

Report No. 193

21 May 2018

## Supporting MSME development through financing

Micro, small, and medium enterprises (MSMEs) account for 99.6% or 911,768 of the 915,726 total enterprises in the Philippines in 2016. Of this number, almost 90% (820,795) are micro, followed by small at 9.46% (86,955), and medium at 0.44% (4,018). This figure could be more considering the three million to four million enterprises listed in the Philippine Business Registry submitted by the local government units.

In terms of economic output, the sector contributes over 35% of the country's GDP, and accounts for a quarter of the Philippine exports. MSMEs also employ 63.3% of the total workforce. This translates to 4.88 million jobs compared to 2.83 million for large enterprises.

### Access to finance

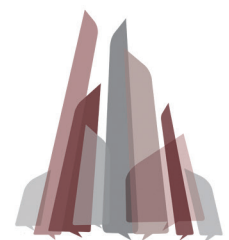
MSMEs thus present a great potential to further increasing its share to the economy. However, they continue to face challenges that impede its growth, particularly the lack or difficulty in securing the necessary capital and funding.

According to the World Bank, about 70% of all MSMEs in emerging markets lack access to credit.<sup>1</sup> Another study by Deloitte Southeast Asia cites that in the Philippines, the total SME loan from banks in 2014 stood at \$9 billion (approximately P471 billion), compared to that in Thailand (the highest in the region) with \$171 billion (approximately P8.95 trillion). Only 39 percent (39%) of SMEs cited bank loans, as personal funds continue to be the main source of funding.

While there are a host of support programs for MSMEs in the Philippines, much still remains to be accomplished to facilitate access to finance for smaller enterprises. From the period 2011-2016, a total of P220.98 billion were released to over 250,000 MSME borrowers and close to 2.8 million jobs were supported under the Access of Small Enterprises to Sound Lending Opportunities (ASENSO) program.

A report by the Bangko Sentral ng Pilipinas (BSP) showed an increase in the direct lending by the banks to MSMEs to P505.08 billion in 2016 from P387.7 billion in 2012. In terms of compliance, the 2016 figure corresponds to only 3.8% compliance ratio of the banking sector's mandatory allocation for micro and small enterprises, and only 5.4% for medium enterprises.

<sup>1</sup> *Small and Medium Enterprises (SMEs) Finance*. <http://www.worldbank.org/en/topic/sme/finance>



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Republic Act 9501 or the Magna Carta for MSMEs provides that all public and private lending institutions shall allocate at least eight percent (8%) for micro and small enterprises and at least two percent (2%) for medium enterprises of their total loan portfolio. The poor compliance ratio over the years suggests wanton disregard to the mandatory lending ratio, where banks would opt to be penalized than to lend to MSMEs.<sup>2</sup> From 2011 to 2016, the BSP remitted P196.29 million to the Treasury from the penalties collected from banks for non-compliance.

## **Policy reforms**

Last April 4, by virtue of Executive Order No. 50, President Rodrigo Duterte approved the MSME Development Plan 2017-2022. The six-year roadmap envisions more globally competitive MSMEs that are regionally integrated, resilient, sustainable, and innovative thus being the key drivers of inclusive economic growth. It is also aligned with the Philippine Development Plan (PDP) 2017-2022, and is likewise intended towards achieving the aspirations of the Filipinos for a strongly rooted, comfortable, and secure life embodied in Ambisyon Natin 2040.

The MSME Development Plan 2017-2022 recognizes that a key strategy to MSME development is improving access to finance. The roadmap outlines specific action steps which include:<sup>3</sup>

- Streamlining and simplifying loan requirements and processes
- Building capacities of financial institutions and cooperatives
- Providing financial literacy trainings
- Instituting policies and programs for innovative financing
- Developing, promoting and expanding alternative financial instruments

The PDP 2017-2022, also identified attaining the prescribed percent of allocation for MSMEs to the total bank loan portfolio as key to MSME financing. The **mandatory loan ratio provision under the Magna Carta for MSMEs is due to expire this year**, ten years after the effectivity of RA 9501 that was enacted in 2008. Amendments to the law should take into consideration the practice of banks that disregard the required lending ratio and pay the fines in favor of more profitable options when lending to bigger companies and projects.

While fund support from formal financial institutions is important, new business models especially brought by digital technology presses the need to create alternative innovative financing options for MSMEs.

The recently launched project of DTI, Pondo sa Pagbabago at Pag-asenso (P3), is the government's response to the popular "5-6" money lending system. Under the P3 program, the government's Small Business Corporation, together with microfinancing institutions will prioritize administering funds in the business centers of the poorest provinces. Loans ranging from P5,000 up to P300,000 will be lent to microenterprises and entrepreneurs at a maximum interest rate of 26% per year without need for collateral.

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<sup>2</sup> *Philippine MSMEs and Entrepreneurship: Pushing Boundaries, 2016.*

<sup>3</sup> *MSME Development Plan 2017-2022*

House Bill 7446 seeks to institutionalize P3 by **providing socialized microfinancing program for microenterprises**. The measure, which promotes entrepreneurship especially in the poorest sectors, is pending second reading in the House of Representatives.

Should collateral be required, another mode of financing for MSMEs could actually involve moveable assets – inventories, account receivables, future receivables, crops, machinery and equipment, intellectual property. The **Secured Transactions bill or the proposed Personal Property Security Act** is nearing its passage in Congress. House Bill 6907 was approved on third reading in the House, while its counterpart Senate Bill 1459 is on second reading.

The measure will strengthen the legal framework to include movable assets as collateral, and in case of delinquency, the same may be sold at a higher valuation so that a portion of the proceeds may be credited to the borrower. It also establishes a centralized registry for movable assets and credit information, and institutionalizes system in cases of insolvency. Overall, MSMEs will have simpler, faster and cheaper processing of loans.

Another mode of obtaining credit particularly in the agricultural sector is by storing goods and assets in a warehouse or through warehouse receipts. While this is covered by Warehouse Receipts Law of 1912 when record system was based on issuance of paper receipts, it obviously needs amendments to keep pace with modern technology. House Bill 6310, or the **proposed Philippine Warehouse Receipts Act** seeks to strengthen and modernize warehouse receipts by providing a secure online registry that is readily available and secured to facilitate loan processes. The measure is pending in the house committee level, while a measure is yet to be filed in the Senate.

The **CongressWatch Report** is a regular publication of the Makati Business Club. Its main mission is to promote accountability and transparency of elected government officials. For inquiries, suggestions, and additional information, please call CongressWatch at telephone nos. 403-3286 or email [patrick.chua@mbc.com.ph](mailto:patrick.chua@mbc.com.ph).

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