

The Evolution of Microfinance
Institutions in Indonesia from 1895 to
2003 and its Contribution to their
Resilience and Prosperity in the Face of
the Asian Financial Crisis of 1997-1998

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Discussion Outline

- Microfinance: Universal and Indonesian
- Indonesian Microfinance Institutions
- Asian Financial Crisis: Overview and Effects on Indonesian Microfinance
- Indonesian Family Life Survey

Why Indonesian Microfinance?

- “In terms of scale, variety, volume of microfinance institutions, market penetration and profitability, the micro-financial services market in Indonesia is the most developed in the world.”
(Berenbach and Churchill, 1997)

Microfinance

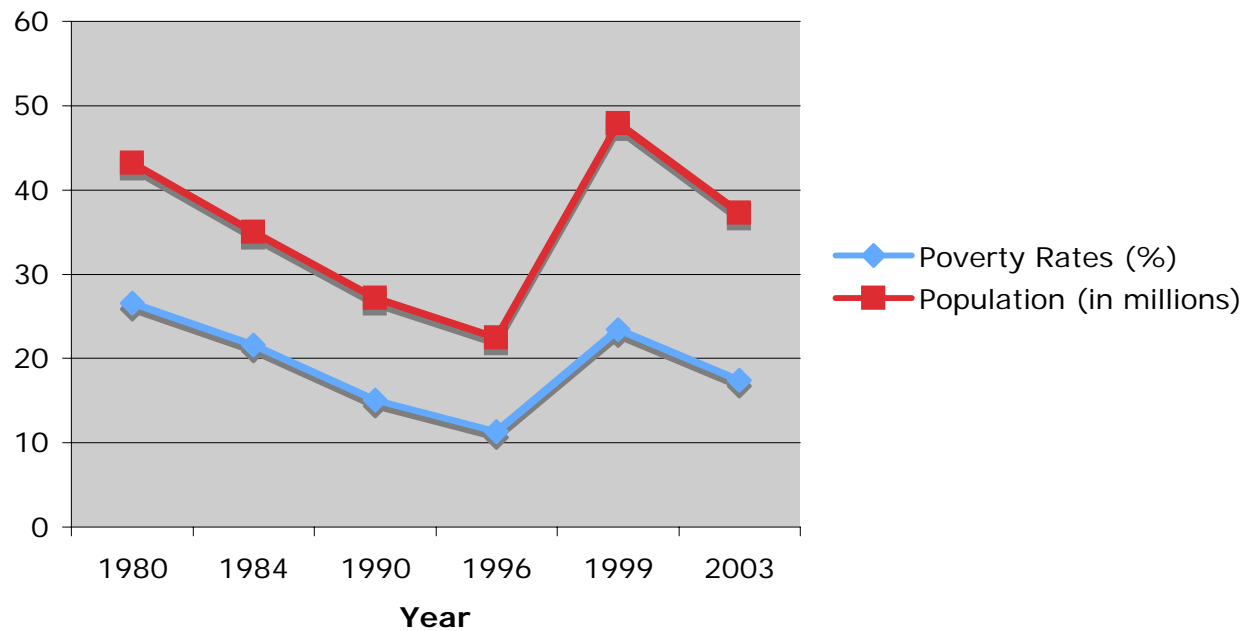
- Muhammad Yunus: Noble Peace Prize 2006
- Microcredit
- Microsavings Accounts
- Social Benefits
- Limitations and Criticisms

Indonesian Microfinance

- Early 20th Century: Rice Banks
- Great Depression: Transformation to Money Banks
- 1970's: Oil Investment
- 1980's: Liberalization of Banking System
 - 1983: Deregulation of Interest Rates and Loan Ceilings
 - 1988: Lift of Restrictions on New Banks
- 1992: Banking Law

Result of Deregulation

Poverty Rates and Population Living in Poverty from 1980-2003



What Makes Indonesia Different?

- Poorest of the Poor
- Government Policy: Help rather than Hinder
- Cross-Subsidize Formal Sector with Informal Sector
 - Example: Bank Rakyat Indonesia

Elements of Indonesian Microfinance

- Formal Sector
- Semiformal and Informal Sector
- Microfinance Clients
- Supervision and Regulation
 - Hybrid Approach
 - Tiered Regulatory Framework

Bank Rakyat Indonesia (BRI)

- 1946: Two Banks Merge
- 1970's: BIMAS
 - Unit Desas
- 1983: KUPEDES and SIMPEDES
- 1998: Three Strategic Banking Units (SBUs)

Semiformal Institutions

- Bank Perkreditan Rakyat (BPRs)
 - Chief rural banks
- Badan Kredit Desas (BKDs)
- Lembaga Dana Kredit Pedesaans (LDKPs)
- Badan Kredit Kecamatan (BKKs)
- Lembaga Perkreditan Desas (LPDs)

Informal Institutions

- Cooperatives
- Non-Government Organizations (NGOs)
- Role of Indonesian Government

Asian Financial Crisis 1997-1998

- Thailand- “Asian Miracle” to Domino Effect
 - Inadequate supervision and regulation of liberalized banking system
 - Excessive short-term debt from excessive capital inflows
 - Government guarantees on shady investment
 - Lack of micro-level accounting reports
 - Pegged exchange rates

Effects of Asian Financial Crisis on Indonesian Microfinance

- “Within the space of one year Indonesia has seen its currency fall in value by 80%, inflation soar over 50%, the economy flip 180 from rapid growth to rapid contraction, unemployment skyrocket, and the stock exchange lose its value.” (World Bank)

Enablers of Asian Financial Crisis

- Private sector short-term foreign debt double the amount of foreign debt of government (able to because of loose supervision and regulation)
- Unprofitable real estate investment
- Drought wiped out entire crop in 1997

Results of Crisis Onset

- Foreign exchange-denominated liabilities increased while banks' assets declined
 - IMF's failed intervention on private sector debt
- Default rate high on commercial and corporate loans
 - Interest rates doubled
- Banks Closing
- Political Instability

Result of Government Deposit Guarantee

- 1.3 million new savers for BRI unit desas
- Working Capital Credit for BPRs
- ‘Social Safety Net’ Programs

Monetary Values of Unit Desa Services at the Start and Height of the Asian Financial Crisis

Aug-97	Rp7.98 trillion	Rp4.41 trillion	Rp3.57 trillion
Aug-98	Rp15.13 trillion	Rp4.61 trillion	Rp10.52 trillion
Increase in %	89.60%	4.50%	194.67%

Reasons for Continued 97% Repayment Rate during Crisis

- Adjustable Loan Rates
- Solely Domestic Activity
- Social Collateral/High Value of Microservices
- Result: Microfinance Institutions Bail Out Rest of Banking System

Indonesian Family Life Survey

- Borrowing
- Assistance
- Employment
- Perception of Economic Hardship

This concludes the brief presentation.

Thank you.