German Savings Banks Foundation for International Cooperation (SBFIC)

Village Banks (*Village Savings and Credit Groups*) in Vientiane Capital, LAO PDR Roadmap Scenarios for a Sustainable Future

By

Prof. Dr. Hans Dieter Seibel

(seibel@uni-koeln.de)

18 February 2010

SBFIC Simrockstraße 4 D-53113 Bonn Phone +49 228 9703-634 Fax +49 228 9703-613
www.sparkassenstiftung.de nicole.brand@sparkassenstiftung.de

Table of contents

List of Tables

List of annexes

List of appendices

Exchange rate 2009: 1US$ = 8,500 LAK (Lao Kip)

Acronyms and abbreviations

ADRA	Adventist Development Relief Agency
BOL	Bank of Lao PDR
CARD MRI	Center for Agriculture and Rural Development Mutually Reinforcing Institutions
CPI	Committee for Planning and Investment (now MPI)
CODI	Community Organisational Development Institute, a Thai government agency
DID	Développement International Desjardins, Canada
DGRV	German Cooperative and Raiffeisen Confederation
EMI	Ekphatthana Microfinance Institution
FIAM	Foundation for Integrated Agriculture Managment, a Thai NGO
GBA	Grameen Banking Approach
GTZ	German Technical Assistance Agency
LCSDPA	Lao Community Sustainable Development Promotion Association
LVCA	Lao Village Credit Association
LWU	Lao Women's Union
MCBR	Microfinance Capacity Building and Research Project
MPI	Ministry for Planning and Investment
MFC	Microfinance Center
NERI	National Economic Research Institute
SBFIC	Savings Banks Foundation for International Cooperation
RFSDP	Rural Finance Sector Development Program
SRDP	Small Rural Development Project
TYM-Fund	Tao Yeu May ("Mutual Affection Fund"), Vietnam Women's Union
UNDP/CDF	United Nations Development Program/Capital Development Fund
VC	Vientiane Capital
VSCG	Village Savings and Credit Groups
VWU	Vietnamese Women's Union
WCEP	Women and Community Empowering Project
WFDF	Women and Family Development Fund
WFP	World Food Program
WIDP	Women in Development Project

1. Introduction

1.1 Microfinance terminology: what are MFIs to be called in Laos?

The term microfinance as introduced in the early 1990s comprises financial intermediation between low-income savers and borrowers without access to commercial banks. In the Lao PDR, the Policy Statement for the Development of a Sustainable Rural and Microfinance defines microfinance as "the provision of a broad range of financial services, such as cash based credit, deposits, insurance, etc, to the poor, low-income households, and their micro-enterprises".[1] Microfinance institutions (MFIs) are formal, semiformal or informal financial intermediaries[2] providing both microsavings and microcredit and possibly other financial services.[3] In recent years the meaning of the term has sometimes been reduced to microcredit. Microfinance overlaps with more recent terms such as inclusive finance, denoting access to finance for all, particularly low-income people, and responsible finance, mostly seen from a commercial banking perspective. There is no agreement on what constitutes microsavings and microloans, which vary widely between countries and institutions, except that the amounts should be *small,* which is relative. There are only few countries which have defined microloans, among them Laos with a ceiling of 10 million Kip ($1,175). Such a definition is best left to individual institutions, varying widely from self-help groups to commercial banks.

There is a large variety of terms for local microfinance institutions or activities in Laos. UNDP/CDF (1996:28), in the mid-1990s, used the term Lao Village Credit Associations (LVCA). The term should now be reserved to networks and organizations falling under the decree on associations of September 2009 under which funds cannot be registered. At the time BOL, APRACA & GTZ (1997: 29) simply used the term microfinance but noted that it "consists mainly of credit components in projects of different donor agencies." In their own terminology such projects promote credit groups, revolving fund groups, village revolving funds, village-based savings and credit societies, savings and credit societies or simply microfinance or rural financial services. The confusion between credit groups and savings and credit groups originally derived from the assumption of donors in Laos that people are too poor to save and therefore need revolving funds, until they realized that Laotians are eager to save, particularly women as the holders of the family purse. There has thus been a trend for credit groups to evolve to varying degrees into savings and credit groups.

In Vientiane Capital village-based microfinance institutions have expanded over the last ten years, covering now 90% of villages. Their main source of loanable funds are savings augmented by retained earnings; there are virtually no externally provided revolving funds. The promoters of these institutions refer to them as Village Savings and Credit Groups (VSCGs), a close translation from Lao. At inception the term group might have been

[1] Endorsed by the Prime Minister, PMO/1760, 17 December 2003. Recently the related action plan has been updated and approved. The definition is close to CGAP's definition: "Microfinance offers poor people access to basic financial services such as loans, savings, money transfer services and microinsurance. People living in poverty, like everyone else, need a diverse range of financial services to run their businesses, build assets, smooth consumption, and manage risks." (www.cgap.org).

[2] Formal financial institutions fall under the regulation and supervision of the central bank (or other officially designated financial authority); semiformal financial institutions are otherwise officially recognized; other financial institutions, such as indigenous savings and credit groups, are informal financial institutions. From a central bank perspective both semiformal and informal financial institutions are *nonformal.*

[3] According to CGAP (2008: xiii) "MFIs are defined as licensed and unlicensed financial institutions that include nongovernmental organizations, commercial banks, credit unions and cooperatives, and agricultural, development, and postal savings banks. They range from specialized microfinance providers to programs within larger, multipurpose development organizations."

appropriate; but as permanent institutions with an average size of 215 members and a maximum above 1,000, the term group is not appropriate.

In recent years the term village bank has widely replaced other terms; it is now used by major donors like ADB, GTZ and ILO. Unfortunately this term is also not appropriate because these institutions are not banks in terms of the banking law; many would not even qualify as licensed MFIs. Yet given the widespread terminological practice we have decided **to use the term village bank in this study** for village-based MFIs. Relatively speaking, the term is more appropriate in Vientiane Capital than elsewhere in Laos, given the size, self-reliance and profitability of these institutions. Note should be taken that Laos does not have a rural banking law that would permit registering small local financial institutions under the banking law, as in Indonesia and the Philippines.

1.2 Objectives of the study

In a population of six million people living in some 10,500 villages in Laos,[4] there are an estimated 5,000 funds, each usually operating within a single village. The vast majority of them have resulted from donor initiatives over the past twenty years, almost all of them in close association with mass organizations – predominantly through the Lao Women's Union (LWU) – and local government agencies. These funds are semi-formal microfinance institutions (MFIs) ranging from purely donor-supported credit funds to fully savings-based financial intermediaries. Given a pronounced drive to save, particularly among women as the holders of the family purse, many funds have built substantial internal resources over time. According to a new microfinance regulation of June 2008 all microcredit and microfinance activities have to be registered with the Bank of Lao PDR (BOL), the central bank, regardless of size and outreach; the larger ones, with more than 200 million Kip ($23,600)[5] in voluntary savings, are required to be obtain a license as prudentially regulated MFIs.

The challenge to register (or licence) is most pressing in Vientiane Capital, a municipality comprising some 500 villages in nine districts. Village-based microfinance institutions have been spreading fast in the municipality over the last ten years. There are now about 450 village banks covering 91% of villages, all of them savings-based, almost 200 of them (43%) with more than 200 million Kip in savings. So far none has complied with the stipulation to register or submit a request for a license, nor has compliance been enforced. LWU, together with its technical partners, has played a prominent role in the establishment and promotion of the village banks and is now concerned with their compliance and sustainability within the new regulatory environment.

Perhaps because growth of village banking in Vientiane Capital has been quite recent little information has been available about them. In fact there was no specific information about village banks in Vientiane Capital in the latest microfinance survey, carried out in 2006 (*see chapter 2.2*). The central bank and the village banks with their promoters occupy different spaces in the world of banking and finance, and there has been little if any communication between them. At the time when preparations for the new microfinance regulation started there was still a rather limited number of village banks in Vientiane Capital, and networking was not yet effective. It is thus not surprising that the village banks were not prepared to articulate any demands or expectations in the process of preparing a regulatory framework; and the central bank and its advisers were not aware of the needs and potential demands of the emerging village banking sector.

The one-year grace period during which all village banks should have registered with the central bank expired in June 2009. During the second half of 2009 it became obvious that there is a lack of information about the village banks in Vientiane Capital, a lack of communication between the central bank and the village banks, and a lack of perspective concerning their registration and regulation.

In this context the German Savings Banks Foundation for International Cooperation (SBFIC), since 2008 a partner of LWU in the *Women and Family Development Fund* project and of the Microfinance Center, a specialized training institution, was asked by the LWU for future recommendations for the village banks in Vientiane Capital. This led to the proposal of SBFIC to conduct this study[6] as an answer to this request and to help the LWU to

[4] For key economic indicators see Annex 2.
[5] Exchange rate as of 31 December 2009: 8,481 Kip to the US$ (reference rate of BOL).
[6] With support from the German Government (Bundesministerium für Wirtschaftliche Zusammenarbeit und Entwicklung, BMZ).

independently find a suitable way for the village banks in the long run. The overall responsibility of this study laid with Prof. Dr. Seibel who was mainly supported by SBFIC's long-term expert in the Lao PDR Mr. Timo Hogenhout while the research was carried out by Mr. Khanthone Phamuang.

The study has two major initial objectives:

- collecting basic information about large village banks in Vientiane Capital;
- and, as main objective, examining options for village banks in the framework of the new microfinance regulatory environment.

To gather information, a survey was carried out in November 2009[7] covering a sample of 40 village banks with more than 500 million Kip in savings in Saithany District, most of them established between 1998 and 2003. Saithany is the district where savings-based village banks were first established in Vientiane Capital and where the largest number of large village banks exists among the nine districts of the municipality, with a continual growth in outreach and size.

In the context of the survey two sources of information were encountered which led to an expansion of the objectives of the study. One source opened up during field work: a network comprising all village banks in Saithany District, with a network center housed since February 2009 in a permanent office provided by the district administration (*Appendix 7*). This in turn led to information[8] on the other districts of Vientiane Capital about similar emerging networks, with monitoring and guidance functions (*Appendix 7*). Additional objectives of the study thus include the following:

- presenting basic information about village banks in all districts of Vientiane Capital
- providing basic information about a networking structure in Saithany District as well as in the other districts
- assessing the potential of the emerging networks as partners of BOL in the process of re-examining the microfinance regulation, registering the village banks, preparing village banks for licensing, and establishing a system of delegated supervision.

[7] By a team from the CODI-supported *Women and Community Empowering Project (WCEP),* including LWU staff working in the project and in the Saithany District network center. The team was headed by Khanthone Phamuang, who has been involved in the establishment and promotion of savings-based village banks (*Village Savings and Credit Groups*) in VIENTIANE CAPITAL since inception.
[8] Provided by Khanthone Phamuang, WCEP.

2. The operating environment of microfinance in Laos

2.1 The microfinance sector

Starting in the early 1990s when the LAO PDR opened up and began evolving towards a market economy, multilateral and bilateral organizations supported the establishment of village-based credit schemes and revolving funds. Between 1994 and 1996 they were followed by NGO. By 1996 more than 20 organizations were involved in rural credit funds, covering all 17 provinces. Projects were implemented through district level administrations with LWU, Agriculture and Forestry service offices and other local government entities. Virtually all projects started with credit; over time many got also involved in savings. Villages are small in Laos, many with less than 100 families on average; accordingly, the emerging credit groups were also small.

With donor support the number of credit schemes and revolving funds grew rapidly. According to a national survey by UNDP/CDF (1996), by mid-1996 their number reached 1,640, operating in about 15% of all villages. They included more than 1,000 rice banks, some livestock banks and revolving credit funds. Given the low degree of monetization of the rural economy, most credit was in kind. All projects were carried out in cooperation with government organizations, particularly mass organizations with outreach down to every village, such as the Lao Women's Union, the Department of Social Welfare and the Lao People's Revolutionary Youth Union (LPRYU). (UNDP/CDF 1996: 23) UNDP/CDF also compiled a list of donor-financed projects, albeit incomplete, with what was called at the time Lao Village Credit Associations. The list comprised 28 projects by 13 NGOs in 1,050 villages (CARE being the largest, covering 649 villages) and 9 projects by multilateral organizations in 518 villages (UNICEF being the largest, covering 489 villages). (Kunkel & Seibel 1997: 65)

The rapid growth in numbers of village funds, their credit bias and donor dependency led to increasing concerns for their viability and sustainability. These concerns were articulated in particular by a Microfinance Roundtable, initiated and coordinated by UNDP/CDF which had emerged as a lead organization in the debate over microfinance. Three major conferences were held in 1995 and 1996[9], focusing on microfinance. Two major concerns emerged: putting greater emphasis on savings mobilization; and improving the regulatory environment for microfinance services. (UNDP/CDF 1996: 63)

These issues were subsequently taken up by a national consultation workshop in March 1997[10], which concluded that,

> Laos needs a well-functioning system of microfinance with viable institutions and sustainable financial services for all segments of the population. There was consensus that such a system:
> - should be savings-driven,
> - comprise basic microsavings, microcredit and microinsurance services
> - must be based on the cultural traditions of Laos in which women play a crucial role in microfinance, decisions are reached with participation at the local level, and microfinance services reinforce the existing networks of solidarity.
>
> (BOL, APRACA & GTZ 1997: 21)

FIAM and CODI. In the development and implementation of a savings-driven approach toward the end of the 1990s – a new paradigm in Laos at the time – two Thai organizations

[9] By GRETT, CCL, IRAM and BOL in October 1995, by UNDP/CDF in August 1996 and by and UN-ESCAP during the same month.
[10] Jointly organized by BOL, APRACA and GTZ (1997).

played a prominent role, both in cooperation with LWU. One was the Foundation for Integrated Agriculture Management (FIAM) with its *Women in Development Project (WIDP) and Small Rural Development Project (SRDP)* which took the lead in 1997; this took off with an exposure program for LWU staff to Thailand. This was followed by the Community Organisational Development Institute (CODI) with its Women and *Community Empowering Project (WCEP).* The initial focus was on poverty alleviation in 20 villages.[11] In 1998 FIAM helped establishing the first savings-based village banks, or village savings and credit groups (VSCG), in Saithany District , expanding in 2002 also to Saysettha District, both in Vientiane Capital. This was followed by CODI as of 2002 in the remaining seven districts of Vientiane Capital, subsequently also in 15 districts in four other provinces[12].

Self-financing, self-management and self-governance were not only the basic principles of the village banks promoted by FIAM and CODI; these principles were also extended to a secondary level of network associations, comprising all village banks within a district (described in greater detail in *chapter 4*). This approach became a model for LWU and other organizations with their partners throughout the country. A growing savings component is now widespread in schemes which started as revolving funds, responding to a strong urge to save among the Lao population. The input of FIAM and CODI is technical assistance. Except for a small grant in 1997 there have been no donor credit lines or capital grants, neither to the village banks nor to the district associations, fostering self-reliance and self-determination. This is different in most replications by other donors, which tend to provide seed capital or credit lines and also support part of the running costs. The savings portfolio of the village banks under FIAM and CODI almost matches the loan portfolio, which is fully financed from savings and income from interest and penalties (*Chapter 3, Tables 9 and 14*). In contrast, in the village banks supported by ILO (*Appendix1*) and GTZ (*Appendix 2*) the percentage of the outstanding loan portfolio financed from savings is 73% and 47%[13], respectively. In the national survey by NERI (*Appendix 3*), the share of savings is 47% of the loan portfolio, indicating on the one hand that savings have indeed become a major source of loanable funds and on the other hand that external resources still are a source of funds of matching magnitude.

ADB has played a prominent role in Laos in financial sector development, with an emphasis on the formal sector, including both banks and MFIs. With hardware and training its Banking Sector Reform Program has contributed since 2003 to capacity building of state-owned banks, and and its Rural Finance Sector Development Program (RFSDP) to the transformation of the Agricultural Promotion Bank, as a provider of rural and microfinance, from a loss-making policy bank into a commercial bank.[14] In microfinance ADB focuses on the policy framework for the transformation of MFIs into regulated institutions and on the strengthening of such institutions as a tool of poverty alleviation. ADB has completed its regulation project, which included the preparation of the three regulations together with the related charts of accounts and the creation and strengthening of the Microfinance Division in BOL. In the ongoing *Catalyzing Microfinance for the Poor* project ADB started with strengthening a selected number of the initially existing 11 MFIs. In a second phase it now

---

[11] Despite the proximity of the villages to the capital city, poverty was widespread. A survey by FIAM in 1997 showed that money was scarce, and the degree of monetization low. Some families had neither savings nor debts, others had debts of 50,000 to 200,000 Kip, some had savings up to 200,000 Kip. As reported by Khanthone, they lacked clean water, toilets and decent accommodation. Employment after the farming season was rare. The initial focal villages also lacked an irrigation system.

[12] Four districts in Luang Prabang, three districts in Champassak, three districts in Bokeo and five districts in Phongsaly. The total number of village banks promoted by CODI in Vientiane Capital and in four provinces is 471, among them 122 with more than 200 million Kip in savings. (Kanthone 2010)

[13] In the case of GTZ the 47% includes a substantial subsidy as an incentive to save.

[14] ADB is now worried about inflated growth of the banking sector not matched by corresponding growth of the real economy, which poses a threat to the reforms of the banks.

supports 18 out of 27 MFIs: 11 licensed as SCUs, 5 licensed as DTMFIs and 8 registered as NDTMFIs. The two main instruments of support are capacity building and the provision of matching grants. Capacity building includes the development of training materials for the Laotian context; training of trainers in business planning; a course on awareness raising, accounting and delinquency management using CGAP training materials; and accounting training with MFC. Matching equity grants between $3,000 and $50,000 per MFI are provided, mostly in 3 tranches over a three-year period, but not more than $25,000 per year. The MFIs' own contribution comprises equity and savings. So far ADB found that the absorptive capacity for matching grants is greatest among profit-oriented DTMFIs funded by private shareholders. But overall the capacity of the selected MFIs to mobilize own resources was found to be limited; perhaps only about half of the $800,000 earmarked for matching grants may in fact be invested. In 2009 ADB also examined the feasibility of an apex microfinance fund. It concluded that, given the small number and scale of qualified regulated MFIs, there would be no scope for such an apex institution within the next five years.[15]

ILO. In five provinces ILO and the Stone Family Foundation provide technical assistance through LCSDPA to a total of 139 village banks in four provinces; in addition 80 village banks have received seed capital. The project started in 2003 with SME training and a revolving fund concept; in 2004 it adopted the FIAM approach of savings-based village banks. ILO has developed training materials in English and Lao adapted to the Laotian context. Two books have been published under the title *Village Banking in Lao PDR (2008)*, one a *Handbook for Village Bank Management Committees and Support Organizations*, the other one a *Ledger Guide*. The village banks are assisted and monitored by the Lao Community Sustainable Development Promotion Association (LCSDPA), a successor organization of FIAM. LCSDPA plans to establish a network system in all four provinces similar to the one in Vientiane Capital, but ILO has been reluctant to support this. Instead, ILO will now focus on the transformation of a select number of village banks into regulated and licensed institutions. Applying the criteria of the BOL regulation ILO found that 13 village banks would qualify as SCUs, two as DTMFIs and one as either SCU or DTMFI. We may assume that the remaining 123 would have to be registered as NDTMFIs. Piloting starts in six villages, (*Appendix 1*)

GTZ. In the framework of its Rural Development in Mountainous Areas (RDMA) project, GTZ has built 181 village banks in three provinces in Northern Laos. GTZ is in the process of building associations of village banks with sustainable support services to their member institutions. Licensing village banks or associations of village banks has met with difficulty: the regulation fits neither the village banks nor the associations. So far, of the five existing networks one – the Hongsa-Nguen Community Credit and Saving Association (CCSA) – is registered as a NDTMFI; another one – Khop CCSA – has a tax and business license but is not yet registered with BOL. (*Appendix 2*)

SBFIC, one of the smaller donors, is taking a different approach; it neither works through village banks nor with an individual technology. In partnership with LWU and CARD[16] as a technical service provider, it is in the process of establishing a *Women and Family Development Fund (WFDF)* as an MFI licensed to take deposits. Starting in October 2009 WFDF is testing a modified Grameen Banking Approach (GBA), successfully applied in Vietnam with the Vietnamese Women's Union. Like the Grameen Bank in Bangladesh, WFDF is designed as a central institution operating through groups of 4-6 women, centers of 8-10 groups and branches with 20-25 centers, serving some 1000-1500 members per branch. In contrast to the Grameen Bank[17], which starts with credit, WFDF is a savings-

[15] The core challenge is a shortage of human capacity and technical assistance, not of financial resources.
[16] CARD MRI Rural Bank & NGO (Philippines), www.cardbankph.com/.
[17] Actually the conventional Grameen I approach; Grameen II, which has been evolving since 2001, has a stronger savings orientation and focuses on individual loans.

based financial intermediary and operates on the principle of *savings first*. With a ratio of 80% voluntary to 20% mandatory savings during the start-up phase total savings will soon dwarf the rotating credit fund provided by the project. Credit disbursement starts in January 2010. WFDF will also be testing the feasibility of weekly repayments during weekly center meetings, based on the finding that most families have various sources of small income. Grameen banking is strict about enforcing timely repayment, and CARD, the technical service provider with nearly one million active borrowers in the Philippines, has an on-time repayment rate of 99.6%.[18] There is no doubt that adaptation of GBA from credit-first to savings-first will be successful in Laos. More interesting will be the results of the test in two respects: (a) Will group lending be embraced in a country where individual lending has been the sole technology of the ubiquitous village banks? (b) Will members repay their installments on the day they are due as required by the system? That would be revolutionary in Laos – perhaps with far-reaching implications for other MFIs.

The MCBR/NERI survey. There are no reliable overall data on the microfinance sector. Since 2003, information on microfinance has been collected and disseminated by the Microfinance Capacity Building and Research Project (MCBR) under the supervision of the National Economic Research Institute (NERI), which is part of the Ministry of Planning and Investment (MPI). The project produced two annual reports on *Rural and Microfinance Statistics in Lao* based on postal surveys among district microfinance providers and projects. To improve data quality the postal survey was replaced by sample field surveys in 2005 and 2006, the latest date. NERI's involvement has been discontinued; a microfinance online resource center (www.microfinancelaopdr.org) established within MCBR/NERI to provide information about microfinance in Laos has not been updated for two years. (*Appendix 3*)

The most frequently quoted estimate of the number of microfinance institutions, including village banks and revolving funds, is 5,000, covering 50% of all villages in Laos. The latest sample survey by NERI (2007) in 2006 identified 190 microfinance service providers at district level who responded to the survey – 23% line government agencies, 37% projects and funds, 32% mass organizations and 7% Agricultural Promotion Bank (APB).
The most prominent partner organization is LWU, accounting for 24% of all partnerships, followed by the Agriculture and Forestry Department (19%) and the Planning and Investment Department (12%) and the Lao Front for National Construction (12%). There is no list of service providers, most of which are active in several districts (like APB). The data are not broken down by provider, with the exception of APB as a single provider category. NERI identified microfinance activities involving 230,000 members[19] with 86 billion Kip in savings and 188 billion Kip in loans outstanding[20] – on average 50 members, 19 million Kip in savings and 49 million Kip in loans outstanding per village. (NERI 2007: 2-3, 15; *Table 2*; *Appendix 3*)

In sum, four major organizations with available data for 2009 report on 915 village banks with about 154,000 members. Total assets amount to almost 200 billion Kip (US$ 23 million), total savings to 155 billion Kip (US$ 17.8 million) and total loans outstanding to 173 billion Kip (US$ 19.9 million). It is difficult to compare these data for 2009 with a wider sample by NERI of 2006. (*Table 1*)

[18] CARD started in 1987 as a credit NGO with a revolving fund and 150 members. It almost folded up when its repayment rate dipped to 50%. When it adopted GBA and weekly meeting the male members left, and the on-time repayment rate surged to nearly 100% where it stood ever since. (Seibel & Torres 1999)

[19] NERI lists an involvement by providers in 4664 villages; but this includes multiple counting as two or more providers may be active in the same village.

[20] The late payment rate is given as 3.0%, which seems questionable.

Table 1: Selected data on village banks, 2009 (amounts in billion Kip)

	Starting date	Village banks	Members	Savings	Loans outstanding	Total assets
FIAM, VC (Saithany)	1998	107	34,946	52.07	62.08	62.49
FIAM, VC (Saysettha)*	2002	44	8,883	10.61	10.00	13.0
CODI, VC (7 districts)	2000	300	54,815	64.05	62.87	77.95
CODI, 4 provinces		144	15,089	9.56	10.74	11.91
ILO, 5 provinces	2003	139	25,517	16.62	22.87	24.97
GTZ, 3 provinces	2006	181	14,394	2.18	4.66	5.99
Total		915	153,644	155.09	173.22	196.31
NERI survey in 2006		4,664	229,579	86.15	188.01	193.82

* Loans outstanding and total assets extrapolated.

Regulated MFIs. By the end of 2009, almost half a year after the expiration of the registration deadline, only a fraction of the estimated 5,000 microfinance institutions have followed the call of BOL for registration and licensing. There are now 16 licensed MFIs: 11 SCUs and 5 DTMFIs; five of them are located in Vientiane Capital. There is a major difference between SCUs and DTMFIs. Most SCUs reportedly had their origin in village banks and are member-controlled. In contrast the DTMFIs reportedly are private investor-driven (like Beer Lao as one of the investors) and under the control of major investors; small investors have little if any control. 8 institutions have registered as NDTMFIs, all with donor support. Compliance with the regulation among the 5,000 MFIs is a long way off. (*Table 2*)

Table 2: Microfinance institutions registered with BOL, November 2009

No	*Name*	*Province*	
Deposit taking MFIs:			
1	Lao Postal Service Savings Institute	120 offices in Vientiane Capital and all provinces	
2	Ekphattana DTMFI	Vientiane Capital	
3	Newton DTMFI	Vientiane Capital, Vnt Prov. and Oudonsay	
4	Saynyaisamphanh DTMFI	Savannakhet	
5	Champa Lao DTMFI	Luang Phabang	
Non-deposit taking MFIs:			
1	Development Microfinance Institution Phongsaly	Phongsaly	
2	Community Credit and Saving Association Hongsa-Nguenh	Sayabouli	
3	Development Fund Association Bokeo	Bokeo	
4	Community Credit and Saving Association Khop-Xienghon	Sayabouli	
5	Oudomxay Development NDTMFI	Oudomxay	
6	Suaykan Pattana NDTMFI	Huaphanh	
7	Hom NDTMFI	Vientiane Province	
8	Mimaity NDTMFI	Khammouane	
Savings and Credit Unions:			
1	Rural Development Cooperative Naxaythong	Vientiane Capital	
2	Credit Cooperative for the Support of Small Production Units	Vientiane Capital	
3	SCU Vientiane	Vientiane Prov.	
4	SCU Seno	Savannakhet	
5	SCU Louang Prabang	Louang Prabang	
6	SCU Thakhek	Khammouane	
7	SCU Houamchay Phattana	Savannakhet	
8	SCU Paksong	Savannakhet	
9	SCU Huasae Chaleunouaxe	Champasak	
10	SCU Thoulakhom	Vientiane Prov.	
11	SCU Mittaphap	Vientiane Capital	

Performance of regulated MFIs. Among eight MFIs[21] for which data are available (June 2009), four (50%) were found loss-making. Only 13% had a legally required portfolio-at-risk (PAR) ratio of <5%; 38% had a PAR <20%. The average PAR was 17% (excluding write offs for loans overdue >180 days). The average gross portfolio size was 2.1 billion Kip; the average loss amounted to 8.8% of the portfolio. (*Appendix 4*) The contrast to the unregulated village banks studied in Vientiane Capital is striking. Have members of SCUs and shareholders of DTMFIs lost control (or they did not have control from the outset)?

Ekphattana Microfinance Institution (EMI) was established in 2005, licensed in February 2006 as DTMFI under the old, and in July 2009 under the new, regulation. Lending started in April 2006. As of 31 Dec 2008 total assets amounted to 4.35 billion Kip, loans outstanding to 2.75 billion Kip, savings to 2.94 billion and total equity to 1.03 billion Kip; losses amounted to -187.6 million Kip. PAR >30 days stood at 27.5%, requiring an increase in provisioning. According to the tax law EMI pays 1% of its losses in taxes. It also reports that provisions are not fully recognized as expenses by the tax office.

EMI has five branches and a total staff (including management) of 43. It takes financial services to the client, providing daily, weekly and monthly collection services – an expensive technology. EMI pays 8% p.a. on compulsory savings and 9% to 16% p.a. on term deposits (2% above commercial bank rates). Loan periods are 1-12 months. EMI charges 4% flat per month on loans from 0.5 million Kip to 9 million Kip (88.6% effective per annum, disregarding compulsory savings) and 4% p.m. on the declining balance on loans above 9 million Kip (48% effective p.a.).[22] A new product of small loans below 9 million Kip, is under consideration, with an interest rate of 6.5% p.m. on the declining balance (78% effective p.a.).[23]

In EMI high losses and high interest rates come together, both due to high transaction costs related to small loans, short loan periods and client-oriented collection services. For EMI to become sustainable losses and interest rates will have to come down, but loan sizes would have to go up; this would run against regulatory restrictions, requiring DTMFIs to hold at least 80% of their portfolio in microloans not exceeding ten million Kip ($1,175). EMI is still it its start-up phase. Since the end of 2008 ADB and SBFIC through its partner CARD RMI provide technical assistance, ADB also provides financial assistance. All this is expected to contribute to EMI's viability. An assessment of the prospects of regulated MFIs to become viable and sustainable would require an in-depth analysis. Note should be taken that in a comparable situation (but on a quite different scale), in the late 1990s, the Grameen Bank found it necessary to fundamentally change its policy (Hulme 2008).

Naxaythong Rural Development Cooperative is a credit cooperative which has been profit-making since inception. It was licensed by BOL in 2001 based on a no longer valid BOL regulation on credit cooperatives issued in 1994. In 2004 it was licensed under a pilot SCU regulation; it has not yet received a license under the SCU regulation of 2008. According to DGRV it is still unclear whether it should come under SCU or DTMFI regulation.[24] In 2001 Naxaython RDC started with 18 founding members, 386 ordinary share

[21] Two DTMFIs, five SCUs and Hongsa CCSA, a NDT MFI.
[22] By comparison, commercial banks banks charge 12% effective p.a. on large loans and 30% on small loans of 10 million Kip and above (eg, Acleda, a subsidiary of Acleda Bank in Cambodia, an NGO transformed into a microfinance commercial bank).
[23] By comparison, moneylenders reportedly charge 15% to 50% per month (180% to 600% eff. p.a.)
[24] Adapting Naxaython to the new regulation meets with some reluctance, as it would require changes in the capital structure, as some members have more than the regulatory limit of 10% (Art. 5) and in the loan portfolio, as some related party loans exceed the limit of 5% of capital (Art. 44). (Appendix 6)

members and a total of 582 savers in 17 villages. As of Dec 2008 the number of shareholders had increased to 1,015 and the number of savers to 2,041; there were 951 borrowers with a loan outstanding. Area coverage had expanded to 52 villages. Total assets amounted to 2.61 billion Kip, loans outstanding to 2.14 billion, total savings to 1.99 billion and paid-up share capital to 0.30 billion. Net profit after taxes amounted 0.13 billion Kip. 0.12 billion Kip were distributed as dividends, equivalent to 6.1% of total savings. (*Appendix 5*)

Naxaython RDC vs EMI. The loan portfolio of SCU Naxaython is not much smaller (17%) than that of EMI, yet it manages with a total staff of nine, compared with EMI's 43. Moreover, 82% of Naxaython's total assets are lent out to borrowers, compared with 59% in the case of EMI. These may be some of factors contributing to the difference in profitability: 5.1% in the case of the Naxaython, -4.1% in the case of EMI (in terms of year-end total assets, 2008). Age alone is no explanatory factor; Naxaython RDC has yielded a profit from the first year on, EMI not even in its third year. A deeper analysis would be required to arrive at a full picture.

2.2 The regulatory framework of microfinance

2.2.1 Background

The basic legal framework of the financial sector of Laos was laid down in the early 1990s. BOL was created in 1990[25] as a central bank with licensing, supervision and prudential regulatory powers over financial institutions, defined as legal persons doing banking or similar business. The framework for the regulation of financial institutions was laid down in 1992[26], covering commercial banks and non-bank financial institutions. The non-banks were restricted from mobilizing funds from the general public and issuing shares or bonds. BOL was empowered to make separate regulations for banks and non-banks. During the same year a draft law on credit cooperatives was prepared but not enacted, due to the negative experience with credit cooperatives and their collapse in the late 1980s.

By the mid-1990s the number of village funds had reached about 1,650; they were credit-based, unregulated and thus considered unsustainable. Initiatives in the mid-1990s led to a consensus on the need to promote sustainable microfinance institutions. Sustainability would require an emphasis on self-reliance through savings mobilization and a legal framework. In the districts of Vientiane Capital, starting in 1998, village savings and credit groups, or village banks, had emerged which were fully self-reliant in terms of resource mobilization, with rapidly growing savings portfolios. By the mid-2000s the number of village funds throughout Laos had surged to several thousand, many of them mobilizing savings. This increased pressures to create a regulatory framework.

Similarly, in the global microfinance community, due to rapid increases in number and size of MFIs, earlier resistance gave way to numerous regulatory initiatives for institutions variously named rural banks, MFIs, deposit-taking MFIs or savings and credit cooperatives. Yet, while authors like Christen & Rosenberg (2000:2) "believe strongly that the future of microfinance lies in a licensed setting, because it is the only setting that will permit massive, sustainable delivery of financial services to the poor", they also warned against a rush to regulate, "raising questions about timing, and about certain expectations that may turn out to be inflated." Much depends on whether regulation is simply imposed or the result of deliberation and communication between the regulator and the regulated – not always a cautionary and balanced process.

[25] Law No 04/PSA of 27 June 1990.
[26] Decree No 3 of 23 January 1992.

In 2004 a Microfinance Division was created under the Banking and Financial Institution Supervision Department of BOL, with guidance, monitoring and supervision of the implementation of microfinance regulations as its tasks. On 22 June 2005 BOL launched *the Regulation on the Establishment and Implementation of Microfinance Institutions in Lao PDR* (No.10/BoL), announcing that large microfinance institutions had to apply for licenses while smaller ones such as credit unions, cooperatives, saving and loan associations and village funds have to be registered, depending on their scale of operation. The first MFI following the call was Ekpatthana Microfinance Institution (EMI), which received its license in 2006.

2.2.2 The microfinance regulation of June 2008

Deliberations in various circles and conferences led to a Notice of the Prime Minister on microfinance supervision in 2007[27], a proposal from the Banking and Financial Institutions Supervision Department of BOL and finally the announcement of three regulations, issued in June 2008:

- No. 02/BOL on Non-Deposit Taking Microfinance Institutions, of 20/06/2008 (EN)
- No. 03/BOL on Savings and Credit Unions, of 02/06/2008 (EN)
- No. 04/BOL on Deposit-taking MFIs, of 20/06/2008 (EN) *(www.bol.gov.la/english/microfinanceeng.html)*

There are two basic provisions in the regulation: the first pertaining to the universality of registration of any microfinance institution or activity, the second to the conditions under which they are to be licensed as prudentially regulated institutions:

- **Registration as NDTMFI:** Any organization, group or enterprise – governmental, non-governmental or private – that carries out microfinance activities, including village banks, savings groups, village funds, development funds and others, is required to register (***Regulation No. 02/BOL Art. 3)***;
- **Licensing as SCU or DTMFI:** Any microfinance entity with voluntary deposits exceeding 200 million Kip or annual revenues exceeding one billion Kip is required to be licensed as a prudentially regulated MFI, either a savings and credit union (SCU) or as a deposit-taking microfinance institution (DTMFI) (***Regulation No. 02/BOL Art. 20)***

All three types of MFIs are permitted to mobilize loans or grants from Laos and, with approval of BOL, from foreign entities and to deposit funds with BOL or commercial banks. There are no interest rate restrictions. Penalties for non-compliance with the regulation can be imposed on any of the three types of MFIs including managers or officers, individually or as a group.

To date compliance with registration and licensing requirements has not been enforced, even though the one-year grace period has expired in July 2009. BOL seems prepared for further communication on the details of the regulation and to accept an unspecified trial period, which may result in modification of the regulation. This is in line with a worldwide realization in the context of the global financial crisis – not just microfinance! – that regulation is an evolutionary process subject to learning.

Non-deposit taking MFIs (NDTMFIs) which do not exceed voluntary deposits of 200 million Kip or revenues of one billion Kip are required to register with BOL and relevant government authorities as so-called non-deposit taking MFIs; there is no minimum size below which registration would not be required. Within this framework NDTMFIs are authorized to mobilize savings, and grant microloans up to 10 million Kip. They have to apply BOL's

[27] No. 05/PM, dated 04 April 2007

provisioning rules and submit annual reports using BOL's chart of accounts. The highlights of the NDTMFI regulation are summarized in *Table 3*; an overview is given in *Annex 3*.

Table 3: BOL regulation: Non-Deposit Taking Microfinance Institutions – Summary

Requirement to register	Any and all microfinance activities by groups, individuals or legal entities
Required registrations	With BOL and relevant government authorities
Resource mobilization	Compulsory and voluntary deposits of members Loans or grants from Lao and foreign entities
Regulation	• Micro-loans only, not exceeding 10m Kip • Voluntary deposits not exceeding 200m Kip in aggregate and 10m Kip per depositor unless authorized by BOL • Quarterly review of all loans, provisioning as prescribed • Annual reporting to BOL
Requirement of conversion to a prudentially regulated MFI	Voluntary deposits >200m Kip, or annual revenues >1 billion Kip
Penalties for non-compliance	100,000 Kip per day to NDTMFIs incl. managers or officers individually or as a group

Source: www.bol.gov.la/english/mf_reg02eng.pdf

With the expectation in mind that the regulation will have to be adjusted after a communication and learning period some observations are in order:

- The term "non-deposit taking MFI" is a misnomer as the regulation entails permission to mobilize voluntary deposits up 200 million Kip. This should be corrected.
- The deposit ceiling of 200 million Kip excludes compulsory deposits, which are defined as "a condition for receiving a loan or as collateral for loan either as a percentage of the loan or as a nominal amount" (Art. 2). As no loans are given by village banks in Vientiane Capital without prior savings, the concept of compulsory deposits might be interpreted widely, which would lead to a substantial increase in the total amount of permissible deposits. The village banks in Vientiane Capital only list "savings" in their book, without distinguishing between compulsory and voluntary. To be legally on the safe side, NDTMFIs might introduce both categories in their balance sheet. Note should be taken that the regulation does not define compulsory deposits as mandatory regular savings, which is a practice among certain types of MFIs.
- There is a wide variety of village funds, village banks, groups and other microfinance entities with widely differing operational practices. It is not clear how these fit into the prescribed chart of accounts. Some flexibility on the part of BOL and adaptation to different types of charts might enhance the motivation of MFIs to register.
- There is no reference to taxation in the regulation, which falls under the Ministry of Finance. So far taxation of semi-formal village banks has not been enforced.
- Local financial activities and institutions have been registered with the governors of the respective provinces; NDTMFIs are also expected to be locally registered under the new regulation. It is not clear to what extent the governors have been involved in the consultation process and whether they are willing to comply with the registration (there is some evidence that they might not).

Savings and credit unions (SCUs) can be local single units or have branches and offices nationwide. 10 founding members together with 100 initial members, or 250 members with voluntary deposits of 300 million Kip, can establish a SCU; minimum capital requirements are 100 million Kip. SCUs are only allowed to provide financial services to members. With regard to credit the regulation does not restrict SCUs to microloans. Prudential requirements include a maximum NPL ratio of 5%, provisioning, writing off loans overdue >180 days, a risk-weighted CAR of 12% and liquidity ratios of 4% of cash in hand and 20% overall. SCUs have to be externally audited and are supervised by BOL. Reporting is quarterly and annual. Of the two prudentially regulated types of MFIs SCU seems to be the legal form most likely to appeal to village-based financial institutions required to convert. This is not surprising as the the leading village bank system, in Vientiane Capital, has taken its inspiration from international credit cooperative law. The highlights of the SCU regulation are summarized in *Table 4*; an overview is attached in *Annex 3*.

Table 4: BOL regulation: Savings and Credit Unions – Summary

Requirement of conversion to a regulated MFI (DTMFI or SCU)	Voluntary deposits >200m Kip, or annual revenues >1 billion Kip
Legal status	Financial cooperative
Location and outreach	National, members only
Portfolio restriction	No restriction to microloans
Establishment requirements	10 founding members and 100 initial members; or 250 members and voluntary deposits of 300m Kip No member shall own more than 10% of capital
Voting rights	One member one vote (irrespective of the no. of shares held)
Resource mobilization	Member deposits, loans or grants from Lao and foreign entities and member share capital, retained earnings
Prudential regulation:	• Minimum registered capital 100m Kip • Provisioning for loans overdue >30, >90, <180 days; 1% on performing loans • Maximum NPL ratio: 5% of loans outstanding • Write-offs: loans overdue >180 days • CAR 12% (risk-weighted) • Liquidity ratios: cash in hand 4%; overall 20%
Auditing and supervision	Internal and external auditing, supervision by BOL Quarterly and annual reporting
Penalties for non-compliance	100,000 Kip per day to SCUs incl. managers or employees Suspension and cancellation of license
Interest rate restrictions	None

Deposit-taking microfinance institutions (DTMFIs) can be local single units or have branches and offices nationwide. Establishing a DTMFI takes five shareholders and one major shareholder with at least 20% of registered capital, a total registered capital of one billion Kip divided into shares, and a five-year business plan demonstrating sustainability. Voting is by simple majority of shares. DTMFIs may provide financial services to the general public; but at least 80% of their portfolio must be comprised of microloans not exceeding ten million Kip. Prudential requirements include: voluntary deposits not exceeding 10 times the capital, a single-brrower limit of 10% of capital, provisioning as prescribed by BOL including 5% on performing loans, a maximum NPL ratio of 5%, a risk-weighted CAR of 12%, liquidity ratios of 4% of cash in hand and 20% overall, and investments up to 10% of registered capital but restricted to other MFIs. DTMFIs have to be externally audited and are supervised by BOL. Reporting is monthly, quarterly and annually. The highlights of the DTMFI regulation are summarized in *Table 5* below; an overview is attached in *Annex 3*.

Table 5: BOL regulation: Deposit-taking MFIs – Summary

Requirement of conversion to a regulated MFI (DTMFI or SCU)	Voluntary deposits >200m Kip, or annual revenues >1 billion Kip
Legal status	Financial institution incorporated as a limited liability company under the enterprise law
Location and outreach	National
Establishment requirements	5 shareholders, 1 major shareholder Five-year business plan
Voting rights	One share one vote, resolutions by simple majority of shares
Resource mobilization	Member deposits, loans or grants from Lao and foreign entities and shareholder capital, retained earnings
Portfolio restrictions	Microloans up to 10 million Kip at least 80% of loan portfolio
Prudential regulation:	• Minimum registered capital 1bn Kip, divided into shares • Voluntary deposits not exceeding 10 times the capital • Single-borrower limit 10% of capital • Provisioning for loans overdue >30, >90, <180 days; 5% on performing loans • Maximum NPL ratio: 5% of loans outstanding • Write-offs: loans overdue >180 days • CAR 12% (risk-weighted) • Liquidity ratios: cash in hand 4%; overall 20% • Investments up to 10% of reg'd capital, restricted to MFIs
Auditing and supervision	Internal and external auditing, supervision by BOL Monthly, quarterly and annual reporting
Penalties for non-compliance	100,000 Kip per day to SR-MFIs incl. managers or employees Suspension and cancellation of license
Interest rate restrictions	None

3. Village banks in Vientiane Capital

3.1 The practice of village banking in Vientiane Capital: results of a survey

This chapter gives an introduction to the operational practice of village banking as it has evolved in Vientiane Capital. It is based on the results of a survey of a sample of 40 large village banks in Saithany District, the first district of Vientiane Capital where FIAM started promoting village banks in 1998. Information on village banks in the other eight districts of Vientiane Capital is not available in such detail; they are modeled after those in Saithany. As they were established later they are generally not as advanced as the more mature village banks in Saithany. They survey was carried out by Mr Khanthone Phamuang, who has been involved in the design of village banking in Vientiane Capital from inception.

The objective of village banking as introduced by LWU is poverty alleviation. The village banks were designed to activate self-help, provide mutual assistance, finance income-generating activities, help to smoothen pre-harvest income to avoid selling the crop prematurely, prepare for and protect against emergencies and life events, improve living conditions, and support village development.

Principles. The village banks were established as self-reliant local financial intermediaries, collecting savings and recycling them as loans within the village. Self-help, or self-reliance, is the core principle. It is based on five strategic principles:

(i) self-determination by the general assembly through equal votes of members,
(ii) self-financing through member savings,
(iii) self-management through an elected management committee,
(iv) self-governance[28] through an advisory committee of representatives of the community political establishment , and
(v) self-supervision through district networks.

The target population comprises all local residents of a village, including women and men, with a focus on women as holders of the family purse as is customary in Lao culture. In most families both husband and wife hold separate memberships. All members save; in some village banks only women borrow.

Early impact. Members of the initial 20 focus villages quickly felt the impact of their involvement in village banking. Based on the collection and accumulation of small personal savings they were able to borrow money when they were sick; this had previously been a major drain on their resources when they had to turn to moneylenders. Now they could buy rice during periods of shortage instead of selling the paddy before harvesting; they were able to raise livestock; they had clean drinking water; and their overall living condition improved. This inspired other villages to join the project, and other organizations to start new projects establishing village banks. An immediate replicator was CODI with its Women and Community Empowering Project (WCEP).

Ownership: The village banks are owned by the members as active savers; ownership is constituted by individual voluntary savings and payment of a membership fee (similar to a share, but considered part of savings). Membership is restricted to the residents of the village where the village bank is located; it is not the community as a corporate entity which is the

[28] Self-governance in the sense that it follows the rules of Lao village and society and not of a donor, as is common in credit NGOs and other MFIs in donor ownership. The advisory committee comprises various types of village representatives or authorities confirmed, according to the bylaws of the village banks, by the general assembly “through election”.

owner. This is similar to the cooperative ownership model, with its *one member one vote* rule, except that in village banks it is savings, not shares, which constitute ownership.

Management and governance are in the hands of elected **c**ommittees, all from within the village. Most of them are educated older and respected community members. Management committees comprise five to seven members, on average six; 97% of the committee members in the sample are women. Advisory committees which represent the local power structure (including the local women's union) comprise four to seven members, on average six; 92% of the committee members are male. All committee members are reportedly elected by the general assembly, though in actual practice advisory committee membership is probably in many cases by appointment through some political process and confirmation, or ratification, by the general assembly. Committee heads tend to be re-elected and thus gain experience over time (an important prerequisite for effective capacity building). Presidents in the 40 village banks were in office up to nine years (*median:* five years), management committee members up to 12 years (*median:* seven years), and advisory committee members up to ten years (*median:* six years).

Ultimate power lies with the general assembly of members where each member has one vote. The ultimate instrument of member control in case of general and substantive dissatisfaction with the running of the institution or unacceptable external impositions would be withdrawal of savings.

Bylaws were reportedly inspired by international credit cooperative regulation. Model bylaws were provided by FIAM but each village shapes its own regulation. The bylaws specify membership criteria, general assembly terms and meetings, electoral procedures, terms and responsibilities of management and advisory committee members, accounting system and financial reporting, membership fee, minimum monthly savings, deposit and loan disbursement date and place, loan criteria and terms, collateral and guarantees, interest rates for general and emergency loans, penalties for late payment and infraction of rules, profit distribution at the end of the year (including dividends to savers, compensations to management and advisory committee members, allocations to village development funds, social welfare fund, reserves), and membership as shareholders of district networks.

Guidance and supervision are provided by self-organized district networks comprising a two-tier zonal and district structure (possibly to be extended to the municipality as a tier above). In addition oversight is provided by LWU at all administrative levels and by the district authority.

Financial products include savings, credit and life insurance. **Voluntary monthly savings** are set in Saithany at a minimum of 5,000 Kip ($0.60). In 2001 SRDP, with FIAM support, prepared a savings handbook, revised in 2005.

Credit. There are two loan products: general and emergency loans. Initially most loans are emergency loans; with increasing maturity the share of general loans increases. As of 2009 70% of the loans in Saithany reportedly are general loans. Emergency loans are for a maximum period of three months, at 1%-2% interest per month on the declining balance (12%-24% effective per annum), with payments due not before the second month. General loans are mostly for periods up to one year. The interest rate has recently been reduced from 5% to 4% per month (ie, from 60% to 48% effective per annum). Mature village banks may charge as little as 3% per month (36% effective per annum). This is to be compared to effective interest rates of up to 100% per annum on small loans (<10 million Kip) among some licensed MFIs. In the sample of large village banks the maximum loan size is mostly 20 million Kip ($2,350); in ten villages it is 50 million Kip and in one village 100 million Kip. In some village banks the maximum any member can borrow is five times the savings. If two people of a family are members (which is mostly the case) both can borrow. For loans up to

500,000 Kip ($60) personal guarantees are accepted; for larger loans physical collateral is required.

Late payments. Installments of principal and interest are due monthly. Delays in repayment are widespread; but all borrowers reportedly continue paying interest on a monthly basis. There is no sense of urgency to meet all installment payments of the principal; penalties for late payment are in fact a major source of income. Monthly interest dues are reportedly met regularly. 14.9% of payments of principal in 40 village banks are overdue more than 30 days:

4.1% 31-90 days
7.5% 91-180 days
3.3% more than 180 days.

Loans which are not repaid within the contract period are rescheduled. Borrowers who fail to repay a rescheduled loan have to meet with the management committee to work out a solution. There is no record of any bad debts to be written off.

Balance sheet. Below is a simplified consolidated balance sheet (including income and expenditure items) of 40 village banks, each with more than 500 million Kip in savings.[29] On average each of these large village banks has 230 members and 890 million Kip in savings; average total assets are above one billion Kip. Net profit amounted to 23% of the amount of savings. 53% of the members are reportedly borrowers, approximately one per family.

Table 6: Adjusted balance sheet of 40 large village banks in Saithany District, October 2009 (in billion Kip)

Assets:	*Amount*	*Liabilities:*	*Amount*
Cash	4.76	Savings	35.56
Bank deposits	3.68	Interest income	6.88
Loans outstanding	34.56	Other income	0.03
Expenditure	0.80	Reserve Fund:	1.33
Total	**43.80**	**Total**	**43.80**
No of borrowers	4,864	No of saver-members	9,142

Loan purpose. The main loan purpose among the 40 large village banks is trading, followed by rice farming, family assistance and education. Identifiable income-generating activities account for about half the loan portfolio.

Table 7: Loan purposes in 40 large village banks in Saithany District, 2009 (amounts in million Kip)*

	Amount outstanding		Number of loans		
Loan purpose	Amount	Percent	Number	Percent	Av. size
Family assistance	4,086.0	16.3	1,090	20.1	3.7
Rice farming	3,391.9	13.6	1,152	21.2	2.9
Gardening	293.0	1.2	214	3.9	1.4
Livestock	425.5	1.7	63	1.2	6.8
Trading	9,023.8	36.1	1,237	22.8	7.3
Education	3,131.8	12.5	744	13.7	4.2
Sanitary facilities	415.9	1.7	163	3.0	2.6
Emergencies	869.2	3.5	440	8.1	2.0
Other	3,356.7	13.4	322	5.9	10.4
Total	24,993.8	100.0	5,425	100.0	4.6

*Incomplete data

[29] Consolidation with the objective of arriving at a matching balance sheet required some adjustments by the survey team.

Transactions usually take place during two consecutive days of the month: on one day savings and installments are paid, the next day loans are disbursed. The money collected is kept overnight by the cashier, who is chosen for his reliability, economic position in the village and the safety of his house; frequently he is the head of the management committee or the head of the village. Five village banks have their own office space (owned by LWU or the village); the remaining 35 share facilities of the village authorities.

Liquidity management. The high season for savings is January and February, and for loans August. Conversely, the low season for savings is October and November, and for loans November and December. The main period of surplus liquidity is thus January and February; the main period of liquidity shortage is August. There is no mechanism of liquidity exchange among the village banks in the district.

Taxation. Village banks, as semi-formal MFIs, do not pay taxes.

Profit distribution. Depositors do not receive a fixed interest rate; similarly committee members do not receive a fixed monthly compensation; the village banks do not employ any salaried staff. Instead the net profit is calculated at the end of the year and allocated according to the following key:

70% dividend to savers (based on the amount of savings)
15% compensation to management committee members
5% compensation to advisory committee members
4% reserve fund
4% development fund
2% network services.

Perception of microfinance regulation. 18 months after the announcement of the new microfinance regulation village banks are still not aware of its contents. This has raised fears which may or may not be justified. Despite the similarity between village banking and cooperative finance there is a deep distrust of credit cooperatives, due to the collapse of credit cooperatives and their association with the former command economy. The village banks have a strong preference for their own system based on self-determination and voluntary savings; they would strongly object against impositions from above which are not in line with their own interests. At the same time they see the necessity of registering with BOL, provided they can do so with their current system.

Development perspectives and demand for support. The village banks have voiced the following concerns and suggestions:

- Management training and capacity building of committee members
- Own office, computers, an improved accounting system
- Increased savings, introduction of term loans, lower interest rates
- Safekeeping and better use of surplus liquidity
- More information about the microfinance regulatory framework
- Microenterprise management, marketing and skill training.

3.2 Outreach and performance of village banks in Vientiane Capital: an overview

Vientiane Capital, a municipality, comprises nine districts[30] with 499 villages and a total population of 712,000 inhabitants[31] in 126,000 households (ie, 5.65 members per household). On average each village has 1,427 inhabitants in 253 households (*2006 data*).

Early beginnings. It is not clear whether there has been any continuity between beginnings of village banking in the early 1990s supported by two NGOs and later beginnings reported below; or whether any of the early 114 village banks or groups have survived in the villages not covered by FIAM and CODI. Adventist Development Relief Agency (ADRA) has been involved in Laos since 1991. With funding from World Food Program (WFP) ADRA helped establishing rice banks in 112 villages of Vientiane Capital. Loans outstanding to 6,136 rural households in 1996 amounted to $594,080. In three villages ZOA Refugee Care, with an interest-free loan of $25,000, reportedly helped establishing "sustainable village credit associations (groups) that can be profitable and are managed by the villagers themselves." Loan sizes varied from $22 for handicraft loans to $329 for buffaloes. ZOA also introduced a revenue-sharing model as a precursor to FIAM's later profit-sharing model: 40% of interest income goes into an emergency fund, 12% into an inflation reserve, 36% into committee, one district staff and administrative expenses, and 12% into net profit. (UNDP/CDF 1996: 41, 59-61)

The NERI survey, 2006. According to a survey by NERI (2007) in 2006 there are 190 microfinance service providers in Laos. 15 are in Vientiane Capital, including projects & funds, mass organizations and line government agencies. Reportedly they cover 97% of villages; this makes Vientiane Capital the number three in the country, after Savannakhet with 25 and Vientiane Province with 17 providers. The survey does not offer information about the number of village banks or other microfinance institutions. Key information, albeit incomplete[32], provided by NERI on the municipality as of 2006 includes the following (*Appendix 3*):

- 26,582 savers, 18.54 billion Kip in savings, 0.70 million Kip per saver
- 8,190 borrowers[33], 15.71 billion Kip in loans, 1.92 million Kip per borrower
- Equity 3.07 billion Kip, 12% of total assets
- Total liabilities and capital 25.48 billion Kip
- Profit 2.17 billion Kip

FIAM and CODI data, 2009. There are no recent comprehensive survey data on Vientiane Capital. However, as of September 2009, 91% of the villages of the municipality were covered by village banks supported by two providers, both in cooperation with the Lao Women's Union, who are active in all nine districts of the municipality: the Foundation for Integrated Agriculture Management (FIAM), a Thai NGO, and the Community Organizational Development Institute (CODI), a Thai development agency, both starting during the second part of the 1990s. The two projects have two basic features in common: (a) village banks start with mobilizing savings and remain savings-based; (b) within a few years of their establishment they build self-managed and self-financed network structures for monitoring and supervision:

[30] Chanthabuly, Hadxaiphong, Pakngum, Naxaithong, Sanghtong, Sikhottabong, Saithany, Saysettha and Sisattanak.
[31] 67.0% of the population of the municipality is 15-64 years of age.
[32] All 15 providers gave information on total capital (presumably comprising liabilities and equity).and savings, 14 on loans, 10 on equity and 11 on profit.
[33] The late payment rate is given as 0.6% – a most unlikely figure, lending little credence to reliability of survey results.

- LWU and FIAM jointly started the **Small Rural Development Project for Women (SRDPW)** and began establishing village banks in Saithany District in 1998, with a total of 107 village banks as of 2009. Since 2003. LWU and FIAM have been building a network structure in Saithany District in charge of monitoring and supervision. In 2002 they started building village banks in Saysettha District; their total number reached 44 as of 2009, comprising 39 directly promoted by FIAM, four by an affiliate local NGO and one established at local initiative. However, there is no network structure in that district, and there is only limited information about outreach and finances. Thus, the total number of village banks under FIAM together with five indirectly associated village banks is 151.

- Following the lead of its project with FIAM, LWU started a similar project in the remaining seven districts with CODI, the **Women and Community Empowering Project (WCEP)**, The first village banks were set up in Pakngum District in 2000 and in Sangthong and Naxaithong in 2002, followed by building a network structure in 2003 and 2006, respectively. In the remaining four districts implementation started in 2003-04, followed by building a networking structure in 2008-09. The total number of village banks has reached 302 as of 2009.

Note should be taken that both providers have succeeded in building up a functioning reporting system, as indicated by the fact that data as of 30 September were available during the first part of November. Key information by the two providers as of September 2009 is summarized below. This also includes information about Saysettha District[34], which is not part of regular reporting by the existing village bank networks:

- 453 village banks (out of 499 villages) under LWU with FIAM and CODI in all 9 districts of Vientiane Capital
- 48% of the families in Vientiane Capital are members in one of the village banks, usually both wife and husband.
- 103,902 member-savers, 229 per village bank;
- 126.73 billion Kip in savings, 280 million Kip per village bank
- 29,565 borrowers, 65 per village bank;
- 135.36 billion Kip loan portfolio, 299 million Kip per village bank
- 25,445 life insurance participants (excluding Saysettha)
- Reserve funds 4.52 billion Kip
- Total liabilities and capital 164.56 billion Kip
- Interest received 19.42 billion Kip
- Dividend to savers in percent of total savings 10.74%
- Around 193 village banks with more than 200 million Kip in savings
- (70 in Saithany District, 105 in seven districts under CODI and an estimated 18 in Saysettha)

3.3 Laying the foundation: village banks in Saithany District

Saithany is one of nine districts in Vientiane Capital, and is reputed for the strength of its village banks. They account for more than a quarter of the total number of village banks in the eight districts under FIAM and CODI, the two main promoters in the municipality, and around half the total funds and the loan portfolio. The district has therefore been selected for a special study.

[34] Data on the number of village banks, the number of members and the amount of savings in Saysettha were provided by Khanthone; the other consolidated data were adjusted accordingly (except the number of participants in life insurance, which presumably does not exist in Saysettha).

System preparations started in 1997 in the framework of SRDPW, under adverse conditions: first, the credit cooperatives had collapsed, then, in 1997/98, the Asian financial crisis hit Laos, seriously affecting its financial sector; in both cases Laotians lost their savings. Yet, they were not discouraged and ready for a local institution under their own control. FIAM, in cooperation with LWU, worked out the methodology of establishing village banks: self-financed through member savings, self-managed through an elected management committee, self-governed through an advisory committee of elected representatives of the community power structure, and self-reliant through an ingenious system of cost control. Project implementation was actively supported by the Women's Union at Vientiane Capital and district level as well as by the deputy mayor of Vientiane Capital and the Saithany District chief.

System and financial reporting specifics. According to the system developed by FIAM and subsequently adopted by CODI, very few costs are incurred during the year, while income is generated through interest payments on loans, penalties for late payment and membership fees of new members. At the end of a financial year net income is calculated and allocated according to a generally agreed-upon key: as dividends to savers (70%), compensations to management (15%) and advisory committee members (5%), reserves (4%), special funds (4%) and network services for monitoring and guidance (2%). Preparations also included a manually administered accounting system, adjusted during 1998-2000 to the needs of evolving institutions. The financial year starts with the month in which a village bank was established. The following are the main specifics which deviate from the reporting requirements of BOL:

- No salaries and compensations appear as expenditure on the income statement.
- Income and minor expenditure items are integrated in the balance sheet, respectively on the liability and asset side.
- On the basis of the annual income and expenditure statement net income is calculated and allocated to various categories, including dividends to savers, compensations to management and advisory committee members, reserves and funds, and network & supervision costs.
- The financial year is not standardized and varies by the foundation date of each village bank.

An example of an actual annual financial report, by the village bank of Phaksapkau**,** is given in *Annex 4*.

The first village banks were established in Saithany District in 1998. They comprised only women as members who also elected management committees of women only. In 2000 men were given access, which gradually led to a balanced membership. But there is still a number of village banks which lend only to women while taking the savings from both women and men. During the same year, advisory committees were introduced, comprising appointed representatives of the local power structure, mostly male. This completed what Khanthone Phamuang, author of a handbook of village banking in 2001 called the *tripod of governance*: member-owners, an elected management committee and an elected advisory committee or board. The handbook, and with it the model developed in Saithany, was used in the further propagation of village banks by FIAM and CODI as well as the Ministry of Planning and Investment and distributed country-wide. The data reported below are based on monitoring information[35] by the network center of village banks, established with assistance by FIAM.

[35] These data were not available at the beginning of the field work, but turned up during a visit of the district administration office where the existence of a network center was discovered, equipped with a room (since February 2009) and a staff of four.

There are 107 village banks in Saithany District under the umbrella of the center. This number comprises 102 village banks from 104 villages plus five special institutions from the police, military, district administration, public health unit and district education unit. Total membership is 35,000, who are all savers. It is common that both wife and husband are members; almost 18,000 families are covered by the village banks. Nearly 10,000 members have currently a loan outstanding, ie, 28% of members. The average number of members and borrowers per village bank is 327 and 91, respectively.

Total funds are 63.2 billion Kip ($7.4 million), comprising savings of 52.1 billon Kip ($6.1 million), interest income of 8.2 billion Kip ($0.97 million), a reserve fund of 2.0 billion Kip ($0.24) and a development of 0.14 billion Kip ($0.02 million). Total loans outstanding amount to 62.1 billion Kip ($7.3 million) – 98.2% of total resources. The village banks operate on a zero-cash principle and keep very little liquidity; almost all liquid resources are normally lent out within two days after the monthly date of receiving deposits and repayments. Average savings per village bank amount to 487 million Kip ($57,253), average loans outstanding to 580 million Kip ($68,255). Average savings per member are 1.5 million Kip ($175), average loans outstanding per borrower 6.4 million Kip ($752), average loan size disbursed is probably above 10 million Kip ($1,200). (*Table 8*)

Table 8: Village banks under FIAM in Saithany District, Sep. 2009 (in Kip and US$)

Outreach data:		
	Total	*Av. per VB*
No of VBs	107	
No of members	34,946	327
No. of families (est'd.)*	17,622	165
No of borrowers	9,716	91
Lift insurance participants	4,643	
Financial data:		
	Million Kip:	*Million US$:*
Loans outstanding	62,078.1	7.30
Savings	52,071.3	6.13
Interest received	8,236.9	0.97
Other income (net)**	737.7	0.09
Reserve fund	2,043.9	0.24
Development fund	135.1	0.02
Total. funds	*63,224.9*	7.44
Average amounts:		
	Million Kip:	*US$:*
Av. savings per VB	486.6	57,253
Av. reserve fund per VB	19.1	2,247
Av. loan portfolio per VB	580.2	68,255
Av. savings per member	1.5	175
Av. loan outst. per borrower	6.4	752
Exchange rate:	8500	

* Estimated at a rate of 50.4% as in 7 other districts of Vientiane Capital for which data exist by CODI.
** Penalties + membership fees – expenses

Dividends on savings: The village banks pay no interest on savings and no monthly salaries or other regular compensations. Instead, the profit of the year is allocated according to a scheme adopted by FIAM, including dividends to savers, management and advisory committee members. As of September 2009 total profit amounted to 9.0 billion Kip, 70% of which (6.3 billion Kip) were allocated as dividend to savers, equivalent to 12.1% interest.

Table 9: Consolidated profit allocation of 107 village banks in Saithany District, 2009 (in million Kip)

Profit allocated to::	Percentage	Amount
Savers	70	6,282.19
Management committee	15	1,346.18
Advisory committee	5	448.73
Reserve fund	4	358.98
Development fund	4	358.98
Network services	2	179.49
Total profit	100	8,974.56

Saithany District is divided into twelve zones, ranging from four to twelve village banks per zone, with an average of nine. The number of members and the savings balance per zone, and the averages per village bank within each zone, are given in *Table 10*.

Table 10: Saithany District: Savings of >200 mn and >1 bn Kip by zone, Sep 2009 (in mn Kip)

Zone		*No of VBs*	*Members*	*Av./VB*	*Savings*	*Av./VB*	*Sav >200m*	*Sav >1bn*
1	Houaxieng 1	8	3,961	495	7,628.0	953.5	7	2
2	Houaxieng 2	4	1,138	285	2,312.6	578.2	2	1
3	Khoksivilai	11	2,310	210	3,907.8	355.3	7	0
4	Houaychiam	10	1,685	169	1,933.5	193.4	4	0
5	Dongbang	12	2,465	205	3,624.9	302.1	7	<1*
6	Banxai	10	3,249	325	4,227.9	422.8	8	<1*
7	Dongdok	9	4,000	444	7,226.4	802.9	8	5
8	Sivilai	8	4,607	576	7,588.1	948.5	7	2
9	Thangone	12	4,936	411	6,282.6	523.6	9	<2*
10	Veukham	7	1,332	190	355.4	50.8	0	0
11	Hatkiang	8	2,903	363	2,966.2	370.8	6	0
12	Banxang	8	2,360	295	4,017.9	502.2	5	1
	Total	***107***	**34,946**	**327**	***52,071.3***	486.6	***70***	**11 + <4**
	Percent of VB with resp. >200 million and >1 billion Kip in savings						*65%*	*14%*

*Slightly below one billion Kip

Village banks in Saithany District vary widely in outreach and resources, ranging from newly established village banks with less than 50 members and less than 10 million Kip in savings[36] up to one village bank, established in 1998, with 1,356 members and a savings balance of 2.7 billion Kip or $320,000 – that is 2.0 million Kip or $237 per member; and another village bank, established in 2001, with 964 members and a savings balance of 3.2 billion Kip or $375,000 – that is 2.2 billion Kip or $392 per member. Age of village bank and size of village together with economic potential are major determinants of growth, but so is governance. Among the early village banks, established in 1998, are two (both in zone 3) with approximately 70 members and less than 30 million Kip in savings – that is 0.4 million Kip or $49 per member. With the existing data an analysis of growth and strengths (or weaknesses) is not possible. Data on individual village banks are given in *Appendix 6*.

Village banks with >200 million Kip in savings. The regulator has established a floor of 200 million Kip as one of the indicators above which a village bank has to be regulated. In

[36] The smallest with 5.3 million Kip in savings, established in June 2009.

three zones 80% or more of the village banks have more than 200 million Kip in savings. In one of the zones five of the eight village banks have more than one billion Kip in savings. Overall, among the 107 village banks 70, or 65%, have more than 200 million Kip in savings; 11 village banks have more, and another four almost one, billion Kip in savings, together 15.

In sum the village banks in Saithany District show an impressive strength, with a large number of them exceeding the regulatory savings threshold. Here are the key data:

Table 11: Key data of village banks in Saithany District, Vientiane Capital, Sep 2009

Number of village banks	107	
Average number of members	327	
Average savings balance per VB	486.6 mn Kip	$57,253
Average reserve fund per VB	19.1 mn Kip	$2,247
Av. loan portfolio per VB	580.2 mn Kip	$68,255
Dividend to savers in percent of savings	12.1%	
VBs with more than 200 million Kip in saving	70	
VBs with approx. 1 billion Kip in savings or more	15	

3.4 Expansion to the remaining eight districts of Vientiane Capital

Expansion to the remaining districts in Vientiane Capital has been promoted by two agencies: FIAM in one and CODI in seven districts.

3.4.1 Expansion to Saysettha District

In Saysettha District 44 village banks have been established, all following the FIAM model. FIAM itself promoted the establishment of 39 village banks; another four were initiated by NALD under Khanthone Phamuang who also promoted village banks in the remaining seven districts; one village bank was established through local self-help. There is no network organization in Saysettha District to provide monitoring data. No data beyond those in *table 12* are available.

Table 12: Village banks in Saysettha District

No of village banks	44
Estimated no of VBs with >200m Kip in savings	18
No of members	8,883
Amount of savings in million Kip	10,609.2

3.4.2 Expansion to seven Districts

Following the model established by FIAM in Saithany District, CODI, a Thai government development organization, has been promoting village banks in seven other districts of Vientiane Capital.

There are 302 village banks in the seven districts, six of them under the umbrella of a network center and the guidance of a promotional office[37]. The data reported below are based on monitoring by the network centers. The total number of members is almost 60,500 who are all savers. It is common that both wife and husband are members; some 30,500 families are reported as being covered by the village banks. 17,000 members have currently

[37] Headed by Mr. Khanthone Phamuang (cdealaos@yahoo.com), who was also the leader of the Saithany survey team.

a loan outstanding, that is 28**%** of members. The average number of members and borrowers per village bank is 202 and 57, respectively. The village banks in the seven districts are thus smaller than in Saithany, which may be due to their later establishment.

Total funds amount to 77.95 billion Kip ($9.2 million), comprising savings of 64.05 billon Kip ($7.54 million), net income of 8.8 billion Kip ($1.04 million), a reserve fund of 1.84 billion Kip ($0.22), a development fund of 0.47 billion Kip ($0.05 million), a study tour fund of 0.61 billion KIP ($0.07 million) and a welfare insurance fund of 2.14 million Kip ($0.25 million). Total loans outstanding amount to 62.9 billion Kip ($7.4 million) – 80.7% of total resources.

Average savings deposits per village bank amount to 214 million Kip ($25,118), average loans outstanding to 210 million Kip ($24,656) – that is 44% and 36% of the respective average amounts in the village banks of Saithany.

Average savings per member are 1.06 million Kip ($125), average loans outstanding per borrower 3.69 million Kip ($434) – that is 79% and 58% of the respective amounts in the village banks of Saithany. (*Table 13*)

Table 13: Village banks in 7 districts of Vientiane Capital, Sep. 2009 (in Kip and US$)

Outreach data:		
No of VBs	302	
No of members	60,470	
No. of families	30,477	
No of borrowers	17,029	
Life insurance participants	20,802	
Av. no of members per VB	200	
Av. no of borrowers per VB	57	
Financial data:	*Million Kip:*	*Million US$:*
Loans outstanding	62,872.4	7.40
Savings	64,050.5	7.54
Interest received	8,424.3	0.99
Other income (net)*	417.6	0.05
Reserve fund	1,837.7	0.22
Development fund	466.1	0.05
Study tour fund	613.4	0.07
Welfare insurance fund	2,141.4	0.25
Total funds	77,951.0	9.17
Average amounts:	*Million Kip:*	*US$:*
Av. savings per VB	212.1	25,000
Av. loans per VB	208.2	24,500
Av. savings per member	1.06	125
Av. loan outst. per borrower	3.7	434
Exchange rate:	8,500	

* Penalties plus membership fees minus expenses

Dividends on savings: As in Saithany District, the profit of the year is allocated according to the same scheme as in FIAM, including dividends to savers, management and advisory committee members, allocations to the reserve fund and a development fund and a fee for network services. As of September 2009 total profit amounted to 8.8 billion Kip, 70% of which (6.2 billion Kip) were allocated as dividend to savers (almost the same amount as in the single district of Saithany), equivalent to 9.7% interest on savings. (*Table 14*)

Table 14: Consolidated profit allocation of village banks under CODI in seven districts of Vientiane Capital, 2009 (in million Kip)

Profit allocated to::	Percentage	Amount
Savers	70	6,189.31
Management committee	15	1,326.28
Advisory committee	5	442.09
Reserve fund	4	353.67
Development fund	4	353.67
Network services	2	176.84
Total profit	100	8,841.87

The number of village banks in the seven districts under CODI varies from 24 in the most recently added district to 55, the average number of members per village bank from 126 to 355, the loan portfolio from 51.3 million Kip to 405.7 million Kip. The number of members in District 5, Chanthabouly[38] is estimated at 5,700; including that number brings the total number of members up to 60,470. 105 village banks (35% have more than 200 million Kip in savings. (*Table 15*) More detailed information by district is given in *Appendix 7*.

Table 15: Village banks under CODI by district, 30 Sep. 2009 (in million Kip)

District	*Name of district*	*No of VBs*	*Members*	*Av./VB*	*Savings*	*Av./VB*	*Sav >200m*
1	Pakngum	55	13,016	237	17,461.2	317.5	30
2	Sangthong	37	5,350	145	4,512.6	122.0	8
3	Naxaythong	55	19,511	355	22,311.3	405.7	40
4	Sisattanak	42	5,290	126	4,294.2	102.2	8
5*	Chanthabouly	37	*5,700*	*154*	6,628.6	179.2	6
6	Sikhottabong	52	8,188	158	7,610.6	146.4	11
7	Hadsayphong	24	3,415	142	1,232.1	51.3	2
	Total	*300*	*60,470*	*202*	*64,050.6*	*213.5*	*105*

*Number of members in District 5 estimated

Key data on the village banks in the seven districts under CODI are summarized in *table 16*.

Table 16: Key data of village banks in Vientiance Capital under CODI, Sep 2009

Number of village banks	302	
Average number of members	200	
Average savings balance per VB	212.1 million Kip	$25,000
Average reserve fund per VB	6.1 million Kip	$721
Av. loan portfolio per VB	208.2 million Kip	$24,500
Dividend to savers in percent of savings	9.7%	
VBs with more than 200 million Kip in saving	105	
VBs with 1 billion Kip in savings or more	15	

[38] The number of village banks in Chantabouly has been recently updated from 35 to 37. There is no information about the two additional village banks.

4. Village banking networks in Vientiane Capital

4.1 Overview

Initiative and coverage. Self-sustaining networks of village banks have been initiated by LWU together with FIAM and CODI in all but one districts of Vientiane Capital. The first network was established by FIAM in Saithany District in 2003. This was followed by CODI during the same year in Pakngum District, next in Sangthong and Naxaithong in 2006, and finally in Sisattanak, Chanthabouly, Sikhottabong and Hadxaiphong in 2008-09. By the end of 2009 eight of the nine districts of Vientiane Capital had their own networks; the remaining district, Saysettha with 44 village banks, is expected to be included in 2010.

Table 17: Networks of village banks in Vientiane Capital

Name of district	*Promoter*	*Year of establishment*	*No of VBs*
Saithany	FIAM	2003	107
Pakngum	CODI	2003	55
Sangthong	CODI	2006	37
Naxaythong	CODI	2006	55
Sisattanak	CODI	2008-09	42
Chanthabouly	CODI	2008-09	37
Sikhottabong	CODI	2008-09	52
Hadxayphong	CODI	2008-09	24
Saysettha	FIAM	*Expected in 2010*	44
Total number:		*8*	*453*

4.2 The village banking network in Saithany District

The network in Saithany has served as a model for the networks in the other districts of Vientiane Capital and in other provinces and has inspired a number of donors. It was established as a nonformal organization (ie, without a legal status), on 31 January 2003. It was initially run by a honorary staff from within the district administration premises which also houses the District Lao Women Union, the prime mover of the networking process.

Objectives. Each network has a multi-tiered structure with an interrelated set of purposes:

- Disseminating village banks in the area
- Strengthening them in response to member demands
- Sharing experience within the zones and the district,
- strengthening member participation to develop their village, zone and district
- training village bank and committee members,
- information gathering and reporting
- monitoring and supervision
- managing a voluntary life insurance fund, referred to as welfare fund
- cooperation with partners
- *more recently:* setting up a communication link with the regulator.

Principles. The networks are built on similar principles as the village banks: self-reliance and sustainability based on cost coverage and self-financing, self-management, self-regulation and self-supervision.

Costs are borne by the village banks. 2% of their profits are allocated for the salaries and expenses of the chairperson and adviser at the center and the allowances of the zonal committee members.[39] Until 2010 the two accountants are paid by FIAM. As of 2011 they are expected to be paid from the profit allocation of the village banks.

Structure of the network. In Saithany the network is comprised of a center with a permanent staff and a committee, 12 zones each with their own committees, 107 village banks each with a management committee and an advisory committee and, at present, 35,000 members as owners of the network.

At the central level the district network has two organs: a network committee of representatives elected by the zonal committees and a network center. The network committee has 17 members: one delegate from each of 12 zones in Saithany, one representative each of the Women's Union of Vientiane Capital (who is also the head of Center office), of the District Women's Union and of the Rural Development Project (FIAM), and two advisers. Committee meetings are quarterly.

The network center has a full-time staff of four women: a chairwoman, an adviser who is a retired president of the District Women's Union, and two accountants: one in charge of center finances, the other one administering a welfare-com-life-insurance fund with voluntary participation. Since February 2009 the network center has been given a room as a permanent office in the premises of the district administration, equipped with four desks and a computer.

Zonal committees. The 107 village banks of Saithany District are divided into 12 zones (*khumban*), each with a zonal network of nine village banks on average and a committee representing the member institutions. The size of the zonal committee thus depends on the number of village banks in the zonal network. Each village bank elects a representative and a substitute. Each zonal committee elects an executive board of three, comprising a chairwoman and two deputies, one of them serving as an accountant. Elections are usually held every two or three years. Meetings are quarterly. Committee members receive a remuneration from the 2% profit-sharing allocation of the village banks. Each zonal committee elects a representative to the district committee and a substitute.

The zonal committees occupy an intermediate position between the committees of the village banks and the district committee without any power of their own. In terms of governance their function reportedly is a mere *sharing of experience – leak pian kham han,* involving communication up and down the line, but without any decision-making or enforcement power. The zonal committees reportedly "do not give advice"; all issues requiring decision-making, "advice" and action are passed on to the district committee.

The representatives of the village banks collect monthly financial data from their respective institutions which are passed on through the zonal board to the district network center. The zonal committee meets quarterly and discusses all information gathered from the village banks and received from the network center. In addition to reporting, the functions of the zonal committees and their representatives include monitoring and inspection, guidance in accounting and other matters, discussing issues and suggesting possible solutions. The board of the zonal committees prepare quarterly financial reports and other reports, eg, on activities and problems, and submit them to the center.

Ownership of the village banks as shareholders of the network is based on members with their savings as the main source of funds. While there is a membership fee, this is not considered as share capital. It is savings which constitute ownership and are the foundation of member power. This is most visible when members become dissatisfied with the running

[39] In actual fact most are chosen from management and advisory committees and may receive no extra honorarium.

of a village bank (due to internal or external factors) and withdraw their savings, thus leading to the decline of the village bank as a financial institution and at the same time of member dividends and of remunerations to committee members, which are a major source of income. In that respect the members are ultimately more powerful than their various network committees and even the regulator. Thus, any process pertaining to the village banks must be accepted by the member, lest they withdraw their savings.

Ownership of the network at zonal and district level is based on shareholder by the village banks, who elect representatives at zonal and district level and finance all expenses of the network from a fixed share of the profit. The zonal and district committee members thus have a direct material interest in the profitability of the village banks.

Governance of the network is bi-polar, reconciling the power of the people and the power of the center. Governance rests at the bottom with the members of the village banks who elect the members of the zonal committees, which in turn elect the district representatives, and finance the network; and at the top with the district committee and network center. The representatives of the LWU are involved at all network levels – in village bank, zonal and district committees – and are linked to the LWU at provincial and national levels.

Reporting and supervision. The district center has assigned responsibility for inspecting the books and collecting financial data and other information – including problems encountered by the village banks – to the zonal and village committees, to be reported from the village up the line to the center. The center staff consolidates manually transmitted financial data of the village banks at zonal and district level, using a computer, and prepares monthly, quarterly and annual reports. The reports are sent to the LWU at district, Vientiane Capital and national level. As the reporting system is relatively new and still evolving in the districts of Vientiane Capital, there is as yet no central processing and reporting facility at the LWU. There is no evidence that any of this information is shared with the central bank.

Inspection of the village banks is placed in the hands of the zonal committees; it does not seem to be professionalized. Center staff is directly involved in only two inspections: the chairperson of the center inspects dividend payment in village banks; the adviser inspects the share books of village banks which hold shares in the center. The two accountants at the center are internally controlled by the district committee.

A case of effective supervision. The reports submitted to the center are discussed quarterly by the district committee. Action to be taken is normally delegated to the zonal committees. The instrument is persuasion rather then enforcement of compliance. An example is the village bank of Thongmang. Due to poor management and governance many members withdrew their savings. After the problems had been reported to, and discussed by, the district committee, the zonal committee, in cooperation with the district center, took action by discussing the problems with the members. This led to new elections of the management committee and the advisory committee, including a new president. Proper procedures were installed, and confidence was restored, leading to the recovery and subsequent progress of the village bank. Overall it is claimed that supervision is fairly effective and has strengthened the village banks, resulting in an increase in membership and savings.However, this claim requires further corroboration; meanwhile the overall effectiveness of governance by representatives of village authorities my be questioned.

Life insurance. The networks in Vientiane Capital have established welfare funds with voluntary participation functioning as life insurance, managed by the respective network centers. In Saithany District, under guidance from FIAM, every participant pays 1000 Kip in case of a death, and the family of the deceased receives three million Kip, the same amount being allocated to the network's reserves. The scheme has 4,643 participants. One of the accountants is responsible for the administration. In Saithany the welfare fund is not reported on the consolidated balance sheet. In the other seven districts, under CODI, a total of 20,802 village bank members participate in the scheme, which obviously functions as an effective mobilizer of savings. As of September 2009 total resources accumulated in the welfare fund amounted to 2.14 billion Kip ($250,000).

4.3 Response of the network to the microfinance regulation of 2008

The district network center welcomes BOL's initiative to take responsibility for microfinance and shares its concern for the development of a strong and sustainable sector. The center has received the regulation of June 2008 and has participated in a seminar. Three steps are being taken: (i) examining the regulation (ongoing); (ii) disseminating the information among the village bank members and hearing their views; and (iii) asking for directions from LWU. The members of the village banks are of crucial importance because they own the groups and the savings. The process of registration and regulation of village banks must involve the village bank member as active partners, lest they withdraw their savings.

Compliance uncertainty. By the end of 2009 none of the village banks has responded to the requirement of registration and licensing within the one year period ending June 2009 set by BOL, nor has BOL so far shown a determination of enforcing compliance with the regulation. LWU seems to assume that given a three years extension of its village banking project in Vientiane Capital and other provinces, the need to be registered or licensed, respectively, under one of the three options of the regulation is also being deferred. Tentatively we may conclude that there is an implicit readiness for communication and adjustment.

Regulation as an evolutionary process. Appropriate regulation is an evolutionary process, requiring communication between the stakeholders. This implies a double challenge: for the village banks to learn communicating with the central bank; for the central bank to learn listening to the village banks. Effective communication involves at the core the village banking networks and BOL, together with major service providers and donors, LWU and BOL – a process yet to be initiated. The communication process is likely to lead to adjustments at both sides, the regulator and the regulated, as will be discussed below.

SCU preference if regulation can be adjusted. Groups with savings of more than 200 million Kip have to be licensed: as deposit-taking MFIs or savings and credit unions. Members are likely to prefer the SCU model, provided the regulation can be adapted to some of the practices of the village banks. The regulation is not adjusted to the practice of profit-sharing at the end of a financial year, which includes not only dividends to members as a substitute for interest payments on savings but also remunerations paid to management and advisory committee members instead of paying fixed monthly salaries or compensations.

Indeed, not only BOL but microfinance experts worldwide can learn from the village banks in Laos how to keep costs under control and guarantee viability: by avoiding fixed salaries and interest payments on savings during the year and deferring all remunerations to profit-sharing after the year's end. The quality of regulation could be improved by adapting to reasonable operational practices in the village banks. However, remaining questions are about governance, transparency and accountability within village banks.

Regulation will also impact operational practices. Village banks in Laos have been reluctant to enforce timely repayment. Penalties on loans overdue are a major source of income; and the management committees have been generous in rescheduling loans. At the same time it has been noted that defaulting rarely happens, if ever; even when someone dies his debts – for spiritual reasons – are settled by his relatives. Thus, village banks are notorious for high portfolio-at-risk ratios (PAR); yet this does not signify terminal illness, as it might in microfinance institutions in other countries. However, perpetual delays in repayment have a negative impact on cash-flow and the availability of resources for new loans, which are generally in short supply as the financial reports of the village banks indicate.[40] It may also undermine the investment culture, leading to complacency among the borrowers who may pay less attention to cash-flow management and may be less inclined to put their loans in high-yielding investments. It may be difficult for committee members to enforce repayment in a tightly knit community if not compelled by an outside force. Via training on incentives for timely repayment[41] and good governance in general, appropriate regulation is likely to have a positive impact on the credit and repayment culture.

4.4 Network responses to other policy options

Feasibility of a central fund. The network center of Saithany District has no definite view on the establishment of a central fund at district level, but is considering this as an option once FIAM support stops. A central fund at national or municipality level is not taken into consideration. As a source of finance, the network center would consider selling special shares to village banks, who would be owners of the fund as a subsidiary of the network.

Attitude to solidarity group lending. According to the network center staff of Saithany district, confirmed by survey findings by Khanthone, village banks are adverse to two aspects of a Grameen Bank Approach (GBA): (a) regular weekly meetings and (b) mutual guarantees within solidarity groups. However, this attitude is confined to urban and periurban areas as in Vientiane Capital, where urbanization has undermined trust and honesty that were characteristics of traditional Lao society.

This finding does not apply to rural areas, particularly in remote and poor districts, where traditional values and practices are still upheld. It is being emphasized that solidarity and mutual help persist in the countryside. So far SBFIC has found no objection in its WFDF project against weekly meetings and mutual guarantees. In the cities trust has broken down, and it is more difficult to enforce repayment. Reportedly it takes strong powers in Vientiane Capital to counteract this trend, such as LWU mobilizing local authorities as members of advisory committees to make village banking members honor their obligations.

---

[40] Incoming funds are normally lent within two days, and liquidity reserves are minimal.
[41] As in the microbanking units of Bank Rakyat Indonesia (Seibel 2009).

5. Strengths and weaknesses of village banks and village banking networks

5.1 Strengths

5.1.1 Strengths of village banks

Cultural integration. Village banks in Vientiane Capital have evolved over the past ten years as a uniquely Laotian microfinance model. Technical assistance from neighboring Thailand together with cultural sensitivity of Lao program management has played a formative role in designing a culturally adapted system. Without exception the community of residents of a single village is the preferred social and economic space of a village bank in Vientiane Capital. Membership is voluntary and self-selected; compulsory or automatic membership would not be accepted. Two factors of Lao culture find their expression in membership and ownership. One is the financial power and responsibility of women in village society and their role as holders of the family purse and in cash income-generating activities. Both women and men are members, in fact, usually both husband and wife; but women are prominent as founding and management committee members, and they decide whether men may also borrow. The other one is a pronounced propensity to save as a strong cultural preference throughout Laos. Depositing savings is the first purpose of a village bank in Vientiane Capital; access to credit is secondary. Membership and ownership are constituted by saving; a saver is a member, and a member is a saver. There is also a religious element involved in the credit culture. Payments may be delayed, and loans may be rescheduled; but ultimate defaults are rare as these would affect reincarnation.

Outreach. In purely quantitative terms outreach is the greatest strength of village banks in Vientiane Capital. At 91% of villages coverage is almost total. Half the families are members. Out of 104,000 member-savers, 30,000 are borrowers (with a loan outstanding) and 25,000 life insurance participants. Total assets amount to 153bn Kip ($18m) – a remarkable figure in a generally undermonetized economy. Average membership per village bank is 229, with 338m Kip in total assets, 280m Kip in savings, 65 borrowers and 299m Kip in loans outstanding. Outreach is strongest in Saithany District, with a coverage of 98% of villages, an average of 327 members and 91 borrowers per village bank, 487m Kip in savings and 580m Kip in loans outstanding.

Village banks with more than 200m Kip in savings are to be prudentially regulated. Nearly 200 village banks (43%) in Vientiane Capital fall into that category. Seven village banks have more than 1,000 members. Saithany District has the highest density of large village banks, with 70 out of 107 (65%), accounting for around half the total funds and loan portfolio of village banks in the municipality; it also has the strongest self-organized network structure.

Self-governance of village banks in Vientiane Capital comprises a "tripod of governance" (*Khanthone*): member ownership with ultimate decision-making power, self-management through a mostly female management committee, and internal control through a mostly male advisory committee (or *board*) representing the local power structure. LWU plays a prominent role and is a part of all three legs of the tripod.

Financial self-reliance. Village banks in Vientiane Capital are fully self-financed through savings as a major source of loanable funds and a motor of growth, and profits as a source of funds to compensate savers and committee members and for other purposes. There is a complete absence of donor seed funds, capital grants and credit lines and thus no temptation to develop a dependency syndrome.

The financial technology is demand-driven and individual; reportedly due to a lack of solidarity in an urban and peri-urban environment, there are no group loans. Almost all assets are earning assets; almost all liquid resources during the year are lent out to members within a day (*zero-cash principle*).

Cost-effectiveness and profitability. Transaction costs of village banks and of members (as depositors and borrowers) are minimal. The village banks practice a highly cost-effective model adjusted to the small size of villages and the small number of transactions, usually during a two-day period every month. There are no fixed regular costs. Compensations for savers and committee members are paid as dividends out of profits at the end of the bank's financial year. Thus there is no risk of cost overruns. The village banks in Vientiane Capital are very profitable. Dividends paid to committee members are an attractive source of income, perhaps overly attractive in large village banks. Dividends to savers stood at 10.7%, equivalent to 3% in real terms (adjusted for inflation).

5.1.2 Strengths of networks of village banks

Network structure. In eight of the nine districts of Vientiane Capital village banks are organized in self-financed, self-managed and self-governed networks; in the ninth district a network is under preparation. The networks comprise two tiers: zonal and district. Federating the district networks at Vientiane Capital level is under consideration; a national federation or apex is not in sight.

Ownership and governance. Ownership of the network is based on member ownership of the village banks which in turn own shares of the respective district network. The networks are self-financed; network expenses for committees at zonal and district level and of the administrative center are paid from a fixed share (2%) of the village banks' profit. The networks are governed by elected committees at zonal and district level and managed by a district center. At the central level the district network has two organs: a network committee of representatives (eg, 17 in Saithany District) as governing board, elected by the zonal committees, with delegates from each zone, and an administrative network center.

The networks as organs of supervision. The main objectives of the networks are reporting, monitoring and supervision. The networks also manage voluntary life insurance funds. The zonal committees have the responsibility of inspecting the books and collecting financial data and reporting them to the center. The center staff consolidates the financial data and prepares monthly, quarterly and annual reports – in a timely manner! Center staff inspects dividend payment in village banks. Zonal committees also report problems encountered by the village banks to the district center and committee which deliberates on steps to be taken. Initiatives to remedy the problems are normally delegated to the zonal committees, which in turn enter into a dialog with the village bank committees, in extreme cases where the committees are not functioning directly with the general assembly of a village bank.

Dissemination and sustainability. The village banking and related networking model in Vientiane Capital is designed as an integrated sustainable structure, based on principles of self-reliance, self-financing, self-management and self-governance. It has been developed with technical assistance by FIAM and subsequently by CODI in cooperation with LWU. The staff and functions of the FIAM project have been transmitted to LCSDPA as a domestic organization. Both CODI and LSCDPA have been involved in disseminating the model of village banking and networking to other provinces and adapting it in various ways to local socioeconomic conditions and donor strategies. Donor support in the provinces usually comprises both technical and financial assistance, with the ultimate objective of sustainability.

5.2 Weaknesses

5.2.1 Weaknesses of village banks

Delays in repayment. There is little concern for on-time repayment in the village banks. This might be a relic of savings and loans in kind traditions, prevalent in the early 1990s, where the timing of payments is determined by the rhythm of nature rather than the calendar. Little effort is made to enforce timely repayment. In fact, penalties on overdue loans are a major source of income. The relaxed attitude is backed by confidence that all loans will eventually be repaid. The overdue loan ratio prescribed by BOL is thus a more realistic performance indicator than the portfolio-at-risk ratio. However, a high overdue loan ratio cuts down on liquidity available for new loans. It also promotes complacency among borrowers and diminishes the productivity of loan usage.

Low rate of capital formation. In the FIAM/CODI model only 5% of profit are allocated to reserves. This is insufficient to protect the value of the capital against losses due to inflation and against internal crises or external shocks. It is also a restraining factor in any effort of upgrading village banks to formal institutions. Note should be taken that that wealth of credit cooperatives in many European countries is due to the fact that over a century or longer all dividends have been ploughed back as retained earnings.

The chart of accounts (COA) of village banks does comprise a balance sheet and a separate income statement; but it does not follow BOL's format or international standards. No financial reporting forms are provided to be filled in a prescribed manner. Income and expenditure items are mixed up with the balance sheet. The following are the main deviations from the BOL COA:

- The order of items is idiosyncratic.
- No salaries and compensations appear as expenditure on the income statement.
- On the basis of the annual income and expenditure statement net income is calculated and allocated to various categories, comprising dividends to savers, compensations to management and advisory committee members, reserves and funds (as on the BOL COA), and network & supervision costs.
- Income and minor expenditure items are mixed up with the balance sheet, respectively on the liability and asset side.
- The financial year is not standardized and varies with the foundation date of each village bank.

Taxation issues. Unregulated village banks do not pay taxes. This will change with licensing and might require some prior adaptation. As remunerations to savers and committee members do not appear as cost items in the income statement, they might not be tax deductible. The tax implications of the two models of accommodating remunerations either as costs or as dividends need to be further studied in due course.

Manual accounting is not necessarily a weakness in a village setting – it may in fact be a strength under conditions of power failures, lack of IT maintenance and limited numbers of transactions. However, it might be a constraint if monthly or quarterly reporting is required by BOL.

Transactions take place only once a month: cash in on one day, cash out on the next. There are no regular services during the rest of the month. The members could change this; but as they have not done so we have to assume that there might be a lack of demand for regular services.

5.2.2 Weaknesses of networks of village banks

Networking without federating. The networks in Vientiane Capital operate at district level; there is no structure or interest organization beyond this. They are thus not able to speak with one voice to represent their members and express their interests; and there is no systematic data consolidation and reporting at the level of the municipality. This is not surprising, as the networks are still in an early stage of formation. However, there is an informal incipient structure through CODI, which provides TA to seven districts and is able to provide basic consolidated information (in Lao), but only if directly requested to do so.

Lack of recognition by BOL. The district networks are not recognized as interest organizations or as lower-level supervisory agencies by BOL. They do not report to BOL, and BOL does not consolidate their financial data.

Capacities of management and board, or management and advisory committee members, are limited, and there is ample room for capacity building. However, capacities are not easily built by offering training services. There is no professional permanent management, and the composition of the management committee changes every so often when elections take place, similarly among advisory committee members. As a result there is a limited professional commitment among both management and advisory committee members. Training providers (like MFC and EBIT Consultancy together with supporting donors) who are trying to build capacity over an extended period thus face changing compositions of training participants and find it difficult to cater to the needs of both newcomers and more advanced members.

5.2.3 Wider problem areas in Laos

Lack of stakeholder coordination. During the initial period of microcredit and microfinance development in Laos, UNDP/CDF took the lead and coordinated a Microfinance Roundtable as a communication forum, with regular meetings. This came to a standstill when UNDP/CDF pulled out over conflicts of a project of its own,1997-2001. The Roundtable was eventually replaced by a Microfinance Working Group, an informal gathering without regular meetings, coordinated by two co-chairs as individuals[42], with BOL participation. Regretfully, this group was not active in recent years. Similarly, a microfinance online resource center (www.microfinancelaopdr.org) providing information about microfinance in Laos, initiated by NERI in the context of the MCBR/NERI microfinance surveys of 2005 and 2006, has not been updated for two years. As a result there is lack of communication and information among stakeholders. At the turn of 2009 to 2010 steps are being taken to revive the Microfinance Working Group.

[42] Timo Hogenhout, microfinance consultant and Somphone Sisenglath, director of Microfinance Center, a leading private training and consulting firm

6. Options for village banks in Vientiane Capital

6.1 Presentation of options

Option 1: Establishment of a stakeholder forum of communication at the level of Vientiane Capital

Vientiane Capital has the strongest network organizations of village banks in Laos, which are evolving into representative and supervisory bodies. Up to now none of the village banks in the municipality has followed the call for registration and regulation by BOL. None of the stakeholders has taken steps to register village banks as NTMFs or as licensed MFIs, nor has BOL announced its intention of actually enforcing its MFI regulation. All this signifies a waiting stance on the part of BOL and a willingness to engage in communication about the way forward. The following presentation of options for village banks in Vientiane Capital is based on this assumption.

Recommendations. We recommend the establishment of a stakeholder forum of communication at the level of Vientiane Capital:

- The forum should comprise the following participants:
  - the village bank network organizations of Vientiane Capital
  - BOL
  - LWU
  - local government
  - service providers (CODI, FIAM)
  - donor agencies
- The district network centers of village banks, with assistance by LWU and service providers, establish a federation or representative body at Vientiane Capital level.
- The federation or representative body of village banks, BOL, LWU, local government and service providers establish a forum of communication and enter into regular dialog.
- As long as a federation or representative body does not exists representatives of the district networks participate directly in the forum.
- Representatives of network organizations might be the head and advisor at the network center and the chairperson of the district network committee.
- **Organization:** The forum is governed by a committee of stakeholders, and managed by an executive committee which is supported by a permanent secretariat.
- The forum may appoint task forces or working groups for particular tasks.
- The forum establishes a task force for the preparation and implementation of appropriate prudential regulation.
- The forum receives technical assistance through one of the donor agencies in Laos.

Option 2: Village banking networks

Village banking networks at district level which follow the village banking principles of self-financing, self-management and self-governance have been established in Vientiane Capital starting in 2003. In cooperation with LWU networks were first initiated by FIAM in Saithany District, subsequently by CODI in seven other districts; establishment of a network in the remaining district is expected in 2010. The networks are self-reliant organizations owned, managed and financed by the village banks in a given district. The networks have no legal status and are not officially recognized by BOL. They would be sustainable once they obtain a legal status and are given a function within BOL's regulatory framework.

There is only scant information; no systematic study of the networks exists. The network and network centers are at various stages of development. While Saithany District has served as a model, it is not clear to what extent the networks in the other districts mirror the zonal and district network and district center structure of Saithany and how well they function. We may assume that particularly the recent ones might be quite rudimentary structures. There is no network or network federation at the level of Vientiane Capital. The district networks, or at least the one in Saithany District (the only one on which we have collected basic information), are the only system designed to actually carry out basic support functions for village banks on a sustainable basis: registration, guidance, monitoring, reporting and supervision. They thus carry out functions informally which BOL set out to provide formally as regulator. From a demand and member perspective, the village banks recognize their networks as representative bodies and submit to their authority as an informal supervisor (informally sanctioned by LWU). This is a framework through which BOL might initiate a process of communication regarding the reformulation of regulation and the practical implementation of registration, licensing, reporting and supervision of village banks as well as guidance and capacity building.

Recommendations: We suggest to donors to focus their support on the strengthening of sustainable networking structures as self-organized instruments of village banking development in concertation with LWU and BOL, aiming at the promotion of a properly registered, licensed and supervised system of village banks in Vientiane Capital:

- Establishing a communication forum as described under Option 1 with several task forces to examine the appropriateness and feasibility of the options and recommendations presented, facilitate donor linkages, initiate feasibility studies, prepare business plans and monitor their implementation
- Strengthening existing support agencies (eg, initiated by FIAM and CODI) in Vientiane Capital
- Strengthening the district networks of village banks as self-organized and self-reliant business associations, service providers and informal monitoring & supervisory bodies
- Initiating a network or federation of district networks at Vientiane Capital level as an advocacy agency of the village banks and their district networks
- Building network services or subsidiaries at district or Vientiane Capital level such as:
  - Training services (in cooperation with existing training providers)
  - Central fund(s) for liquidity exchange and refinancing
  - Auditing services
- Facilitating appropriate registration, licensing and legal forms for the networks (most probably as *associations* under association law) and their subsidiaries
- Facilitating a revision of the regulatory framework for village banks
- Facilitating the process of bringing village banks under an appropriate regulatory framework
- The process of communication, network strengthening and licensing process facilitation may start in Saithany District, which has the strongest network and village banks.

This would require initial funding by donor agencies as it will take time for the networks to become fully operational and sustainable.

Option 3: Village-based NDTMFIs

Village banks in Vientiane Capital have evolved since 1998, covering more than 90% of the villages. The community of residents of a village is the area of operation. There is no willingness of branching out or merging with neighboring village banks which will limit the possibility of "economics of scale" for the individual units. The village banks in Vientiane Capital have developed a unique system of operation; all are profit-making. There is thus no cause for the regulator to rescue and restructure any village banks. Accordingly there is no immediate justification for imposing a system of prudential regulation that does not take into consideration the good practices that have evolved and the actual demand of village banks for supportive intervention by the central bank. Moreover, in a survey among 40 village banks in Saithany District the respondents emphatically stated that they were very satisfied with the existing set-up and would by no means want to change the existing system. At the same time, they were not aware of details of the new regulation and their advantages and what changes licensing would entail. All this means that it would not be wise, and in fact ineffective, to impose the new regulation without the consent of the members of the village banks. Their power lies in their savings, the main and almost exclusive source of funds; if members were dissatisfied and withdrew their funds, there would be no institutions left to regulate. Therefore a two-way process of confidence building and learning is required during which the village banks become familiar with the new regulation and with BOL as an institution, perhaps as a well-meaning partner; at the same time BOL would become familiar with the existing village banking system, its strengths and its need for improvement. A process of communication and interaction of the village banks and their representative bodies with BOL would bring the village banks and BOL closer together and create an atmosphere of mutual learning. The forum proposed under Option 1 would play a crucial role in that process.

Recommendations. We therefore propose an evolutionary and interactive approach to prudential regulation, building on the existing village banking system in Vientiane Capital. Such a process would best be initiated within the framework of registering all village banks in Vientiane Capital as NDTMFIs with BOL through their networks during 2010, without any expectation or pressure of transformation into SCUs or DTMFIs during that year. The forum described under Option 1 would assume a facilitating role. The following steps may be taken in a participatory process:

- The Vientiane Capital forum re-examines the regulation for NDTMFIs, particularly on maximum loan size (10m Kip), maximum deposit balance per village bank (200m Kip) and maximum deposit size per single depositor (10m Kip).
- The forum agrees on an appropriate name for MFIs which are registered with BOL but not prudentially regulated; the name should indicate that these MFIs are authorized to collect voluntary savings (up to a certain amount).
- The forum agrees on a COA adjusted to the specifics of the village banks and approved by BOL.
- The village banks adjust their financial year to the calendar year and report annually to BOL through their network centers.
- For annual reporting and tax purposes dividends to savers and committee members may be recalculated at year's end as interest expenses and compensations for committee members, respectively.
- The forum, in close association with the district networks and zonal committees, discusses strategies of improving on-time repayment, eg, through incentives for timely repayment, and offers guidance to village bank committees.
- All village banks register as NDTMFIs with BOL through their networks as facilitators.
- Annual reports of the village banks are monitored by the district network centers and forwarded to BOL.
- BOL recognizes the district networks as monitoring agencies.

- Once a federation of district networks is established, its role in reporting and monitoring is agreed upon with BOL.

Option 3A: District network-based NDTMFIs

As an alternative to Option 3 the forum of district networks, BOL and other stakeholders may decide, with approval by BOL, that all village banks register with their respective district networks and that the district networks register as NTMFIs with BOL, submitting consolidated annual reports. This might be a temporary solution for a transitional period until a satisfactory solution has been found for the village banks themselves. However, note should be taken that this would distort the nature of the district networks which have not been designed as financial institutions.

Recommendations. As the existing networks of village banks in Vientiane Capital are of recent origin and as yet have not found official recognition by BOL, recommendations can only be procedural and exploratory:

- The forum examines the feasibility of registering the district networks of village banks as NTMFIs and initiates the implementation of its recommendations if any.

Option 4: Village-based SCUs

Village banks and SCUs share a common philosophy: both are member-controlled and follow the democratic principle of one member one vote; savings are the main source of funds; the general assembly of members is the highest authority deciding over policy, management and governance. Yet, no effort has been made to build a modern credit cooperative system on the foundation of some 5,000 village banks or funds as they evolved over the past twenty years. This is only partially due to the negative image of cooperatives, a term and institution affiliated with the collapse of the former command economy, which included the credit cooperative sector.

Among the village banks there has been no rush to register as regulated SCUs. There is only a minute number of regulated SCUs in Laos: eleven out of an estimated 5,000 mostly semi-formal MFIs (village banks or funds). Not all of the eleven are licensed under the SCU regulation of 2008; eg, Naxaython RDC is still registered under the old regulation. Moreover, not all SCUs are well-performing. All this indicates that the regulation has not been demand-driven. (See chapter 1.2)

Most village banks would fulfill the establishment requirement of ten founding members and 100 initial members, though payment of the minimum share might be an issue. External auditing services could be provided by the respective district networks if recognized by BOL as monitoring and auditing agencies. Several stipulations of the SCU regulation would require adjustments by the village banks: a minimum registered capital of 100 million Kip (which is zero in village banks), a liquidity ratio of 20% (kept at an absolute minimum) and a maximum NPL ratio of 5%. Paid-up capital formation could be arranged by members allocating the membership fee and part of the dividend to share capital until the (possibly reduced) required minimum is reached. Credit discipline, bringing the NPL ratio below 5%, would probably be a greater challenge, but one to which village banks should respond in any case.

On the whole there is an affinity between village banks and credit cooperatives (or unions); this is backed by the fact that the village banking system in Vientiane Capital has been shaped after international cooperative regulation. Also most of the few existing SCUs reportedly are former village banks transformed into licensed institutions. If Naxaython RDC may serve as a model, then larger cooperatives (in the case of Naxaython RDC covering 52 villages) would gain in professionalism of management. Yet it is not clear what village banks would gain from registering as SCUs, except, indirectly, an inducement to promote credit discipline. There is a definite preference among village banks for single-village MFIs, without branches or coverage of several villages. It appears that the SCU regulation is designed for a different size of financial institution, with a branch network and a wider outreach at district or provincial up to national level; the regulation does not fit small village-based local MFIs. At the same time there is an explicit resistance among the village banks in Vientiane Capital to register as SCUs: partly out of fear of regulatory impositions, partly because of the negative image of cooperatives in Laos, but partly also out of ignorance of what the regulation entails.

The SCU regulatory framework in Laos is in sharp contrast to most systems of SCUs as local institutions, including the People's Credit Funds of Vietnam (PCFs), one of the most successful credit cooperative movements of recent origin in the developing world. The Vietnamese PCFs are organized at commune level (ie, an administrative unit covering three to four villages) and backed up by a central fund for liquidity exchange. SBV, the central bank, has been in the driver's seat from inception, providing the system design, the regulatory framework, guidance, training and effective supervision (Seibel 2009, 2010). It appears that the SCU regulation of Laos has not benefited from international experience. The experience of Vietnam in particular shows that it takes more than regulation and a COA to build a successful credit cooperative movement. Imposing regulation without a system design, a strategy of expansion and a framework of guidance, training and effective supervision may do more harm than good.

Recommendations: LWU, BOL and the service providers have missed a historic change in 1998 when FIAM and subsequently CODI helped LWU establishing village banks. An appropriate regulatory framework could have been established for single-village SCUs (as has been historically the case in Germany, the Netherlands, India and many other countries); and all newly founded village banks might have been licensed as SCUs.

Laos has no design and strategy for building a self-reliant credit cooperative sector comprising local credit cooperatives, a central fund for liquidity exchange and guidance (possibly with provincial branches) and a national association as a business and advocacy organization. The regulation of June 2008 has not been a response to demand by village banks and is not perceived as fitting their needs. In the given situation we recommend the following:

- The district network centers of village banks, with assistance from LWU and service providers, establish a forum of communication with BOL (as outlined under option 1) to re-examine, and possibly reformulate, the SCU regulation in a participatory process.
- It is recommended to redesign the SCU regulation for local institutions based on the area principle, covering a single village or an adjacent group of villages. This is not excluded by the present regulation, but also not emphasized. Once BOL engages in intense communication with the village banks and their networks, minor adjustments could be made to the regulation. To have the result accepted, BOL would have to promote an image of responding to a demand and strengthening the existing village banks with a regulatory framework, supporting their evolution, rather than imposing a framework by a distant regulator.
- In order to learn from international cooperative experience BOL together with the communication forum should establish a task force and examine the approach taken by SBV, the central bank of Vietnam, in designing, regulating, establishing, promoting and supervising a credit cooperative system (comprising 1015 PCFs with 1.35 million members as of 2008). The objective would not be replication of the Vietnamese

model; such replication might convert *best practice* into *worst practice* if mechanically applied. Rather, the purpose of exposure visits, or a consultancy by the Central Fund of People's Credit Cooperatives of Vietnam (CCF), would be an understanding of the complexity of the process of building a successful credit cooperative system.
- BOL could also benefit from the cooperative experience of Germany, the Netherlands and Canada or other countries and from support by their cooperative development organizations (DGRV, Rabobank Foundation and DID, respectively – all three involved in either Laos or Vietnam or both) – if applied to system development rather than to single institutions.

Option 4A: District network-based SCUs

As an alternative to Option 4 the forum proposed under Option 1 might consider the registration of the existing district networks of village banks as SCUs, with village banks either as branches or members. However, at present this would be a rather artificial construct (a response to the imposition of regulation, rather than a demand-driven choice). The district networks as they emerged were not intended to be MFIs but umbrella organizations for guidance, monitoring and supervision of village banks within the network, albeit for the time being without formal approval by BOL. Of the existing two legal forms, SCU (comprising village banks as founding members with equal votes) would be more appropriate than DTMFI, which are controlled by share capital rather than individual or corporate members and would be more attractive to private investors. If district networks or a (as yet non-existing) network federation of Vientiane Capital should decide to establish a subsidiary for liquidity exchange and refinancing, an appropriate legal form for such an apex fund would have to be found.

Recommendations. As the existing networks of village banks are of recent origin and as yet have not found official recognition by BOL, recommendations can only be procedural and exploratory:

- The forum examines the feasibility of registering the district networks of village banks as SCUs and initiates the implementation of its recommendations if any.
- The forum examines the feasibility of apex funds as subsidiaries of the district network of an apex fund by a network federation at Vientiane Capital level and initiates the implementation of its recommendations if any.

Option 5: DTMFIs

There is no information that any village bank has registered as DTMFI. Out of 16 licensed MFI only five are registered as DTMFIs. High operating costs, poor performance, lack of self-reliance and, at least in one prominent case in Vientiane Capital, a combination of high losses with high interest rates do not make a convincing case for village banks and their network associations to consider DTMFI a feasible legal form. DTMFIs are large institutions by legal definition, with a minimum capital requirement of 1 billion Kip: this is far beyond the capacity of village banks – even in Saithany, the district with the most prosperous village banks in Vientiane Capital. By necessity DTMFIs extend their outreach to a large area, incurring high transaction costs in the process; they cannot subsist in a single village. DTMFIs may be attractive for private investors, but not for village banks. Apart from minimum size, the fundamental incompatibility of the DTMFI and the village banking models in Vientiane Capital lies in the difference of ownership and governance: DTMFIs are owned and governed by private investors according to their share capital (among them at least one *major shareholder*); in contrast village banks are democratic institutions which are saver-driven, member-controlled (each member with the same vote regardless of the amount of savings) and community-governed. Dividends in DTMFIs are paid to shareholders, in village banks to savers.

Recommendations. The shareholder-based DTMFI model and the member-based village banking model of Vientiane Capital are incompatible:

- No attempt should be made to register village banks or their network associations as DTMFIs.

Option 6: Delegated supervision implemented by village banking networks

Networks of village banks in Vientiane Capital provide guidance, monitoring, reporting and supervision services to their member institutions. The network in Saithany District, established in 2003, is the one which is most advanced. By the end of 2010 presumably all village banks in the nine districts of Vientiane Capital will be covered; services are evolving.

Recommendations: BOL does not have the capacity of providing monitoring and supervision services to large numbers of village banks (approximately 450 in Vientiane Capital). Learning from the experience of countries with systems of delegated supervision over large numbers of local financial institutions, we recommend the following:

- Establishing a task force of the communication forum (see Options 1) to initiate a dialog between BOL, LWU, district networks and service providers on delegated supervision
- Examining the feasibility of a system of delegated supervision, comprising:
    - BOL as the ultimate financial authority,
    - auditing services by village bank networks as implementing agencies on behalf of BOL,
    - possibly a federation of networks in Vientiane Capital with coordinating functions
- Establishment of auditing services (or auditing federations or agencies as subsidiaries) as supervisory organs of networks
- Facilitation by the networks of the registration of village banks as NDTMFIs
- Provision by the networks of services to NDTMFIs such as reporting and monitoring, guidance and supervision (over and above what the regulation for NDTMFIs presently requires)
- Facilitation by the networks of the transformation of qualified village banks into prudentially regulated MFIs (such as SCU)
- Capacity building of networks and their auditing services
- Supervision by network auditing services of prudentially regulated village banks on behalf of BOL
- Pilot-testing delegated supervision in Saithany District
- Possibly learning from experience in Germany with banking supervision delegated by Bafin and Bundesbank (as financial authorities) to *auditing federations* of large numbers of savings banks and cooperative banks, historically preceded until 1934 by self-regulation and self-supervision through the respective network agencies (Seibel 2003).

Option 7: Village banks as facilitators of access to bank loans

In 2006-07 there were 88,045 registered enterprises in Laos, on average eight per village. 29.5% of the registered enterprises are in Vientiane Capital. Most of the enterprise sector in Laos consists of private micro and small enterprises and unregistered household businesses or income-generating activities. 70% of employment is in agriculture, 11% in manufacturing. 97% of manufacturing enterprises are small-scale, with less than 10 employees.[43]

In 2007 GTZ surveyed 490 enterprises, or 5.9%, out of a total of 8290 registered enterprises (21% in Vientiane Capital) in 15 target districts in five provinces[44]. Microenterprises are rarely registered; hence the sample is tilted towards larger enterprises. In terms of size, 19% of the sample enterprises were microenterprises (1-2 employees), 62% small enterprises (3-19 employees), 15% medium-scale enterprises (20-99 employees) and 4% larger enterprises (100 and more employees). Closure rates are high. 4198 enterprises were registered in 2005 in the 12 sample districts in four of the five provinces; 2895 closures were reported as of 2007, equivalent to 69% (not exactly evidence of higher sustainability than among informal enterprises).

46% of the sample enterprises took a loan in 2007, about the same as in 2005 (48%). The respective percentages by enterprise size are as follows: microenterprises 35%, small enterprises 45%, medium enterprises 63% and large enterprises 55%. 2007 marks a shift from supplier credit to bank loans. Reportedly, banks accounted for the vast majority of loans, namely 69%; microcredit schemes accounted for only 1.5%, among them presumably village banks (not specifically mentioned). Family members and relatives accounted for 12%, friends for 6% and moneylenders for 9%.

From 2005 to 2007 the number of bank-sourced loans increased dramatically from 4% to 69%, while reported supplier credit fell from 52% to 2%. GTZ (2008:109-110) suggests that this might “reflect(s) the ongoing improvements and reforms in the banking sector, including the promulgation of the Commercial Bank Law in early 2008 and ongoing efforts by the Bank of Lao to improve portfolio quality at the state-owned commercial banks.” In 2007 bank loans dominated in number (and almost certainly even more so in size) across all categories of enterprise size, most pronounced in large enterprises (91%) and medium enterprises (75%); the respective percentages for micro and small enterprises were 71% and 66%.

There is no information on the size of loans obtained, but only on loan demands. 63% of the enterprises stated they would need a loan for expanding their business, with little variation by enterprise size. The average loan size reportedly needed is 8.6 billion Kip (double the average of 4.3 billion in 2005); we may assume that actual loans received were much smaller. By enterprise size, loans desired ranged from 289 million Kip among microenterprises (77 million Kip in 2005) and 1.0 billion Kip among small enterprises (1.8 billion in 2005) to 22 million among medium enterprises (3.9 billion in 2005) and 105 billion among large enterprises (42 billion in 2005). The much larger desired loan sizes in 2007 reflect the new outreach policy of banks. (GTZ 2008: 109-113)

Most of the registered micro and small enterprises in the sample are obviously in a different league from those served by village banks (or VSCGs). Even if we assume that average loans to registered microenterprises may be around or below 100 million Kip and small enterprise loans below 500 million Kip, they are still far above the average loan of around 10 million Kip disbursed per borrower in 2008-09 in Saithany District, 6 million Kip in seven other districts of Vientiane Capital and 3-4 million Kip in four other provinces (where CODI supports village banks). However, maximum loan sizes are a multiple of that amount and may well be a source of finance for registered micro and small enterprises, and, most importantly, for start-ups.

[43] GTZ 2008: 28, 18
[44] Vientiane Capital, Champasack, Luangprabang, Luangnamtha, Savanakhet. This is not a random sample; in each province three districts were selected: the central district, a peri-urban district and a more rural district accessible by road.

Recommendations: Once micro or small enterprises grow beyond a certain size, their credit needs surpass the capacity of village banks. The village banks may still provide short-term working capital loans; but larger and longer-term loans would have to be accessed from banks. Here the village banks, through their networks or associations and service providers, could help facilitating access to banks. As members of a village bank they have a track record as savers and borrowers, which could be documented and help overcoming the information asymmetry between bank and borrower. Their awareness of the importance of a track record might also improve timely repayment. Establishing such a system would require a special effort by the village bank networks and their technical assistance providers. We therefore recommend the following:

- Establishing a task force of the stakeholder forum to examine the feasibility of a referral service of village banks to larger bank loans
- Building capacity in district networks of village banks to organize a referral service
- Monitoring bank referrals through the stakeholder forum or a federation of networks in Vientiane Capital.

Option 8: Bank linkages for liquidity management and refinancing

Village banks experience seasonal liquidity shortages and surplus situations. Being seasonal they cannot be resolved through liquidity exchange within networks of village banks. Moreover village banks are unable to meet the demand for loans exceeding their own resources.

Recommendation: Once village banks are registered with BOL, seasonal liquidity mismatches as well as overall shortages or surpluses of liquidity of village banks may be resolved through bank linkages. The forum, under the leadership of BOL, may play a vital role in establishing a system of bank linkages:

- Examine the feasibility of bank linkages for liquidity management, depositing of surplus funds and refinancing
- Facilitate business relations of registered village banks with commercial banks.

6.2 Assessment of options

(1) Establishment of a stakeholder forum of communication in Vientiane Capital

Vientiane Capital has network organizations of village banks with evolving services covering all eight, and by the end of 2010 presumably all nine, districts, with a total of around 450 village banks, presumably more than 150 village banks with over 200 million Kip in savings. The network organizations together with their service providers have not been involved in the preparation and implementation of the regulation of June 2008. As a result the regulation does not adequately fit the needs of the village banks and has not met with a demand for registration and licensing by the village banks. We therefore propose the establishment of a stakeholder forum of communication in Vientiane Capital comprising the village bank network organizations and BOL together with LWU, local government and the service providers, supported by donor agencies. Through a participatory process the forum aims at the adjustment of the regulation to the needs and demands of village banks and their networks and at the facilitation of registration, licensing and effective supervision of village banks. The forum should examine all options presented below and initiate appropriate action.

(2) Village banking networks

Village banking networks, which have evolved in Vientiane Capital since 2003, are self-reliant organizations owned, managed and financed by the village banks in a given district. To-date they operate as informal organizations, Their functions are registration and reporting within the network, monitoring, guidance and supervision. We propose to donors to focus their support on the strengthening of the emerging networking structures as self-organized instruments of village banking development. Once legally registered and recognized as partners by BOL they may facilitate the promotion of a properly regulated and supervised system of village banks in Vientiane Capital.

(3) Registration of village banks as NDTMFIs

Village banks in Vientiane Capital are internally registered and monitored by their respective network organizations, which have evolved since 2003; to-date none is registered with BOL. As a first step we propose to the forum facilitating the registration of all village banks as NDTMFIs with BOL through their network organizations. The networks will also provide reporting and monitoring services as well as guidance and supervision, over and above stipulations by BOL for NDTMFIs. Special efforts should be made to establish an atmosphere of mutual learning and confidence building between the village banks and BOL, as a prerequisite of regulatory adaptations on the part of BOL and a positive attitude to the advantages of an adapted regulation on the part of the village banks.

The forum may also examine the feasibility of registering the network organizations as NDTMFIs comprising village banks as members. However, this would lead the networks in a different direction as they have not been designed as financial institutions, and their financial activities would have to be newly developed. This might also create a conflict of interest of the guidance and supervision functions of the networks with their any new financial operations. This is not recommended.

(4) Licensing of village banks as SCUs

Both village banks and SCUs share a common philosophy, being member-owned and member-controlled. However, the regulatory framework for SCUs is designed for larger organizations, covering far more than a single village. We recommend to re-design the SCU regulation to fit small single-village MFIs (as has been historically the case in many countries of Europe), particularly with regard to minimum capital requirements. At present the village banks strongly object to major changes in their system and, for historical reasons, to the cooperative model. The forum and the networks could play a crucial role in the adaptation of the revised regulation and in the acceptance of a suitably adapted regulation by the village banks.

SCUs have a great potential in Laos, despite a negative historical experience with cooperatives. However we note that Laos has no design and strategy for building a self-reliant credit cooperative sector, and that it takes more than a regulatory framework. We therefore suggest to the communication forum and BOL establishing a task force to examine successful international cooperative experience in credit cooperative development, particularly in Vietnam, in order to develop an understanding of the complexity of the process of building a successful credit cooperative system. Vietnam is also a country which has overcome the negative image resulting from the collapse of the credit cooperative sector. The learning process may be backed by cooperative development organizations such as DGRV, Rabobank Foundation and DID, all three involved in either Laos or Vietnam or both.

The forum may also examine the feasibility of registering the network organizations as SCUs. However, as indicated above, this would turn them into financial institutions, which they are not intended to be. There is also no valid reason for establishing large institutions which would incur substantially higher administrative costs and possibly make losses, while the existing village based institutions are very cost-effective and profitable. The village banks prefer single-village MFIs – we have no reason to disagree.

(5) Licensing of village banks as DTMFIs

There is a fundamental incompatibility of the DTMFI and the village banking model as it evolved in Vientiane Capital: DTMFIs are owned and governed by private investors according to their share capital, driven by the profit motive; village banks are democratic institutions which are saver-driven, member-controlled and community-governed. This incompatibility would also pertain to DTMFIs as a legal form for networks, which are not designed as financial institutions. By legal definition DTMFIs are large institutions, with a minimum capital of 1 billion Kip – far beyond the capacity of village banks. DTMFIs extend their outreach to a large area, incurring high transaction costs; they cannot subsist in a single village. DTMFIs may be attractive for private investors (if they succeed in turning a profit), but not for village banks or their networks.

(6) Delegated supervision implemented by village banking networks

Networks of village banks in Vientiane Capital are self-organized supervisory agencies with evolving services to their member institutions. As BOL does not have the capacity of effectively supervising large numbers of small institutions, we propose to BOL establishing a system of delegated supervision, building on the existing networking foundation and strengthening them as effective supervisors under the ultimate authority of BOL. With support from donor agencies with experience in delegated supervision, pilot-testing may start in Saithany District, which has the largest village banks and the strongest network.

(7) Village banks as facilitators of access to bank loans

Village banks have a limited capacity of extending larger-scale loans to small and medium enterprises of their members. Capitalizing on the track record of members with a demand for larger loans, district networks of village banks under the guidance of the stakeholder forum may organize a referral system by which village banks refer members to banks for larger loans.

(8) Bank linkages for liquidity management and refinancing

Village banks experience seasonal liquidity shortages and surplus situations which cannot be resolved through liquidity exchange within networks. They also are not able to respond to the demand for loans which exceed their own resources. The stakeholder forum, under the leadership of BOL, may examine the feasibility of bank linkages and, in due course, facilitate business relations of registered village banks with commercial banks.

7. Roadmap for village banks in Vientiane Capital in the next years

Based on the analysis in chapters 2-5 and the discussion of options in chapter 6 we propose the following steps and strategies.

A. Establishment of a stakeholder forum of communication in Vientiane Capital

As a first step a forum should be established at the level of the municipality, comprising the district networks of village banks, BOL, local government and LWU together with service providers and donor agencies involved in the development of village banks and their networks. The forum aims at the initiation of a communication process of BOL with the main actors of village bank development, particularly the district networks of village banks as their evolving representative bodies, and the initiation of a participatory process geared at three main tasks:

- adjusting the microfinance regulation to the reality of some 450 village banks in Vientiane Capital,
- bringing them under the regulatory framework of BOL ,and
- establishing a system of effective guidance and supervision capable of coping with large numbers of small village-based institutions. The forum should be governed by an executive committee and managed by a secretariat, assisted by task force groups as seen fit.

B. Strengthening the district village banking networks

The emerging district village banking networks are designed as self-reliant and sustainable self-help organizations of the village banks. They have a crucial role to play in the development of the village banks and their interaction with BOL, but this requires further strengthening. Support should focus on capacity building of the zonal and district committees and the district center management and their ability to carry out or promote the core functions of the networks: registration of village banks within the network, reporting, monitoring, guidance and supervision. In due course support might also include the establishment of special services or subsidiaries for training, liquidity exchange & refinancing, and auditing – either at the level of districts or Vientiane Capital. Efforts should be made to have the networks legally registered and recognized by BOL as facilitators of a process aiming at a properly regulated and supervised system of village banks. Piloting may start in Saithany District.

Capacity building may also include the establishment of a federation of district networks at the level of Vientiane Capital as an interest organization of all village banks in the municipality and as an active participant in the revision of the regulatory framework for village banks.

C. Registration of all village banks in Vientiane Capital with BOL as NDTMFIs

Under guidance of the forum the district networks should be enabled to facilitate the registration as all village banks as NDTMFIs – as an initial step prior to licensing. Besides registration the networks will also provide monitoring and guidance services. By the time the registration process starts the regulation for NDTMFIs should have been revised through a participatory process involving the district networks of village banks. The term *Non-deposit Taking MFI* should be revised, indicating that all village banks mobilize deposits.

The forum may also examine the feasibility of registering network organizations as NDTMFIs, realizing however that the networks have not been designed as financial institutions. Should networks decide to carry out financial functions (eg, liquidity exchange), these should be placed in a subsidiary.

D. Licensing of village banks

Once the regulation has been adjusted to the reality of savings-based single-village institutions and an atmosphere of communication and trust has been established between the village banks and BOL, the process of licensing village banks as SCUs may be initiated. Guided by the forum the capacity of the networks should be built to act as facilitators in the adjustment of the village banks to the revised regulation and in the implementation of the process of registration as SCUs. A major challenge for the networks as well as for BOL is the resistance of the village banks against cooperatives, partly for historical reasons related to the collapse of the credit cooperative system under the former command economy, partly out of fear of imposition of an unwanted (though as yet unfamiliar) model. The forum may also examine the feasibility of registering network organizations as SCUs, realizing however, as noted above, that the networks have been designed as associations, not funds or financial institutions.

Building a self-reliant credit cooperative sector in Laos goes beyond providing a regulatory framework and registering village banks as SCUs. To-date Laos has no design and strategy for building such a sector into which village banks as regulated SCUs could be integrated. In this context the forum may initiate an exposure program in Vietnam aiming at an understanding of the complexity of the process of building a successful credit cooperative system. The learning process may be backed by international cooperative development organizations such as DGRV, Rabobank Foundation and DID.

DTMFI is not a suitable legal form for village banks (nor for their networks) and should be ruled out. This is due to a fundamental incompatibility between MFI owned and governed by private investors and village banks as democratic institutions which are member-owned and community-governed.

E. Establishing a system of delegated supervision through village bank networks

BOL does not have the capacity of effectively supervising large numbers of small MFIs. Once village banking networks are fully functioning, village banks are registered and the process of licensing has started, a system of delegated supervision may be installed. Guided by the forum the capacity of the district networks and their yet-to-be-established specialized auditing services should be built to supervise the village banks on behalf of BOL. Support may be provided by donors with experience in delegated supervision. Piloting may start in Saithany District.

F. Establishing relations with commercial banks

Village banks may serve as facilitators of access to bank loans for members with a demand for larger-scale small- and medium-enterprise loans. District networks under the guidance of the forum may organize a referral system by which village banks refer members with a good track record to banks.

Bank linkages may be installed by village banks for liquidity management during seasonal liquidity surplus and shortage periods and for refinancing.

G. Ancillary activities

The Microfinance Working Group, a successor to the Microfinance Roundtable of the 1990s, needs to be revitalized as an informal gathering for the exchange of information and coordination of interventions in the microfinance sector at national level. To assure continuity one of the major donor agencies working with BOL should act as lead agency providing the chair.[45]

Policy seminars under the auspices of BOL should be supported by a secretariat or a secretary-general to assure the implementation of action plans as a follow-up of the results of the seminars. The feasibility of an organizational affiliation between the Microfinance Working Group and the proposed secretariat of the policy seminars, both with a national outlook, and their relationship with the proposed Stakeholder Forum of Communication of Vientiane Capital should be examined. An appropriate structure of coordination and cooperation should be installed as seen fit.

[45] It appears that an initiative of reviving the Working Group is under preparation as of January 2010.

References

BOL, APRACA & GTZ, 1997: National Consultation-Workshop on the Promotion of Rural and Microfinance in the Lao PDR, Vientiane, March 1997

Christen, Robert Peck, & Richard Rosenberg, 2000: The Rush to Regulate: Legal Frameworks for Microfinance. CGAP Occasional Paper No. 4

GTZ, 2008: Enterprise Survey 2007. Vientiane, Lao-German Resource Development for Market Economy Programme (HRDME), Vientiane [Finance: pp.109-113]

Hogenhout, Timo, & Daniel Taras, 2008: Village Banking in the Lao PDR. Vientiane & Eschborn, GTZ

Hulme, David, 2008: The Story of the Grameen Bank: From Subsidised Microcredit to Market-based Microfinance. Brooks World Poverty Institute Working Paper 60, www.manchester.ac.uk/bwpi

ILO, 2008: Village Banking in Lao PDR: Handbook for Village Bank Management Committees and Support Organizations (by Linda Deelen & Eva Majurin). Bangkok, Subregional Office for East Asia

ILO, 2008: Village Banking in Lao PDR: Ledger Guide. (by Linda Deelen & Eva Majurin). Bangkok, Subregional Office for East Asia

Khanthone Phamuang, 2010: Report on Village Savings and Credit Groups in Saithany District, Vientiane Capital. Vientiane

Kunkel, Carmen R., & Hans Dieter Seibel, 1997: Microfinance in Laos. APRACA-GTZ Publication 1997/1. Bangkok, APRACA

Seibel, Hans Dieter, 2003: History Matters in Microfinance. Small Enterprise Development 14/2: 10-12; www.uni-koeln.de/ew-fak/aef Working Paper 2003-5

–, 2009: Restructuring of State-owned Financial Institutions: Lessons from Bank Rakyat Indonesia. Manila, Asian Development Bank, www.adb.org

–, 2010: The People's Credit Funds of Vietnam: A Prudentially Regulated Credit Cooperative Movement. Enterprise Development & Microfinance vol. 21 (in press)

–, & Carmen R. Kunkel, 1999: Microfinance in Laos: A Case of Women's Banking? University of Cologne, www.uni-koeln.de/ew-fak/aef, Working Paper 1999-3

– , & Dolores Torres, 1999: Are Grameen Replications Sustainable, and Do They Reach the Poor? The Case of CARD Rural Bank in the Philippines. Journal of Microfinance 1/1:117-130

UNDP/CDF, 1996: LAO PDR Microfinance Profile: A Working Document for Discussion. Vientiane, UNDP

VWU/TYM – Vietnam Women's Union (TYM Fund) in cooperation with Lao Women's Union, 2009: Research Report on the Demand for Microfinance Services, Borikhamxay Province, Lao PDR

Annex 1: Persons met

ADB – Asian Development Bank 021 250444

Hammerich Ursula, Project coordinator, Catalyzing Microfinance for the Poor
020 5502377 uhammerich@maxwellstamp.com
Phantouleth Louangraj, Economics officer, 21 250 333 plouangraj@adb.org
Soulinthone Leuangkhamsing, Economics officer 21 250 333
sleuangkhamsing@adb.org
Jon_Wynne-Williams@coffey.com (ADB consultant to BOL, *not met*)

BOL - Bank of The Lao P.D.R.,
Bank and Financial Institution Supervision Department 021 264486

Phouthaxay Sivilay, Acting Director 020 5725730
Ms. Keasorn Manivong, Head of Microfinance Institution Division 020 5655753
Kesone88@yahoo.com

Consultants:

Behrle Sebastian, Rural and Microfinance Consultant 020 6994010

DGRV 021 261 895

Von Walther Hildegard 020 433 7430 von.walther-dgrv.laos@gmx.net

GTZ 021 353605

Artjom Wolf, RDMA artjom.wolf@gtz.de
Bandith Sisoukda, RDMA bandith.sisoukda@gtz.de

Prochaska Klaus, Access to Finance Program 020 5527526 klaus.prochaska@gtz.de
Schultze, Michael, HRDME michael.schultze@gtz.de

ILO SME Promotion and Development Office 021 450318

Mme. Phetphim Champasith, National project coordinator 020 5696906

LWU – Lao Women's Union

Mme Onesy Sengmuang, Deputy Director General, Development Department
020 9801262
Mme Kaysamy Latuslayvong, Chief, Development Division 5685350

MFC – Microfinance Center 021 262917 www.mfclao.com

Somphone Sisenglath, Director 020 5513895 somphone.s@mfclao.com

Microfinance institutions

Deposit-taking MFIs:
EMI – Ekphatana Microfinance Institution:
Somphone Sisenglath, Director 020 5513895
Chantha Mingboupha, Deputy Director 020 5509588 chanthabp@yahoo.com

Savings and Credit Unions:
Rural Development Cooperative, Nusaythong District:
Somchith Bounleum 020 551 3278

Village Savings & Credit Groups/Funds:
Phaksapkau VSCG:
Management and advisory committee members, members
Thongmang VSCG:
Management and advisory committee members, members

SBFIC

Hogenhout Timo H., Microfinance consultant 020 7845133 timo@zzphogenhout.nl
Field study team:
Khanthone Phamuang, Survey team leader 020 5527559 cdealaos@yahoo.com
Khamphone Keophoxay, Translator 2286572 kkeophoxay@yahoo.com
Interviewers

Women and Family Development Fund (WFDF):
Werthenbach Bernd, Country representative & WFDF project director 020 7493865 bernd.werthenbach@sbfic.de
Mme. Khonevilay Sengsourinha, Director WFDF
Kheungthong Vongsaya, WFDF operations manager

Annex 2:

Lao People's Democratic Republic: Country Economic Indicators (2005–2009)

(Percentage of GDP, unless otherwise indicated)

Item	Fiscal Year				
	2005	2006	2007	2008	2009 Projected
A. Income and Growth					
1. GDP per Capita ($, current)	492.4	568.3	672.6	840.0	866.0
2. GDP Growth (%, in constant prices)	7.1	8.1	7.9	7.2	5.5
a. Agriculture	2.5	3.5	6.2	2.0	2.5
b. Industry	15.9	21.5	6.5	10.0	8.0
c. Service	6.7	5.3	12.1	9.7	5.0
B. Saving and Investment (current and market price, % of GDP)					
1. Gross Domestic Investment	30.2	31.1	39.7	37.1	35.2
2. Gross National Saving	11.7	20.3	21.9	18.2	16.6
C. Money and Inflation (annual % change)					
1. Consumer Price Index	7.2	6.8	4.5	7.6	0.7
2. Total Liquidity (M2)	8.1	17.2	38.7	18.3	23.0
D. Government Finance (% of GDP)[a]					
1. Revenue and Grants	13.2	14.6	15.8	17.8	13.4
2. Expenditure and Onlending	17.6	18.4	18.6	20.9	18.4
3. Overall Fiscal Surplus (Deficit)	(4.4)	(3.8)	(2.9)	(3.1)	(5.0)
E. Balance of Payment					
1. Merchandise Trade Balance (% of GDP)	(19.0)	(12.8)	(20.0)	(21.9)	(20.0)
2. Current Account Balance (% of GDP)	(16.9)	(10.3)	(16.2)	(17.3)	(14.6)
3. Merchandise Export ($) Growth (annual % change)	30.1	62.6	16.6	24.1	(21.0)
4. Merchandise Import ($) Growth (annual % change)	20.3	25.1	35.7	30.6	(13.5)
F. External Payments Indicators					
1. Gross Official Reserves (including gold, $million by month of current year's imports of goods)	2.8	3.2	3.9	3.4	3.5
2. External Debt Service (% of exports of goods and services)	8.1	5.7	12.5	10.3	11.1
3. Total External debt (% of GDP)	77.1	63.1	59.1	53.1	54.5
G. Memorandum Items					
1. GDP (current prices, kip billion)	29,663.0	35,983.0	40,858.0	46,700.0	49,269.0
2. Exchange Rate (kip/$, average)	10,642.0	10,415.0	9,694.0	8,707.0	8,550.0
3. Population (million)	5.7	5.8	5.9	5.9	6.0

( ) = negative, GDP = gross domestic product.
[a] Based on fiscal year (October to September).
Source: Asian Development Outlook, IMF Article IV Consultation, Department of Statistics, Bank of Laos and Ministry of Finance.

Annex 3: Microfinance regulation: Summaries and overviews

3.1 Non-Deposit Taking Microfinance Institutions (NDTMFIs)

Summary

Requirement to register	Any and all microfinance activities by groups, individuals or legal entities
Required registrations	With BOL and relevant government authorities
Resource mobilization	Compulsory and voluntary deposits of members Loans or grants from Lao and foreign entities
Regulation	• Micro-loans only, not exceeding 10m Kip • Voluntary deposits not exceeding 200m Kip in aggregate and 10m Kip per depositor unless authorized by BOL • Quarterly review of all loans, provisioning as prescribed • Annual reporting to BOL
Requirement of conversion to a prudentially regulated MFI	Voluntary deposits >200m Kip, or annual revenues >1 billion Kip

Non-Deposit Taking Microfinance Institutions regulation: overview

Regulation No. 02/BOL	***20/06/2008 (EN)***
3. Requirement to register	Any organization, group or enterprise that carries out microfinance activities, including village banks, savings groups, village funds, development funds and others
4-5. Required registrations	Certification of registration from BOL Registration with the relevant government authorities
10. Registration fee	200,000 Kip
13./14.d. Capital	No minimum capital requirement Loans or grants from LAO PDR. foreign organizations and other legal entities subject to approval of BOL
14.. Financial services to members only	Micro-loans up to 10m Kip, compulsory deposits, voluntary deposits not exceeding 200m Kip in aggregate and 10m Kip per depositor unless authorized by BOL
14.Other financial activities	Mobilizing loans or grants from Lao and foreign entities Deposit funds with BOL or commercial banks
16. Loan classification and provisioning	Quarterly review of all loans. Provisioning: Overdue 30-90 days: 25% Overdue 31-180 days: 50% Overdue >180 days: 100%
18. Accounting and reporting	Chart of accounts provided by BOL Annual reporting (balance sheet, income statement, loan portfolio report, loan classification report)
20. Requirement of conversion to a prudentially regulated MFI)	Voluntary deposits >200m Kip, or annual revenues >1 billion Kip
75. Implementation: Compliance requirements	Any state, provincial, district, village level or group organization, individual, international or private organization or enterprise which are currently carrying out Microfinance or similar activities or is planning to do so is required to within a period of 12 months from the effective date of this Regulation to comply with the requirements as stipulated in this Regulation Penalties for non-compliance: 100,000 Kip per day.
76. Effectiveness	Replacing Regulation No. 10/BOL, effective as from the date of its signature

Source: www.bol.gov.la/english/microfinanceeng.html; http://www.bol.gov.la/english/mf_reg02eng.pdf

3.2 Savings and Credit Unions (SCUs)

Summary

Requirement of conversion to a regulated MFI (DTMFI or SCU)	Voluntary deposits >200m Kip, or annual revenues >1 billion Kip
Location and outreach	National, members only
Establishment requirements	10 founding members and 100 initial members; or 250 members and voluntary deposits of 300m Kip
Voting rights	One member one vote
Resource mobilization	Member deposits, loans or grants from Lao and foreign entities
Prudential regulation:	• Minimum registered capital 100m Kip • Provisioning for loans overdue >30, >90, <180 days; 1% on performing loans • Maximum NPL ratio: 5% of loans outstanding • Write-offs: loans overdue >180 days • CAR 12% (risk-weighted) • Liquidity ratios: cash in hand 4%; overall 20%
Auditing and supervision	Internal and external auditing, supervision by BOL Quarterly and annual reporting
Penalties for non-compliance	100,000 Kip per day to SCUs incl. managers or employees Suspension and cancellation of license
Interest rate restrictions	None

Savings and Credit Union (SCU) regulation: overview

Regulation No. 03/BOL	***03/06/2008 (EN)***
Requirement of conversion to a regulated MFI (DTMFI or SCU)	Voluntary deposits >200m Kip, or annual revenues >1 billion Kip (*NDTMFI regulation Art. 20*)
1. Terms: Microloans Capital: Compulsory deposit:	Up to 10m Kip Initial capital, regulatory reserves, grants and retained earnings Condition for receiving a loan, a percentage or nominal amount
3. Legal status	Financial cooperative licensed by BOL
4. Location	Allowed to open a head office, branches or service units in the entire country. subject to the prior approval of BOL
5. Establishment requirements	• Either 10 founder members and 100 initial members who pay the minimum share; • or 250 members and voluntary deposits of 300m Kip. • Minimum registered capital: 100m Kip • No individual with its relatives is allowed to own more than 10% of the initial capital • BOL checks educational background and experience in finance, banking, accounting, auditing and management
14. Licensing fees	Application fee: 500,000 Kip Issuance fee if registered capital is:: >100m up to 300m: 1m Kip >3m 1.5m Kip
15. Annual supervision fee	500,000 Kip
17. Minimum initial capital	100m; maximum share size 100,000 Kip
19. Depositor protection	Member of the Depositors' Protection Fund (fee based on total deposits)
21. Organisation	General assembly of members as the highest body, board of directors (5), audit committee (3), credit committee (5), manager
23. Resolutions of the general assembly	One member one vote cast by secret ballot
37. Financial services to members only	Loans, voluntary and compulsory deposits, payment and transfer services within the country, insurance as a broker
37. Other financial activities	Mobilize capital in the form of loans or grants (*not equity!*) from Lao PDR and foreign organizations or legal entities

	Deposit funds with any commercial banks
38. Restrictions	Leasing; dealing in precious metals or commodities, real estate and derivatives; payment services through checking accounts; foreign exchange…
44. Credit to related parties	Loans outstanding to related parties shall not exceed 5% of capital to each related party and 25% in the aggregate
45. Loan classification and provisioning	Performing loans: 1% Overdue 30-90 days: 25% Overdue 31-180 days: 50% Overdue >180 days: 100% NPL limit 5% of loans outstanding
48 Write-offs	Loans overdue >180 days
49. CAR (risk-weighted)	12%
50. Liquidity ratios	Cash in hand 4%.; overall 20%
54. Regulatory reserve	5% of net profit up to 20% of registered capital
56. Taxation	Taxable according to the prevailing tax law
57. Auditing	Internal audits by internal auditor or audit committee External audits by external auditors and examination by BOL
58. Accounting and reporting	Accounting system and chart of accounts by BOL *Quarterly reporting:* Balance sheet Income statement Loan and deposit report Loan classification report *Annual reporting:* 6 additional reports
72. Penalties for non-compliance	100,000 Kip per day to SCUs incl. managers or employees Temporary suspension and cancellation of licence
75. Implementation	Any state, provincial, district, village level or group organization, individual, international or private organization or enterprise which are currently carrying out Microfinance or similar activities or is planning to do so is required to within a period 12 months from the effective date of this Regulation to comply with the requirements as stipulated in this Regulation Penalties for non-compliance: 100,000 Kip per day
76. Effectiveness	Replacing Regulation on Cooperatives Number 02/BOL dated 19/11/94 and Regulation on Pilot SCUs Number 256/BFSD dated 12/05/04, effective as from the date of its signature

Source: http://www.bol.gov.la/english/mf_reg03eng.pdf; www.bol.gov.la/english/microfinanceeng.html

3.3 Deposit-taking Microfinance Institutions (DTMFIs)

Summary

Requirement of conversion to a regulated MFI (DTMFI or SCU)	Voluntary deposits >200m Kip, or annual revenues >1 billion Kip
Legal status	Financial institution incorporated as a limited company under the enterprise law
Location and outreach	National
Establishment requirements	5 shareholders, 1 major shareholder Five-year business plan
Voting rights	One share one vote, resoluations by simple majority of shares
Resource mobilization	Member deposits, loans or grants from Lao and foreign entities
Prudential regulation:	• Minimum registered capital 1bn Kip, divided into shares • Voluntary deposits not exceeding 10 times the capital • Single-borrower limit 10% of capital • Microloans at least 80% of loan portfolio • Provisioning for loans overdue >30, >90, <180 days; 5% on performing loans • Maximum NPL ratio: 5% of loans outstanding • Write-offs: loans overdue >180 days • CAR 12% (risk-weighted) • Liquidity ratios: cash in hand 4%; overall 20% • Investments up to 10% of reg'd capital, restricted to MFIs
Auditing and supervision	Internal and external auditing, supervision by BOL Monthly, quarterly and annual reporting
Penalties for non-compliance	100,000 Kip per day to SR-MFIs incl. managers or employees Suspension and cancellation of license
Interest rate restrictions	None

Deposit-taking MFI (DTMFI) regulation: overview

Regulation No. 04/BOL	***20/06/2008 (EN)***
Requirement of conversion to a regulated MFI (DTMFI or SCU)	Voluntary deposits >200m Kip, or annual revenues >1 billion Kip (*NDTMFI regulation Art. 20*)
1. Purposes of regulation	Safeguarding the financial system, protecting depositors
2. Terms: Microloans Major shareholder Capital: Compulsory deposit:	Up to 10m Kip Holding at least 20% of capital Initial capital, regulatory reserves, grants and retained earnings Condition for receiving a loan, a percentage or nominal amount
3. Legal status	Financial institution incorporated as a limited company under the enterprise law
4. Location	Allowed to open a head office, branches or service units in the entire country. subject to the prior approval of BOL
5/6. Establishment requirements	• Minimum of 5 shareholders: individuals, partnerships, sole proprietorships, companies under Lao PDR law • One major shareholder with experience in banking and microfinance • Minimum registered capital: 1 billion Kip • Five-year business plan demonstrating sustainablity • BOL checks educational background and experience in finance, banking, accounting, auditing and management of board of directors, managaging directors. major shareholder
13. Licensing terms	Payment of registered capital in full Application fee: 1m Kip Issuance fee if registered capital is: 1-3bn: 10m Kip >3bn 15m Kip
14. Annual supervision fee	0.05% of average assets, minimum of 0.5% of registered capital

16. Minimum registered capital	1 billion Kip, divided into shares with equal value
19. Depositor protection	Member of the Depositors' Protection Fund (fee based on total deposits)
21. Organisation	General assembly of shareholders as the highest body, board of directors incl. the chairman (5-10), audit committee (at least 3), managing director (34. May not also be the board chairman)
23. Resolutions of gen. assembly	One share one vote, resolutions by simple majority of shares
29. Meetings of board of directors	Monthly meetings, quorum of two-thirds of total members
35. Financial activities	Microloans in Kip, other loans not exceeding 20% of total loans, hard currency loans with approval of BOL, voluntary and comp. deposits in Kip, hard currency deposits with approval of BOL, payment and transfer services within the country, insurance as an agent, selling shares or bonds to the general public Determining deposit and loan interest rates acc to the market mechanism and regulation by BOL Lloans and grants (*not equity!*) from Lao PDR and, with approval of BOL, from foreign organizations Depositing funds with BOL or domestic commercial banks
36. Restrictions	Leasing; dealing in precious metals or commodities, real estate and derivatives; payment services through checking accounts; foreign exchange…
38. Fund mobilization restrictions	Voluntary deposits not exceeding ten times the capital Total borrowings not exceeding 30% of loans outstanding
39/41. Credit restrictions	Single borrower limit 10% of capital Microloans at least 80% of loan portfolio BOD, managing director, deputy managers, credit officers
43. Loan classification and provisioning	Performing loans: 5% Overdue 30-90 days: 25% Overdue 31-180 days: 50% Overdue >180 days: 100% NPL limit 5% of loans outstanding
46 Write-offs	Loans overdue >180 days
47. CAR (risk-weighted)	12%
48. Liquidity ratios	Cash in hand 4%; overall 20%
50. Investments	Not exceeding 10% of registered capital, restricted to MFIs
53. Regulatory reserve	5% of net profit up to 20% of registered capital
55. Taxation	Taxable according to the prevailing tax law
56. Auditing	Internal audits by audit committee External audits by external auditors and examination by BOL
57. Accounting and reporting	Accounting system and chart of accounts by BOL *Monthly reporting:* Balance sheet Income statement Loan and deposit report Loan classification report *Annual reporting:* 6 additional reports
71. Penalties for non-compliance	100,000 Kip per day to DTMFIs incl. managers or employees Temporary suspension and cancellation of licence
75. Implementation	Any state, provincial, district, village level or group organization, individual, international or private organization or enterprise which are currently carrying out Microfinance or similar activities or is planning to do so is required to within a period of 12 months from the effective date of this Regulation to comply with the requirements as stipulated in this Regulation Penalties for non-compliance:100,000 Kip per day
76. Effectiveness	Replacing Regulation Number 10/BOL dated 22/06/05, effective as from the date of its signature

Source: www.bol.gov.la/english/microfinanceeng.html; www.bol.gov.la/english/mf_reg04eng.pdf

Annex 4: Village bank of Phaksapkau: Basic data and annual financial report, May 2008–April 2009 (amounts in million Kip)*

Basic data:	
Date of establishment	May 2000
Number of members/savers	315
Percent women	69%
Number of outstanding loans	152
Percent women	100%
Management committee members	6
Percent women	100%
Advisory committee members	100%
Percent women	17%
Balance sheet:	
Savings	464.69
Interest income	132.57
Reserve fund	8.00
Development fund	5.10
Membership fees from new members	0.08
Education fund	1.70
Fines	1.37
Total capital	**613.50**
Cash at hand	121.02
Loans to members outstanding	491.85
Investments in Center shares	0.10
Expenditures	0.52
Expenditures for small books	0.01
Total assets	**613.50**
Income and expenditure statement:	
Interest income	147.24
Fines (for late payment)	1.62
Membership fees from new members	0.09
Total income	148.95
Expenditure	0.52
Net profit	148.43
Without rounding:	148.42
Member savings	464.69
Profit allocation:	
Member dividends	103.89
Management committee	22.26
Advisory committee	7.42
Reserve fund	5.94
Development fund	5.94
Network services	2.97
Total	**148.42**
Profit in % of savings:	31.94
Dividends to members in % of savings:	22.36

* The items of the financial report are given in the order in which they appear in the books, except the last two items on profits and dividends in % of savings, which have been added. The village bank was established in May; according to their rules the annual report therefore covers the financial year May to April.