

The Microfinance Revolution

Volume 1: Sustainable Finance for the Poor

Volume 2: Lessons from Indonesia

Volume 3: The Emerging Industry

Marguerite S. Robinson

The World Bank, Washington, D.C.

Open Society Institute, New York

Contents

Foreword	Ira W. Lieberman	xxi
Introduction	Ali Wardhana	xxv
Preface		xxxiii
Acknowledgments		xliv
PART 3 COMMERCIAL MICROFINANCE IN INDONESIA		1
Overview		2
Chapter 8 An Introduction to Indonesia		18
The Javanese Wayang Shadow Theater		24
Indonesia's Environment, Demographics, Early History, and Struggle for Independence		25
The Sukarno Era, 1949–67		28
The Soeharto Era, 1967–98		30
The Javanese concept of power		33
Pancasila, the guiding principles of Indonesian government		33
The economy, 1966–96		34
The government, the military, and politics during the Soeharto period		40
Corruption and the growth of the conglomerates		45
Indonesia on its 50th birthday, 1995		46
The Indonesian Crisis and the Resignation of President Soeharto		47
The nature and extent of the crisis		48

The roots of the crisis	50
Indonesia in Transition	56
The economy and the financial system, 1998–99	57
Governance and politics, 1998–99	58
President Abdurrahman Wahid, 1999–2001	60
President Megawati Soekarnoputri	71
Democracy and the Messy State	76
Notes	78

Chapter 9 Rural Development and Rural Financial Institutions in Indonesia

	82
Geographic and Demographic Diversity	86
Rural Development	88
Varieties of agriculture	88
Cultivation on Java in the early 20 th century	89
The green revolution	90
Rural development during the Indonesian crisis	93
Developing Rural Financial Institutions	93
European background	95
The early Indonesian people's banks	96
Bank Perkreditan Rakyat (People's Credit Banks, or BPRs)	98
Rural Finance in the 1980s	99
Government Microfinance Initiatives in the 1990s	102
The 1992 Banking Law and BPRs	102
KUK and commercial banks	104
Levying corporations and wealthy individuals for funds for subsidized credit programs	105
“Left-behind” villages: INPRES Desa Tertinggal	105
Bank Indonesia, government ministries, and rural credit programs	106
Rural Finance in the 1990s	107
Developing the BPRs	109
Six examples of rural financial institutions and programs	115
Rural Financial Institutions in Indonesia in 2000:	
What Have We Learned?	136
Policies and politics	136
Financial intermediation	137
Rural financial institutions: public and private	138
Learning from experience	138
Stability	139
Notes	139

Chapter 10 Where the Microfinance Revolution Began: Bank Dagang Bali

	144
Bank Dagang Bali: Formative Elements	147
Oka family history	147
The Okas as informal commercial lenders	148
Bank Pasar Umum	149
Bank Dagang Bali: Development and Performance, 1970–96	150

Customer Relations, Organization, Products, and Services	155
Organization and management	156
Loan products	157
Savings products	157
Lotteries	158
Mobile savings teams	158
Public relations	159
Bank Dagang Bali's Savers	160
Low-income savers	161
Lower-middle- and middle-income savers	162
High-income savers	163
Notes	163

Chapter 11 How to Fail in Financing the Poor: Bank Rakyat Indonesia's Unit Desa System, 1970–83 **166**

Bank Rakyat Indonesia's History, 1895–1970	172
The Development of the Unit Desa System, 1970–83	175
BIMAS loans to rice farmers	180
Kredit Mini and Kredit Midi loans	184
Deposit mobilization in the unit desa system, 1970–83	186
Losses in the unit desa system, 1970–83	187
Why Did BIMAS Fail?	187
The program's goals were incompatible	188
BIMAS credit was tied to input packets	188
Other agencies selected BIMAS borrowers, but BRI had to collect the loans	189
BIMAS did not reach many poor rice farmers	189
Policies for loan forgiveness and rescheduling during crop failures were badly planned and encouraged corruption	190
BRI did not have the organization, human resources, or motivation to manage unit desas effectively	190
Successful agricultural credit programs require successful agriculture—but insecticides supplied in the BIMAS input packet caused severe crop destruction	191
Examples of BIMAS in Four Rice-growing Environments	194
Village G (East Java): BIMAS results in an ideal rice intensification environment	195
Village C (West Java): Most households benefit from rice intensification, but not necessarily from BIMAS	198
Village R (South Sulawesi): A village with large potential for rice intensification and low participation in BIMAS	200
Village P (South Sumatra): A village where nearly everything that could have been done wrong in BIMAS implementation was done wrong	202
Implications of BIMAS: Results in four villages	205
The End of the BIMAS Era	208
Notes	210

Chapter 12	Success in Microlending: The KUPeDES Credit Program, 1984–96	216
	Indonesia's Enabling Conditions	219
	Bank Rakyat Indonesia's New Approach to Microlending at the Unit Desas	221
	Implementing KUPeDES	221
	Microcredit: subsidized and commercial	222
	Perception Gaps among Policymakers, Bureaucrats, and Villagers	224
	Policymakers	225
	Bureaucrats	226
	Villagers	228
	The Transition from BIMAS to KUPeDES	229
	Policy issues	231
	Three crucial decisions	232
	Cutting back on credit subsidies	233
	Starting the KUPeDES credit program	234
	Basic Principles of KUPeDES	235
	KUPeDES and unit desa reorganization	237
	Selecting KUPeDES borrowers	238
	Characteristics of the KUPeDES Loan Product	239
	Loan purposes	239
	Loan sizes	240
	Interest rates	240
	Loan terms	241
	Implementation of the KUPeDES Credit Program	244
	From application to collection	244
	Measuring and managing delinquency	245
	Outreach	246
	KUPeDES Performance, 1984–96	252
	Outreach and repayment history	254
	Geographic coverage	255
	Unit desa profitability	256
	Notes	258
Chapter 13	Mobilizing Massive Savings: Bank Rakyat Indonesia's Unit Desas, 1984–96	262
	Why Did BRI Emphasize Savings in Its Unit Desas?	265
	To finance the demand for credit and enable institutional sustainability	265
	To limit government risk	267
	To encourage rural savings mobilization	267
	Developing and Testing the New Savings Program	267
	Early field research	268
	The planning stage	269
	The first SIMPEDES pilot project	270
	The second-stage SIMPEDES pilot project	276
	Expansion and Market Penetration of the New Savings Program	279
	Preparing to expand the savings program, January–March 1986	280

Expanding the savings program to all unit desas, April–September 1986	291
Learning market penetration, 1987–89	293
Unit Desa Savings Products, 1996	296
SIMPEDES and SIMASKOT	297
TABANAS	297
Deposito Berjangka and giro accounts	298
The interest rate structure	298
Cost of funds	299
Lotteries	299
The transfer price	300
Performance in Savings Mobilization, 1984–96	301
Performance by instrument	302
Notes	304

Chapter 14 Institutional Development for Large-Scale Sustainable Microfinance: The Transformation of the Unit Desas, 1984–96 **306**

Old and New Cultures	309
Restructuring the Unit Desas: The Transition Process	311
From branch windows to profit centers	312
Changes in organization and management	313
Unit desa location	316
Marketing and public relations	319
Learning from mistakes	321
Organization and Management of the Unit Desas, 1996	322
At the head office	323
At the regional offices	327
At the branches	327
At the unit desas	328
At the village posts	331
The unit desa system and other bank divisions	331
Reporting Unit Desa Performance at the Unit, Branch, and Regional Levels	332
The unit development reports of two unit desas	333
The aggregated unit development reports of two branches	335
Unit performance in two regional offices	335
Staff Incentives and Training	337
Incentives	337
Training	339
Retention	342
Bank Rakyat Indonesia: Microfinance Outside the Unit Desa System	343
The Badan Kredit Desa	343
Pembinaan Peningkatan Pendapatan Petani–Nelayan Kecil	347
Microfinance at BRI's branches: comparing the BKDs and P4K	350
Microbanking in a Division of a Multipurpose Commercial Bank:	
Structural Issues	352
External dangers to sustainable microfinance	354

Internal dangers to sustainable microfinance	355
Why Do Structural Issues Matter?	359
Notes	362
Chapter 15 Commercial Microfinance in Indonesia: Stability in Crisis, 1997–98	364
Indonesia's Financial Crisis	369
The collapse of the banking system	373
Bank reforms and corporate debt restructuring	375
Challenges ahead	380
The Stability of Microbanking during the Crisis	382
The Badan Kredit Desa, 1997–98	382
Bank Dagang Bali, 1996–2000	384
BRI's unit desa system, 1996–2000	388
The unit desas at the start of the 21st century	396
Commercial Microfinance in Indonesia: What Has Been Learned?	402
Commercial microfinance can be both economically and socially profitable	403
Stability in crisis	403
Notes	407
Appendix Rupiah–U.S. Dollar Exchange Rates, Consumer Prices, and Performance of Bank Rakyat Indonesia's Unit Desa System, December 1996–December 2000	410
Table of Contents for <i>The Microfinance Revolution, Volume 1: Sustainable Finance for the Poor</i>	414
Glossary and Acronyms	421
Bibliography	433
Index	451
Tables	
8.1 Economic indicators for Indonesia, 1996–2000	35
9.1 Outstanding loans in Indonesia's financial system, 1985	100
9.2 Loans and savings in Indonesia's financial system, 1995	108
9.3 BPRs and BRI unit desas: number of units and clients, September 1998	110
9.4 BPRs and BRI unit desas: average loans and deposits, 1997	111
9.5 Loans and savings in five rural financial institutions and the PHBK program	116
9.6 Estimated earnings adjusted for subsidies and bad debt for 34 original BKKs/SK and 3 LKPs of Nusa Tenggara Barat, 1995	121
9.7 Viability indicators for Bank Shinta Daya and Mitra Karya, 1995	129

9.8	Estimated subsidy dependence index and required interest rates to cover the program costs of the PHBK program, fiscal 1991–96	135
10.1	Bank Dagang Bali profit and loss statement, 1970–96	151
10.2	Bank Dagang Bali balance sheet, 1970–96	152
10.3	Bank Dagang Bali outstanding loans, 1970–96	152
10.4	Bank Dagang Bali savings, 1970–96	153
10.5	Size distribution of Bank Dagang Bali loans and savings, 1996	154
11.1	Features of BIMAS and Kredit Mini	185
11.2	Household borrowing in three Indonesian villages by source of the largest loan, 1980–81	195
11.3	BIMAS participation in four Indonesian villages, 1980–81	196
11.4	Evaluation of BIMAS in four Indonesian villages	206
12.1	A comparison of BIMAS and KUPEDES	220
12.2	Size distribution of KUPEDES loans at disbursement, 1995	241
12.3	Excerpts from responses to KUPEDES borrower survey, 1996	249
12.4	Number and value of KUPEDES loans, 1984–96	253
12.5	Loss ratios for KUPEDES loans, 1984–96	253
12.6	Geographic distribution of KUPEDES outstanding loans and unit desa deposits, 1996	255
12.7	Unit desa profits and losses, 1984–96	256
13.1	Unit desa savings in the Sukabumi pilot project, 31 October–31 December 1984	274
13.2	The most important characteristic of SIMPEDES: responses of 144 SIMPEDES savers in the Sukabumi pilot project, January–February 1985	275
13.3	Savings mobilization in the second stage of the SIMPEDES pilot project, June–December 1985	277
13.4	The most important characteristic of SIMPEDES: responses of 76 SIMPEDES savers in the 12 new branches of the second-stage pilot project, September 1985	278
13.5	“Would you still save in SIMPEDES if the annual interest rate were 6 percent?”: responses of 74 SIMPEDES savers in the 12 new branches of the second-stage pilot project, September 1985	279
13.6	Annual interest rates for unit desa savings instruments, September 1996	297
13.7	Estimated cost of savings mobilization in the unit desa system, 1996	299
13.8	Value of savings accounts by account type in the unit desas, 1984–96	302
13.9	Number of savings accounts by account type in the unit desas, 1984–96	303
14.1	Employment in the unit desa system by organizational level, 1996	325
14.2	Unit development reports of two unit desas, December 1996	334
14.3	Aggregated unit development reports of two branches, 1995–96	336

14.4	Performance indicators for the unit desas of two regional offices, 1995–96	337
14.5	Curriculum of training centers for unit desa staff, 1996	340
14.6	Curriculum of training centers for unit desa branch supervisors, 1996	341
14.7	Performance of the Badan Kredit Desa, 1992–96	345
14.8	Indicators of financial self-sustainability for the unit desas, 1985, 1990, and 1995	360
15.1	Performance indicators for the Badan Kredit Desa (BKD), 1996 to August 1998	383
15.2	Bank Dagang Bali profit and loss statement, 1996–2000	385
15.3	Bank Dagang Bali balance sheet, 1996–2000	386
15.4	Bank Dagang Bali savings, 1996, 1998, and 2000	387
15.5	Bank Dagang Bali outstanding loans, 1996, 1998, and 2000	387
15.6	Unit desa savings and lending, 1996–2000	388
15.7	Unit desa pretax profits and returns on assets, 1996–2000	388
15.8	Value of unit desa savings by account type, 1996–2000	392
15.9	Number of unit desa savings accounts by account type, 1996–2000	392

Figures

11.1	Main reasons for the failure of the BIMAS credit program for rice farmers	170
11.2	Default rates for BIMAS rice cultivation loans, 1970–84	182
11.3	Amount of outstanding BIMAS rice cultivation loans, 1970–84	182
11.4	Number of outstanding BIMAS rice cultivation loans, 1970–84	183
11.5	Area covered under BIMAS rice cultivation loans, 1970–84	183
12.1	The evolution of microcredit at Bank Rakyat Indonesia, 1970–96	223
13.1	The evolution of microsavings in the unit desas, 1984–96	264
14.1	Restructuring unit desa organization and management	310
14.2	Number of unit desas, 1983–96	318
14.3	Bank Rakyat Indonesia's organizational structure, 1996	323
14.4	Government administrative levels and Bank Rakyat Indonesia's organizational levels, 1996	324
14.5	Organizational structure of the Business Unit Desa Division at Bank Rakyat Indonesia's head office, 1996	325
14.6	Organizational structure of a unit desa and its supervising branch, 1996	329
15.1	Exchange rates in Indonesia, December 1996–December 2000	371
15.2	Consumer price index in Indonesia, December 1996–December 2000	371
15.3	Value of unit desa loans and savings, December 1996–December 2000	389
15.4	Number of unit desa outstanding loans and savings accounts, December 1996–December 2000	389
15.5	Real value of unit desa loans and savings, 1984–2000	391