MICRO BANKING IN INDONESIA

OVER

THE PERIOD OF MONETARY CRISIS

THE AVERAGE BPR
(Bank Perkreditan Rakyat/People's Bank)

of

JUNE 1996, JUNE 1999 and DECEMBER 1999

NEVER OFF TRACK

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JULY 2000

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1. Paper's Purpose: Show How the Average BPR Performed – From Pre-Monetary Crisis to Post-Crisis.

The BPRs - Bank Perkreditan Rakyat or *People's Banks* - are Micro Finance Institutions, licensed by central bank Bank Indonesia to operate as secondary banks. They are thus authorized for loan and deposit services. Current account and overdraft services are not allowed. They mainly service rural and suburban ' micro ' clientele and may thus be called Micro Finance Institutions (MFI s).

The purpose of this paper is to highlight the level of performance of BPRs in June 1996, June 1999 and December 1999. More specifically, the purpose is to show the performance level of *the average BPR* at the *pre-crisis period* June 1996, at the *end-of- crisis period* June 1999 and at the *post-crisis period* December 1999.

2. The Average BPR Profiled – Balance Sheet Data of June 1996, June 1999 and December 1999.

The number of BPRs licensed as secondary banks increased between June 1996 and December 1999 with 460, or with 23.5 %. In other words, additional licenses were given in the same period in which the total of national commercial banks decreased, due to the monetary crisis that started towards end 1997 and lasted until mid 1999. These licenses were however mainly given to already existing MFIs - to LDKPs - meaning that few new MFIs were licensed over the period of monetary crisis.

The BPRs report to Bank Indonesia's Directorate for BPR Supervision with monthly reports. Bank Indonesia publishes main data of these reports bi-annually, in January and June, in *Informasi Bank Perkreditan Rakyat*.

The average BPR could thus be calculated, by simply dividing the aggregate balance sheet data published in *Informasi BPR* by the number of reporting BPRs [1], and this BPR is therefore inclusive of the average LDKP who received BPR status [2].

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[1] The BPRs are officially called BPR Non-BKD (BPR Non -Badan Kredit Desa), because there are also BPR-BKD that were established earlier than these BPRs licensed by Bank Indonesia. There are 5240 active BKDs, on Java only. They are the smallest micro finance institutions. Outreach is therefore limited, in spite of their large number. They are supervised by Government-owned commercial bank Bank Rakyat Indonesia, on behalf of Bank Indonesia.

[2] The LDKP-type of micro finance institutions is the second largest group, in terms of numbers. They are not allowed to take in time deposits. In December 1999, there were 1620 of such LDKPs, most of them on Java. They are owned by the Provinces and/or Subprovince levels, and supervised by the Provincial Development Banks.

In terms of Total Assets and Sources of Funds, the average BPR developed over the 3.5 year period as follows:

THE AVERAGE BPR

	June 1996	June 1999	December 1999
Average BPR: Total Assets and Sources of Funds	Rp. 1,236 million	Rp. 1,235 million	Rp. 1,385 million
Calculation Base	1967 BPRs with Rp. 2.43 Trillion in Total Assets.	2420 BPRs with Rp. 2.99 Trillion in Total Assets	2427 BPRs with Rp. 3.36 Trillion in Total Assets

With total assets at Rp. 1.2 billion in June '96 and June '99 (now, January 2002, US $ 120,000 equivalent), and in December '99 at Rp. 1.4 billion (US $ 140,000 equivalent), the average BPR is relatively small. Taking all BPRs together, they are thus not bigger than one single medium-sized commercial bank in Indonesia.

This average small-sized BPR has remained profitable over the period of economic crisis and has never been off track, although the crisis has impacted on performance, as will be illustrated below. The average BPR could thus continually be rated healthy or sufficiently healthy by the central bank [3].

On average, the BPRs remained profitable for two reasons: (1) They operate solely in the Rupiah economy, unlike the national commercial banks, and (2) They applied prudent lending policies, again unlike a number of national commercial banks.

[3] For rating, the central bank used the CAMEL system, distinguishing four categories: healthy, sufficiently healthy, not sufficiently healthy and not healthy.

3. **Main Trends June 1996 – December 1999.**

Performance levels of the average BPR (thus non-existant) are summarized in the table below, with in addition observations on main trends.

The average BPR of June '96, June '99 and December '99.

	June 1996		June 1999		December 1999	
Main Balance Sheet Items	**N**	**%**	**N**	**%**	**N**	**%**
Total Assets and Sources of Funds; Rp. Million	1235.8	100	1235.5	100	1384.8	100
Loans Outstanding Rp. Million Number of Accounts	 989.8 871	 80	 831.6 808	 67.3	 969.5 865	 70
Demand Deposits Rp. Million Number of Accounts	 265.6 1984	 21.5	 283 1656	 22.9	 327.2 2429	 23.6
Time Deposits Rp.Million Number of Accounts	 503.2 67	 40.7	 402 93	 32.5	 476.3 92	 34.4
Equity/Own Capital; Rp. Million	198.6	16.1	241.6	19.5	270	19.5

<u>Total Assets and Funds</u>. Both the Pre-Crisis average BPR of June '96 and the End-of-Crisis average BPR of June '99 had Rp. 1.2 billion in assets and sources of funds. In real terms this indicates some contraction over the period of monetary crisis, because inflation rates have been in the two digits.

The Post-Crisis BPR of December '99 shows meanwhile some real growth, since total assets and sources of funds grew between June '99 and December '99 from Rp. 1.2 billion to nearly Rp. 1.4 billion, with the overall inflation rate for this 6-month period well below 10 %.

<u>Loans Outstanding and Accounts</u>. Loans outstanding was 80 % of total assets in June '96 and 67.3 % in June '99. With no nominal change in total assets, this shows a rather sizeable reduction in lending activity over the period of monetary crisis. This reduction was mainly caused by lack of funds, as time deposits were switched to commercial banks (see below), and not by reductions in the demand for loans during the crisis period.

The reduction in lending activity remained limited in comparison to the reductions in lending by the commercial banks, making very few new loans.

The lending volume of the average BPR quickly expanded again after June '99, defined as the end-of-crisis period, observing that loans outstanding had risen to 70 % of total assets by December '99; in Rupiah thus coming back to almost the level of June '96.

Demand Deposits and Accounts. Demand deposits show uninterrupted growth for the 3.5 year period; both in terms of total Rp. deposits and in terms of deposits as percentages of total sources of funds.

The BPRs have thus notwithstanding the monetary crisis been able to attract additional savings, despite the fact that the deposit rates were at around 12 % in the June ’96 – June ’99 period; well below the rates of commercial banks and the rates of main competitor BRI Units.
The number of passbook holders decreased however over the June ’96 – June ’99 period, but quickly rose again during the 6-month period June ’99 – December ’99. This should be attributed to the rise in deposit rates to between 16 and 18 %; as such above the rates of the commercial banks (at 12 % in this period), but still below the rate of BRI Units’ *SIMPEDES* saving facility.

Time Deposits and Accounts. Time deposits were in the pre-crisis situation 40.7 % of total sources of funds, but dropped to 32.5 % over the monetary crisis; nominally a reduction of Rp. 100 million per BPR. The number of accounts rose meanwhile in the same period. The causes for these trends have been: (1) Big depositors transferred their funds to the commercial banks offering rates as high as 55 %, (2) a few savers switched to the time deposit category, and (3) some new deposits could be attracted by ‘ passing them on ‘ to the commercial banks as interbank assets.

The data for December ’99 show that the average BPR has been able to attract around Rp. 75 million in time deposits in the 6-month period June ’99 – December ’99. This certainly relates to increases in deposit rates, sometimes to as high as 22 %, and as such around 10 percentage points above the rates in commercial banks.

Equity/Own Capital. Remarkably, equity grew over the crisis period for the average BPR; both nominally and as percentage of total sources of funds. In June ’99 equity was
19.5 % of total sources, and this level was maintained over the post-crisis period June ’99 – December ’99.

With equity growth coming from retained earnings, the average BPR remained profitable over the crisis period, and this by applying a low risk strategy: (1) maintenance of the spread margin, (2) placements of funds with commercial banks, (3) serving well-known repeat borrowers, often with reduced loan amounts, and (4) serving new micro borrowers from the Micro Credit Project credit line [4]. Profitability continued during the post-crisis period June ’99 – December ‘99, although equity as a percentage of total sources did not grow, remaining stable at 19.5 %. This has been the result of slightly narrowing net spreads, mainly caused by the rises in deposit rates referred to.

[4] Thus, without this credit line from Bank Indonesia – already ongoing before the crisis - few new first-time micro borrowers would have obtained loans during the crisis period.

4. Two Closing Observations

<u>Financial Sustainability Prospects</u>. With steady growth in equity, the average BPR performed quite well over the monetary crisis period, unlike the commercial banks that nearly all experienced negative equity growth, or saw equity drying up. Equity is as a result for the average BPR at 20 % of total sources of funds.

The BPRs should on average be able to strengthen this strong equity position further, because they have opportunities to grasp rather than problems to cope with. A BPR manager once referred to this indirectly when saying ‘ there is no need to change my strategy (of maintaining a wide spread margin) because people are lining up for my BPR’s services anyway ‘.

This being true in the short run, there are however reasons to introduce new policy ingredients that may narrow the spread margin, but *simultaneously* result in even better financial sustainability: E.g. somewhat lower lending rates coupled with continually competitive deposit rates will most likely result in additional demand for loans ánd in the funds for that. Through this, further increases in nominal profits may be expected, and profits are obviously are needed to finance growth, and are perhaps also needed to meet the Rp. 500 million minimum own capital requirement, applying to new BPRs but also being contemplated for existing BPRs [5].

<u>Competition and Further Development Options</u>. The 3700 BRI Units are in the financial sector the main competitors for the BPRs, while the BPRs are main competitors for the moneylenders of the informal sectors. This typically positions the BPRs as Micro Finance Institutions.

The BPRs are in the short run well-positioned to continue with what they are doing:
(1) Offer short maturity working capital loans to mainly micro borrowers in the ‘ informal ‘ trade sectors - against flat rates higher than the BRI Units’ flat rates - but competitive to money lenders, and (2) offer deposits against rates somewhat lower than the rates of again the BRI Units. In the long run however, and to combine financial sustainability with growth, additional strategy seems needed: (1) further competitive deposit rates to attract the funds for growth, (2) introduction of diversified loan products with longer maturities and with lower flat rates (e.g. home improvement loans and loans for solar energy sets), and (3) efficiency improvements (through e.g. further computerization).

In the long run, starting today, the BPRs are well positioned to continually combine financial sustainability with serving increasing numbers of micro clientele, inclusive of new first-time micro depositors and micro borrowers.

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[5] Although many BPRs are indeed small, it seems that being profitable and capable of adding retained earnings to equity is crucial rather than a specific minimum level of equity.