland	37	2.2%
	Others	256	15.2%
	Total	1,685	100.0%

Unit: million USD

Source: OECD

However, the number of projects is not so large with regard to development assistance on Myanmar's "The Finance System for Small-Medium Enterprises", "Credit Guarantee", "Capacity Building of Financial Institutions". Among them, the International Finance Corporation (IFC), which is an organization of the World Bank Group and provides private sector support for developing countries, has provided support to financial institutions and the central bank of Myanmar. For example, IFC started support to Yoma Bank in 2014 that it could develop and implement a comprehensive risk management framework, and strengthen the SME finance business. In September 2014, IFC agreed to finance the bank with \$ 5 million to improve SME finance. This support has been extended through convertible bonds and

is then positioned as a pilot project of a total of \$ 30 million in the form of the planned equity, senior notes, trade credits, etc. If convertible bonds purchased by IFC are converted into shares in Yoma Bank, it is also anticipated that IFC will become the first foreign institution holding the shares of Myanmar company. And in 2015, IFC supported Myanmar Oriental Bank (MOB) in investing in capital that it could increase lending to small and medium enterprises, and in 2016, IFC provided support to MOB for portfolio management of SME loans. As for the central bank of Myanmar, in 2014, it supported the development of personnel for staff on the audit of the credit report, the development of regulations on the credit report.

Except for the international organizations, the German international cooperation company (Deutsche Gesellschaft für Internationale Zusammenarbeit, GIZ) was supporting "Banking and Financial System Development" from 2012 to 2016. Based on our interview with the GIZ office in Myanmar, GIZ had implemented some supports to Myanmar through this project,

- 1) GIZ dispatched staff to KBZ, YOMA, SMIDB and implemented technical cooperation on loan tracking, risk management etc. (Of these, GIZ discontinued support for SMIDB),
- 2) GIZ provided support for legal matters and monetary policy planning etc. for about 2 years to the Central Bank of Myanmar (CBM),
- 3) GIZ assisted the drafting of Financial Institutions Law in legal affairs.

Also, the KfW Development Bank, which is engaged in public development aid activities at the German KfW Group, has implemented a SME lending program in Myanmar in connection with the support by GIZ. According to press release of KfW Development Bank, it financed the credit facility for the refinance to the Co-Operative Bank (CB Bank) as the first phase.

Fig 11: Status of supports by donors

Donor	Title / Project	Detail
Germany (GIZ)	Banking and Financial System Development	<p>Overall term: 2012 to 2016</p> <p>The project supports local partner institutions at different levels of the financial sector. This includes advisory services to the Central Bank of Myanmar on creating a supportive legal framework, support for training providers for the banking sector, and cooperation with individual banks to pilot the provision of financial services for SMEs.</p>
Germany (KfW)	SME Lending	<p>It is the project partner of KfW Development Bank for the SME Lending Programme (SELP). The Myanmar Economic Bank (MEB) acts thereby as the Paying Agent</p> <p>SELP aims to provide access to financial services for SMEs tailored to their investment needs, to build capacity of financial institutions and to raise awareness on best SME banking practices.</p> <p>In the first phase KfW finances a refinancing facility to Co-Operative Bank Ltd. (CB Bank), which has its headquarters in Yangon and 162 branches throughout the country. As the first participating bank CB Bank is supported in providing sustainable and needs-based financing to SMEs and in developing a SME lending segment. Further, via a capacity building component institutional capacity building and training for an adequate level of implementation efficiency of the refinancing facility is funded. This comprises technical consulting services to CB Bank as well as training measures for its management and operative staff in Yangon and selected branch offices. The first selected bank will thereby serve as model for all future participating financial institutions.</p> <p>(as of November 2016)</p>
IFC	Myanmar Oriental Bank	<p>IFC will support the Myanmar Oriental Bank on two main aspects:</p> <ol style="list-style-type: none"> <li>1. Institution Building and Risk Management: Clear and streamlined operations related to core functions of the bank including credit risk, finance and treasury, trade and international operations, human resources, and information technology.</li> <li>2. SME Banking: Development and implementation of an expanded SME portfolio, related new products and portfolio. The project expects to support growth and expand reach, and ultimately contribute to the development of the nascent banking sector in Myanmar.</li> </ol> <p>Disclosure Date: Jan 9, 2017                      IFC Approval Date: Feb 4, 2016                      Status: Active                      Estimated Total Budget: \$1,000,000.00</p> <p>(Project budget includes all project-funded activities)</p> <p>Last Updated Date: Jan 9, 2017                      Project Estimated Start Date: Apr 1, 2016                      Project Estimated End Date: Mar 31, 2018</p>
	Maha MF (Awba)	<p>The Maha project is intended to create demonstration effect for innovative and non-traditional banking models that expand access to financial services in a cost effective and sustainable manner in Myanmar. The project will focus on three components: (1) Institutional Capacity Building, (2) Product Development, and (3) Channel Development</p> <p>Disclosure Date: Nov 16, 2016                      IFC Approval Date: Feb 4, 2016                      Status: Hold                      Estimated Total Budget: \$1,393,447.00</p> <p>(Project budget includes all project-funded activities)</p> <p>Last Updated Date: Nov 22, 2016                      Project Estimated Start Date                      Project Estimated End Date: Jun 30, 2018</p>



IFC (Cont.)	Yoma	<p>The advisory engagement will support Yoma Bank in its efforts to upgrade operations, expand its financial services offering, and build a competitive market position. The project will focus on three components : 1. Developing and implementing a comprehensive risk management framework. 2. Strengthening of SME banking operations. 3. Conducting assessment to develop complementary intervention to support Yoma's business.</p> <p>Disclosure Date: Feb 11, 2015  IFC Approval Date : Aug 27, 2014  Status: Active  Estimated Total Budget: \$2,169,782.00</p> <p>(Project budget includes all project-funded activities)  Last Updated Date: Feb 11, 2015  Project Estimated Start Date:  Project Estimated End Date: Jun 30, 2017</p>
	<b>MOB Equity (Mynmar Oriental Bank)</b>	<p>Myanmar Oriental Bank ("MOB" or the "Bank") is one of the first established private banks in Myanmar. The Bank commenced business in 1993 and is the first private bank in Myanmar to obtain international banking license. Today its focused customer base is small to medium enterprises.</p> <p>IFC's investment will provide MOB with long term funding to allow the Bank to capitalize on new lending opportunities, which will ultimately increase access to finance to SMEs in Myanmar.</p> <p>(Associated Advisory Engagement)  IFC's investment is integrated by a package of advisory services designing to support the growth and development of the Bank, and help the Bank absorb and implement skills as well as operational changes in a sustainable manner.</p> <p>Date SPI Disclosed: Mar 19, 2015  Projected Board Date: Apr 20, 2015  Status: Active  Last Updated Date: Mar 19, 2015</p>
	<b>A2F - Myanmar CB</b>	<p>The project will work with the Central Bank of Myanmar (CBM) on the following aspects: (i) Developing a credit reporting regulation; (ii) Strengthening the credit reporting supervisory capacities of CBM; and (iii) Improving public education and consumer protection.</p> <p>Disclosure Date: Oct 15, 2014  IFC Approval Date: Apr 23, 2014  Status: Active  Estimated Total Budget: \$1,185,569.00</p> <p>(Project budget includes all project-funded activities)  Last Updated Date: Oct 15, 2014  Project Estimated Start Date  Project Estimated End Date: Jun 30, 2018</p>
World Bank	<b>Myanmar Financial Sector Development Project</b>	<p>Commitment Amount: US\$ 100 mln  Status: Active  Approval Date: December 20, 2016</p>

Source: created from websites of GIZ, KfW, IFC and World Bank

## Chapter 2. Lessons learned from “JICA SME Two-step-loan”

### 2-1 Overviews of end-borrowers and use of loan funds

#### 2-1-1 Overviews of end-borrowers and studies on their use of funds

The study team had interviews with selected 31 companies from all end-borrowers from May 30th, 2017 to June 16th 2017. The main interview items are as follows;

Chart 12 : Main interview items

	Items
1	Year of establishment
2	Number of employees (including change between before and after the loan disbursement)
3	Loan amount of TSL
4	Loan period
5	Repayment (repayment period, frequency of repayment)
6	Use of loan funds (including price)
7	Contribution to sales and profit (actual or planned increase)
8	Collaterals (including collateral items and assessed value of collateral)
9	Photos and movies of outputs by loans
10	Compliance with the environmental and social considerations
11	Opinion for the improvement of SME TSL

Source : Prepared by the study team

In selection of interviewees, end-borrowers at SMIDB, which was the sole PFI participated in TSL from the 1<sup>st</sup> batch, were given higher priorities, in order to review the positive effects by TSL. Other end-borrowers were selected from all PFIs avoiding any imbalances among PFIs.

When selecting interviewees, the study team also paid attention to business sectors and geographical locations of end-borrowers. Thus the interviewees were selected from as many business sectors as possible and also from the end-borrowers located not only in Yangon but also in other areas.

End-borrowers interviewed in this study are as follows;

Chart 13 : List of interviewee end-borrowers

Number	Business	Area	PFI	Loan amount
				Million MMK
1	Food processing (tea)	Yangon	SMIDB	480
2	Distribution of impo Tires, Leasing of Backhoe	Yangon	SMIDB	240

3	Garment	Yangon	CB Bank	350
4	Production of paints	Yangon	SMIDB	480
5	Production of aluminium pots	Yangon	CB Bank	500
6	Water transportation, Garment	Yangon	SMIDB	480
7	Lumbermill, Sales of steel construction materials	Yangon	KBZ	100
8	Production and sales of construction materials	Yangon	SMIDB	480
9	Second hand car dealer, Other related business	Yangon	SMIDB	480
10	ophthalmological clinic, sales of glasses	Yangon	KBZ	250
11	Production of ice	Yangon	KBZ	200
12	Construction, Operating hotel	Yangon	SMIDB	488
13	Production of constructing materials	Yangon	KBZ	500
14	Construction, Operating hospital	Yangon	SMIDB	480
15	Construction, Production and sales of construction materials and interior materials	Yangon	APEX	200
16	Plastic injection mold	Yangon	MCB	400
17	Production of plastic packaging bag	Yangon	MCB	300
18	Production of steel construction materials, Construction	Yangon	APEX	500
19	Production and sales of furnitures	Mandalay	AYA	25
20	Production and sales of furnitures	Mandalay	AYA	50
21	Production of incense sticks	Yangon	AYA	85
22	Production of plastic goods	Yangon	AYA	90
23	Garment	Mandalay	CB Bank	300
24	Production of steel goods	Mandalay	CB Bank	500
25	Manufacturing plastic goods	Yangon	SMIDB	200
26	Garment	Yangon	SMIDB	35
27	Production of plastic bottle	Yangon	MCB	300
28	Production of compound fertilizer	Yangon	MCB	500

29	Services related to agriculture	Ayeyarwaddy	SMIDB	480
30	Production of bottled water	Bago	SMIDB	480
31	Oilmill, Production of construction materials, Leasing of construction machinery	Shan State	SMIDB	240

Source : Based on the information supplied by PFI

## 2-1-2 Survey of all end-borrowers by questionnaire

In addition to interviews of the selected end-borrowers, the study team conducted a questionnaire survey of all end-borrowers. In the survey, the study team, receiving assistances by PFIs, distributed and collected the answers to questionnaires by end borrowers through PFIs. The number of target end borrowers was 188, while the number of the answers that the study team received was 141.

The study team was unable to obtain answers from 47 end-borrowers including 44 companies that received loans from AYA Bank.

The questions in the questionnaire include basic information such as industry, establishment year, borrowing situation of each end-borrower, and the effects of TSL on their sales, profits, recruitment activities. In addition to these questions, the study team requested the end borrowers to make general comments on TSL.

## 2-2 Effects of JICA SME Two-step-loan

### 2-2-1 Result of interview survey

During the interviews, many interviewees mentioned that the loan periods of TSL were longer and interest rates were lower compared to the loan usually provided by banks in Myanmar. Many interviewees mentioned that TSL were beneficial for them to promote their businesses. In fact, there were many end-borrowers whose sales and profits increased or were expected to increase due to the expansions of business scales, improvements of qualities of products, and start of new businesses by the capital investments achieved by the loan funds from TSL.

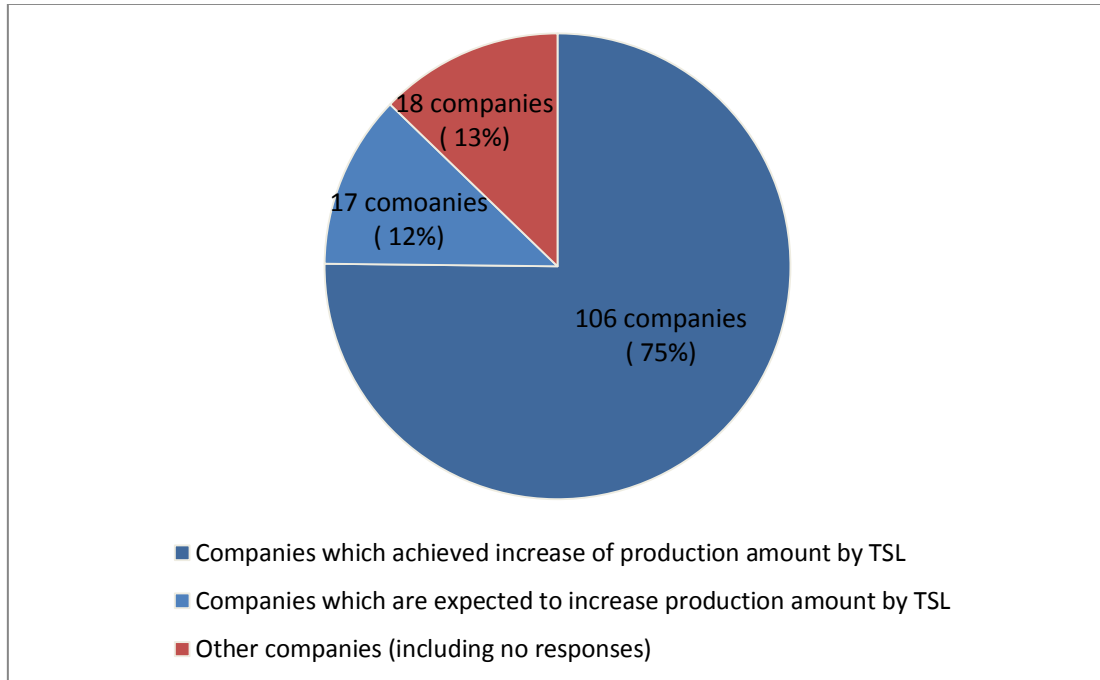
It was also confirmed that many end-borrowers hired new employees as the result of capital investments carried out by the loan funds from TSL. Therefore, it is possible to say that TSL contributed to the creation of employment in Myanmar.

### 2-2-2 Result of survey by questionnaire

#### (1) Effects on production amounts, qualities and sales

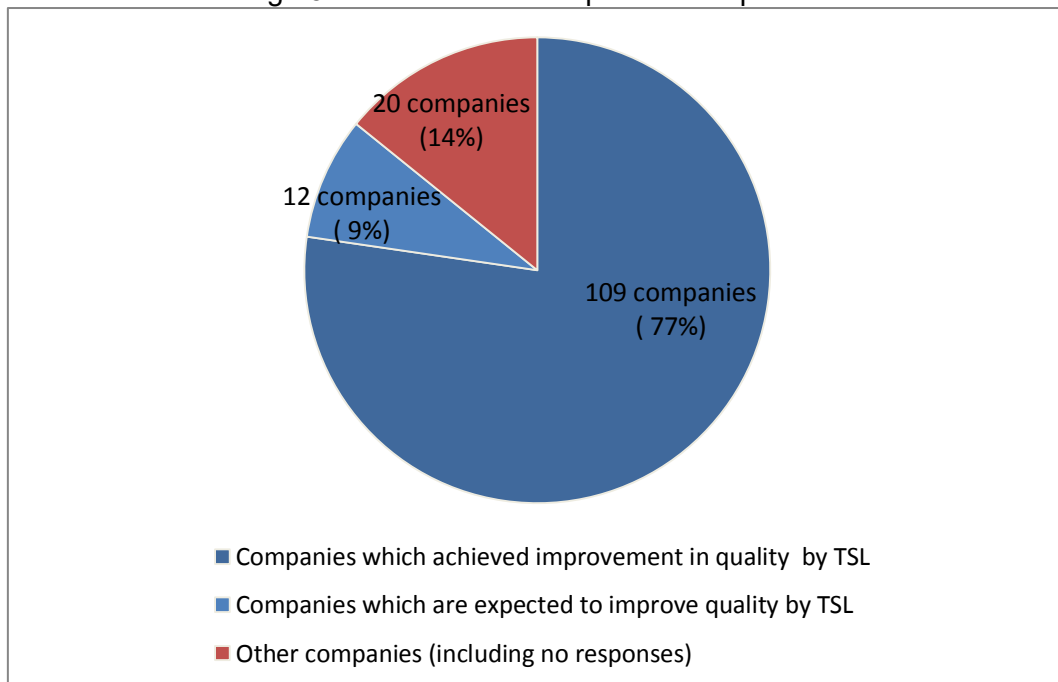
As shown in the following chart prepared based on the answers to the questionnaire, about 80% of the end-borrowers have achieved or expected to achieve improvements in qualities, increases in productions and sales.

Fig 14 : Effects of TSL on production amounts



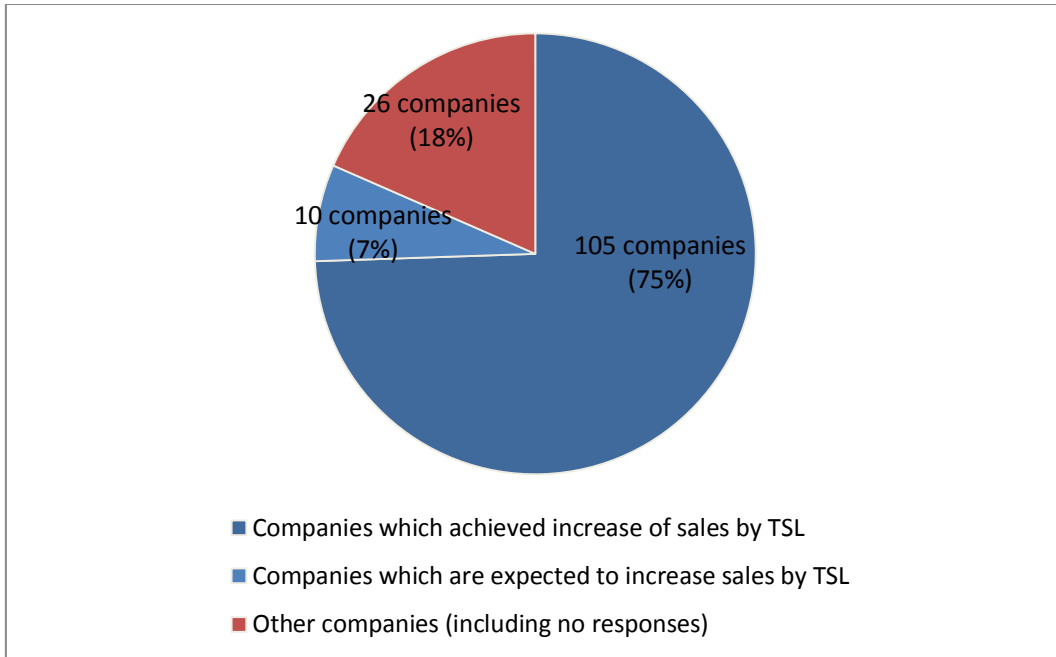
Source : Prepared by the study team based on the responses to questionnaire

Fig 15 : Effects of TSL on production qualities



Source : Prepared by the study team based on the responses to questionnaire

Fig 16 : Effects of TSL on sales

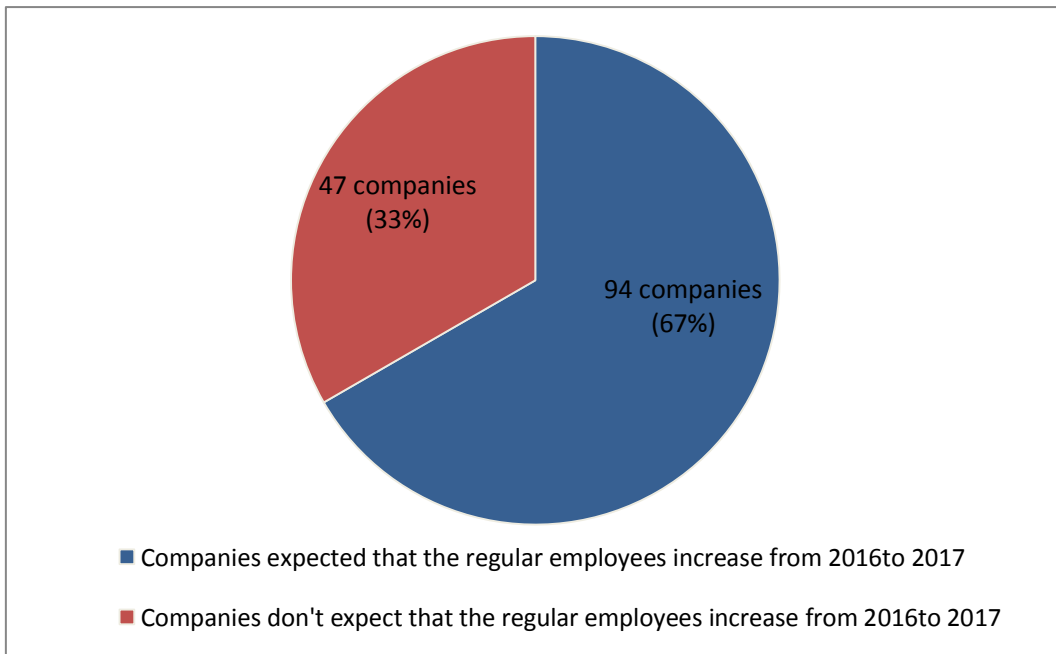


Source : Prepared by the study team based on the responses to questionnaire

(2) Effects on employment

As shown in the following chart prepared based on the answers to the questionnaire, about 70% of the end-borrowers expected that the regular employees increase from 2016 to 2017.

Fig 17 : Expectations in the increase in regular employees



Source : Prepared by the study team based on the responses to questionnaire

### 2-2-3 Issues recognized through interviews

As described above, it is confirmed through interviews that many end-borrowers have achieved improvement of quality, increase of number of employees, production amount and sales using the funds from TSL. However, several issues were identified through this study.

#### (1) Collaterals

During the interviews, some interviewees mentioned that collateral evaluation procedures take long time on. Some interviewees also mentioned that PFIs requested additional collaterals because collateral values were not sufficient for applied loan amounts. Such collateral requirements by PFIs would have made it difficult for end-borrowers to obtain loans.

In addition, some end-borrowers claimed that the loan amounts provided by PFIs to end-borrowers were only about 30% of collateral values in general.

### 2-2-4 Other points confirmed through survey

During the interviews, some interviewees mentioned that loan funds were insufficient for the capital investments they planned and they needed to use their own funds and additional loans. Other end-borrowers also mentioned that they needed additional loans in order to make new capital investments. Similarly, 28 end-borrowers which answered to the questionnaire mentioned that the amount of the loan was not sufficient, or they needed more loans. Based on these survey results, it was found that there are strong demands for loan funds even after loans were provided through the TSL project.

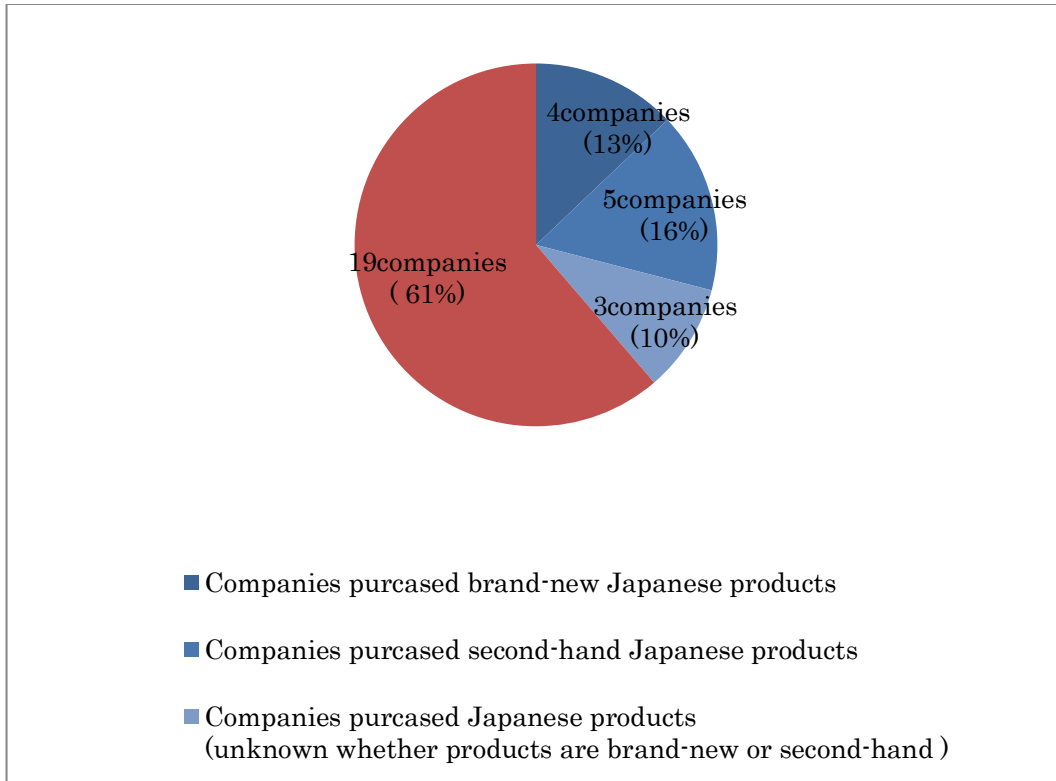
### 2-2-5 Relationship between end-borrowers and Japanese companies

#### (1) Procurements of Japanese products

As shown in the following chart, more than 30% of the interviewee end-borrowers, (12 companies) mentioned that they have purchased products of Japanese companies, such as machineries, construction machines, agricultural machines and vehicles, using TSL funds. Among these companies, there were some companies which mentioned the quality of products had been improved by introducing high quality Japanese equipment.

Although there were many companies in Myanmar which wish to purchase high quality Japanese products, some of them gave up buying such products due to the high costs. Others purchased second-hand Japanese products, whose costs were affordable. Actually, five interviewee companies purchased second-hand Japanese products and introduced high quality equipments.

Fig 18 : Procurement of Japanese products by TSL funds



Source : Prepared by the study team based on the responses to interviews

(2) Export to Japan

Among 31 interviewee end-borrowers, one company, which is doing a labor intensive sewing business, answered that they export most of its products to Japan. However, other end-borrowers in manufacturing industries mentioned that it was difficult for them to fulfill the quality requirements in other countries, and that export to foreign countries including Japan was not possible.

On the other hand, there were some end-borrowers who wished to export their products to foreign countries including Japan, after achieving quality improvements.

In fact, there were several end-borrowers which had acquired or intended to acquire international quality standards, such as ISO 9001, HACCP, and Good Manufacturing Practice. In addition, some companies answered that they had negotiations on the exports to Japan and provided production samples. Therefore, it is expected that some end-borrowers start exporting products to Japan in the future.

(3) Other relationship with Japanese companies

Among 31 interviewee end-borrowers, four companies in a construction or a construction material industry answered that they were doing or planning to do business with Japanese companies such as for the construction and maintenance of Thilawa Special Economic Zone, the implementation of other construction projects in Myanmar, and manufacturing of construction materials.

Some of interviewee had clear policies on obtaining orders from Japanese companies.

In addition, there were some end-borrowers in the manufacturing industry which were trying to start negotiations on technical collaboration with Japanese companies.



## 2-3 Issues and possible improvements in ODA loan projects in SME financial function enhancement project based on 2-2

### 2-3-1 Enhancement of understanding of the concept, frameworks, and requirements of TSL

Through the interviews, it suggests that the end-borrowers did not properly understand the concept, framework, and requirements of TSL. Therefore the enhancement of such understanding through more detailed explanation would be needed.

### 2-3-2 Strengthening of monitoring of fund use

As mentioned above, there were some end-borrowers which used the loan funds for the capital investments of other companies. There were other end-borrowers which used more than 20% of the total loan amounts for working capital or which used loan funds for other capital investment purposes which were not described in loan applications. One of the reasons behind such problems is that PFIs did not confirm the loan purposes of end-borrowers.

Therefore, in order to solve such problems, it would be necessary to make sure that PFIs monitor the use of funds.

### 2-3-3 Execution of loans proportional to each company's creditworthiness

In the current SME-TSL project, PFIs are supposed to monitor how end-borrowers use funds, based on the operation guidelines.

In the loan appraisals, PFIs are supposed examine whether loan purposes that applicants declared in loan applications meet the conditions of the TSL.

After loan disbursements, PFIs are also supposed to prepare reports on the status of end-borrower's capital investment projects, using predetermined formats. Such reports will explain purposes, places and amounts of capital investments carried out by end-borrowers.

When end-borrowers completed capital investments, PFIs then need to prepare reports on end-borrower's actual use of funds including actual amounts, timing of investment and other detailed information, and submit them to PMU. Such reports also include information on the activities actually carried out by PFIs for the monitoring purpose.

In addition to the monitoring activities mentioned above, PFIs examines the actual use of funds, reviewing evidence documents of investments. End-borrowers are obliged to submit evidence documents of capital investments, such as receipts and invoices, as described in the operation guidelines.

Although monitoring activities and procedures are defined in operation guidelines, as described above, there are some issues in the monitoring by PFIs. As explained in 2-2-3, end-borrowers used the loan funds for capital investment of other companies or they used the loan funds for working capital rather than capital investments.

For this point, it is beneficial to revise the formats used for monitoring activities and provide guidance on implementation method of monitoring activities.

### 2-3-4 Promoting competition among PFIs

One of the underlying issues behind the problems mentioned above would be the fact that the financial market is dominated by lenders. In order to improve the financial market environment, improvement in Myanmar's financial system, such as liberalization of interest rates or liberalization of funding would be

necessary.

In order to fill the demand gap in the financial market, it would be essential to increase the TSL project budget. It would be also beneficial to introduce a competition mechanism to PFIs through revising the fund allocations of PFIs and also by revising the PFIs themselves.

## 2-4 Possible improvements on loan criteria and documents used in TSL based on the suggestions in 2-3

### 2-4-1 Preparation of a guidelines for reviewing the use of funds

As mentioned above, the confirmation of the use of loan funds by PFIs were not necessarily sufficient. One of the reasons would be the fact that the policies, methods and processes on the confirmation of the use of loan funds were not clear enough.

Therefore, when implementing a TSL project, it is essential for each PFI to prepare guidelines on the confirmation of use of loan funds and also to carry out such monitoring on the use of loan funds according to the guidelines. When preparing such guidelines, it is recommended to review the existing workflows and formats for the monitoring of end-borrowers and to revise them upon necessity.

## Chapter 3. Credit Guarantee System in Myanmar

### 3-1 Preexisting Policies and Schemes Related to Credit Guarantees in Myanmar

#### 3-1-1 Overview of Credit Guarantee Insurance (CGI), provided by Myanmar Insurance (MI)

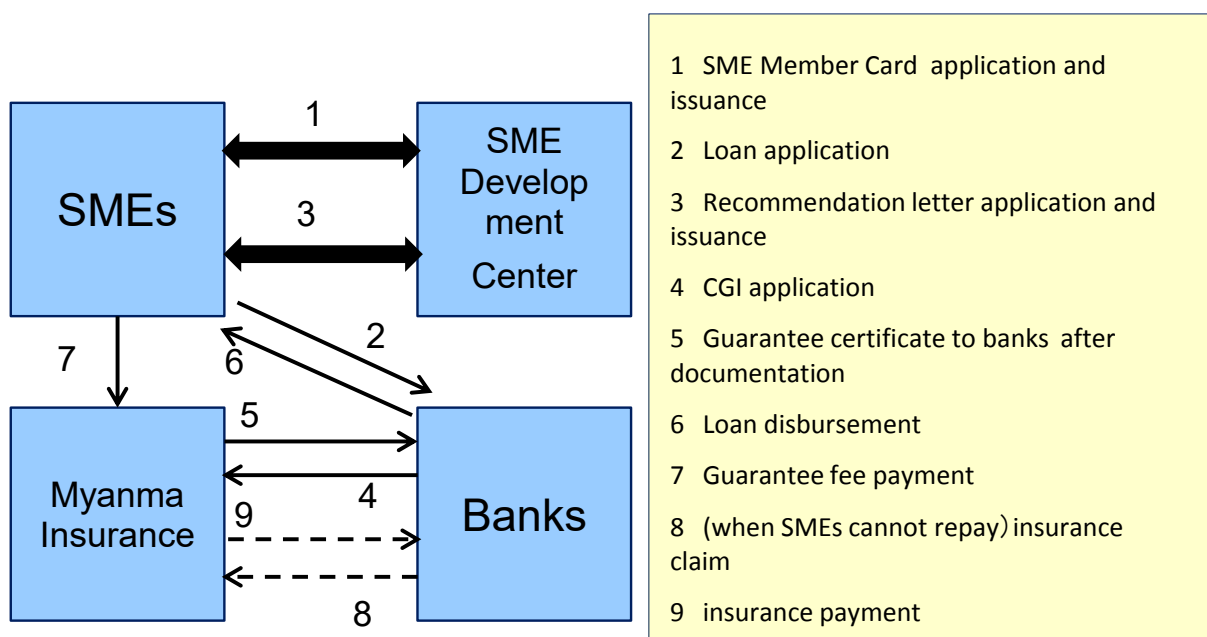
Currently, state-owned insurance company Myanmar Insurance (MI) provides Credit Guarantee Insurance (CGI), which Commercial banks can use in lending for SMEs. Although MI started to sell CGI in June 2014 in order to expand bank loan for SMEs, there have been no use of previous CGI scheme because insurance payment was limited up to 60% of bank final loss, which commercial banks found it less attractive. As maximum amount of insurance payment was changed into 60% of guaranteed loan amount in September 2015, the number of CGI policies has increased since 2016.

#### 3-1-2 Guarantee Scheme of CGI

Any SMEs defined by Small and Medium Enterprises Development Law can use CGI, since CGI was introduced to expand bank lending for SMEs..

Below is interaction chart of credit guarantee under the CGI scheme.

Fig 19: Interaction Chart of Credit Guarantee under the CGI Scheme



Sources: Created by the consultant team based on interview with organizations in interest

As a noteworthy characteristic of CGI, they can point out that SME Development Center, which is SMEs development agency under the Ministry of Industry, takes part in application of CGI. SMEs which demands guarantee by CGI have to fill out application form of SME Member Card and get it issued in advance (Fig 18 No.1).

Items to be registered on application form of SME Member Card are below.

- Company information (name of company, date of establishment and date of commercial operation, ownership, business overview, etc.)

- Individual information of the owner(name of owner, address, etc.)
- Other information of business(depending on business sector)

Fig 20: SME Member Card  
(Surface)



(Back)



Source: photos taken by the consultant team

In application of CGI, SMEs have to submit required documents and get recommendation letter issued (Fig 18 No.3). Major required documents are below. SME Member Card is valid in 2 years.

- application form
- business overview
- license issued by district where the company operates
- photocopy of SME Member Card (both sides)
- Photocopy of the owner ID card
- tax certificate
- (for manufacturing business ) list of immovable assets

SMEs submit to banks documents such as financial statements and business plan to be screened after they got recommendation letter issued by SME Development Center. The documents are to be investigated by MI head office in Yangon after screening by bank (Fig 18 No. 4). When MI approves guarantee, MI issues policy wording for banks (Fig 18 No. 5). If loan term exceeds 1 year, insurance contract is to be renewed every year. While they can renew the contract in the second year, in the third year, MI will investigate the applicant SMEs once again.

After banks provide loan to SMEs (Fig 18 No. 6), and SMEs pays guarantee fees to MI (Fig 18 No. 7), when SMEs cannot pay back that loan, lender banks can claim insurance payment to MI (Fig 18 No. 8). The loss happens despite collateral execution, MI will pay insurance whose maximum amount is up to 60% of loan amount (Fig 18 No. 9).

As was mentioned above, under the current CGI scheme, up to 60% of loan amount will be guaranteed when debtors cannot pay it back. However, some banks have their own regulation that limits the amount of loan to be guaranteed. For instance, CB Bank, one of the CGI-user banks, uses CGI for up to 20million Kyat loan. In addition, insurance payment will be fixed after collateral execution if there is collateral with the loan.

One of the product characters is that it is possible for banks to lend with no collateral thereby. SMEs with few collateral assets have had to rely on microfinance institutions with high interest rate because banks fundamentally require strong collateral in lending due to CBM regulations. In that sense, there are quite a few SMEs which could lend from banks for the first time and banks are able to extend their customer base thanks to CGI.

### 3-1-3 Utilization of CGI

As of the end of May 2017, 84 loans with CGI have been provided, 17 loans were prepared by banks after CGI approval, and 199 CGI applications were on investigation. Also, SME Development Center has issued 1,479 recommendation letters and 8,500 SME Member Cards. Since the first loan with CGI was made in March 2016, CGI utilization has spread rapidly.

By contrast, only 3 commercial banks have used CGI in lending their money to their customers; CB Bank (the number of loans with CGI: 80), KBZ Bank (3), SMIDB (1) and almost all of the loans were provided by CB Bank. Though most of CGI loans are no-collateral and relatively small with 10~20 million Kyat, KBZ Bank have provided 100million Kyat with CGI at 1loan.

## 3-2 Overview of Myanmar Insurance

### 3-2-1 History

MI was established in 1952. At the beginning MI provided exclusively life assurance but started to undertake non-life insurances later. In 1964 the millitary ruling era, Myanmar government integrated insurance business into MI and prohibited private sector players from running insurance business. Insurance business was reopened for private sector in 2013. Also as of June 2017, it is planned to open insurance business for foreign enterprises, which right now are allowed to run insurance business only within special economic zones.

### 3-2-2 Supervision and Governing Law

MI is public corporation under the Ministry of Planning and Finance, MoPF and supervised by the Deputy Minister of MoPF. While private insurance companies are regulated by Insurance Business

Regulation Board (IBRB) and Financial Regulatory Department (FRD), both of which are under the MoPF, MI is independent from regulations from IBRB and FRD.

The governing law of MI is The Myanmar Insurance Law (The State Law and Order Restoration Council Law No.10/93).

### 3–2–3 Organizational Structure

The Board of Directors is responsible for MI decision making. Based on The Myanmar Insurance Law, the central government shall form the Board of Directors and determine its chairman and secretary, and their tenure.

MI has four departments divided in accordance with insurance products which each department undertakes; Fire & Engineering Insurance, Maritime Insurance, Motor Insurance and Life Insurance. MI has totally 40 offices; the head office at Yangon and 39 branches around the nation. The head office has approximately 500 employees and 39 branches has about 300 employees in sum.

### 3–2–4 Business Overview

According to The Myanmar Insurance Law, MI shall undertake the following 17 kinds of insurance products.

- Life Assurance
- Third Party Liability Insurance
- General Liability Insurance
- Fire Insurance
- Marine Cargo Insurance
- Marine Hull Insurance
- Aviation Insurance
- Engineering Insurance
- Comprehensive Motor Insurance
- Oil and Gas Insurance
- Cash-in-transit Insurance
- Cash-in-safe Insurance
- Fidelity Insurance
- Travelling Insurance
- Bodily Injury Insurance
- Other classes of Insurance
- Insurance determined by the Ministry[of Finance and Planning]

### 3-2-5 Financial Situation

MI makes their own financial statements, however they are not open in public. Approximately 60% of total insurance premium revenue comes from insurance products undertaken by Fire & Engineering Insurance Department. Share of life assurance revenue is more or less 10% of total insurance premium revenue.

### 3-3 Current Situation of CGI(Legal System and Internal Procedures within MI)

#### 3-3-1 Governing Laws and implementation regulations of CGI

CGI is classified as “Insurance determined by the Ministry [of Finance and Planning]” and Ministry of Planning and Finance issued instruction of CGI.

According to interview with the person in Financial Institutions Supervision Department, although CBM has tacit approval that banks can provide no-collateral loans by CGI, it have not enacted any laws or regulations admit no-collateral loan through CGI scheme.

#### 3-3-2 Internal Procedures regarding to CGI within MI

##### (1) Department in Charge

Both MI head office and branch offices accept CGI application from banks. While in Japanese system, SMEs can apply both to credit guarantee corporations and to financial institutions, in the CGI scheme commercial banks apply to MI. At the MI head office, Fire & Engineering Insurance Department is responsible for off-site CGI-related tasks such as investigation of documents. According to the person in charge of CGI, there are 4 persons who take care of CGI at the head office as of June 2017, none of whom are dedicated staff. Also, there is no plan to employ or distribute new staff for CGI tasks. On the other hand, MI branch offices are responsible for on-site monitoring.

##### (2) Guarantee Fee

Guarantee fee rate for SMEs is determined as below. MI does not decide it in accordance with risk of each SME. Even if SMEs redeem their debt earlier than the initial due, insurance premium cannot be reimbursed.

Fig 21: Guarantee Fee Rate (% of loan amount)

Year	Without collateral	With collateral
1	3	2
2	2.5	1.5
3	2.0	1.0

Sources: created by the consultant team based on interview with MI

##### (3) Financial Statements

Although MI does not disclose financial statements, it manages CGI separately from other kind of items. Accumulated insurance premium revenue of CGI until June 2017 is 8,175 thousand Kyat.

#### (4) Operation Manual for Investigation and Insurance Payments

There is no operation manual or guideline dedicated for CGI.

#### (5) Insurance Payment Date

According to the policy wording by MI, banks have to inform MI of it within 30 days once the debtors get unable to repay. However, how MI approves insurance payment is unclear because there is no reference to the definition and banks' reporting obligation of default at the policy wording. Right to insurance claim will be invalid if banks do not use the right within 1 year after the report.

As was mentioned earlier, it is not until bank loss is fixed that MI fixes insurance and do payment under the CGI scheme. According to interview with some banks, it typically takes several years to dispose pledged assets as collateral by auction.

MI manages guaranteed credit data by Microsoft Excel not by dedicated database. Banks have to report to MI if SMEs repayment is delayed more than 1 month. There is no dedicated reserve fund for CGI because CGI reserve is accumulated as a part of MI general reserve fund.

#### (6) Sales Channel of CGI

Both MI head office and branches accept CGI application by banks. However as of June 2017, all the CGI applications are made from just 5 regions; Yangon, Ayeyawady, Bago, Mandalay and Magway. When MI starts to sell CGI, it explained of CGI to 6 commercial banks; CB Bank, KBZ Bank, SMIDB, AYA Bank, Myanmar Citizens Bank, Myanmar Oriental Bank. Right now, SME Development Center and CGI-user banks promote CGI to SMEs through seminar.

### 3-4 Attitude toward CGI of Myanmar Government Agencies and Commercial Banks

#### 3-4-1 Attitude of Government Agencies

##### (1) Myanmar Insurance

Attitude of MI toward CGI is ambivalent. When the consultant team proposed an idea that they would provide specific part of Two Step Loan with CGI, MI staff reaction was relatively positive. On the other hand, a person in charge of CGI tasks stated that they did not themselves of being responsible CGI.

##### (2) SME Development Center

SME Development Center, which participates in CGI application, positively tries to issue more SME Member Cards and recommendation letters. Also, it understands that CGI is of importance in indirect finance for SMEs. However, some banks and SMEs which have used CGI represent that it takes time for the Center to finish documents procedures, which suggests that it may be necessary to improve the procedures.

#### 3-4-2 Attitude of Commercial Banks

##### (1) CGI-User Banks

Among current CGI-user banks, CB Bank, which has provided the largest number of CGI loan, takes forward-looking attitude toward no-collateral loan with CGI. That may be partly because CB Bank has sense of urgency against the fact that its total asset and number of branches are smaller than its competitors like KBZ and AYA Bank. CB Bank is assumed that they would like to reach SMEs by



introduction of CGI. Other 2 CGI user banks; KBZ and SMIDB are said to be so negative against CGI utilization that they have not seen successive loans after a few loans guaranteed.

## (2) Non CGI-User Banks

Non CGI-user banks stated that they did not want to run the risk of unsecured amount of loan despite guarantee by CGI and there was no advantage like additional interest for no-collateral loan with CGI. On the other hand, some banks exhibit understanding for an idea that banks can avoid loss if they require collateral and use CGI.

### 3-5 Establishment background of credit guarantee systems and their utilizations in Japan and neighboring countries

#### (1) Credit Guarantee Schemes in Southeast Asian Countries

In a lot of Southeast Asian countries, credit guarantee schemes began to be developed from 1970s. The figure below represents current credit guarantee schemes in ASEAN member countries (except Brunei and Singapore).

Fig 22 : Credit Guarantee Schemes in ASEAN countries

Country	Existence of Credit Guarantee	Overview
Cambodia	N	The government referred to establishment of credit guarantee at Industrial Development Policy until 2024
Indonesia	Y	State-owned credit guarantee corporations (“Jamkrindo”), private guarantors, and guarantee institutions of local governments provide credit guarantee. Recently users of special credit guarantee program (“KUR”) are increasing (*to be mentioned later)
Lao PDR	N	Both credit guarantee and credit information bureau are still undeveloped
Malaysia	Y	CGC (Credit Guarantee Corporation) provides credit guarantee. CGC is funded jointly by the central bank and private banks
Myanmar	Y	State-owned insurer, Myanmar Insurance provides CGI
Philippines	Y	State-owned financial company (Small Business Corporation) and Credit Surety Fund established by coop, NGO and banks provide credit guarantee
Thailand	Y	TCG (Thai Credit Guarantee Corporation), under the Ministry of finance provides credit guarantee. They guarantee SMEs in the scheme of “portfolio guarantee”, for innovative companies and for companies operating at Special Economic Zones
Vietnam	Y	State-owned VDB (Vietnam Development Bank) and local governments provide guarantee separately. VDB have not given guarantee since 2011

Source : Asian Development Bank “Asia SME Finance Monitor 2014”, Keiichi FUJITA & Seigo ITO 「ラオスにおける金融アクセスの現状と課題」 (July 2017, PRI Discussion Paper Series)

(No.17A-11)), PricewaterhouseCoopers 「中小企業・小規模事業者の海外展開に係る金融環境等に関する調査事業 最終報告書」 (October 2015), et al.

Credit guarantee schemes in Japan, Indonesia and Philippines will be explained from the following sections on.

(1) Establishment background of the credit guarantee system and its utilization in Japan

(i) Background and overview of the credit guarantee system in Japan

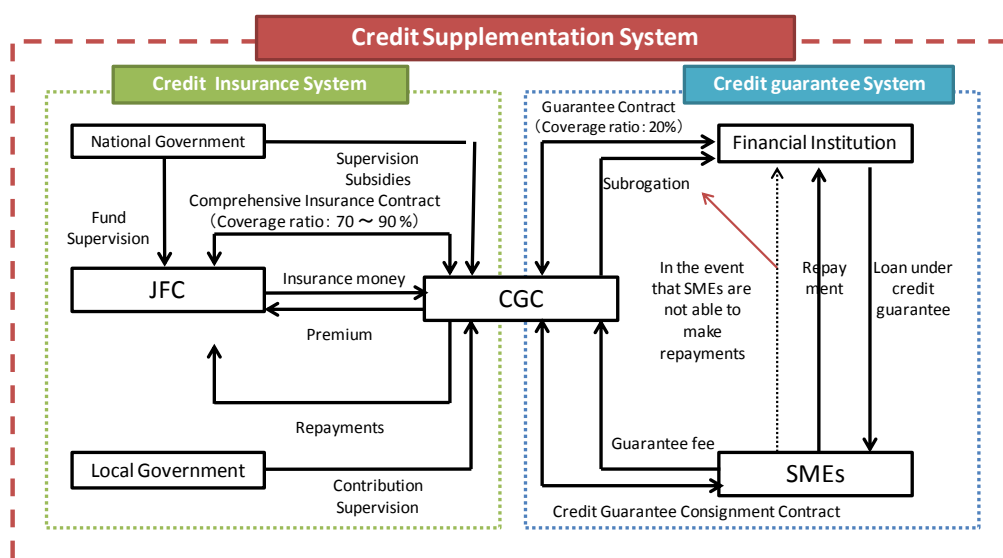
The credit guarantee system in Japan, which was first established in 1937, has been regarded as one of the measures to enhance the access to finance of small and medium enterprises since 1948. Since then, credit guarantee associations were established in all prefectures in Japan.

As of 2015, at least one credit guarantee association exists in each prefecture in Japan and the number of total credit guarantee associations in Japan is 51. The overall outstanding credit guarantee amounts are slightly decreasing, but it still consists of 10.9% of the overall loan balances in Japan. The statistics also says the proportion of the SMEs which obtain loans utilizing credit guarantees is 37.1%.

One of the characteristics of the Japanese credit guarantee system is the collaboration between “credit guarantee” and “credit insurance” which can be depicted in the following diagram.

When credit guarantee associations in prefectures issue credit certificates, the certificates covers 80% of the credit risks of the relevant loans. Then, the credit risks born by associations tend to be big. In order to avoid excessive concentrations of credit risks at credit guarantee associations, Japan Finance Corporation, a governmental financial institution, has provided “credit insurance” to credit guarantee associations, which covers 70-90% of the credit risks taken by credit guarantee associations.

Fig 23: Overview of the credit guarantee system in Japan



Source: Japan Economic Research Institute (2013), Basic Study on Financial Inclusion in Indonesia

The maximum amount of a credit guarantee issued by a credit guarantee association in Japan is JPY 80 million (approximately USD 0.7 million) when unsecured and JPY 200 million (approximately USD 1.7 million) when secured by collaterals. The guarantee fees, which are determined by the assessment results of “Credit Risk Database”, vary from 0.45% to 1.90%. There are not any upper limits of loan interest rates.

(ii) Credit guarantee application and appraisal processes

In most cases, SMEs submit applications of loans and credit guarantees to financial institutions. Financial institutions carry out their own loan appraisals and then send credit guarantee application documents with their comments to credit guarantee associations. Credit guarantee associations examine the business status and business plans to make decisions on credit guarantee, before issuing credit guarantee certificates.

(iii) Guarantee claims and reimbursements

If the borrower SMEs are unable to repay loans, financial institutions make guaranteed claims, and then credit guarantee associations make reimbursements. The amount of reimbursements is 80% of loan amounts, as mentioned above.

Upon such reimbursements, the ownerships of loans and collaterals are transferred from the financial institutions to credit guarantee associations.

(iv) Debt recovery after guarantee claims

As the ownerships of loans and collaterals are transferred from financial institutions to credit guarantee associations, credit guarantee associations carry out debt recovery procedures, including disposal of collaterals.

(2) Establishment background of credit guarantee system and its utilization in a neighboring country (an example of Indonesia)

In this section, examples of the credit guarantee system in Indonesia are explained. In Indonesia, there are several public and private credit guarantee corporations, such as Jamkrindo (Jaminan Kredit Indonesia, Credit Guarantee Indonesia) a state owned credit guarantee corporation, and Penjamin Kredit Pengusaha Indonesia, a private credit guarantee corporation. There are a few local credit guarantee corporations established by local governments, such as PT Jamkrinda Jatim and PT Jamkrinda Bali Mandara.

In addition, the government is running a special credit guarantee program called as KUR (Kredit Usaha Rakyat or People's Business Credit), which has been increasing its guarantee balances recently.

This section mainly explains the credit guarantee system by Jamkrindo or the state-owned credit guarantee corporation and KUR, the special credit guarantee program by the government of Indonesia.

1) Credit guarantee by Jamkrindo, a state-owned credit guarantee corporation

(i) Background and overview of the credit guarantee system

Jamkrindo (Jaminan Kredit Indonesia, Credit Guarantee Indonesia) was established in 1985, and the current form of Jamkrindo was formulated in 2008 after several reorganizations. Jamkrindo has wide ranges of branch networks in Indonesia and it operates about 70 branches in the country. Jamkrindo provide its own credit guarantees to SMEs and it also provide credit guarantee under KUR. The credit guarantee provided by Jamkrindo covers maximum 75% of loan amounts with 1.5% of guarantee fees.

(ii) Application and appraisal processes

When borrowers apply for loans and credit guarantees, they submit applications to financial institutions. After financial institutions reviewed application documents, the financial institutions submit the documents with their comments to Jamkrindo. Jamkrindo then reviews credit guarantee application documents, to examine the creditworthiness of borrowers. If the appraisal results are not very sufficient, Jamkrindo decreases the coverage amount (from 75%) or increase credit guarantee fees.

(iii) Guarantee claims and reimbursements

There is no clear information on how long it takes from the guarantee claims to the reimbursements.

As financial institutions and Jamkrindo carry out debt collections together, the ownerships of loans and collaterals do not seem to be transferred from financial institutions to Jamkrindo.

(iv) Debt recovery after guarantee claims

As mentioned above, financial institutions and Jamkrindo carry out debt collections together, including disposals of collaterals.

The amounts recovered from loans are divided to financial institutions and Jamkrindo according to the credit guarantee coverage. If the credit guarantee coverage is 75%, 75% of recovered loans goes to Jamkrindo and remaining 25% goes to financial institutions.

(v) Others

In the Philippines, Small Business Corporation (SBC), a state-owned financial institution and a credit guarantee company, provides credit guarantees. SBC carries out its own credit guarantee appraisals before making decisions, reviewing all necessary documents, such as financial statement and information of business and collaterals. It has been pointed out that it takes about three month for SBC to complete appraisals.

Therefore, it is estimated that Jamkrindo, which also carry out credit guarantee appraisals by itself also need a few months to complete its appraisals.

2) Credit guarantee program by the government of Indonesia, KUR<sup>15</sup>

(i) Background and overview of the credit guarantee system

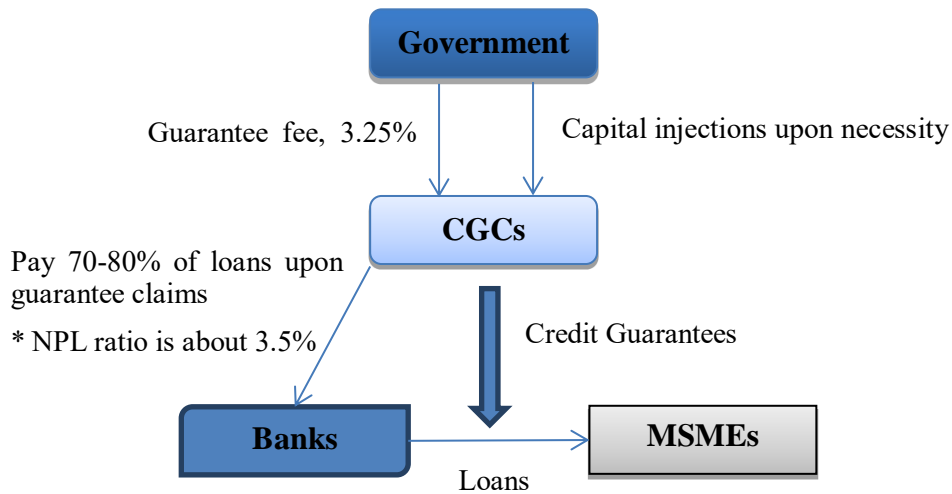
A government credit guarantee program called as KUR (Kredit Usaha Rakyat, People's Business Credit) has been getting more common in Indonesia. This is a credit guarantee program arranged by the government of Indonesia started in November 2007, in order to achieve continuous development of micro, small and medium enterprises through improving their access to finance.

In this program, the government bears credit guarantee fees. Credit guarantees are then issued by state-owned or local credit guarantee corporations automatically after the loan decisions are made by financial institutions. Therefore, the credit guarantees under this program are widely accepted by many financial institutions and MSMEs.

---

<sup>15</sup> This section was prepared based on "Basic Study on Financial Inclusion in Indonesia" by Japan Economic Research Institute (2013).

Fig 24: Overview of KUR



The percentage covered by credit guarantee is 80% for agriculture, fishery and forestry and 70% for other industries. Other credit guarantee conditions are as in the following table.

	For micro enterprises: KUR Micro	For medium and small enterprises: KUR Retail
Maximum guarantee amount	IDR 20 million <sup>16</sup>	IDR 500 million <sup>17</sup>
Maximum loan interest <sup>18</sup>	22%	13%
Collaterals	Not allowed	Allowed

As credit guarantees cover only 70-80%, there are some financial institutions which cover the remaining 20-30% by collaterals, such as real estate.

As of 2013, the amount of guaranteed debt by KUR was approximately 112 IDR trillion and the number of KUR users was 8.46 million. Guaranteed debt amount per user was about 13.23 IDR million (approx. 22.48 JPY million).

(ii) Application and appraisal processes

Borrowers apply for credit guarantee when they apply for loans. After financial institutions reviewed application documents, financial institutions submit the credit guarantee application documents to one of the credit guarantee corporations. The credit guarantee corporation which received the application documents issues credit guarantee certificates automatically without carrying out any appraisals.

(iii) Guarantee claims and reimbursements

Financial institutions issue guarantee claims when the relevant loans are categorized as “4<sup>th</sup> category” whose overdue dates are from 120 to 180 days and when borrowers are bankrupted. If all necessary

<sup>16</sup> Approximately USD 1,500.

<sup>17</sup> Approximately USD 37,000.

<sup>18</sup> This is higher than ordinary loan interest rate, which stands at 11%.

documents for guarantee claims are appropriately prepared, credit guarantee corporations make reimbursement within 15 business days. However there are some banks which claim that it takes a few months to receive the reimbursements.

(iv) Debt recovery after guarantee claims

Although there are no specific rules, financial institutions and credit guarantee corporations carry out debt collections together, including disposals of collaterals. The amounts recovered from loans are divided to financial institutions and the credit guarantee corporations according to the credit guarantee coverage.

(v) Others

Credit guarantee corporations receive 3.25% of credit guarantee fees from the government, while they lose about 3.5% for the reimbursements for non-performing loans. Therefore, credit guarantee corporations make losses from this credit guarantee program. In order to compensate such losses, the government sometimes injects additional capitals.

Moral hazard issues have been pointed out both at borrower side and at lender side. Some MSMEs tend to reluctant to make repayments once they knew that the loans were made under the government credit guarantee program. There are some financial institutions too whose non-performing loan ratio reached up to 15% most possibly due to the moral hazard issue.

### 3-6 Demands for Credit Guarantee System

Bank loan is not major way for SME finance in Myanmar. According to the survey in 2015 by German Institution for Development Evaluation (DEval), just about 20% of SMEs have borrowed from banks<sup>19</sup>. Also, for banks it is risky to finance SMEs with small collateral margin. Considering these situations, credit guarantee system will contribute to activation of indirect finance SMEs and what is more, to Burmese economic development by playing role of an enabler for no or less collateral loan. Demands for credit guarantee from SMEs and commercial banks will be stated in detail below.

#### 3-6-1 Demands from SMEs

For SMEs, credit guarantee system is strongly needed in sense of collateral and interest rate. As mentioned before, CGI is virtually sole no-collateral scheme. It is important for finance from banks by SMEs, a lot of which had difficulties of it due to their poor collateral margin.

In this survey, SMEs which have borrowed money from banks by CGI were interviewed about utilization and opinion of CGI. Most of them have never used bank finance and relied on their own fund or microfinance institutions with high interest rate when they demanded finance for starting or expanding of their business. The interest rate of microfinance lenders are generally 2.5-3.0% per month. It is much higher than 13% per annum; the maximum loan interest rate of commercial banks, and is less favorable in considering with real rate 16% of CGI (interest rate 13% + guarantee fee 3%). Few of CGI user SMEs have complained of interest rate of CGI.

On the other hand, loan amount provided by banks are generally 10-20 million Kyat. SMEs usually use this loan as working capital such as material because it is hard to do overall capital investment such as factory building or purchase of machinery. Also, quite a few SMEs have trouble with repayment since loan term is limited to 1 year and if they want to finance more than 1 year, banks make loan after principal repayment. Effectivity of current CGI for business expansion and starting of brand-new

---

<sup>19</sup> DEval "Small and Medium Enterprise Survey Myanmar 2015"(October, 2015)

business of SMEs may be limited. It shall be necessary to increase guaranteed loan amount and to guarantee long term finance with more than 1 year.

### 3-6-2 Demands from Commercial Banks

Commercial banks will demand credit guarantee system in aspect of customer base extension and more probability of debt collection. They will get able to finance SMEs with no or limited collateral margin, and when they can not collect their debt fully, their loss is filled partly by credit guarantee system.

However, few banks are risk-taking since loss may happen on banks in case of no-collateral loans. In effect, some banks stated that under the less competitive environment due to current strict lending regulations, they have no positive reason for daring to do no-collateral loan with CGI. It will be necessary to establish system where banks can supplement their loss by partial collateral coverage, to create regulatory system which is pro-competitive among banks and to reinforce risk management capacity of banks.

### 3-7 Challenges in introducing a credit guarantee system

#### 3-7-1 Challenges of current CGI

Although CGI is the only way for no-collateral loan by banks, its number of its use is much smaller than 40 thousand SMEs (based on the survey in 2014)<sup>20</sup> and it is not as helpful as it can be for SME finance.

The figure below divides CGI scheme into its components and summarize each current situations and challenges.

---

<sup>20</sup> Asian Development Bank “Asia SME Finance Monitor 2014”

Fig 25: Challenges of CGI Use

Component	Current Situation and Challenges
Scheme	Insurance; gurantee coverage is up to 60% of loan amount(partial guarantee)
	Most cases are small amount, hard to use for ca;ital investment and long-term loan
Governing law	The Myanma Insurance Law; special approvement by MoPF
	Instable legal system; no clear CBM regulations about no-collateral loan
Supervisor	Ministry of Planning and Finance
Finance	Reserve is part of general reserve fund
	Confidential finaical statement; hard to grasp finaical situation
	Guarantee fee depends on loan term and collateral
Application	Many required documents, getting and submitting by paper base
	Approcvl takes time; multiple application windows
Investigation and debt management	No investigation manual
	As many as 4 staff at the head office, no dedicated staff
	Few cooperation b/w MI and banks; hard to manage
Insurance payment and debt collection	Payment after cooling-off period and collateral execution(collateral loan)
	Collateral execution by banks takes much time
Infrastructure	No credit information bureau in operation (to be 2017)
	No mutual use of information at banks and SME Development Center
Publicity	Low popularity both of banks and SMEs
	Some SME get to know of CGI by seminar and via online media
	Application from limited areas
Other areas	Low credibility and negative attitude of SMEs for information disclosure
	Less incentive of banks to use CGI due to loan and collateral regulations
	Low responsiveness for SME demands; procedures at SME Development Center takes months

Source: created by the consultant team based on interview with CGI-user SMEs, banks and related organizations

### 3–7–2 Overview of new credit guarantee system

Among the challenges pointed out the previous section, the fact that loss compensation takes much time and MI has inadequate investigation capacity is critical in light of principle of credit guarantee system; preservation and development of SME finance. Establishment of dedicated organization for CGI is needed for further SME finance development since CGI is quite different from ordinary insurance products and MI capacity may turn out to be limited for ever-growing CGI use.



Fig 26: Reform flow of credit guarantee reform

Components	(now)	Reform Phase 1	~3Year	Reform Phase 2	5Year~
	Current		Short term		Medium/Long term
<b>Scheme</b>	Insurance product 60% of loan amount (partial) For small no-collateral loan	Collaboration with CGI	Insurance product For collateral/large loan guarantee (partial)	Drafting of article of corporation and rules Analysis of finance of SMEs	Credit guarantee scheme Extension of coverage /Portfolio guarantee Preferential treatment for priority sectors
<b>Governing Law</b>	The MI Law (special instruction) no CBM regulation of no-collateral lending	Drafting of revised MI Law *Negotiation with CBM, drafting no-collateral loan reg	The MI Law (parmanet CGI) Clear CBM regulation of no-collateral lending	Drafting of governing law Drafting of contract documents	Enactment of the new governing law Contract documents with details of guarantee
<b>Supervisor</b>	MoPF, MI		MoPF, MI	Making discussion material for inter ministerial meeting	MoPF
<b>Finance</b>	Part of general reserve No F/S disclosure Fixed rate of guarantee fee	Making clear MI financial condition Developing reserve management Default rate fee rate	Developing of CGI financial information Accumulation of CGI reserve Lower guarantee fee	Transfer of MI reserve Contribution from banks Setting indices for financial stability	Initial capital based on CGI reserve Riskmanagemtn by financial indices
<b>Application</b>	Many paperworks Time consuming	Developing document format Developing application guideline	Making application process easier Prevailing application guideline	Collaboration b/w guarantor and user banks	Application at banks window
<b>Investigation and debt management</b>	No credit investigation manual No dedicated staff (only 4 staff) Few cooperation with banks	Developing investigation manual Training of accounting and financial analysis Developing reporting guideline/format	Use of investigation manual Dedicated staff Higher capacity for investigation and management	Spinning-out of CGI staff of MI Making principles of guarantee Analysis and reform of debt management system	initial specialist staff for credit guarantee Higher capacity for investigation and management
<b>Insurance payment and debt collection</b>	Cooling-off period and after collateral enforcement Takes time for enforcement	Revise of policy wording *Analisys/reform of collateral system	Payment right after default (with cooling-off period) Faster collateral enforcement	Making contract form with clear payment conditions *Developing collateral system (Considering of debt collection servicer)	Subrogation by guarantor or cooperative debt collection b/w guarantor and banks (collection by debt servicer)
<b>Infrastructure</b>	No credit information bureau No mutual use of information holders	Aggregation of information of MI, banks, SME Development Center (introduction of IT system)	Operation of credit bureau (2017e) Mutual use of 3 players information	Grasping actual condition of credit bureau (Considering of reinsurance)	Partial collaboration with credit bureau (reinsurance by credit insurance)
<b>Publicity</b>	Low among SMEs and banks Online media is used Application from limited areas	Distribution of CGI leaflet Active use of online media	Higher publicity (used by SMEs in local areas and medium sale cities)	Seminar and Q&A session with Mol and banks	Higher publicity (used by contrywide SMEs)
<b>Other areas</b>	Low credibility and negative attitude of SMEs for disclosure Less incentive to use CGI Time-consuming SME Development Center proceures	Training of making F/S Strengthen monitoring by tax authority Negotiation with CBM, drafting no-collateral loan reg Collaboration with TSL Making procedures go-online with database	SME ability to prepare their tax and financial information Clear CBM regulation of no-collateral lending More user banks More SME Member Cards/recommendation letters	Loan scheme fro SMEs (new business, emergency etc.) More competitive banking sector by liberalization of interest Setting forced loan commitment for SMEs	Fulfillment of SME finance needs Higher demands for SME finance Higher incentives for banks SME finance

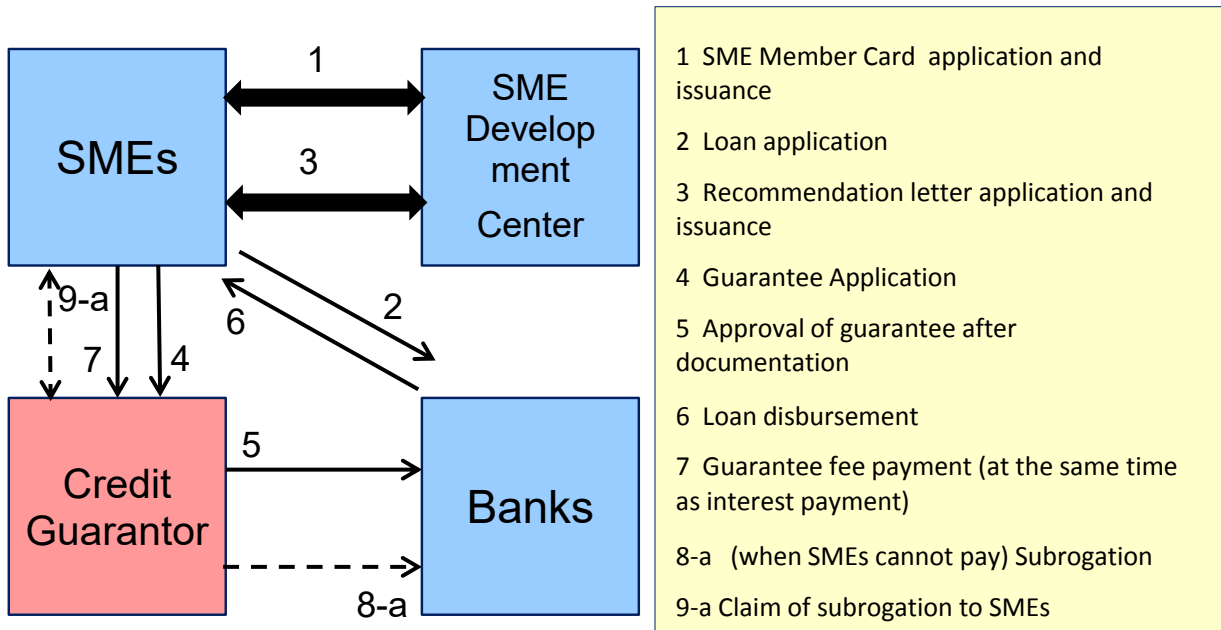
However, considering the current situation where CGI is prevailing and MI can accept CGI application from local companies by its branch network, in short term reinforcement of CGI scheme and guarantee by it will be useful for users.

A figure above represents flow for reform of credit guarantee scheme. In short term, Japanese government will support MI for each components reform (Reform Phase 1). This phase aims at CGI having fundamental elements as credit guarantee scheme within next 3 years. Then, independent credit guarantee organization (guarantor) will be built by transferring tangible and intangible assets such as fund, human resource, IT system, and credit information from MI into a new guarantor and by developing systems necessary. It should result in smooth scheme reform without expense of users convenience (Reform Phase 2).

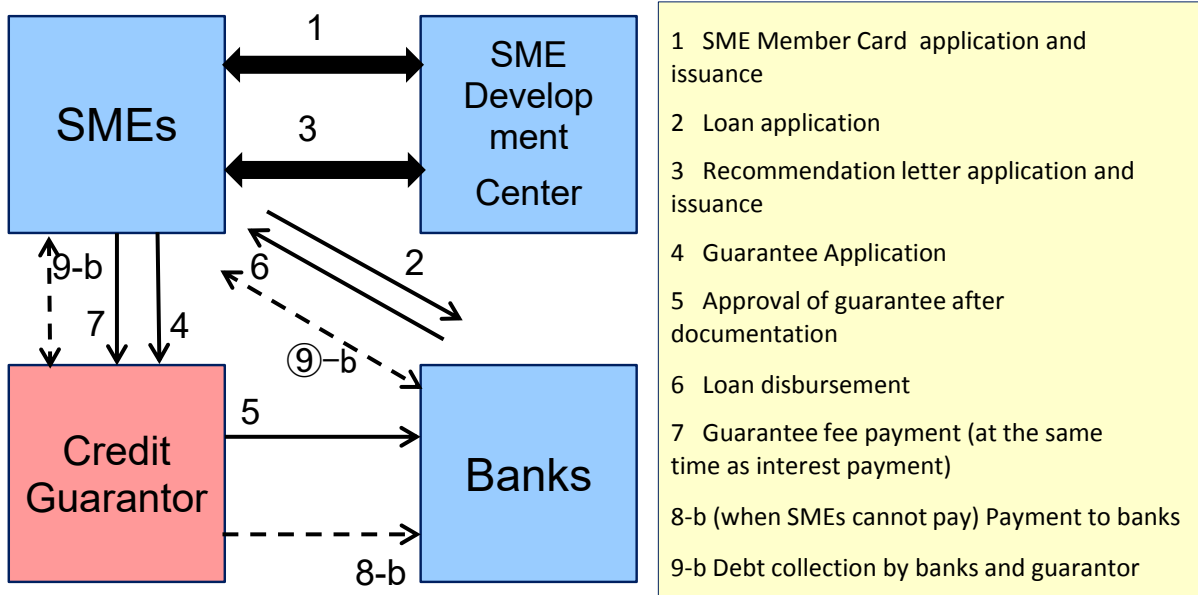
A figure below represents a draft of new credit guarantee system formulated based on Japanese and surrounding contries system. Major difference from current CGI are that SMEs apply guarantee, that a guarantor could pay in place of SMEs if SMEs cannot repay, and that the guarantor will claim its amount to debtor. We assume here 2 models; subrogation or collecting debt in cooperation with banks.

Fig 27: Draft of Credit Guarantee System

(Model 1)



(Model 2)



Source: created by the consultant team

### 3-7-3 Challenges in introducing new credit guarantee system

In this section, challenges and possible assistances by Japanese government for introducing of credit guarantee system will be summarized. Figure 26 represents reforms with multiple choices.

Fig 28: Choices of reform

Component	Choice	Recommended Choice
Scheme	Public corporation under the federal government	Public corporation under the federal government
	Special account of the federal government	
Supervisor	Ministry of Planning and Finance	Ministry of Planning and Finance
	CBM	
	Ministry of Industry	
	SME Development Center	
Finance	Reserve fund of MI	Reserve fund of MI and contribution from financial institutions(if necessary, fund from ministries)
	Fund from local bodies	
	Fund from central ministries	
	Contribution from financial institutions	
Insurance payment and debt collection	Subrogation and collection based on indemnification	(depending on collateral scheme reform, collection ability of banks and guarantor)
	Payment by guarantor, debt collection by banks and guarantor	
	Payment by guarantor, debt collection by dedicated organization	

Source: created by the consultant team

### (1) Scheme

#### [Current Situation]

Current CGI is one of the MI products to cover up to 60% of guaranteed loan amount. Most of guaranteed loans are small amount and no-collateral. It is difficult to find cases of large amount and long-term with collateral for capital investment or for starting up new business.

#### [Reform Phase 1]

In short term while it will remain MI product, it will expand its usage and user banks by collaborating with TSL for SME by JICA. By making some of loan amount with CGI and providing preferential rate for PMIs, current non-user banks can easily start to use CGI even for long-term lending.

#### [Reform Phase 2]

In medium and long term, brand-new independent governmental organization is needed to be built to provide credit guarantee. Glancing at world credit guarantee schemes, while a lot of European and American ones come from voluntary units such as credit unions with a long history, in many cases of developing countries like Southeast Asian ones credit guarantors have been established led by their central government<sup>21</sup>.

Central governmental bodies can be divided into stand-alone public corporation and partial body of government budget (special accounting). Public corporation is desirable because of light fiscal burden; only when MI reserve could be transferred smoothly. If it was found difficult, it is possible that for the time being government provides credit guarantee as special account, then changes it into public corporation. Japanese government can help Myanmar government drafting article of corporation and statement of operation procedure for details of guarantee.

For avoiding moral hazard, partial guarantee is better as it is. However it will be helpful some flexible scheme like extending guarantee coverage, treating well priority business which can create large

<sup>21</sup> Thorsten Beck, Leora F. Klapper, Juan Calros Mendoza “The Typology of Partial Credit Guarantee Funds around the World”(2008)

employment, and introducing special scheme like portfolio guarantee (providing guarantee up to fixed maximum amount without according investigation). For considering of them, Japanese government can provide some information about financial demands and ways of SMEs, industrial development plan, and derivative guarantee schemes.

## (2) Governing law

[Current Situation]

Its legal basis is unstable because CGI is exceptionally approved by Ministry of MoPF based on The Myanmar Insurance Law and CBM have not issued any regulations about no-collateral loan by CGI. Policy wording issued by MI is so simple that there must be much room for discretion of each MI staff.

[Reform Phase 1]

In short term priority challenge is to change such unstable legal basis into solid one. First, CGI should be made permanent by inserting an article saying MI can undertake CGI into The Myanmar Insurance Law. At the same time, specifying no-collateral loan by CGI at the CBM loan regulations is needed. Japanese government can assist in drafting of revised MI Law and CBM regulations, and giving CBM some information about effect and necessity of no-collateral regulations.

[Reform Phase 2]

Governing law of newly built guarantor is necessary. Major contents of the law are like this; 1. Purpose (credit guarantees scheme and this law), 2. Establishment of guarantor (authorization, how to establish, conditionality), 3. Operation of guarantor (institution, board of director, business, winding-up), 4. Supervision (supervisor, authority of supervisor). Japanese government can assist as legal advisory because this new law must not contradict with existing laws and regulations.

Specific guarantee conditions (fee, term, coverage, etc.) are to be clarified at the contract document between guarantor and banks or between guarantor and SMEs. In Myanmar legal system, there are many cases where laws give just brief overview while their implementation rules give the details. In Japanese scheme, fixed form of contract is used for saving troubles in making contracts every time. Japanese government can help guarantor making their own contract form.

## (3) Supervisor

[Current Situation]

CGI is MI product and MI is supervised by MoPF.

[Reform Phase 1]

In short term supervisor is unchanged.

[Reform Phase 2]

In medium and long term, it is necessary to identify supervisor. Possible options are MoPF, CBM, Ministry of Industry and SME Development Center. Among these candidates, MoPF seems the best because there would be no need to change current supervisor and it has power to get involved in surrounding areas to be reformed like accounting and taxation. On the other hand, other candidates'

capacity for supervision is thought to be weak because CBM tends to leave supervised entities working by their self-initiative and ministry of industry is said to be relatively weak in inter-ministry negotiation.

#### (4) Finance

##### [Current Situation]

There is no dedicated reserve fund of CGI, which is a part of MI General Reserve Fund. It is extremely hard to grasp MI financial situation because it does not disclose their financial information. Also, guarantee fee is fixed according to collateral and term.

##### [Reform Phase 1]

In short term, financial circumstances of CGI should be gripped by getting MI financial statement. Then CGI reserve should be accumulated. This accumulation is transition step for the Reform Phase 2 and must be useful for making MI aware of its financial soundness. Japanese government can help MI to do financial analysis and consider of reserve accumulation according to guaranteed credit and estimated default rate.

Also, guarantee fee rate can be lower in accordance with the growing number of CGI loans. It is expected to be more user-friendly by lowering rate based on default rate and operation expenses.

In this phase, it is critical to discuss and reach agreement about Reform Phase 2 with MI and related entities.

##### [Reform Phase 2]

In medium and long term, major challenge is how to raise initial capital for new credit guarantor. The easiest way is to transfer MI reserve for CGI into the new guarantee body. If it does not reach required amount of capital, MoPF and relevant ministries should pay the rest. Local bodies cannot be major contributor like in Japan because in some states quite a few amount of their revenue is subsidy from the the federal government<sup>22</sup>.

On the other hand, in order to prevent banks moral hazard it must be effective to require banks to contribute according to their capital and deposit amount. Japanese government can assist in arrangement of negotiation with MoPF and MI about fund transfer and in setting of contribution rate.

#### (5) Application

##### [Current Situation]

Applicant SMEs sometimes have to visit banks or SME Development Center to submit required documents because submission of documents are basically print media and there is no clear list of documents and procedures. It results in long waiting time until guarantee approval which discourages SMEs from using CGI.

##### [Reform Phase 1]

In short term, making application process more clear and simple must be significant by preparing document formats at the MI website and by making application process guide. In Japan, users can

---

<sup>22</sup> Council of Local Authorities for International Relation, Singapore “Local Administration in Myanmar” (October 2014)

download application documents at the credit guarantee corporation website. Japanese government can help MI to make such documents.

[Reform Phase 2]

For building the new credit guarantee scheme, SME should be able to apply CGI to banks as well as guarantor. This reform can make credit guarantee more attractive because SMEs can talk with bank about the scheme there.

## (6) Investigation and debt management

[Current Situation]

Currently what MI is doing at the documentation step must be just confirm banks screening results because there is no manual for documentation and there are only 4 staff responsible for CGI at the head office. Furthermore, none of these staff members are dedicated to CGI. Also, whether capacity of MI about guaranteed debt management is adequate or not once default happens. There is little information from Banks submitted to MI because they are scarcely obliged to report critical events like disbursement, condition change, and repayment. Where some banks have little capacity for risk management, MI institution for CGI cannot be said to be enough.

[Reform Phase 1]

In short term, MI capacity should be improved so that MI could tell whether result of banks screening is appropriate or not. Also, there should be sound debt management system built by closer collaboration between MI and banks. Considering of banks inadequate capacity and know-how for risk management, MI should have a certain screening capacity in order to prevent moral hazard of SMEs like KUR case in Indonesia.

For the first step, it is necessary for MI staff to use investigation manual exclusively for CGI, which is quite different from ordinary insurance products. As Japanese government, they may be able to help making the manual.

Furthermore, CGI section composed of dedicated and well-trained staff should be teamed up by giving MI staff some training about financial analysis and accounting, which are essential skills to examine banks screening. If MI does not have enough number of proper persons, MI may need to employ some new staff or MoPF will send its staffs to MI. Japanese government can help MI by sending trainer like staff in credit guarantee corporations, or by considering training and education programme. Japanese credit guarantee corporations have accepted trainees from abroad, especially Asian countries.

Finally, MI should make a guideline with conditions of reporting from banks and formats for reporting in order to make this process easier. Formats are to be electronically registered for preservation. Specific events which banks have to report to MI are disbursement of loan, loan condition change (payment, term and collateral), repayment, and default. Japanese government can assist in drafting of guideline and formats.

[Reform Phase 2]

In medium and long term, it is desirable to make credit investigation different procedure from banks screening in its purpose. First, the new credit guarantor should have some specialists from the beginning of its operation by spinning-out CGI team in MI.

Also, principles of credit investigation should be confirmed. While banks screen their customers by focusing on their repayment ability from the point of private company, guarantor should neutrally judge

enterprises potential as a public body. It is critical that the guarantor establish the guideline and principles of credit investigation in order to investigate applicants without being biased by others' options.

Lastly, database for debt management must be more important. The troubles in management of guaranteed debt is expected to be enormous as the number of guarantees increase and guarantees for refinancing loan happens. Japanese government can help guarantor developing its system by grasping current management system (Microsoft Excel).

## (7) Insurance payment and debt collection

### [Current Situation]

Currently, payment of insurance will be done after 90days passes from claim by banks. In case of collateral loan, MI pays insurance only if loss happens after collateral enforcement. However it is said to take several year to finish collateral sales process by court which may discourage banks from lending with long term and collateral assets in CGI.

### [Reform Phase 1]

In short term, both collateral system reform and making MI payment immediate after banks claim. While lately we can see a instance of easing of regulation about assets eligible for collateral(see 1 – 1 – 3. “Recent Deregulations”). However, it is limited cases that they can sale collateral based on private contract, so vitually there is no choice but going to the court for enforcement. Also, collateral system is fragmented in several laws; The Transfer of Property Act, The Registration Act, The Company Act, etc. Moreover, the definition of terms in these laws are different each other. Japan can do survey about legal system of collateral to make its challenges clear and to consider of the solutions.

Furthermore, policy wording of CGI should be revised so that MI can pay insurance right after banks claim. In this phase, banks do not pay back to MI if they managed to collect their loan by sales of collateral because there must be much time needed for enforcement and much trouble for procedure.

### [Reform Phase 2]

In medium and long term, immediate payment is still necessary. Unlike the previous phase, in this phase banks and the guarantor collect their debt in cooperation and allocate in accordance with the guarantee coverage ratio or the guarantor subrogates SMEs debt and collect it based on the right to reimbursement. Which scheme is better will be decided depending on progress of collateral system reform and collection capacity of banks and guarantor. Japanese government can analyze such preconditions and propose the better method to Myanmar government.

If there are larger number of claims than guarantor's capacity, it is worthy of consideration to establish a debt collection servicer like in Japan. Japan can propose necessary scheme and operation for debt collection servicer based on cases in Japan or foreign contries.

## (8) Infrastructure

### [Current Situation]

There are no major infrastructures for credit guarantee in Myanmar like credit information bureau or reinsurance system. Public credit bureau under the CBM is planned to start the operation soon, but the actual condition remains unclear (as of July 2017).

[Reform Phase 1]

Accumulation of borrower information is a critical condition for investigation with better quality. In short term, it is preferable that MI can use information submitted for SME Member Card application at SME Development Center and for loan application to banks. Japanese government can assist in introducing of information sharing system and database.

[Reform Phase 2]

In medium and long term, the guarantor should improve its skill for information analysis and consider of collaboration with public or private credit bureau. When credit bureau under the CBM is in operation as it was initially planned, Japanese government may help the guarantor to grasp its circumstances and may arrange meeting about possibility of collaboration.

## (9) Publicity

[Current Situation]

Current publicity among SMEs and banks of CGI is relatively low even 3 years have passed since its launch. Major promotion channels of CGI are introduction by banks, SNS by banks, and seminars held by SME Development Center for SME Member Card holders. However, contribution by banks is limited since managers of some banks have little knowledge of CGI and most of banks have never used CGI. This low publicity is one of the reasons that CGI have been applied from small number of areas.

[Reform Phase 1]

In short term, it will be effective to make brief guide for CGI and distribute them at bank or SME Development Center or to promote CGI at SNS, TV and newspaper in order to extend CGI user basis into local region and medium scale cities.

[Reform Phase 2]

In medium and long term, it is desirable that new the credit guarantee system gain high publicity and is used nationwide. In addition to existing promotion, Seminar or Q&A session of the new scheme for SMEs held by cooperating with Ministry of Industry and banks will be effective for smooth increase of users.

## (10) Other areas

[Current Situation]

Players other than MI should be reformed in several points. Especially mismatch between demand and supply of CGI is one of the critical challenges. On the one hand, SMEs find hard to use CGI because of flaws of required documents like tax certificate and financial statements while they have strong demands for CGI. On the other hand, banks do not want run the risk of SME lending by CGI because of less competitive business environment derived from inadequate collateral system and lending regulation.

Also, some user SMEs have complained of time-consuming process at SME Development Center, an issuer of Member Card and recommendation letter. Nonetheless, this center plays a role as primary screener to supplement banks and MI capacity.



[Reform Phase 1]

In short term, SMEs are required to disclose their tax and financial information precisely. It is necessary to instruct SMEs to have precise tax certificate through reinforced monitoring by tax authorities, and to make their financial statements assisted by auditing company.

For banks, incentives of CGI by collaboration with TSL and clear regulatory framework for no-collateral lending will be helpful.

For SME Development Center, if it succeeds to increase the number of Member Card and recommendation letter CGI application will be simple. This increase will be encouraged by making the center procedures go online and by developing database of applicants to make renewal of Member Card easier.

[Reform Phase 2]

In medium and long term, developing a variety kinds of loan and guarantee scheme (e.g. for new business and emergency) and gradual liberalizing interest of banks are effective for more demands for SME finance. However some mandatory political measures like setting commitment line for SMEs loan should be considered because there is possibility that large banks may get reluctant to provide loan for SMEs. Anyway, these reforms must be accompanied with inevitable upheaval. Japan can gather existing cases of these kinds of reforms abroad, and propose soft-landing system reform to Myanmar government.

**3-8 Support by international organizations or foreign agencies for credit guarantee system**

For creating the current CGI, Sumitomo Mitsui Banking Corporation (SMBC) has supported the Myanmar government in establishing the scheme, extension users, collecting data of CGI use.

## Chapter 4. Implementation structure of SME loans by financial institution in Myanmar

### 4–1 Overview of private financial institutions

	A Bank	C Bank	D Bank	E Bank	F Bank	G Bank
As of	2016/3	2016/3	2016/3	2016/3	2015/3	2016/3
Established in	1996	1992	2010	1991	2010	1996
Employees (person)	494	6,032			4,166	-
Number of branches	19	149	96	20	107	123

(Unit: billion MMK)

### 4–2 Funding methods by private financial institutions

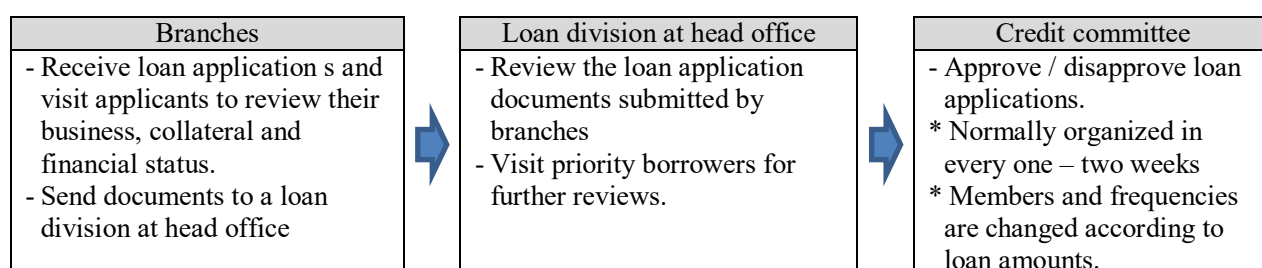
Basically, the funding source of private financial institutions is deposits<sup>23</sup>.

Therefore, the ratios of deposit to total liability at banks tend to be very high and they exceed 85% (other liabilities, include advances received or provisions, are not regarded as funding).

### 4–3 Loan appraisals at private financial institutions

#### 4–3–1 Loan appraisal, approval and decision making

Normally, financial institutions in Myanmar take following processes upon loan appraisals and loan approvals. In these processes, branches, loan divisions and credit committees are involved.



Such processes are different among banks. Some banks do not include branches even in initial loan screening, while other banks authorize branches to approve loan application of small amounts.

#### 4–3–2 Analysis on financial statements upon loan appraisals at banks

One of the financial institutions mentioned in the interview that it emphasized debt service ratio. This suggests that the repayment capacity of borrowers is one of the main aspects that the banks review in loan appraisals.

On the other hand, other banks seem to be analyzing mainly sales growth and profitability of borrowers upon loan appraisals, as they mentioned that the business strength of borrowers is the major issue.

<sup>23</sup> A private institution mentioned that it tried to issue bonds before but it could not obtain the approval by the central bank.

Financial institutions have common understanding that the qualities of financial statements of borrowers are not reliable. Based on this understanding, financial institutions emphasize qualitative information, such as repayment records, relationship with banks and business outlooks and also the values of collaterals upon loan appraisals, rather than financial analysis based on financial statements.

#### 4-3-3 Loan approval criteria

As mentioned above, many banks emphasize qualitative information (e.g. repayment records, relationships with banks and business outlooks) and collateral values upon loan appraisals, rather than financial analysis results.

According to financial institutions interviewed on this study, they first examine the businesses of borrowers and then review the values of collaterals to determine loan amounts. In case there are any issues in business outlooks of borrowers, financial institutions decline loan applications, no matter if borrowers have sufficient amounts of assets for collaterals. Therefore, it is possible to say that financial institutions provide loans based only on collaterals.

However, it is obvious that the values of collaterals are the major determinant factor of loan amounts. Many banks determine loan amounts by multiplying certain percentages on asset values.

Financial institutions calculate market values of the assets, in many cases by external assessors, and then obtain forced sales values by multiplying market values by 80-90%. Financial institutions then determine loan values by putting certain percentage on forced sales values.

The ratios of loan amounts to market values of collateral assets differ among banks and borrowers. If financial institutions judge that the business of borrowers are strong enough, the ratio of loan amount to market value of collateral assets that financial institutions allow to borrowers tend to be bigger.

Loan amounts are determined by financial institutions, based on the market values of collateral assets, as follows;

Only one financial institution mentioned that it operated credit scoring model and two other banks were under the process of developing credit scoring model.

In the credit scoring model of the financial institution mentioned above, about 50% of total scores are given by financial indicators (such as indicators on solvency, liquidity, growth and repayment capacity) and the remaining 50% is by qualitative information such as business, quality of management and market conditions.

The financial institution use credit scoring results basically to determine the loan policies of borrowers. Even though scoring results are satisfactory, the financial institution does not make loan decisions automatically. After obtaining scoring result, it reviews several aspects of borrowers, such as business and collateral conditions, in order to make loan decisions.

#### 4-4 Collaterals and credit guarantees

Collaterals provided by borrowers to financial institutions are mostly real estates, although other assets such as gold and jewelries are allowed as collaterals.

In many cases, financial institutions accept the assets of the family members of business owners or the assets of board members, as collaterals. The owners of assets also need to be a part of borrowers (co-borrowers).

In case borrowers cannot make repayments, loans are ultimately repaid through selling collateral assets through auctions, based on decisions by courts. However, financial institutions do not necessarily bring all overdue or default loans to courts.

When borrowers cannot keep up loan repayments, borrowers are requested to prepare repayment plans and financial institutions and borrowers have discussion based on it. If the repayment plans are realistic and acceptable for financial institutions, they would agree to reschedule loans and borrowers continue repayment according to rescheduled repayment schedules. If borrowers further overdue repayments, the ownerships of collateral assets are sometimes transferred from borrowers to financial institutions. Borrowers then continue business using the assets to make repayments.

In the interviews with financial institutions, it was observed that financial institutions are trying to avoid bringing cases to courts, most probably because it takes considerable amounts of time and efforts to have decisions at courts. It takes at least 1.5 years and sometimes more than 5 years to have decisions by courts. According to a financial institution, the number of the cases brought to court for the last seven years is only 10.

However, there were other banks which think having court decisions are inevitable in case borrowers have problems in repayments. No matter if borrowers try to sell collateral assets through property market, it is difficult to find buyers due to the limitation of markets. Another obstacle is that borrowers think that the market values of collateral assets are much bigger than the amount of loans, and thus borrowers do not agree to transfer the ownerships of the assets to financial institutions.

#### 4-5 Credit risk management

and

#### 4-6 Loan asset management at financial institutions

##### 4-6-1 Internal credit rating at financial institutions

As mentioned above, only one financial institution operates internal credit rating system (credit scoring model) and two financial institutions are under the process of developing internal credit rating system. The credit scoring model is basically constructed based on credit experiences of financial institutions and not based on statistical analysis on the probability of defaults (statistical analysis on the relationships between default status and financial and non-financial indicators).

##### 4-6-2 Loan management after disbursements

Financial institutions capture loan repayment status of borrowers without any delays. This is because repayments of loans are normally made at the end of month and financial institutions check repayments on the same day or the following day.

When repayments are missed by borrowers, financial institutions, through branches in many cases, communicate with borrowers to examine the business and other status of borrowers. In general, credit committee is responsible for the management of such overdue loans.

Financial institutions review business or financial status at least once a year after loan disbursements. This is because the maximum loan terms are generally one year, financial institutions carry out regular loan appraisals, reviewing business, financial status or collaterals of borrowers, when loans are renewed.

##### 4-6-3 ALM (Asset liability management)

All financial institutions (except 1 bank) mentioned in the interviews that they have not taken any actions on ALM (asset liability management), such as establishment of ALM policies or ALM committee.

Financial institutions do not recognize necessities for ALM because both loan terms and deposit terms are within one year and thus there are no gaps between loan terms and deposit terms. Similarly, because

interest rates are fixed, they do not feel necessity to examine the positive and negative effects by the fluctuations in interest rates or the gaps between long term and short term interest rates.

#### 4-6-4 Asset quality review and provisioning

Based on the regulations by CBM, financial institutions are supposed to account general provision (2% of all loans) and specific provision on substandard loans and bad loans. Loans are classified as substandard and bad loans based on overdue periods.

Fig 29 : Provision based on overdue period

Watch: 31 to 60 days past due	5%
Sub-standard: 61 to 90 days past due	25%
Doubtful: 91 to 180 days past due	50%
Loss: Over 180 days past due	100%

Source: CBM Notification (No. (19/2017))

As mentioned above, loan classifications and thus provision rates are determined based only on overdue periods, not by internal rating results of borrowers and coverages by collaterals. Therefore, asset quality review, which loans are classified based on internal rating or collateral coverages, is not carried out by any financial institutions.

The status of provisioning is different among financial institutions. Although all financial institutions mentioned that they accounted general provisions following CBM instructions (2% of general provision), the ratio of provisions for bad debts tend to be smaller than 2%<sup>24</sup>.

#### 4-7 Marketing methods by private financial institutions

Many financial institutions are expecting increase in loan balances in the future. However the main obstacles to increase loan balances is funding or deposits. This is because financial institutions are not allowed to issue bonds and thus deposit is the only funding source for loans. Similarly, due to the regulations on loan to deposit ratio, financial institutions cannot increase loan balances without increasing deposit amounts.

Therefore, financial institutions, which are active in expanding loan balances, set target on the increase in deposit amounts.

Some banks mentioned that they were planning to open new branches in order to increase deposit amounts, but this they need to bear considerable time and expenses to open and maintain branches. Therefore, financial institutions are also planning to increase deposit accounts utilizing internet banking or mobile banking in order to penetrate to the area where bank branches have not existed or to the people who did not have bank accounts.

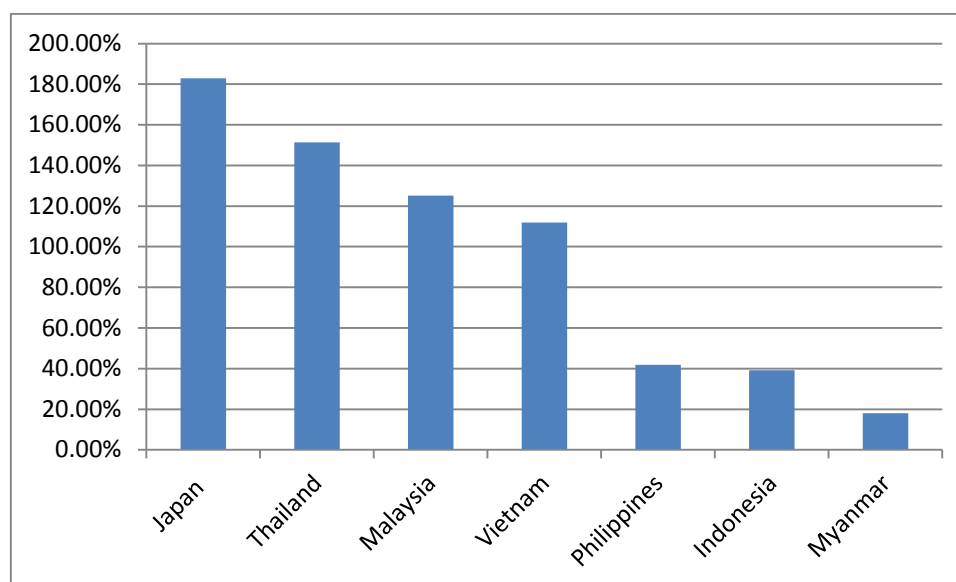
---

<sup>24</sup> Financial institutions distribute net profits to statutory reserves, dividend provisions, loan loss provision and others respectively. Financial institutions seem to have prioritized statutory reserves and dividend provisions to loan loss provisions.

#### 4–8 Loan appraisal capacities of private financial institutions in neighboring countries

The ratio of domestic credit to GDP in Myanmar is 18.1% and this is very low compared to neighboring countries, such as Thailand (151.3%), the Philippines (41.8%) and Indonesia (39.1%).

Fig 30 : Comparisons of domestic credit / GDP among neighboring countries



Source: Prepared by the study based on the information from World Bank, World Development Indicators

One of the main reasons for this is that financial institutions in Myanmar are regulated not to provide loans more than the values of collaterals, although financial institutions in other countries do not always rely on collaterals when providing loans.

In order to provide loans without relying too much on collaterals, financial institutions need to capture the credit risks of borrowers through analyzing quantitative information such as financial information and qualitative information such as business and quality of management. In addition, financial institutions determine loan amounts, loan interest rates and collateral condition based on the captured credit risks. It would be possible to say that the capacities of financial institutions which capture credit risks of borrowers are higher than financial institutions which provide loans relying on collaterals.

One of the issues in loan appraisals at financial institutions would be the availability of credit information of borrowers (especially overdue and default information at other banks). At the moment, there are not any available credit information systems in Myanmar, as depicted in the following table.

Fig 31 : Coverage of borrowers by public and private credit information institutions (Unit: %)

	Public	Private
Japan	0.0	100.0
Thailand	0.0	53.0
Malaysia	62.4	76.4
Philippines	0.0	10.2
Indonesia	51.8	0.0
Myanmar	0.0	0.0

Source: World Bank, World Development Indicators

Unlike in Myanmar, banks in neighboring countries operate internal credit rating system and determine loan loss provision amounts based on the credit risks of borrowers, following Basel regulations. Banking supervising body also carry out asset quality review at financial institutions, in order to examine loan loss provision made by financial institutions are appropriate or not.

For example, in the Philippines, there are several categories of financial institutions, such as Universal and Commercial Banks (36), Thrift and Saving Banks (71) and Rural banks (552), and large sized banks, such as Universal and Commercial Banks, operate internal credit rating system (or credit scoring model) and use them in loan appraisal processes.

At the same time, banks tend to be less dependent on collaterals, because the competitions among banks are getting more severe (loan balances are increasing drastically, but the amounts of collaterals are not increasing as fast as loan balances). Therefore, such banks emphasize more on credit risk assessments.

Nevertheless, banks in the Philippine think that there are many obstacles in providing unsecured loans based on credit risk assessments. One of the main reasons pointed out by banks is the quality of financial statements of borrowers. According to banks, many borrowers understate their financial statements, especially sales, profits and assets. Therefore, banks try to capture the credit risk of borrowers by estimating the actual sales and profits, through observing the amounts of inventories in factories and also by observing the deposits and payments made through bank accounts.

In contrast to this, banks operated in rural area, which do not face such severe competitions among banks, still provide loans based on collaterals. The capacity of such banks might be also another reason why they cannot provide loans without relying on collaterals.

Another issue pointed out in the Philippines is the delays in the establishment of credit information system. Although a governmental institution, Credit Information Corporation, is supposed to receive necessary information (such as names of borrowers and their overdue status) from financial institutions, financial institutions are not very willing to provide such information, and thus sufficient amount of necessary data is not stored in its database of Credit Information Corporation.

## Chapter 5. Policy recommendations toward improvement of SME finance system

---

### 5-1 Outline of policy recommendations and its priority

#### 5-1-1 Summary: Multiple and cross-interactive policies are necessary

Multiple and cross-interactive policies are necessary. If some policies miss, we will face a risk of severely harmful effects. For example, if CBM relaxes interest rate regulation before we resolve demand-supply gap of fund, lending interest rate may increase steeply from 13%. As mentioned in chapter 1, regarding liberalization of interest rate, we need to prevent banks to take too much credit risks. Strengthening supervision by CBM and preparing infrastructure, e.g. credit guarantee system and credit bureau system, are also necessary.

The following picture shows issues and policy recommendations for SME finance system.

#### 5-1-2 Demand-supply gap of fund

The most severe issue in SME finance and further more indirect finance is demand-supply gap of fund. We can find two reasons of the gap: (1) one is depositor's behavior. Myanmar national does not believe banks, and it tends to keep its own fund in its house. (2) The other is loan to deposit ratio regulation.

##### (1) Improving deposit insurance

As mentioned in chapter 1, although Myanmar Insurance (MI) has already started deposit insurance and CBM recommend its usage, many banks do not use the insurance. The insurance can cover only 1 mil Kyat per an account. The coverage is not enough for depositor comparing the Japanese case<sup>25</sup>. We recommend mandatory insurance coverage, its enforcement thoroughly, and increase of the coverage, e.g. 10 mil Kyat per an account.

##### (2) Relaxing loan to deposit ratio regulation

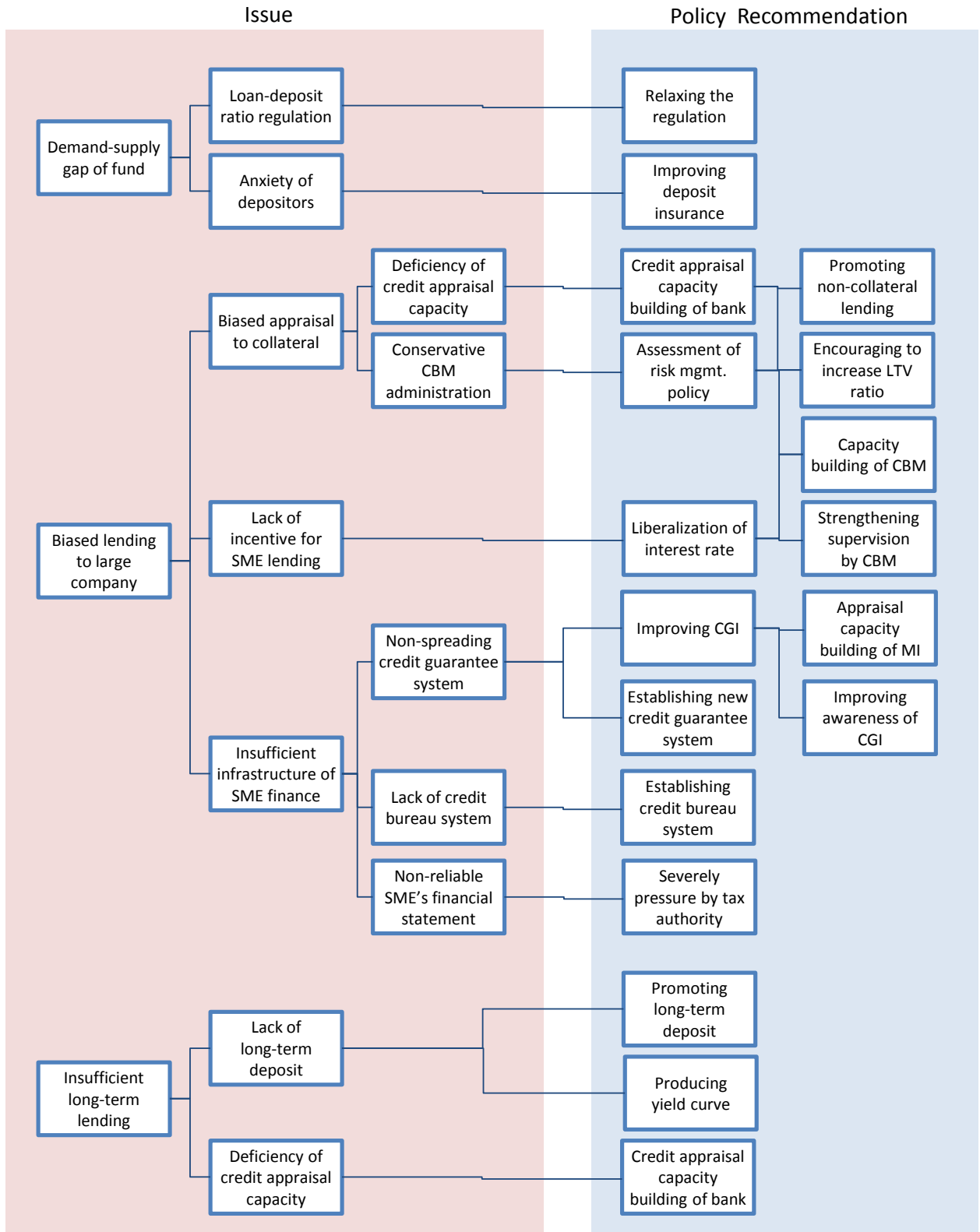
We recommend relaxing loan to deposit ratio regulation, although its effect is just limited. For example, even if loan to deposit ratio would increase from 80%, current regulation, to 100%, total loan amount could increase only 25% ( $100 \div 80 = 1.25$ ). That is, in order to solve essentially demand-supply gap of fund, behavior change of depositor is inevitable. Improving deposit insurance is more important and relaxing loan to deposit ratio regulation is just complementary. Basically, banks need to strengthen depositor confidence steadily through long time track record.

---

<sup>25</sup> Japanese deposit insurance covers 10 mil JPY. Because price level between Japan and Myanmar differs by 10 times, we recommend Myanmar deposit insurance should cover 10 mil Kyat.



Fig 32: Issues and policy recommendations for SME finance system



Source: Compiled by JICA study team

### 5-1-3 Biased lending to large company

In Myanmar, banks tend to lend to large and medium company. We point out three reasons: (1) biased appraisal to collateral, (2) lack of incentive for SME lending, and (3) insufficient infrastructure of SME lending. Detail is mentioned below.

#### (1) Biased appraisal to collateral

The strongest trigger of this problem is CBM instruction issued in 2005. The regulation has been relaxed step by step from 2012, and it is drastically changed in 2017, c.f. section 1-1-3. A bank has to submit to CBM individual risk management policy. If CBM agrees that the policy is appropriate, the bank can start lending without collateral and can set LTV ratio. Proper operation of this new regulation by CBM results in quite a change in collateral biased culture. For the sake of proper operation, CBM requires assessment capacity for risk management policy submitted by a bank. Assessment capacity building of CBM is effective.

One more issue is improving credit appraisal capacity of a bank. A bank tends biased appraisal to collateral and it does not evaluate business model and business risks adequately. If CBM relaxes collateral regulation prematurely, we may face with financial crisis risk by default rash. Credit appraisal capacity building of banks is necessary, while CBM relaxes the regulation in parallel.

#### (2) Lack of incentive for SME lending

The maximum lending interest rate is now 13%. Although some banks reduce lending interest rate under severe competition between banks, basically a bank lend to SME by 13% lending interest rate. If a bank has to lend to all customers by the same interest rate, 13%, it is economic intelligent decision for a bank to focus on only reducing credit risks.

In order to encourage a bank to focus on SME finance, it is necessary to increase interest margin of a bank, that is lending interest increase and liberalization of interest rate.

However, we have to keep in mind the following risks of liberalization of interest rate; (i) Lending interest rate may increase steeply, if demand-supply gap of fund remains, (ii) a bank may take a huge risk in order to gain more high interest margin. The measure of (i) is mentioned already. The measure of (ii) is strengthening of banking supervision by CBM, and strengthening of risk management capacity of a bank through credit appraisal capacity building.

In order to avoid the above risks, we recommend gradual increase of lending interest rate. For example, we recommend to increase maximum lending interest rate by 0.5% per a year. Comparing to completely liberalization, CBM can control additional bank's interest margin and a bank does not easily shift to customers with huge risk. A bank is expected to expand target customers gradually in accordance with increase of additional margin and improvement of credit capacity. From the view point of banking supervision, CBM has a merit to control the timing to increase interest rate in accordance with improvement of credit appraisal capacity of banks.

#### (3) Insufficient infrastructure of SME finance

Credit guarantee system is important infrastructure for SME finance and especially for finance for micro- and small-enterprise which does not have enough assets for collateral. As mentioned in chapter 3, Myanma Insurance (MI) has already started Credit Guarantee Insurance (CGI), and MI provided CGI to 62 SMEs as of end of May 2017. However, only 3 banks utilize CGI and just limited SMEs have used CGI, because of several reasons as follows; banks have not incentive for SME lending; only 3years have passed from the start of CGI; no experience about payment of insurance claim results in uncertainty for

MI to execute payment of insurance claim smoothly. We will mention, in detail, the measure of improvement of credit guarantee system in section 5-2.

Credit bureau system is also important infrastructure. In credit appraisal by a bank, a bank does not have enough information to appraise, if a SME does not have credible financial statement, a SME does not have enough collateral, and track record between a SME and a bank is short. If a credit bureau exists and it provides track record between a SME and relevant banks and non-banks, it is quite helpful for credit division of a bank. As mentioned in chapter 1, credit bureau is now in the midst of establishment proceedings. As soon as the detail becomes apparent, we can start to consider how to encourage using the credit bureau.

Regarding the low credibility of a financial statement of SME, at first, strengthening tax collection is necessary. SME's financial statement does not gain credibility for banks. Although Japanese government and private agencies have already provided bookkeeping training, not only technical problem but also inappropriate mind for tax cheating is serious problem. In order to encourage SME to create proper financial statement, both incentive and penalty is important. A bank already takes a role to provide incentive to SME by requiring audited financial statement. Typical entity which takes a role to provide penalty to SME is a tax collection authority. It is effective that tax collection authority encourages SME more to create correct financial statement by strengthening authority.

#### 5-1-4 Insufficient long-term lending

Banks have started long-term lending (1-5 years) in the case of Two Step Loan project for SME by JICA. More than 57 bil Kyat was already disbursed to SMEs as mid- to long-term loan. However, otherwise loan is mostly short-term. The examples of long-term loan are limited as just a part of items of AYA bank. In order to promote long-term lending, we recommend the following three measures.

##### (1) Promoting long-term deposit

CBM instruction requires long-term deposit for long-term lending from a viewpoint of Asset Liability Management (ALM)<sup>26</sup>. Although the instruction has been removed by new instruction in April 2017 (introduction of risk management policy), long-term deposit is still necessary from a viewpoint of ALM in any case. The bottle neck to expand long-term deposit is not rules and regulations, but just banking business strategy. We need to encourage management awareness-raising for long-term deposit.

##### (2) Producing yield curve (introduction of long-term interest rate)

Currently, neither long-term deposit nor long-term lending exists practically. Government bonds exist for 2.5 years, 3 years and 5 years and average closing bidding interest rate is 9.1-9.2% for 2.5 years and 9.0-9.7% for 5 years. It means like gradual forward yield. However, such yield curve is insufficient as benchmark, because secondary market for government bonds does not exist and therefore it results in rigidity of interest rate for fluctuation range and frequency. If liquidity of government bonds increases and it provides yield curve, a bank can set long-term interest rate much easier by referring to the yield curve as a benchmark. Of course, relaxing interest rate regulation also should be executed at the same time.

##### (3) Credit appraisal capacity building of bank

In order to encourage long-term lending, much more credit appraisal capacity of bank is necessary. Although JICA already provided capacity building program under TSL project for SME, the program

---

<sup>26</sup> CBM, "Permission of mid-term and long term loans in addition to short term ones", Instruction No. (2/2013), 2 August 2013.

does not suit actual need of each bank, because the program is just group training where all PFIs come together. Moreover, PFI does not mention its actual issue in front of other banks. As mentioned in section 5-3-2, we recommend capacity building by consultants who stay bank in all time.

## 5-2 Necessity and Feasibility of Credit Guarantee System and Measures to Establish it

This section is samary of issues and measures of credit guarantee system. Please refer section 3-7 for detail.

### 5-2-1 Necessity of Credit Guarantee System

As mentioned in section 5-1, credit guarantee system is effective tool to promote SME finance. Moreover, it can be combined with non-collateral lending and ease collateral conditioned. In order to encourage new eased banking regulation introduced from April 2017, and to improve biased credit appraisal system to collateral, credit guarantee system has an important role.

### 5-2-2 Strengthening CGI by Myanma Insurance (Short-term measure)

Because CGI has already started as a credit guarantee system, realistic measure for short-term is strengthening existing CGI. Among the issues for CGI, which is mentioned in chapter 3, we would like to focus on the measures regarding MI. That is strengthening credit appraisal capacity building of MI and advertisement of CGI.

MI does not have any staffs in charge of credit appraisal for applicants. MI is considered not to have credit appraisal capability. If MI does not have, we concern moral hazard where a bank may foist extremely low credibility SME on MI. To avoid such situation, we recommend recruitment from banking sector, e.g. headhunting of key person in charge of credit appraisal department in a bank, and also recommend credit appraisal capacity building of MI, which is like the capacity building of PFI.

Further promotion and advertising activity is necessary, collaborating with the banks which have already utilized CGI, i.e. CB bank, KBZ bank and SMIDB. If MI and SME Center under Ministry of Industry provide budget for promotion activity, a bank has more incentive for using CGI, because the bank can take free ride on such promotion activity to advertise itself.

### 5-2-3 Establishing new credit guarantee system (Long-term measure)

From a long-term view, we consider appropriate credit guarantee agency is not MI, but specialized independent agency to be newly established. We point out the following three reasons.

#### (1) Introduction of subrogation repayment

As mentioned in chapter 3, one of the problems of CGI is that a bank cannot take insurance reimbursement as soon as it claims to MI, because amount of insurance reimbursement is fixed only after collateral disposition. If MI pays before collateral disposition, MI needs to gain right and ability to subrogation repayment and indemnification. However, MI is not appropriate for subrogation and indemnification, because MI is just an insurance company. In order to introduce subrogation and indemnification, we recommend establishing new credit guarantee agency, which is different from insurance company.

## (2) Applicability of credit appraisal capacity building of MI

MI is just an insurance company. CGI is anomalous service in MI comparing to other insurance services. If credit capacity building is executed to MI, the educated staffs are also anomalous in MI. They can utilize their experience and expertise in only CGI departments and they cannot move to other departments. From the view point of organization structure and personnel strategy, it is not sustainable. After capacity building of MI, MI is recommended to spin off the department of CGI as a newly specialized independent agency of credit guarantee. The educated staffs should be the central players in the new agency.

## (3) Appropriateness of CGI in law

CGI is just “an insurance which MOPF designates” in MI law. Minister of Planning and finance specially approved CGI in accordance with MI law. Although CGI is legal insurance under MI law of course, it seems tentatively established insurance service.

### 5-2-4 Introduction of re-insurance system (long-term measure)

Credit guarantee fee is not usually set by strictly utilizing default probability, but set as cheaper price in terms of SME finance policy. Therefore, credit guarantee has a risk to get a loss. If a private bank invests to the credit guarantee agency, re-insurance system is useful in order to reduce capital damage risk caused by users' default.

### 5-2-5 Other policies (long-term measure)

As mentioned repeatedly, only credit guarantee is not enough to promote SME finance. Comprehensive policies, e.g. strengthening incentive of SME finance, mentioned in section 5-1, are necessary. Otherwise, a bank does not utilize credit guarantee system even if we improve it.

## 5-3 Proposal for credit appraisal capacity building of banks

### 5-3-1 Encouraging breakaway from credit appraisal biased to collateral

Some progressive banks intend to break away from credit appraisal biased to collateral. CB bank aggressively utilizes CGI and Yoma bank provides comparatively big volume of loan to a SME with high LTV ratio. The objective of these activities is limited as just promotion for business building, because demand-supply gap of fund is still large and a lender has superior position to a borrower. In such situation, we cannot expect other banks to voluntarily follow these activities.

Thus, it is important to increase incentive, that is to provide some compensation to these progressive banks. For example, we recommend to select these progressive banks as PFIs (Participating Financial Institutes) for Two-Step Loan by JICA, and to take into account these progressive activity track records when CBM evaluates risk management policy of a bank.

### 5-3-2 Directly capacity building

JICA Two-Step Loan project for SME has already provided group training to all PFIs. However, with caring about other PFIs' eyes, group training discourages a PFI from disclosing internal real problems in each PFI. As a result, group training does not match with the reality of a PFI and it is just training in general matter.

Effective training scheme is constant consulting service to a bank, which GIZ already provided to Yoma bank, KBZ bank and SMIDB. In particular, a consultant has a desk and a sheet in a bank, has a position of an adviser to board members, figures out also internal confidential information, and provides intelligent advice.

Many banks, e.g. KBZ bank, Yoma bank, AYA bank, CB bank, and Citizens bank, etc., have already hired international advisors by themselves. Our recommendation has a different role from such existing advisors with clearly focusing on “credit appraisal capacity building, establishing risk management policy, and negotiation with CBM for the policy”.

If a consultant repeatedly negotiates with CBM and requires CBM to explain how to evaluate risk management policy submitted by a bank, it results in also capacity building of CBM. The objective of the consultant is not only capacity building of a bank, but also implicitly capacity building of CBM.

#### 5-4 Proposal toward enhancing Two-Step Loan for SME

##### 5-4-1 Problem and issues of existing Two-Step Loan for SME

###### (1) Effort: Getting used to long-term lending

###### ① Average lending term is 4.0 years

Limited to Two-Step Loan for SME, PFIs provided long-term loan, of which term is 1-5 years, as planned. Average lending term is 4.0 years, as of January 2017 (regarding 1<sup>st</sup> batch and 2<sup>nd</sup> batch).

###### ② A case of AYA Bank

AYA bank, one of the PFI of Two-Step Loan for SME, started education loan and the loan term is for 5 years in maximum. According to Eleven Myanmar, on 22 March, 2017, AYA bank plans to provide housing loan, cooperating with Shwe Taung Development company and the loan term if for 15 years. Long-term lending is spreading to other than Two-Step Loan.

###### (2) Issue: Piling up for issues other than long-term lending

The objective of the existing Two-Step Loan is only promoting long-term loan. Other issues have not been focused on in the project design. Therefore, most issues in section 5-1 have not resolved yet. We pick up two of these issues to be resolved by our proposals mentioned after section 5-4-2.

###### ① Collateral biased credit appraisal is not resolved

Almost of all borrowers' collateral in TSL are immovable assets. The cases utilizing eased collateral regulation are only limited. Although we have no data about LTV ratio limited to TSL, many SME borrowers complained that LTV ratio is considered obviously low.

###### ② Credit guarantee system does not spread

So far, any borrowers in TSL do not utilize CGI. If CGI is utilized in TSL, which is one of featured SME finance policies, advertisement effect is significant. Furthermore, TSL and CGI are an acceptable combination for SME, because interest rate of TSL (8.5%) + CGI fee (3.0%, in case of non-collateral) = 11.5% and it is still less than usual lending interest (13.0%).

Other issues inherent in TSL designing are as follows;

③ Interest margin of PFI is too high

Interest margin of PFI is set by 4.5% in existing TSL. Strictly speaking it is calculated by the following equation;

$$\text{Interest margin of PFI} = (\text{maximum lending interest rate} - \text{minimum deposit interest rate}) \times 90\%.$$

Theoretical banking margin (13% – 8% = 5%) is discounted by 10%. The reason of discount is that PFI does not need to pay cost for financing activity.

On the other hand, banking competition has become severe and severe after TSL started. Deposit interest rate in many banks increases widely from minimum interest rate 8.0%. Banks cannot enjoy the 5% interest margin.

Fig 33: Deposit and lending interest rate as of 22 June, 2017 (same as Figure 3)

	Deposit Rate (%)						Lending Rate
	Savings Deposit	Time Deposit (# of months)					
		1	3	6	9	12	
KBZ	8.25	9.00	9.25	9.50	9.75	10.00	13.00
CB	8.25	9.00	9.25	9.50	9.75	10.00	13.00
Yoma	8.25	9.00	9.25	9.50	9.75	10.00	13.00
APEX	8.50	8.50	9.25	9.50	9.75	10.00	12.00
AGD	8.60	9.00	9.25	9.50	9.75	10.00	12.00
AYA	8.25	9.00	9.25	9.50	9.75	10.00	n.a.
SMIDB	8.50	9.00	9.25	9.50	9.75	10.00	12.00
GTB	8.50	–	9.25	9.50	9.75	10.00	12.00

Source: Website of banks

Note: A bank collects service charge as about 1% from a borrower in addition to loan interest.

④ Little competition between PFIs

A certain amount of budget allocation is provided to each PFI in existing TSL. PFI accepts loan application from SME as far as total amount of applications are within budget. The budget size for each PFI is up to only few billion Kyats. Thus, PFI accepts only a few dozen applications from SMEs. Lender is obviously prior to borrower and therefore many SMEs complained in interview that “only SMEs very close to a bank can get TSL” and “neighbor SMEs was refused to submit application to a bank”. From the view point of SME, it may be more acceptable scheme that SME has a right apply to TSL at least and then is declined by credit appraisal process in terms of business model, profitability, and safety. Furthermore, process of application subscription and discussion with bankers in credit appraisal have effect to improve SME’s business model and sales and profit forecast.

5–4–2 Proposal for 2nd phase of Two-Step Loan for SME

Existing Two-Step Loan for SME has successfully introduced long term loan in banking sector in Myanmar. However, long term loan does not spread generally and widely. We have to keep encouraging

long term loan through Two-Step Loan. Meanwhile, there are still many issues mentioned in the above section. In order to keep encouraging long term loan and to realize the issues, we propose 2nd phase of Two-Step Loan for SME. In the 2nd phase, in order to overcome problems mentioned in 5-4-1, we propose to decrease PFI number, periodic updating PFI (establishing M-League), and selecting borrowers by PMU.

#### 5-4-3 Decrease of PFI interest margin (Proposal 1)

As mentioned in section 5-4-1 ③, the PFI interest margin (4.5%) in existing TSL is too high comparing to current margin level. We propose to decrease interest margin from 4.5% to 4.0%. Strictly speaking, it is calculated in the following equation:

$$\text{Interest margin of PFI} = (\text{maximum lending interest rate} - \text{minimum deposit interest rate}) \times 80\%.$$

#### 5-4-4 Mechanism to breakout from collateral biased lending (Proposal 2)

We propose non-collateral lending, eased collateral lending (eased LTV ratio), and CGI utilization in TSL for SME. We don't recommend these ideas in all budget of TSL, but we recommend to set a certain special allotment.

##### (1) Non-collateral lending

Non-collateral lending should be just limited to short-term. The reasons are non-collateral lending is too high risk and banking common practice that borrower should take some responsibility, i.e. providing collateral, in long-term borrowing for capital investment. Target of TSL is usually long-term lending because TSL is backed by the finance long-term Yen-loan. However, to promote short-term lending is also important in this TSL toward breakdown from collateral biased culture, which is one of the bottleneck in SME finance.

We propose the interest rate of non-collateral lending as 13%, maximum lending interest rate. PFI interest margin is calculated as 9.0%. 9.0% is profitable level if default probability is assumed to be 6%, which is the highest NPL ratio among banks, mentioned in chapter 4. Otherwise, that is if a bank cannot enjoy more than 6% interest margin, a bank may not take part in TSL.

##### (2) Eased collateral lending

Eased collateral lending is useful in the following case, for example. A SME has already borrowed and requests additional loan. However, a SME cannot receive loan because loan allotment was already run up for existing loan. In such case, if a bank eases LTV ratio, the SME can receive additional loan without any additional collateral. The loan-term can be long-term, because certain amount of collateral was provided. We propose that the loan with over 50% LTV ratio satisfies with the condition for the certain special allotment. Interest margin of PFI should be increased a little from 4.0% (usual interest rate, c.f. section 5.4.2) to 4.5% in order to strengthen PFI incentive.

##### (3) CGI utilization

Regarding CGI utilization, there are two types of combination. One is the combination between non-collateral and CGI, and the other is between eased collateral and CGI. In case of non-collateral and CGI, it should be short-term loan, because SME's responsibility is low. Interest margin of PFI is recommended 6.0%, which is calculated to deduct 3.0% from 9.0% (the PFI margin in non-collateral lending). If default probability is 6%, it is still profitable level, because 60% of loss is covered by CGI.



In case of eased collateral and CGI, we recommend that loan term is long-term and interest margin of PFI is 4.0%. PFI margin should be less than the rate in the case of eased collateral lending (4.5%). Otherwise, PFI threatens to guide all borrowers to use CGI to reduce PFI’s own risk.

Fig 34: Proposal for eased collateral lending

	End-borrower interest	PFI margin	CGI margin	PMU and MOPF margin	Loan term
SME TSL (existing)	8.5	4.5		4.0	Long
SME TSL (proposal)	8.0	4.0		4.0	Long
Non Collateral	13.0	9.0		4.0	Short
Non Collateral+CGI	13.0	6.0	3.0	4.0	Short
Eased Collateral (LTV >50%)	8.5	4.5		4.0	Long
Eased Collateral+CGI	10.0	4.0	2.0	4.0	Long

Source: Compiled by JICA study team

#### 5-4-5 Measure to encourage competition between PFIs: “M-League” (Proposal 3)

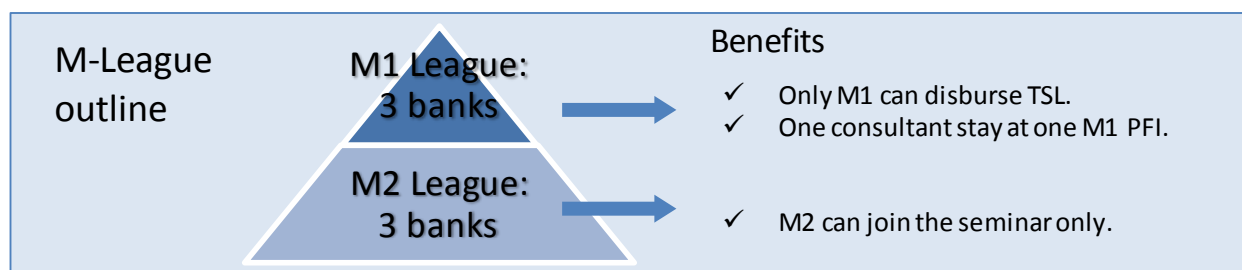
It is necessary to constantly revise PFI, e.g. annually, in order to slash away vested interest and to keep a principle to promote SME lending. We recommend to narrow PFIs down to three banks out of current 6 PFIs (seventh PFI is already approved in the existing TSL, although it has not lent to any SME).

Moreover, we propose to introduce competition mechanism, named “M-League”, where banks compete to gain only three sheets of official PFIs in a fair and clear rating method. After competition, top 3 banks are named “M1” and next 3 banks are named “M2”.

M1’s benefits are disbursement of TSL and credit appraisal capacity building by all-time consulting service, c.f. section 5.3.2 for the detail of capacity building. M2’s benefit is only capacity building in group training. M2 cannot disburse TSL at all.

Selection method of M1 and M2 should be considered later. The important things are clearness and transparency, because the reason of encouraging competition is to slash away the environment of lender advantage and to make banks to step forward to SME finance voluntarily. Therefore, we have to show banks clear target to do. As concrete criteria, number of non-collateral lending, average amount of LTV ratio, average amount of LTV ratio in top 10 borrowers, number of CGI lending, proportion of long-term deposit (over 1 year) to total deposit, proportion of long-term loan (over 1 year) to total loan amount, and lending experience to Japanese related company mentioned in section 5-4-6.

Fig 35: Outline of M-League



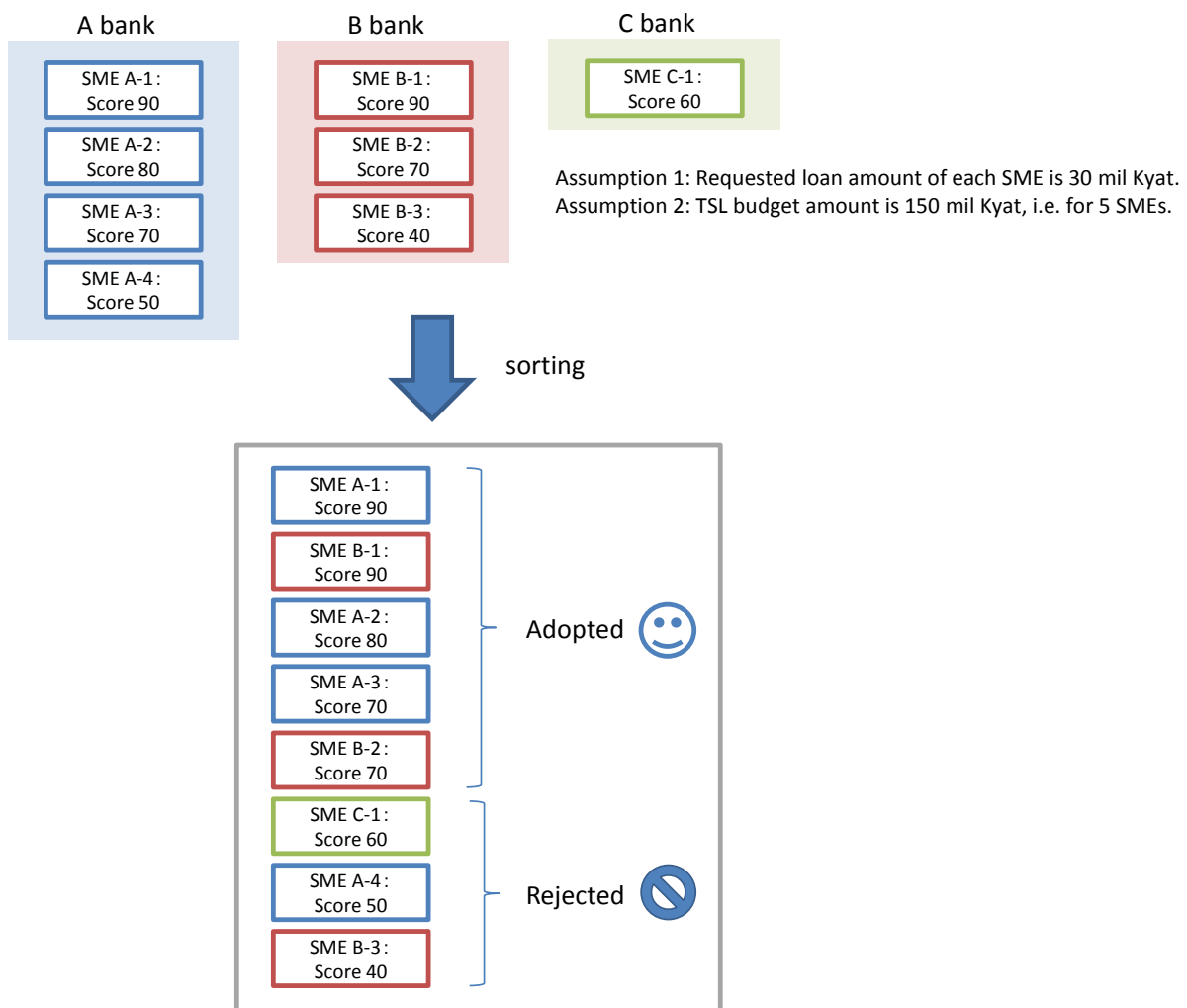
Source: Compiled by JICA study team

#### 5-4-6 Measure to select end-borrowers by PMU (Proposal 4)

One of measures to slash away situation of lender advance is to select end-borrowers by PMU. Of course, PFI takes a default risk and end-borrower should be passed in credit appraisal by PFI. We propose that PFI executes initial screening, i.e. credit appraisal, and then PMU executes the second-stage screening. In the second-stage screening, PMU rates applicants score by LTV ratio, CGI usage, loan term, proportion of working capital to loan amount (maximally 20%), capital investment item, amount of invested to Japanese item, increase in employment accompanied with capital investment, and proportion of export amount to total sales. Then, PMU chooses end-borrowers in order of score.

Important point in second screening is transparency. In order to avoid criticism of PMU arbitrariness, score calculation method should be clear and opened in public. It is desirable for PFI to be able to calculate its customer (SME) score in advance by itself. PFI anticipates acceptance line and choose customers strategically as applicants. The following figure is screening flow image. Just for simplicity, we assume that all SME applicants require 30 mil Kyat borrowing and total TSL budget in the month is 150 mil Kyat, i.e. for 5 SMEs. PFI is expected not to recommend low scored SME, because PFI can estimate each applicant's score. In the case of the following figure, acceptance line is score 70. Non-selected SMEs can re-apply in the next time if SMEs desire. In some cases, PFI and SME may consider strategy to change lending conditions to increase score.

Fig 36: PMU's Screening flow image



Source: Compiled by JICA study team

#### 5-4-7 Promoting trading with Japanese related company (Proposal 5)

In order for SME to enhance its technology and supply value-added items sustainably, cooperation with a foreign company is effective. “Cooperation” has many meanings, e.g. JV with a foreign company and technological collaboration. As a model case of technological collaboration, we introduce one company, which joined “Myanmar CEO sales meeting & seminar” on 26 January, 2016 by “SME support, Japan”. The company is SME in Myanmar manufacturing small electric transformer and sells them as parts of air-conditioner to Japanese company in Thailand. The Japanese company transfers technology to the SME to improve its transformer quality.

Such Myanmar SMEs to trade with Japanese related company is considered to exist to some extent, where Japanese related company is Japanese company and its subsidiaries in abroad, From the view point of both of support to SME by a foreign company and benefit of Japanese company, we propose a special allotment of TSL for the SME to have sustainable trading track record with Japanese related company.

#### 5-4-8 Requirement for company registration (Proposal 6)

At first, company registration was necessary condition for TSL application in existing TSL. However, Working Committee, which is multi-ministry committee to deliberate on and decide rules of TSL, decided to exclude company registration from conditions in order to promote micro- and small-enterprises applies TSL, which are not registered. Owing to the decision, micro- and small-enterprises’ application actually increased.

On the other hand, we have questions about the decision in terms of strengthening tax collection. Taxing authority cannot recognize the non-registered SME existence as a company. That results in the risk of tax cheating. Of course, some non-registered SMEs pay tax correctly with appropriate declaration of business income as personal income. However, if taxing authority cannot recognize the company, it is difficult for tax authority to determine adequacy of the business income amount.

Currently, Myanmar government considers strengthening tax collection as one of the important policies. In terms of consistency of the policy, we recommend requirement for company registration again.

#### 5-4-9 Requirement for SME card (Proposal 7)

PMU confirms the adequacy of SME-ness for applicant in existing TSL. SME cards, which SME Center provides, currently spread to more than 7,000 SMEs. In order to reduce burden of PMU paperwork, we propose to require an applicant to submit SME card.

The requirement encourages SME to gain SME card. Therefore, it results in collaboration between TSL and SME center policy. It should be pointed that, in such case, a malicious non-SME company may intend to gain SME card in order to apply TSL. SME Center does not assume such malicious applicant in current screening process. Improvement of screening process and further tighten assessment are necessary.

### 5-5 Proposal for other JICA aids (grant and TA) in SME finance sector

#### 5-5-1 Capacity building of CBM

As mentioned in section 5-1, capacity building of CBM is necessary in SME finance sector. In terms of relaxing collateral conditions, it is especially important for CBM to improve evaluation and management function for risk management policy submitted by a bank. In terms of interest liberalization, banking supervision should be strengthened. We propose that JICA sends consultants to CBM to promote to resolve these issues.

As mentioned in section 5-3-2, we also proposed consultants to be sent all-time to PFI in order to

negotiate with CBM regarding risk management policy. The consultants are supposed to implicitly enhance assessment capacity for the risk management policy of CBM through the negotiation. CBM consultants and PFI consultants can collaborate to promote relaxing regulation through the policy management.

#### 5-5-2 Technical assistance for PFI

After regime change, Myanmar government has focused on reducing consultant fee of Yen-loan. Myanmar government has a concern about the all-time consultants' fees in M1 PFI, which are one of benefits for M1 PFI, mentioned in section 5-4-3. We propose not only Yen-loan but also another budget, i.e. technical assistance.