MICRO-FINANCE / MACRO-CHALLENGES

Identifying and responding to the constraints faced by Myanmar microfinance institutions

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Micro-finance / Macro-challenges
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Executive summary

Microfinance institutions (MFIs) play a critical role in Myanmar, providing both rural and urban populations with the credit they need to finance purchases of working capital, agricultural inputs, and other goods and services. The sector experienced rapid growth between 2012 and 2020, with the number of MFI clients reportedly increasing from around 1 million to around 6 million over this period. Alongside fast growth in lending, Myanmar MFIs have contributed significantly to financial inclusion, particularly of women, who comprised 86 percent of MFI clients as of December 2023.

This policy note provides a short overview of the recent history of the microfinance sector in Myanmar, tracing its rapid growth over the decade to 2020 and assessing its contribution to economic activity and the livelihoods of otherwise unserved populations. It analyzes the impact of the COVID-19 pandemic and the February 2021 military coup on MFI lending and operations, drawing on up-to-date data from the Financial Regulatory Department (FRD) and synthesizing the findings of recent studies and surveys.

It shows that while MFIs have exhibited a degree of resilience to the economic and political shocks that have struck Myanmar over the last four years, constrained access to funding and a sharp increase in non-performing loans have limited their ability to support their clients to the extent that they did prior to the pandemic. The number of MFI clients and the total value of outstanding loans have fallen substantially since the end of 2020, by 43 and 32 percent respectively, with the exit of Pact Global Microfinance Fund (PGMF) in June 2023 contributing significantly to these declines. As a result, there is evidence to suggest that large numbers of clients are currently missing out on MFI loans.

Finally, it sets out several interventions – based on precedents and experience in Myanmar and in the region – that could help Myanmar MFIs sustain and expand their operations, at a time when new lending is critically needed. Potential channels for providing financial support to Myanmar’s MFIs include: (i) new credit lines to MFIs to alleviate funding constraints and enable expansion of their lending operations; (ii) risk-sharing arrangements with banks, such as loan guarantees, to reduce collateral requirements and borrowing costs for MFIs; and (iii) equity investments or targeted grants to allow MFIs to write off legacy NPLs and/or provide targeted support in specific areas of need. Such measures, if pursued, could help to support new micro-lending, raise economic activity – particularly of women in lower-income communities – and alleviate ongoing pressure on the livelihoods of some of Myanmar’s most vulnerable people.

A short overview of microfinance in Myanmar

1. Myanmar’s microfinance sector grew rapidly over the decade to 2020. Between 2012 and 2020, the number of microfinance clients reportedly rose from about 1 million to 6 million (to around 17 percent of Myanmar’s adult population).¹ The number of indirect beneficiaries of micro-lending – e.g. members of the same household as MFI clients – is likely to be significantly larger again. Total outstanding microloans reached US$1.2 billion as of early 2020, up from less than $50 million in 2012. As of December 2023, there are 178 MFIs operating in Myanmar: 116 are locally owned, 54 are foreign owned, and 8 are joint ventures. The sector is relatively concentrated, with the top 25 MFIs – almost all of which are foreign owned – controlling around 80 percent of assets.

2. MFIs have played a vital role in providing microloans and other financial services to those who would otherwise have lacked access to credit. Formal access to finance (through banks and other regulated financial institutions such as MFIs) increased markedly from 30 percent of the adult population in 2013 to 48 percent in 2018 (Finscope 2018) – with the bulk of this increase accounted for by the expansion in the number of microfinance clients over the same period (Figure 1). The expansion of MFI loans played a pivotal role in supporting otherwise underserved rural and urban populations. In 2020, over a third of total loans by value were disbursed to the agriculture and livestock

¹ These aggregate data (see also Figure 7) may overestimate total MFI client numbers to the extent that they are affected by double-counting of clients: i.e. MFI clients who take loans from more than one MFI have the potential to be counted more than once in these data.
sector, while most of the remainder went to clients engaged in commercial trade and other services, as well as manufacturing (Figure 2). The proportion of agricultural micro-loans has increased further since 2020 with agricultural borrowers proving to be more resilient than borrowers in other sectors (USAID TIGA 2023). These loans are typically used to buy inputs such as seeds, fertilizers, and pesticides, and are often structured to allow farmers to repay after selling their harvests. MFI loans also help micro and small enterprises engaged in manufacturing, trade and other services to meet their working capital needs, with some also using the loans to fund investment and expansion. Some loans (included as part of the ‘services’ category in Figure 2, or recorded separately as ‘education’) are also used for family purposes, including to cover school fees and medical expenses (IFC 2020).

3. **Total MFI assets (largely loans) comprise a relatively small proportion of total financial sector assets, but MFIs serve significantly more individual clients than do banks.** As of September 2020, MFIs had total loans outstanding of around MMK 2.5 trillion, compared with private banks that had around MMK 27 trillion in outstanding loans, and state-owned banks that had MMK 4.2 trillion in outstanding loans (MMFA et al, 2022, and FRD data). But Myanmar MFIs served up to 6 million clients in 2020 (as reported by FRD) compared to an estimated 2.2 million clients in the banking sector. In some cases, MFI lending is provided alongside lending from the state-owned Myanmar Agricultural Development Bank (MADB; see Box).

**Figure 1: Formal financial inclusion in Myanmar**

![Formal financial inclusion in Myanmar](image1)

**Source:** FinScope 2018

**Figure 2: MFI loans by sector**

![MFI loans by sector](image2)

**Source:** FRD

4. **Unlike banks, MFIs play an important role in providing small loans to clients in rural areas, without collateral requirements.** MFIs are subject to a maximum loan size limit which was introduced to ensure widespread access to MFI credit. The maximum loan size was initially set at MMK 500,000 in January 2014, but later increased to MMK 5,000,000 in October 2014, and further to MMK 10,000,000 (around USD 6700) in April 2017.² The majority of MFI clients and loans are in rural areas outside Yangon and Mandalay (Figures 3 to 5), in sharp contrast to the much more concentrated distribution of private bank loans. In 2020, 77 percent of the value of private bank loans outstanding were made to clients in Yangon, while MFI lending is much more evenly distributed across states and regions (Figure 5). Moreover, despite the much smaller overall loan books of MFIs, in some states and regions (e.g. Ayewarwaddy, Magway, Sagaing, Mon) the kyat amount of MFI lending rivals that of private bank lending (Figure 4), with much larger numbers of clients benefitting from MFI lending in these parts of the country. Finally, all MFI loans are unsecured (by FRD regulation), removing a key

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² Despite the increases in borrowing limits, there is evidence (e.g. see IFC 2020) to suggest that a substantial proportion of clients borrow from two or more MFIs to access the desired amount of credit.
constraint to access to finance among rural populations. In contrast, of the private bank loans outstanding in 2020, only 2 percent were unsecured (MMFA et al, 2022). In some cases MFI lending is provided alongside lending from the state-owned Myanmar Agricultural Development Bank (MADB; see Box 1), though MADB lending also requires collateral in the form of land ownership certificates.

**Figure 3: Geographic distribution of MFI clients**
(as of 2020)

Source: FRD

**Figure 4: Loans outstanding by state and region**
(as of 2020)

Source: FRD

**Figure 5: Distribution of loans by state and region**
(as of 2020)

Source: FRD

5. **Myanmar MFIs play a particularly crucial role in providing access to finance to women.** Women comprised 86 percent of microfinance clients as of December 2023 (Figure 6). MFIs have played an important role in increasing women’s access to finance given they often face additional barriers to accessing other formal forms of credit (including a lack of access to hard collateral). In 2018, the regulated maximum MFI interest rate is 28 percent per annum (2.3 percent per month), compared with maximum interest rates on bank secured and unsecured lending of 10 percent and 14.5 percent respectively, effective May 2020.
85 percent of surveyed female MFI clients relied on microfinance as their only form of formal credit, with women reportedly half as likely as men to borrow from banks.\(^4\)

*Figure 6: MFI clients and loans outstanding*  
(as of December 2023)

\[\text{Source: FRD}\]

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**Box 1: The Myanmar Agricultural Development Bank**

The state-owned Myanmar Agricultural Development Bank (MADB) has branches in about 60 percent of townships, with the majority in rice-producing regions in south and central Myanmar. It is funded almost exclusively by the Myanma Economic Bank (MEB), also a state-owned bank. In 2023, MADB provided loans to approximately 1.8 million farmers, serving a similar market segment to MFIs.

Typically, MADB disburses agriculture loans to small-scale farmers at the rate of 150,000 kyat per acre for paddy (around US$45 at end-2023 exchange rates) and 100,000 kyat per acre for other crops. Farmers can borrow against a maximum of 10 acres of farmland, and MADB takes land ownership certificates from farmers as collateral for these loans. Some farmers have reported borrowing from MADB while seeking additional loans from MFIs (or informal lenders) to top up or bridge delays in MADB loan disbursements.

MADB lending provided financial support to farmers during the pandemic, including via COVID-19 loan top-ups. Over 80 percent of surveyed farmers reported getting regular MADB loans and 45 percent reported receiving COVID-19 special loans in the monsoon lending season. However, MADB lending has fallen significantly since that time: the value of monsoon loans outstanding as of September 2023 was about 50 percent lower than in 2020.

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6. **MFI loans in Myanmar are predominantly group loans, though the importance of individual loans has recently risen.** Group lending accounted for about 92 percent of the total number of loans disbursed in 2019, and in terms of client numbers group lending continues to dominate today – with these loans primarily benefiting women borrowers (*Figure 6*). The group lending model mitigates risks associated with the provision of uncollateralized loans as the burden of repayment is shared collectively. There is also some evidence to suggest that the group lending model has generated social capital within communities by incentivizing borrowers to monitor and moderate the financial behavior of their peers.

The 2022 MFI health check (MMFA et al, 2022) reports that most MFIs (both pre- and post-pandemic)

\(^4\) FinScope (2018) found that 30 percent of men were currently borrowing from a bank, or had done so in the last 12 months, compared to 15 percent of women.
predominantly made group-guaranteed loans for 6 to 12 months for 400,000 to 600,000 MMK (US$200-$300); the relatively small size of these loans reflects the willingness of other group members to provide group guarantees on their repayment. That said, the proportion of individual clients and loans has increased, in part reflecting efforts to provide larger loans to larger businesses who cannot access finance from banks due to interest rate caps and collateral requirements (USAID 2020). As of December 2023, clients benefitting from individual loans comprised around 18 percent of all MFI clients (Figure 6). Average outstanding group loans per client stood at around MMK 400,000, whereas average outstanding individual loans per client were significantly larger at around MMK 1.2 million. Given the larger average loan size, individual clients currently receive nearly 40 percent of the value of all MFI loans (Figure 6).

7. **Myanmar MFIs play a comparatively small role in accepting savings deposits, due in large part to regulatory restrictions.** As of December 2023, only 28 MFIs out of 178 operating in Myanmar were deposit taking. Until late 2016, MFIs had not been allowed to take voluntary savings of more than 5 percent of the loan value from their borrowers (“members”). Although this limit was subsequently lifted, MFIs are still restricted to taking deposits only from their borrowers, and not from the general public. MFIs who wish to take voluntary deposits must apply for a separate deposit taking license, which mandates a minimum requirement of two consecutive years of profitability and operation for a minimum of three years. The maximum amount of voluntary savings from active clients cannot exceed 10 million kyat.

8. **MFIs have historically faced constraints on their ability to borrow from local and foreign financial institutions and international lenders.** With deposits only around 6 percent of loans (MMFA et al, 2022), MFIs are required to either borrow or rely on their equity to fund their loans. But borrowing can also be challenging. Prior to 2015, local MFIs were only allowed to borrow from the Myanmar Economic Bank (MEB). As of 2015-2016, MFIs could borrow from other local private banks, but borrowing was limited by the maximum debt-to-equity ratio of 5:1, and the collateral requirements imposed by local banks increased the effective cost of funds. International MFIs can borrow from formal financial institutions outside the country, subject to the maintenance of a maximum a debt-to-equity ratio of 5:1 and a maximum individual loan amount of USD 3 million. In 2016, a new regulation was issued which allowed international MFIs to borrow from local banks, and local MFIs to borrow internationally: this was an important driver of subsequent growth in MFI lending (USAID 2020). Nevertheless, foreign loans require approval from the Central Bank of Myanmar (CBM) through FRD, which often takes several months. In addition to providing technical assistance to the sector, development partners have played an important role in catalyzing foreign investment, hedging foreign currency risks, and providing guarantees for funding from local banks, mitigating the impact of costly collateral requirements.

9. **The broader regulatory framework has evolved since 2011, supporting the growth of the MFI sector.** The enactment of the Microfinance Business Law in 2011 paved the way for microfinance institutions (MFIs) to become important providers of financial services in Myanmar. The law aimed to establish a legal framework for MFIs to operate transparently and sustainably, with the objective of promoting financial inclusion for low-income households and microenterprises. This framework allowed both local and foreign investors to establish fully privately-owned MFIs, and authorized those foreign-owned MFIs that were operating before the law was established. Several regulatory and supervisory agencies were established. The Microfinance Business Supervisory Committee (MBSC), formerly known as Myanmar Microfinance Supervisory Enterprise (MMSE), was formed under the Ministry of Planning & Finance (MOPF) and chaired by the Minister. In September 2014, the Financial Regulatory Department (FRD) was established under the MOPF to provide support to the MBSC and to regulate and supervise MFIs.
10. **Significant progress in improving the regulatory framework was achieved in the next few years.** FRD, through the MBSC, implemented several key prudential regulations, including on solvency, liquidity, and risk management, in line with international best practices. These regulations played an important role in ensuring the stability, sustainability, and soundness of the microfinance sector. Additionally, regulations were introduced that imposed limits on a single borrower, emphasizing the importance of stringent controls over related party lending to prevent potential risks and failures of MFIs. Separate instructions were issued for loan portfolio monitoring, including directives for loan provisioning and managing NPLs, aimed at enhancing overall financial stability by safeguarding MFIs’ solvency and preventing failures. In 2019, FRD issued a directive mandating that all MFIs should comply with customer due diligence guidelines for AML-CFT oversight.5

11. **However, a new draft MFI law that was prepared in 2018-19 was not subsequently enacted.** The draft law would have allowed MFIs to take deposits from non-borrowing customers who reside in the townships where the MFI is licensed, broadening the pool of potential customers, bolstering access to financial services and increasing MFIs’ access to deposit funding. It would also have allowed MFIs to take collateral on loans, to support their risk management efforts in the context of the recent expansion in individual lending.

**Impact of recent shocks**

12. **The COVID-19 pandemic was a set back to the expansion of the MFI sector in Myanmar.** MFI client numbers plateaued in 2020 (Figure 7). Repeated lockdowns and social distancing measures directly impacted the face-to-face business models of MFIs, hampering both loan disbursements and collections. Growing risk aversion in financial markets exacerbated pre-existing financing issues. And the real economic slowdown stressed clients’ ability to repay, leading to a spike in NPLs. Based on reports prior to the onset of the pandemic, the NPL ratio stood at less than 1 percent in 2019. But COVID-19 spurred a sharp surge in NPLs, with MMFA data indicating that the portfolio at risk (repayments overdue > 30 days) had increased to 12.4 percent of the overall loan book by the end of 2020 (Figure 11).

13. **Nevertheless, the government's efforts to provide policy relief and financial support in 2020 played a significant role in maintaining the resilience of MFIs and driving continued growth in their lending (Figure 8).**

   - As part of its COVID-19 economic relief plan, the government allocated MMK 200 billion from its general reserve fund toward MFIs, which was disbursed through MEB under two loan schemes: i) three-year maturity loans with one year grace period, with max 11.5 percent interest rate; ii) one-year loans at a 1 percent interest rate, to be on-lent to tea shops and restaurants at a maximum 2 percent interest rate, with terms replicating the underlying loan (IFC 2020). Some MFIs were also granted loan deferments.

   - Several policy relief measures were implemented by the FRD through the MBSC. A directive was issued to ease loan loss provisioning requirements from 2 percent to 1 percent of the total loan portfolio (including NPLs and restructured loans). Additionally, MFIs were instructed to temporarily suspend the compulsory requirement for borrowers to make savings deposits, cease loan collections (and interest accruals), and reschedule loan terms and maturities.

14. **The operating environment for MFIs has become much more difficult in the aftermath of the COVID-19 pandemic and the February 2021 coup, with a corresponding drop in lending to populations in need.** There has been a marked decline in both MFI clients and outstanding loans since 2021 (Figure 7 and Figure 8). At the end of December 2023, the sector had 3.5 million clients,

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5 Further directives requiring MFIs to implement AML/CFT risk-based management strategies were introduced in 2022.
with a loan portfolio valued at under MMK 2 trillion, both well down from 2020 levels (Figure 7 and Figure 8). As of December 2023, the number of MFI clients and the value of outstanding loans had declined by 43 percent and 32 percent respectively over the previous three years.

15. There have been several drivers of the fall in MFI lending and clients since early 2021. As of June 2022, 74 percent of MFIs had reportedly experienced declines in client numbers compared to December 2020. The MFI sector had lost 315,000 clients or 8.1 percent of total clients as of June 2022, with the value of loans declining by around 10 percent over the same period (MMFA et al, 2022). MFIs have reported insufficient liquidity to make new loans, including because of a decline in repayments from outstanding loans (as well as a range of other funding issues; see below). Moreover, a sharp increase in NPLs in 2020 and 2021 forced MFIs to reduce their number of customers (through loan write offs/forgiveness) and take a more cautious approach to new lending, leaving them with a smaller client base (USAID TIGA 2023). MFIs also faced several operational constraints over this period, including heightened security challenges for staff and customers; logistics and banking sector disruptions, which made it more difficult to withdraw and move physical cash; and internet outages, which disrupted internal management systems and mobile money operations (IFPRI 2021).

16. The closure of the Pact Global Microfinance Fund in June 2023 had a significant additional impact on overall MFI activity in Myanmar. Prior to closing, the Pact Global Microfinance Fund (PGMF) accounted for around a quarter of all MFI lending in Myanmar, playing a leading role in providing microloans to rural villagers. PGMF began collaborating with nine local NGOs in 2013 to develop and expand microfinance operations in remote areas of the country, supported by funding from the Livelihoods and Food Security Fund (LIFT). Notably, 99 percent of its clients were women, and its lending supported nearly 1 in 10 households across Myanmar. Its closure in June 2023 affected almost a million borrowers, leaving a vacuum of microfinance services in many of the areas in which PGMF previously operated (Box).

**Figure 7: Number of MFI clients**

**Figure 8: MFI loans and saving deposits**

17. There have been particularly severe impacts on MFI clients in conflict affected areas such as Sagaing and Magway, where microfinance has traditionally had a prominent role. In Magway and Sagaing, around 18 and 12 percent of the population respectively (close to 700,000 people in both
cases) were MFI clients as of 2020, but client numbers have since declined by around half in Magway and almost two thirds in Sagaing, and there have been similar changes in the value of loans outstanding (Figure 9 and Figure 10). While the penetration of MFI lending in Rakhine and Kayah was comparatively lower in 2020, client numbers and loans have subsequently fallen by 70-80 percent in both regions. Ayewaraddy, Yangon and Mandalay have also seen significant declines in MFI activity over the past three years.

18. **On the asset side of the balance sheet, the major challenge confronting MFIs is the marked rise in non-performing loans resulting from economic contraction and the escalation of conflict.** The MFI Health Check (MMFA et al, 2022) found that the NPL ratio rose from 9.6 percent in December 2020 to 25.3 percent in May 2021, increasing further to 28 percent as of June 2022. Data from the MMFA shows that the portfolio at risk (PAR) - with repayments more than 30 days overdue – increased from below 1 percent in December 2019 to 12.4 percent in December 2020 and peaked at 33.9 percent in December 2021, before subsequently easing to 23.1 percent as at the end of 2023 (Figure 11). MFIs have indicated that the gradual decrease in NPLs since the end of 2022 has been due mainly to write-offs and restructuring of bad loans. Some MFIs are reportedly writing-off amounts equivalent to about half of new loan disbursements each month, while others are rescheduling repayment terms for legacy loans.° Liaison with MFIs indicates that a significant proportion of the NPLs have originated from loans disbursed in conflict areas, especially in the Sagaing region.

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**Figure 9: Change in number of MFI clients between 2020 and 2023**

**Figure 10: Change in MFI loans outstanding between 2020 and 2023**

*Source: FRD*  
*Source: FRD*

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° Myanmar Microfinance Sector Evolution: MFI Health Check Survey Results, Phase II, November 2022.
While provisioning for loan losses remains too low, MFIs’ reliance on equity financing has ensured a degree of resilience to the deterioration in asset quality. MFIs have been hindered by FRD provisioning requirements that only allowed the equivalent of 1 percent of the total loan portfolio to be allocated to provisions for loan losses. In June 2023, the FRD adjusted these requirements so that MFIs are mandated to set aside 1 percent of their loan portfolio for normal loans and 3 percent for loans that are past due by 30 days: nevertheless, such provisioning levels remain much lower than the amount of NPLs. On the other hand, the historically under-leveraged nature of the MFI sector has meant that balance sheets have remained relatively resilient to the recent deterioration in asset quality.

Prior to the pandemic, the overall solvency (equity to assets) ratio of Myanmar MFIs was reportedly early 75 percent (LIFT 2019). The November 2022 MFI health check (MMFA et al, 2022) found that even in the worst-case scenario of 100 percent write-off of June 2022 NPLs, all three tiers of MFIs (small, medium, and large) would be solvent in aggregate terms with an overall solvency ratio across the three tiers of 13.9 percent.\(^7\)

In contrast to older legacy loans (i.e. those disbursed in 2021 or earlier), a high proportion of which are non-performing, MFI loans provided since the beginning of 2022 appear to be performing relatively well. As of the end of 2023, MFIs reported that the repayment of new loans (particularly agricultural loans) over the previous 15 months had been much stronger than over the previous two years, with conditions on the ground stabilizing (USAID TIGA 2023). MFIs also

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\(^7\) Of the 53 MFIs in the sample, 9 were classified as ‘tier 1’, with over MMK 100 billion (USD 74 million) in total assets, 8 were classified as ‘tier 2’, and 36 were classified as ‘tier 3’ (total assets below MMK 10 billion). At a 100 percent write-off of existing NPLs, three tier 1 deposit-taking MFIs would become insolvent, and two smaller MFIs (one of which is a deposit-taking MFI) would become insolvent.
indicated that non-performing borrowers are still making efforts to pay off their loans as their financial situation stabilizes and improves.

**Figure 11: Portfolio at risk**
Proportion of MFI loans with repayments > 30 days overdue


21. **At the same time, access to the key sources of funding needed by MFIs to facilitate new lending – i.e. new deposits, loans, and/or equity injections – has become much more difficult.** This has meant that MFIs have needed to rely on recycling loan repayments as a source of liquidity for new lending (which does not imply an increase in total loans outstanding). Liquidity shortages were further exacerbated by the FRD’s 2020 directive to MFIs to cease enforced loan collections.

22. **Deposits have come under pressure as clients have needed to draw on savings to cope with recent economic shocks, while FRD restrictions on deposit taking remain a constraint.** Voluntary savings reportedly funded only 6 percent of MFI loans as of mid-2022 (MMFA et al, 2022). The economic shocks of 2021 triggered a sharp reduction of savings balances by 25 percent (MMK 38 billion or USD20 million) between December 2020 and June 2022, with clients reportedly drawing on their savings as a shock absorber to manage the difficult economic conditions and smooth their consumption (MMFA et al, 2022). In addition to a 2020 directive from the FRD to temporarily suspend the acceptance of savings deposits, other restrictions on deposit funding – including limits on depositors’ balances (maximum MMK 10 million per depositor) and the prohibition of deposits from non-borrowers – continue to constrain MFIs’ ability to raise new deposits. Such restrictions reduce the ability of poor and vulnerable households to benefit from access to interest-bearing savings accounts, while also curtailing MFIs’ access to a relatively stable and low-cost source of funds.

23. **International sources of funding have become almost impossible to access due to foreign exchange risks and restrictions, challenges in obtaining approval for international funds transfers, and instructions to suspend repayments on foreign loans.** Between February 2021 and November 2022, only one MFI had reportedly received a foreign loan (from its parent organization), while four MFIs had received foreign equity investments (MMFA et al, 2022). Regulatory approvals of foreign loans now face significant delays of up to 6 months (USAID TIGA 2023). Significant kyat depreciation and the emergence of a multiple exchange rate regime – which has been associated with persistent foreign currency shortages – have made it more difficult and costly for MFIs to hedge and repay existing foreign currency denominated loans, and to obtain new loans. Financial and foreign
exchange regulations introduced since 2021 have made it much more difficult for MFIs to access and transfer foreign currency, while a 2022 CBM direction to borrowers to suspend the repayment of interest and principal on foreign loans has created substantial uncertainty. These factors have all reduced the appetite and ability of foreign investors to lend to Myanmar MFIs.

24. **Borrowing from local banks is costly – in some cases prohibitively so – due to stringent collateral requirements.** Myanmar MFIs are typically required to post cash collateral equivalent to a large proportion of the total loan amount (typically 40 percent) before borrowing from local banks. This means that MFIs can effectively only access 60 percent of the funds they borrow, but are nevertheless obliged to pay interest on the entire loan amount. While some banks offer commercial loans to MFIs at an interest rate of 10 percent, in practice, MFIs end up paying effective interest rates ranging from 18 percent to 20 percent on the borrowed funds that they are able to access and on-lend to their clients. This is because there is generally a wide margin between the deposit rate MFIs receive for the 40 percent of funds held as collateral and the interest rate MFIs are charged on the full loan amount, while additional service fees are also imposed. While these collateral requirements have been a feature of local bank lending to MFIs for many years, interventions from development partners (e.g. in providing credit guarantees to reduce the need for MFIs to post collateral; see next section for details) had previously acted to reduce costs and improve MFIs’ access to local funding.

25. **These funding constraints – in combination with the deterioration in the quality of legacy assets – have made it difficult to meet ongoing demand for MFI lending.** In a rapid assessment conducted in December 2023 (USAID TIGA 2023), each of five sampled MFIs reported considerable excess demand by their customers for more lending, with four of the five noting that they were unable to raise new funds to expand their lending and were constrained to recycling repayments of previous loans. The MFIs reported that loan demand was high in conflict-affected areas and even IDP camps, consistent with the findings of an end-2022 survey of 2372 Vision Fund Myanmar clients (Vision Fund, 2023) that showed that borrowers in conflict areas faced particular financial and operational challenges and were in need of more avenues to access formal lending.

**Potential responses**

26. **Supporting the microfinance sector with financial and technical assistance has the potential to be an effective means of improving livelihoods and economic activity in Myanmar.** Given additional support to deal with the challenges outlined above, MFIs – which remain independent of the authorities – could play a larger role in backing productive private sector activity and cushioning the impact of testing economic conditions, particularly for women in lower-income communities (MMFA et al, 2022). MFIs are particularly well-placed to engage segments of the population that are at risk of sliding into poverty. Data from Myanmar Living Conditions Survey in 2017 shows that 10.3 percent of households in the bottom two quintiles of the distribution had taken loans from MFIs, compared with 8.2 percent of households in the top two quintiles. More recent data from IFPRI’s Myanmar Household Welfare Survey (conducted in 2023) shows that 12 percent of rural and 10 percent of urban households have a loan outstanding with an MFI institution. In comparison, 20 percent of rural households and 27 percent of urban households report having outstanding loans from informal money lenders, suggesting scope for an increase in MFI penetration.

27. **The MFI sector has two distinct and urgent needs: (i) sourcing funding, and (ii) managing a deteriorating loan portfolio.** Greater access to funding would allow loan volumes to increase, meeting currently unmet demand from MFI clients. NPLs, which still comprise a substantial proportion of MFI loan portfolios, hinder new credit growth and raise potential solvency concerns among some MFIs, increasing their funding costs.
28. **There are several possible ways in which financial assistance could help Myanmar MFIs address these needs.** New credit lines would directly provide an additional source of funding to enable new MFI lending. Credit guarantees could help MFIs unlock kyat loans from local banks on more sustainable terms. Recapitalization through equity investments or targeted grants would allow MFIs to write-off legacy NPLs while mitigating the associated pressure on solvency ratios. Such interventions would be supported by a continuation of efforts by international lenders to reschedule and/or write down loan repayments: these efforts have already helped some MFIs improve their financial position and their attractiveness to potential lenders. These ideas are not new: several partners have been and continue to be engaged in interventions along these lines, and other recent analyses of Myanmar’s MFI sector have put forward similar recommendations (see e.g. MMFA et al 2022, USAID TIGA 2023, and IFPRI 2021).

(i) **Credit lines:** As detailed above, key sources of international and domestic funding have become much harder to access in recent years. Development partners could directly provide loans to MFIs on favorable terms to ease their funding constraints and allow them to expand their lending operations (which would at the same time raise MFI profitability and help them to meet the cost of resolving NPLs).

(ii) **Risk-sharing with other financial institutions:** Myanmar MFIs face stringent borrowing terms and cash collateral requirements from local banks. A risk-sharing arrangement (e.g. provision of loan guarantees to local commercial banks that extend credit to MFIs) could reduce these collateral requirements and ease the effective cost of borrowing for MFIs. Reducing constraints to kyat lending from local banks also has the advantage of avoiding risks associated with foreign exchange transactions and cross-border payment flows.

(iii) **Equity investments/targeted grants:** While MFIs were generally well-capitalized in early 2020, lower repayment rates (primarily on legacy loans) and provisioning ratios in the period since imply that write-offs could pose a threat to MFI solvency in some cases (MMFA et al, 2022). A targeted grant or equity injection would bolster the asset and equity positions of beneficiary MFIs, allowing them to write off NPLs and/or increase provisioning levels while maintaining the solvency of their overall balance sheet. Grant funding could also allow partners to support the provision of (subsidized) credit to targeted vulnerable populations through MFIs, in those situations where alternative channels to provide financial support are unavailable.

29. **In practice, the success of such financial interventions would depend on the extent to which they are a) tailored to meet the specific needs of beneficiary MFIs; and b) targeted in a way that facilitates meaningful increases in access to finance among populations in need.** Given that MFIs ultimately require kyat funding, and to the extent that local banks are currently less constrained in lending to MFIs than foreign entities, credit guarantees to local banks – provided under the condition that collateral requirements for the guaranteed portion of the bank loan to the MFI are waived – and other means of unlocking local sources of MFI funding may be most effective in the current circumstances. A related consideration is how to allocate support across individual MFIs. To ensure that any assistance facilitates a sustainable increase in access to finance among vulnerable populations, targeting could be based on several criteria, including the MFI’s financial position and quality of management, the sectoral coverage and geographic location of its client base, etc. Incentives could be provided for loans to be provided in conflict-affected areas or other areas of particular need e.g. through interventions to share the higher risk associated with such loans (USAID TIGA 2023). Coordination with the MMFA would be important in addressing these implementation questions.

30. **There are a range of practical implementation challenges and risks that would need to be addressed as part of any effort to provide financial assistance.** Regulatory restrictions on foreign
funding and foreign currency transactions, combined with ongoing exchange rate depreciation and volatility, could pose significant practical constraints to efforts to directly provide foreign loans or equity to Myanmar MFIs. Completing integrity due diligence on local banks and MFIs, and monitoring the use of any financial assistance provided, will be more challenging in the current context where information is scarce and financial and governance risks have increased. Risks of expropriation have likely increased, with heightened potential for an MFI to be arbitrarily charged with breaching frequently changing rules and regulations.

31. There are several examples of previous and ongoing MFI support projects – in Myanmar and in the surrounding region – that could potentially help inform the design and roll-out of further interventions. Myanmar MFIs have already successfully utilized catalytic investments, loan guarantees, hedging facilities, and technical assistance from partners such as USAID and LIFT. This assistance supported the rapid growth of the MFI sector between 2016 and 2020.

- LIFT initiated its Microfinance Capital Markets Program in Myanmar in 2016 due to MFIs’ high unmet demand for loan funding, due to a lack of access to local bank loans – in part attributable to an interest rate cap of 13 percent on commercial bank lending – and high foreign exchange risk for foreign investors.8 Among several programs designed to support Myanmar MFIs, LIFT collaborated with The Currency Exchange Fund (TCX) to establish a swap market to hedge foreign exchange risks, with LIFT providing a subsidy and TCX providing a hedging product which offsets currency risks for foreign investors. The capital investments made by LIFT through TCX successfully leveraged substantial loan funding from international investors, allowing recipient MFIs to expand their lending. By the end of 2020, USD 112.7 million in new loans had been provided by 22 international investors to nine MFIs. The portfolio outstanding as at the end of 2020 stood at USD 89.8 million, with LIFT’s MFI partners reaching around 200,000 clients in conflict-affected areas alone (LIFT 2020).

- Through its Development Credit Authority, USAID has funded 50 percent loan guarantees provided to MFIs and local commercial banks that extend credit to Myanmar MFIs. The first facility, which commenced in 2016, was USD 10 million provided as loan guarantees to five MFIs to encourage them to offer larger individual loans in rural areas, linked to farmers’ crop cycles. A second DCA facility was subsequently launched in 2018, amounting to USD 20 million, to reduce the costs of the expensive "back-to-back" loans offered to MFIs by a local bank. This facility provided a guarantee for bank loans to MFIs to remove the need for a cash deposit as collateral. It also supported a new phase in lending to MFIs, where the local bank could secure a lien on the MFIs’ portfolio, partially or entirely, in lieu of a cash deposit. These arrangements helped the beneficiary bank manage the credit risk associated with its lending to MFIs, eliminating the need for cash collateral.

- To date, the International Finance Corporation (IFC) has invested over USD 30 million in five local Myanmar microfinance institutions, in the form of both equity investments and loans. Financial support was aimed at positioning the underfunded microfinance sector to engage rural, low-income borrowers, amongst whom demand for microcredit was estimated to exceed supply by three-fold.9 Loans have been used to support MFI lending growth, while equity investments

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8 The Livelihoods and Food Security Fund (LIFT) aims to strengthen the resilience and sustainable livelihoods of poor households in Myanmar by helping people reach their full economic potential. LIFT is managed by the United Nations Office for Projects Services (UNOPS) and has received funding from 16 international donors. The current donors are the United Kingdom, the European Union, Switzerland, Australia, the United States of America, Canada, New Zealand and Norway. LIFT’s Financial Inclusion Program works to ensure that the most vulnerable people in villages and wards across the country, irrespective of their economic and social status, can benefit from a developing rural financial market. Microfinance is the largest component of this program. See https://www.lifl-fund.org/en and https://www.lifl-fund.org/sites/lift-fund.org/files/publication/lift_annual_report_2020_en_final_16aug2021_compressed_0.pdf

have helped to ensure that supported MFIs are adequately capitalized, at the same time providing the foundation for partnership with IFC to drive innovation and spur developments in technology, financial products, and policy. The World Bank has also engaged in several microfinance projects in the broader region. As an example, the Scaling Up Sustainable and Responsible Microfinance Project (2010-15) aimed to scale up access to sustainable microfinance services to the financially excluded in India, particularly in under-served areas, through the introduction of innovative financial products and by fostering transparency and responsible finance. The WB provided USD 290 million in IDA and IBRD resources to the Small Industries Development Bank of India (SIDBI), that was to be lent to MFIs – structured as debt or quasi-equity financing – to allow them to on-lend larger amounts to the under-served and to leverage and crowd in private commercial funds. The project also promoted transparency and responsible microfinance through the development of a common information platform for MFIs to inform policy makers, MFI managers and funders. The Independent Evaluation Group’s (IEG) evaluation of this project found strong evidence of positive impact. In particular, SIDBI’s loan had a strong signaling effect on other lenders. In each year, the disbursed project funds were leveraged around 30 times by other lenders, exceeding the target performance indicator of four times.

- The Asian Development Bank (ADB) has also played an important role in promoting the development of microfinance and expanding financial inclusion across Asia. ADB’s Microfinance Program (MFP) is a credit enhancement and risk-allocation tool designed to promote local currency lending by commercial banks and financial institutions to MFIs.10 Under the Program, ADB shares the default risk—usually up to 50 percent—on wholesale loans to MFIs extended by its Partner Financial Institutions (PFIs). MFIs benefit from improved relationships and wider access to funding from commercial banks that share risk with the ADB, while PFIs benefit from the capital relief derived from ADB’s AAA credit rating, which allows them to mobilize funding for on-lending to MFIs and expand their risk appetite through increased counterparty MFI limits.

32. **Technical support and capacity building can also help MFIs manage their challenging operating environment: again there are several examples in Myanmar to draw on and build upon.** USAID TIGA has provided technical assistance to MFIs to help them diversify their sources of funding, expand their deposit base, develop credit scoring models, expand lending to the agricultural sector, and improve their risk management systems; they have also supported the organizational strengthening of the MMFA (particularly in close collaboration with ADA), including through the recent development of a MFI Certificate Program for MFI staff and earlier collaboration with the MMFA to advocate for key reforms (USAID TIGA 2023). LIFT has worked with MFI partners to promote digital financial services and a broader range of agribusiness lending products (LIFT 2020). The United Nations Capital Development Fund (UNCDF) supported MFIs in transitioning from NGO to company status, building their capacity for client outreach, lending operations, and regulatory processes (LIFT 2020). IFC has provided support to improve MFI operations (e.g. corporate governance, HR, treasury, audit, IT, Risk) and enhance staff and management capacity, including on digital transformation. Other partners have worked with MFIs to train loan officers, develop credit scoring and roll out new tools for credit risk management (MMFA 2023). FCDO is providing support on institutional capacity building and curriculum development to support the MFI sector.

33. **While Myanmar MFIs are currently facing challenges, this note has outlined several ways in which they could be supported in their efforts to meet ongoing demand for micro-loans, in circumstances where such lending is sorely needed.** Myanmar MFIs are currently facing severe constraints in their ability to provide access to finance to those who could make productive use of it. Nevertheless, through the recent period MFIs have continued to play a critical role in providing large

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10 https://www.adb.org/what-we-do/microfinance-program
numbers of Myanmar clients – particularly women – with funding for working capital, agricultural inputs, and family needs that otherwise would not be accessible to them on reasonable terms. Were it not for Myanmar’s MFIs, the impacts on livelihoods from recent political and economic shocks would have been much worse (MMFA et al, 2022). But Myanmar’s MFIs could be playing an even greater role. Despite high levels of demand for credit, the amount of lending that they can offer is limited by funding constraints and other operational disruptions. As a result, there is evidence to suggest that large numbers of clients are currently missing out on MFI loans, a situation exacerbated by the recent closure of PGMF. At the same time, there are several potential interventions – based on precedents and experience on the ground in Myanmar and in the region – that could be drawn and built upon to alleviate the funding and operational constraints that Myanmar’s MFIs are currently facing. Such measures, if pursued, could help to boost economic activity in the agriculture and services sectors – particularly for women in lower-income communities – and alleviate ongoing pressure on the livelihoods of some of Myanmar’s most vulnerable people.
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