

APEC AND FINANCIAL EXCLUSION: MISSED OPPORTUNITIES FOR COLLECTIVE ACTION?

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The Asia-Pacific Economic Cooperation (APEC) has recently recognized the phenomenon of “financial exclusion” in its member economies, in consequence of a realization of the need to deal with the “losers” in the globalization process. With leadership from Mexico in 2002, APEC considered the merits of “microbanking” as a remedy for financial exclusion. With a number of member economies preferring to deal with financial exclusion as a “development” issue, rather than as a general condition in all APEC economies, APEC appears to have settled upon “microfinance”, rather than microbanking, as the solution to financial exclusion.

This paper examines financial exclusion as a generalized problem applicable to all APEC economies. It notes that, in all APEC economies, significant population subgroups are excluded from access to the services of formal financial institutions. It argues that providing such access would bring economic benefits, both in terms of aggregate economic efficiency and of interpersonal equity and equity between households. The paper examines the distinction between microbanking and microfinance, concluding that the latter is a subset of the former and primarily applicable to the developing economies, rather than representing a solution to the generalized problem of financial exclusion. The paper provides an overview of the different forms that microfinance has taken in APEC economies, including Australia. It also reviews the adequacy of the APEC process to discuss financial exclusion effectively.

Financial exclusion is a process that prevents poor and disadvantaged social groups from gaining access to the formal financial systems of their countries. This paper¹ examines the circumstances in which, quite recently owing to the

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initiative of Mexico, the phenomenon of “financial exclusion” has been recognized by the Asia-Pacific Economic Cooperation (APEC). It will consider what potential lies within APEC to address the problems of financial exclusion affecting its diverse populations. These problems are becoming more widely recognized, as seen for instance by the United Nations Capital Development Fund’s sponsorship of an international dialogue on building inclusive financial sectors to mark the United Nations International Year of Microcredit in 2005.²

APEC³ is an intergovernmental grouping established in 1989 to facilitate economic growth, trade and investment, and capacity- and community-building in the Asia-Pacific region. It has 21 member economies located on and within the Pacific Rim. These account for more than a third of the world’s population, over 50 per cent of world GDP and some 41 per cent of world trade. The member economies cover a wide span of development, ranging from transitional economies such as Viet Nam (GDP per capita of around \$420)⁴ to developing market economies in Asia, such as Indonesia (GDP per capita \$810) and Thailand (\$1,990), and in Latin America, such as Chile (\$4,400), to advanced market economies such as Japan (\$31,400) and the United States of America (\$36,400).⁵

Central to achieving APEC’s vision are the “Bogor goals” of free and open trade and investment in the Asia-Pacific region. However, APEC is a multi-faceted process. The member economies engage in policy coordination and cooperative activities at the official and ministerial levels in a wide range of sectors, from environment to telecommunications and from fisheries to financial systems. These wide-ranging APEC activities are conducted in many fora, including working groups and committees composed of officials and representatives of industry, academia and civil society. In this respect APEC resembles the Organization for Economic

² Information available online at <http://www.uncdf.org/bluebook/>.

³ APEC members are Australia; Brunei Darussalam; Canada; Chile; China; Hong Kong, China; Indonesia; Japan; Republic of Korea; Malaysia; Mexico; New Zealand; Papua New Guinea; Peru; Philippines; Russian Federation; Singapore; Taiwan Province of China; Thailand; United States of America; and Viet Nam.

⁴ GDP per capita and other economic indicators for the APEC member economies are available online at http://www.apecsec.org.sg/apec/member_economies/key_economic_indicators.html.

⁵ A classification of the APEC economies for the purpose of this paper, focusing on aspects of financial sector development, is as follows:

- (a) Developing market economies: Brunei Darussalam; Chile; Indonesia; Malaysia; Mexico; Papua New Guinea; Peru; Philippines; Thailand;
- (b) Transitional (developing) economies: China; Russian Federation; Viet Nam;
- (c) Developed market economies: Australia; Canada; Hong Kong, China; Japan; New Zealand; Republic of Korea; Singapore; Taiwan Province of China; United States of America.

Cooperation and Development (OECD). However, as noted above, APEC embraces developed, developing and transition economies, whereas OECD is a grouping of advanced industrial nations.

The outcomes of APEC's sectoral fora are reported to the APEC ministerial meetings held towards the end of each calendar year. In turn, the deliberations of these sectoral ministerial meetings are reported to the primary APEC deliberative body. This is the annual APEC Ministerial Meeting, attended by foreign and economic or trade ministers. The cycle culminates in an annual headline event, the Leaders' Meeting, which is a quasi-summit of the APEC membership.⁶ This paper draws upon the work relevant to financial exclusion conducted by a number of APEC sectoral working groups and committees. In particular, it is based on the deliberations of the APEC Economic Committee and the APEC Small and Medium Enterprises (SME) Working Group.⁷

I. APEC, SHARED PROSPERITY, MICROBANKING AND MICROFINANCE

Meeting in Shanghai in 2001, the APEC Leaders expressed the need to address shared prosperity in the face of the pressures of globalization.⁸ This was to be coupled with attention to the problems of microenterprise, which was seen as providing livelihood to the majority of the populations of the poorer APEC member economies. Then, during 2002, APEC turned its attention specifically to issues of financial exclusion, as a means to achieve greater economic efficiency and equity in the Asia-Pacific region. Under President Vicente Fox, Mexico pressed for APEC members to give more attention to microenterprise development (MED), increase economic participation by the poor and provide social safety nets for those displaced by globalization. APEC's interest in MED has been paralleled by attention to the provision of financial services tailored to the needs of microenterprises and low-income people, known as microbanking. This again was a Mexican initiative.

⁶ APEC eschews the term summit because of political sensitivities, since not all APEC members are independent States. Thus, APEC is the first, and so far the only, international forum which seats both Taiwan Province of China and Hong Kong, China at the same table as China. This sensitivity also explains the use of the term member economies instead of governments to describe participants, and Leaders' Meeting rather than heads of government meeting to describe the annual quasi-summit.

⁷ Information on the complex set of activities in the annual APEC working cycle is in Outcomes and Outlooks 2003/2004 available online at http://www.apec.org/apec/enewsletter/march_vol2/publication.primarycontentparagraph.0001.LinkURL.Download.ver5.1.9.

⁸ APEC Economic Leaders' Declaration: Meeting New Challenges in the New Century, Shanghai, China, 21 October 2001, available online at http://www.apecsec.org.sg/apec/leaders_declarations/2001.html.

During 2002, a number of APEC committees and working groups studied microenterprise development and microbanking or microfinance, while several conferences and symposia also considered the issues. Microbanking was pursued through the Economic Committee, while MED and microfinance both received attention in the work directed by ministers responsible for SMEs and for women. The Economic Committee produced a comprehensive study of the requirements for microbanking development, regulation and supervision in the Asia-Pacific region,⁹ which was endorsed by the 2002 APEC Ministerial Meeting. The study adopted financial exclusion as an analytical principle, and defined microbanking broadly as consisting of “the provision of small-scale financial services, such as credit, savings, insurance, and remittance services, that are targeted towards low-income segments of the population and microenterprises.”

However, in regard to the financing needs of microenterprises, the SME Ministerial Meeting in 2002 saw the solution not in microbanking, but in microfinance, and stated that:

“Ministers recognized the importance of micro-finance as a sustainable development tool for micro-enterprises.....[and] welcomed the recommendations to (1) develop an appropriate risk based regulatory framework for the commercial microfinance industry; (2) incentivize banks and financial institutions to enter the business of microfinance; (3) provide incentives, training and rewards to commercial institutions that demonstrate excellent performance; (4) limit microfinance subsidies to activities that disseminate information, develop financial tools, and train managers and staff; (5) provide capacity-building initiatives for the most promising institutions entering the micro-financing market; (6) and share lessons across APEC regarding the transformation of non-governmental organizations to commercial microfinance institutions.”¹⁰

This statement by SME Ministers is exemplary in a number of respects, including its emphasis on the sustainability and professionalism of institutions. It sets out alternative paths to the creation of workable models for microfinance provision; these may arise either because orthodox financial institutions modify their operations so as to incorporate microfinance clients, or because voluntary

⁹ APEC, chapter 2, “Microbanking Development, Regulation and Supervision in the APEC Region” in *2002 APEC Economic Outlook* (Singapore, APEC, 2002), available online at http://www.apec.org/apec/publications/free_downloads/2002.html.

¹⁰ Joint Ministerial Statement at the ninth APEC Small and Medium Enterprise Ministerial Meeting, Acapulco, Mexico, 24-25 August 2002, available online at http://www.apecsec.org.sg/apec/ministerial_statements/sectoral_ministerial/small_medium_enterprises/2002_small_medium.html.

agencies scale up and professionalize their operations to achieve sustainability, perhaps becoming formal financial institutions in the process. However, the statement does not appear to be directed towards financial exclusion seen as a whole-of-APEC issue. The choice of the term microfinance rather than microbanking and the description of the former as a development tool both appear significant. The Ministers seemed intent upon quarantining the issue strictly within the borders of APEC's developing economies.

At the conclusion of the process for 2002, on 27 October, the APEC Leaders also endorsed microfinance and MED. Their Declaration stated that:

"We agreed that micro-financing is crucial for the expansion of micro-enterprises, and we praise efforts to develop and promote market-based micro-finance to assure micro and small businesses and entrepreneurs have access to capital. We agreed that government action should create an enabling policy environment and a legal and regulatory framework for the growth and expansion of sound and sustainable micro-financing intermediaries, fostering their gradual and full integration into the domestic financial system."¹¹

From these statements of APEC Leaders and Ministers we can draw an important distinction. On the one hand, the Economic Committee report endorsed at the APEC Ministerial Meeting employed the generic term microbanking to describe a range of financial service delivery options. These appear to have the potential to address financial exclusion, seen as a whole-of-APEC problem. On the other hand, the statement from the Small and Medium Enterprises Ministerial Meeting adopted the more narrow term microfinance, which (by implication at least) is seen as the solution to a developing economy problem. This partial rather than whole-of-APEC approach seems to have won the day at the 2002 Leaders' Meeting, and was reflected in their Declaration.

This was unfortunate, because microbanking is the more inclusive concept and has the potential to address a failure of financial sector development common to all APEC economies. The reasons for APEC's adopting the less comprehensive approach are complex and revolve around differing national perceptions of the goals of APEC. Some of the more-developed economies appear to have regarded any examination by APEC of their own financially-excluded subpopulations as irrelevant, although it is interesting that the United States was broadly supportive of a generalized approach to the issue. A number of developing member economies

¹¹ For full text, see the APEC Economic Leaders' Declaration, Los Cabos, Mexico, 27 October 2002, available online at http://www.apecsec.org.sg/apec/leaders_declarations/2002.html.

were content to see the argument for financial inclusion treated simply as a development issue, and this is the view that prevailed. The distinction between microbanking and microfinance is discussed at greater length in section V, below.

II. THE RELEVANCE OF FINANCIAL EXCLUSION TO APEC'S ECONOMIES

If financial exclusion is to be seen as relevant to all economies, it is necessary to frame the discussion in a manner which captures the diversity within APEC. One way of approaching this is to accept that in all APEC economies, whether developed or developing, and whether market-based or transitional, there are population subgroups which are neither adequately served by formal financial systems, nor by conventional financial institutions, especially the banks. Thus in the wealthiest APEC economy, the Economic Committee's report on *Microbanking Development, Regulation and Supervision*¹² notes that "the existence of 40 million Americans who are not using mainstream banking services led the Treasury Department to launch the programme 'First Accounts' in late 2001", and documents this programme.

This failure of access occurs in developing member economies, where the informal or un-enumerated sector is of major importance as a source of livelihood for the poor and the household is the primary unit of both production and consumption. Considerations such as geographic isolation, low population density and gender also play a part in determining patterns of unequal access in economies where financial sector development is limited. Particular sectors, notably smallholder and peasant agriculture, with their associated post-harvest and off-farm economic activities, pose special challenges for financial service provision. A general problem in the developing member economies is the inability of many lower-income households to meet lenders' requirements for formal physical collateral.¹³

Inequality of access occurs also in developed economies, where the forces of privatization and rationalization impelled by the internationalization of finance have wrought massive structural changes in domestic financial markets. In some cases such restructuring has led to the withdrawal of conventional financial institutions from particular geographic areas or demographic categories. In other cases, increasing economic and social polarization has caused conventional financial institutions to focus their services on high-yield market segments and to neglect

¹² See footnote 9 above.

¹³ As Hernando de Soto has shown, however, land tenure and land titling deficiencies often prevent the poor from collateralizing assets they have accumulated.

others, such as low-income and otherwise disadvantaged households. Gender is a variable influencing access in developed as well as in the less developed member economies.

From the above it can be seen that in all economies there are households whose members, in consequence of financial exclusion, face obstacles in realizing their economic and social potential. This is most commonly because their income levels and the quantum of their financial service needs are pitched substantially lower than those of the population groups that have access to formal financial services. This is not to say that the deprived subgroups are always minorities. Indeed, they may be a majority by number, though not by share of income, within their economies. In the least developed economies formal financial institutions may serve only between 15 and 50 per cent of households.

Thus in regard to access to financial services there is a unifying feature, which enables us to bind together the concerns of all economies, developed and developing. In all cases, the household is the economic unit which experiences the least adequate access to financial services. An important distinction exists, however, between the developing and developed economies. In the developing economies, including those in transition, households are disadvantaged both as units of production and consumption. Improved access to financial services has the potential to increase both efficiency in production and equity in consumption in those economies. In the developed member economies, households are disadvantaged primarily in their role as units of consumption, given their very limited importance in production. In the developed economies the benefits of improvements in access are primarily in terms of interpersonal and inter-household equity.

III. THE CONTRIBUTION OF MICROBANKING AND MICROENTERPRISE DEVELOPMENT TO ECONOMIC EFFICIENCY

In all economies, developed as well as developing, microbanking can contribute to the process of financial deepening, which is an important concomitant of economic development. There is real significance for financial sector development in the extension of savings facilities to millions of poor householders. This is true no matter how small the mean balance of their accounts. The poor, especially in the developing economies, can demonstrate a surprisingly high propensity to save. This is particularly true if they have access to safe, liquid, deposit facilities bearing positive real rates of interest. Extension of financial services to the poor, especially deposit-taking, lays the foundation for a cumulative process of financial deepening.

A second important contribution to economic efficiency relates to the developing economies and concerns their competitiveness in international trade. Microenterprises in these economies are, as previously discussed, mainly household-based and are the most numerous units of production as well as the largest source of employment. It is true that microenterprises, especially the typical “survival” enterprises of the poor, make little direct contribution to exports. However in some economies, for example Taiwan Province of China, there are well-established supply-chain relationships in export industries which reach down into the household-based microenterprise sector. Lower wage rates paid in that sector can be a factor in the international competitiveness of industries where such relationships prevail.

The most important, if indirect, contribution to export promotion of microenterprises consists of their capacity to supply wage-goods and services to the industrial workforce. For developing economies to exploit comparative advantage in manufacturing based on low labour costs, it is necessary for workers to have access to low-cost wage-goods and, particularly, services. It is the comparative advantage of microenterprise to produce such goods and services, which can form a substantial proportion of the consumption basket of manufacturing workers. This is especially the case where workers in export-oriented manufacturing are employed away from their homes and families. In such circumstances, microenterprises spring up to serve the needs of an industrial workforce. Street stalls supply food and drink, while other microentrepreneurs offer homestay accommodation, minibus transport, outdoor haircuts, tailoring and a host of other workers’ needs. Microbanking institutions can play an important role in increasing the productivity and profitability of such microenterprises by funding the capital requirements of microentrepreneurs.

Microbanking institutions serving the needs of industrial workers can contribute to export competitiveness in other ways. By providing deposit services they can assist industrial workers to accumulate savings and by providing funds transfer services they can reduce the transaction costs of remittances to families. By increasing the net rewards of participation in the industrial workforce, such services tend to reduce wage pressures in the export industry and thereby act to maintain its international competitiveness.

IV. THE CONTRIBUTION OF MICROBANKING AND MICROENTERPRISE DEVELOPMENT TO DISTRIBUTIONAL EQUITY

The 2001 APEC Leaders' Declaration, as seen above, called for member economies to develop and strengthen social safety nets to protect the vulnerable. This call reflected concern for shared prosperity in the face of globalization. The introduction of microbanking and microenterprise development to APEC's agenda reflects an assumption that these activities act to improve distributional equity within economies.

First, microenterprise conducted at the household level provides income to poor and low-income people in the developing member economies. It is a mechanism that enables the benefits of economic growth to flow to poor and low-income people, and to facilitate their participation in that growth. Action to improve the productivity of microenterprises, including increasing their access to financial services, will have direct distributional benefits, because these enterprises are the major source of non-agricultural employment in developing APEC economies.

Microbanking could be regarded as trivial in financial terms, in the sense that the transactions of microbanking institutions would scarcely register in the consolidated balance sheets of the financial sectors of any APEC economy.¹⁴ Microbanking transactions, however, are significant in the lives of millions of people who are not served by formal financial institutions. Microbanking can assist the sharing of prosperity in developing economies by assisting poor households to meet both their consumption and production needs. In developed economies, microbanking and MED can raise the consumption levels of the financially excluded. Additionally, in all economies, female-headed households are overrepresented among the poor and stand to gain disproportionately from access to microbanking services and MED opportunities.

Finally, support for microbanking and MED has the potential to ameliorate the impact of market-opening measures on those who might otherwise bear the brunt of the costs of adjustment. Such measures may result from multilateral trade negotiations through the World Trade Organization, or as the result of bilateral and/or regional trade agreements. In the case of the APEC economies, such support for microbanking and microenterprise development could increase the political feasibility of moving towards the Bogor goals of free and open trade and

¹⁴ Indonesia, where a range of regulated financial institutions caters to the needs of a substantial proportion of lower-income people, is an important exception to this generalization.

investment. In the meantime, given the proliferation of less comprehensive “free” trade agreements of a bilateral or regional nature, having access to financial services increases the capacity of low-income households and microenterprises to withstand the shocks of adjustment imposed by international trade treaty obligations.

V. MICROBANKING AND MICROFINANCE

The distinction between microbanking and microfinance is important and is discussed at length in this paper. In brief, however, one could say that microfinance is a subset of microbanking, and is more adapted to the circumstances of developing member economies. Microbanking, on the other hand, could be regarded as applicable to the circumstances of all member economies. For the developing member economies, microfinance is often proposed as the solution to the financial exclusion of households operating in the informal economy. It is certainly the most publicized, owing to the many published accounts, both professional and popular, of the achievements of Grameen Bank and its founder, Dr. Muhammed Yunus. The energetic advocacy of the Microcredit Summit has also increased popular awareness of microfinance.

For developing economies of the Asia-Pacific region, it is appropriate to accept the specific definition of microfinance used in the Asian Development Bank’s Microfinance Development Strategy for the region:

“Microfinance is the provision of a broad range of financial services such as deposits, loans, payment services, money transfers, and insurance to poor and low-income households and their microenterprises.”¹⁵

The Asian Development Bank’s definition is a good deal more inclusive than those adopted by many microfinance practitioners, who would apply strict criteria for loan size and targeting of clients, excluding from consideration the supply of services to people who are merely low-income, rather than poor. However, for our purposes, it is appropriate to focus on the supply of financial services to the bottom half or two thirds of the income ladder, as all of the poor and most informal sector entrepreneurs are likely to be found there. Such a frame of reference enables the discussion to consider the achievements of such accomplished formal development financing institutions as the Bank Rakyat Indonesia (BRI), Thailand’s Bank for Agriculture and Agricultural Cooperatives (BAAC) and the Banco del Estado of Chile, which finance the microenterprise sectors in their respective economies.

¹⁵ Asian Development Bank, policy papers, *Finance for the Poor: Microfinance Development Strategy* (Manila, ADB, 2001), available online at <http://www.adb.org/Documents/Policies/Microfinance/default.asp>.

“Microfinance” encompasses access to savings and other financial services, as well as credit. The term has come into greater currency since the early 1990s and has largely, but not entirely, supplanted the term microcredit in the professional literature.¹⁶ The latter term is now recognized as unfortunate because its use has focused attention on a single aspect of microfinancial services, lending to the poor, and diverted attention from the need to develop systems of financial intermediation in which the poor are involved. Savings is often described, in a memorable phrase, as the forgotten half of rural finance. Using the term microcredit perpetuates this amnesia.

Microfinance institutions (MFIs) are developing forms of “microinsurance” to protect the vulnerable from misfortunes, such as ill health, which can tip them over the edge into poverty. In addition, microfinance practitioners are working to introduce newer services, such as money transfers to facilitate remittances by migrant workers. These are valued by poor and low-income workers and their families, given their high degree of spatial mobility, both domestically and internationally, and the difficulty and expense they experience in remitting funds.

VI. MICROFINANCE IN APEC’S DEVELOPING MEMBER ECONOMIES

There is great diversity among APEC member economies in the degree to which systems of microfinancing have emerged, in the institutional forms developed or adapted for them and in the policy and regulatory environments that shape those institutions. This account of patterns of development in the various microfinance sectors is designed primarily to give some indication of the diversity that exists. APEC economies are classified as developed, developing and

¹⁶ The terms used to describe institutional efforts to reduce financial exclusion have evolved with a fuller understanding of the processes involved. Until the mid-1990s the term microcredit was in vogue, until the realization that this failed to capture the importance of financial services other than credit, most notably access to savings services. Now microfinance, which is thought to encompass this wider range of meanings, has very largely superseded microcredit, though it has not done so sufficiently to prevent 2005 being designated as the International Year of Microcredit. The term microbanking is more recent and not yet widely employed although it has excellent credentials. These flow, inter alia, from its use in the title of the *Microbanking Bulletin*, published by the Consultative Group to Assist the Poor, from the Food and Agriculture Organization of the United Nations Microbanker software package, and from Bank Rakyat Indonesia’s Microbanking Division. These uses of the term have in common an approach to eliminating financial exclusion based on the transformation of informal institutions to formal and accountable entities, the standardization of reporting and performance measure and the sustainability of financial services. This is an evolutionary process that may in time see microbanking supersede microfinance as the generic label. This paper notes the use of these two terms as illustrating a divide between the approaches taken to financial exclusion among APEC member economies.

transitional, according to the schema outlined above (see footnote 5) and a distinction is made between activities in Asia and Latin America.

APEC developing market economies in Asia

Among the developing market economies in Asia there are considerable differences, both in the incidence of poverty, which might stimulate microenterprise development and microfinance initiatives as a response to disadvantage, and in the balance between private and public involvement in the process. For example, Malaysia and Thailand have considerably higher levels of per capita income than their APEC neighbours, Indonesia and the Philippines. In Malaysia in particular, absolute poverty was, at least until the financial crisis from 1997, regarded as a residual and diminishing problem which could be eliminated early in this current century.

The official Malaysian approach to microenterprise development, and to the provision of microfinancing services as an element in that process, has been essentially 'social-welfarist'. Microfinance services for households without access to conventional financial institutions have been seen within the framework of a redistributive social policy involving substantial subsidies. For the poorest Malays, the Government has nurtured a major MFI operated by an NGO, while the State agricultural bank has extensive rural outreach. For the off-farm microenterprise sector, another State institution, the Credit Guarantee Corporation, underwrites commercial bank lending to small- and microenterprises, down to the level of street hawkers.

In the case of Thailand, elements of subsidy, and implicit redistribution, have also been present in the financial policy for lower-income rural households. However, there are marked differences between Malaysia and Thailand in microfinance policy and practice. In Thailand, for example, the voluntary or NGO sector of financial service provision is relatively undeveloped. Instead, a government agricultural bank has primary responsibility for microfinancing and has become both an international leader in its field and an integral part of the Thai financial system.

There is a division of labour between financial institutions serving the microenterprise development and informal sectors. The State agricultural bank, BAAC, primarily serves small and medium farms, cooperatives and associations, with the last two serving many microentrepreneurs. The poor and landless are served mainly by informal finance and a few government programmes and NGOs. Agricultural cooperatives and village-level credit unions also reach poorer segments of the rural population to some extent. More recently, rotating credit funds have

been established in most Thai villages, but it is not clear that their financial sustainability is an important objective. From 2001, specialized financial institutions have been employed as instruments for policy lending. This development is discussed in section IX below, in an APEC context.

Indonesia and the Philippines also provide some marked contrasts, both with one another and with Malaysia and Thailand. Indonesia has adopted a model of microfinance service provision based very largely on the operations of regulated financial institutions, whereas NGOs are of relatively limited significance. This is sometimes described as a rural financial systems approach to household and microenterprise financing. The emergence of sustainable and effective models of microfinancing within the formal financial system, many of them privately owned and operated, has been more a by-product of Indonesia's efforts at financial sector development than of any conscious policy to stimulate microfinance, *per se*.

The "village units" of BRI, the State agricultural bank, have acquired an international reputation for the effectiveness of their outreach to middle- and low-income households operating microenterprises in rural Indonesia. Indeed, the profitability and savings mobilization capacity of these units kept Bank Rakyat as a whole afloat during the Asian financial crisis. Indonesia has also developed a range of small regulated financial institutions which serve the communities in which they are embedded effectively.

By contrast, Indonesia also provides some examples of mass microcredit programmes involving NGOs and other community organizations, especially in the late Suharto era, which were politically-driven and not at all concerned with financial sustainability. There is also a long history of ill-targeted and subsidized schemes of directed credit serving the SME sector.

Microfinancing in the Philippines has followed a more conventional course, based primarily on the energies of a burgeoning NGO community. The influence of Grameen Bank methods of service delivery has been very strong in that NGO community and the Philippines also has a regulatory environment favourable to the operation of small regulated banks suitable for microfinance. The Government has explicitly incorporated microfinance into its poverty alleviation strategies, has encouraged NGOs to develop sustainable microfinance programmes, and promotes the transformation of successful microfinance NGOs into regulated financial institutions.

In the Philippines there are three categories of MFI, each of which answers to a different regulator. These are rural and thrift banks, NGOs that provide microfinancial services, and credit unions or cooperatives. Of these three

institutional types, the rural banks appear to deal with somewhat higher-income clients and to make larger loans than the microfinance NGOs. Many of the NGOs have adopted variants of the Grameen Bank model and, in general, group organization of one sort or another is their most common mode of service delivery. The assets of these three types of MFIs were equivalent to only about four per cent of the assets of the commercial banking system in 1996. However, the combined number of MFI offices, some 7,900 outlets, was more than twice the number of commercial bank offices.

Procedures exist for successful MFIs operated by NGOs to transform themselves into regulated financial institutions. The Government has established a second tier financial institution specifically for the purpose of providing loanable funds for MFIs, as well as setting up capacity-building mechanisms for these institutions. The Government has also acted to rationalize the proliferation of ad hoc credit schemes operated by line agencies of government, eliminating subsidies and ensuring that credit provision as part of targeted government programmes becomes the sole preserve of regulated financial institutions.

Microfinance is in its infancy in Papua New Guinea, and indeed financial sector development in general has not proceeded very far by comparison with the other developing market economies of APEC. Variants of the Grameen model are being trialled in a number of centres, and the Asian Development Bank is supporting the creation of a second tier microfinance fund and capacity-building facilities for MFIs. There is a single small regulated financial institution, currently inactive, but seeking restoration of its banking license, with as yet limited outreach, concerned with reaching a low-income clientele and serving microentrepreneurs. The savings and loan movement is in a revival phase, as is the State agricultural development bank.

APEC developing market economies in Latin America

Presented here are some generalizations about microfinance in Latin America, even though APEC's concern is with only three economies in the region, Chile, Mexico and Peru. However, there appear to be some commonalities in the regional microfinance culture, perhaps based on language and intraregional communication, the latter assisted by the activities of international agencies, especially the Inter-American Development Bank, and umbrella bodies with affiliates throughout the region. Commonalities observable in Latin American microfinance provide some interesting contrasts with what is seen in Asian APEC economies.

In general, the focus of Latin American MFIs is on providing financial services to microenterprises as businesses, rather than on providing services to

households of the poor. Loan sizes appear to be larger than in many parts of Asia, and the financing of agriculture and rural economic activities is relatively neglected in favour of servicing an urban clientele.

In a number of countries the commercialization of microfinance has proceeded relatively far, although larger banks which entered the field now have withdrawn in many cases. Instead, commercialization has occurred more owing to the operations of small regulated financial institutions, with many MFIs established by NGOs and community groups transforming themselves into such institutions. The creation of enabling legislative regimes in a number of countries has been a factor in this transformation pattern of commercialization.

Growth has been rapid in the regional microfinance sector. Over the period 1998-2001, according to one report, the sector grew at 25 to 30 per cent annually. With a loan portfolio of around \$1.4 billion in 2000, the continuation of such growth would require as much money again for loanable funds in less than three years. Borrower numbers were estimated at around 1.5 million, while a similar number being served by credit unions. Historically, some credit unions appear to have been established more as conduits for external grant funds than as savings mobilizing institutions. This reverses the normal credit union priorities, and in fact deficiencies in savings mobilization appear to be a general weakness of MFIs in the region.

APEC transitional economies

In the transitional economies, China, the Russian Federation and Viet Nam, there is a range of experience and some marked contrasts in terms of overall economic and financial sector development. China offers a potentially enormous market for microfinance services, but effective financing for microenterprise development is hampered pending the resolution of major macroeconomic, fiscal and financial sector policy issues in the transition to a "socialist market economy". In the meantime, interest rate controls remain a significant impediment to the emergence of sustainable microenterprise financing.

There are a small number of MFIs adapting the lessons of international microfinance experience to Chinese conditions, in association with bilateral agencies and under conditions agreed with central and local authorities. The Chinese NGO sector operates within narrow confines, however, and there is little official tolerance for unregulated financial service "experiments". Without the official approval enjoyed by bilateral projects, MFIs would experience problems with their legal identity and institutional status.

The primary source of microcredit is the Government, which has adopted it as a poverty eradication tool. It is appropriate to call these programmes microcredit rather than microfinance as there is no attempt to incorporate savings into the model. The official policy of providing microcredit primarily in backward, resource-poor regions, rather than in regions (including cities) where greater economic opportunity exists for microenterprise, is another impediment to its success. This, together with the substantial interest rate subsidies involved, reflects the fact that microcredit is seen as a social rather than a financial sector programme. There is a need to allow local-level financial institutions, including the rural credit cooperatives, greater flexibility in setting interest rates for loans and deposits and to develop a range of bank and non-bank financial institutions, the latter including MFIs, engaged in microenterprise financing.

Viet Nam is experiencing a difficult transition to financial liberalization. Among many elements in a poverty reduction strategy, the Government has focused on the financial service needs of the poor, particularly in rural areas. Government efforts in the field have involved central bank regulation of interest rates, direction of the state banking system to provide subsidized credit to target groups and the creation of specialized financial institutions for the purpose. International agencies and NGOs have drawn the Government's attention to the potential of microfinance to alleviate poverty and stimulate Microenterprise development, and have supported a number of projects trialing imported microfinance models.

An autonomous NGO movement, as distinct from mass organizations set up by the State, is still substantially lacking. The mass organizations are important agencies for the provision of credit under official schemes. All these developments have occurred while Viet Nam has been moving to establish the institutional framework for a modern financial system and to introduce elements of liberalization as possible and appropriate. The growth of outreach of State banks during the last few years is a notable feature of the Vietnamese financial system.

In the states which comprised the former Soviet Union, there was typically very little micro- and small enterprise, since the environment of the centrally-controlled economies was not conducive to their development. During the economic difficulties of the 1990s, income inequality increased in the Russian Federation, with some 35 per cent of the population below the official poverty line at the end of that decade. These circumstances might be thought favourable to the flowering of informal sector and microenterprise activity, but the data suggest that less than 10 per cent of the labour force were employed in the microenterprise (up to 10 workers) and small enterprise (up to 200 workers) sectors at that time. This does not, however, allow for underenumeration in the informal sector, where operators have good reason to remain unobtrusive.

Internationally-supported efforts to establish microfinance in the Russian Federation commenced during the 1990s and took one of two forms. One was downscaling. This was a process in which commercial banks were encouraged, in projects supported by the European Bank for Reconstruction and Development, to adapt their financial technologies to the service of lower-income customers. The second approach is described as upscaling, supported by bilateral development assistance and international NGOs. This requires the creation of grass-roots organizations to offer specialized savings and credit programmes, with either group or individual client relationships (by contrast with which the downscaling efforts of the banks were strictly on an individual client basis). The financial crisis of 1998 set back all these efforts, with the systemic problems of Russian banking posing particular difficulty for the downscaling approach.

VII. MICROFINANCE AND OTHER FINANCING ALTERNATIVES IN THE DEVELOPED ECONOMIES

By employing the concept of alternative financing mechanisms for the reduction of financial exclusion, among which microfinance is simply one possibility, we are able to extend the discussion beyond the informal sector in developing economies. This enables us to embrace, in addition, certain deficiencies of financial service provision in more developed economies. There is a wide range of alternative financial mechanisms, outside the conventional operations of commercial banks, which may be observed in these economies. Indeed, the appropriate alternative mechanisms may be a good deal more heterogeneous than those needed in the developing economies.

First, it is appropriate to discuss the status of microenterprise in developed APEC economies and to consider the reasons why conventional microfinance, as practiced in the developing economies, has not flourished in developed economies. Microenterprise in the developed industrial APEC economies is of relatively minor importance. The microsector employs a small proportion of their workforces (for example the self-employed are only around a tenth of the male workforce in the United States) whereas in developing economies a majority of workers may be in the sector. In Australia, Canada or the United States, microenterprise suffers from the competition of large firms, whereas in developing economies there is a marked segmentation of markets, with the poor meeting most of their basic needs for services and commodities from informal sector sources. The industrial structure in Taiwan Province of China is marked by the strength of its SME sector, with firms typically in complex supply chain relationships with one another and with large enterprise, while with economic growth microenterprise has become a diminishing residual.

Microenterprise methods of production and distribution often come into conflict with regulatory standards in developed economies, whereas in developing countries the regulatory environment is often more permissive, or at least more open to negotiation. Also, the existence of social safety nets in high-income countries acts as a disincentive to engagement of the poor in microenterprise.

Attempts to apply microfinance principles in developed industrial economies encounter difficulties for a number of reasons. The poor have access to conventional sources of finance, notably credit cards. Group methods of organization encounter particular difficulties in the urban industrial setting. The reasons for this have to do with trust, and with people's valuations of their own time, influenced in part by the availability of social welfare benefits. Also, the principal vehicle for asset-building in developing economies is incremental investment in home improvement, a process suited to microfinancing. However, this is much more difficult in industrial economies where building codes and the commoditization of housing impede incremental home improvement by owner-occupiers.

The universe of alternative financial service delivery systems in developed member economies is substantial and diverse. Research conducted for the study on microbanking development, regulation and supervision by the APEC Economic Committee in 2002¹⁷ provided some information on the diversity of alternative financing mechanisms in operation. Much successful practice in alternative systems of financial service delivery is based upon local, subnational, action by community groups and agencies and is not usually well publicized. The best approach to our substantial information deficit in this area would be to commission studies, based on a sound analytical framework, of financial service delivery mechanisms in developed economies. Australia is used below as an example of a developed economy situation.

VIII. FINANCIAL EXCLUSION IN AUSTRALIA

A study conducted in Australia noted the withdrawal, or at least the distancing, of commercial banking services from particular geographic areas and social categories, compelled by forces of rationalization and restructuring, discussed above. According to Connolly and Hajaj, the most basic, and the most important, financial service for most Australians is the bank account. The provision of a bank account is essential for receiving pay and benefits and making and receiving

¹⁷ See footnote 9 above.

payments. Having a bank account is no longer a mere convenience, it is a prerequisite for engaging in the economic process'.¹⁸

According to these Australian researchers, the impacts are suffered by households and small business:

"Less affluent communities which have lost banking services have tended to go into a steep decline which in due course touches almost every aspect of community life. This is not surprising in view of the significant manner in which Australian communities are geared through access to banking services. In many cases, 'the bank' acts as the main mechanism for attracting people to a given shopping locale. Over many years, other businesses have developed around a bank site, assuming that consumers would be attracted by the convenience of completing their financial transactions as well as their household shopping in the one place. The banks' presence is critical for individual banking needs (and for the provision, through local knowledge, of the capital needed for business to grow and re-invest."

The accompanying box contains a more detailed discussion of the consequences of financial exclusion drawing on this Australian study. It details conclusions that would probably apply in other developed APEC economies, such as Canada, New Zealand and the United States.

In Australia, there have been a number of responses, both governmental and community-based, to this removal of services. They include the establishment of transaction centres for financial services in post offices, supermarkets and other places in communities from which the banks have departed. They include the emergence of community banks in a growing number of towns and suburbs, facilitated by a franchising operation in which a particular dynamic provincial bank (Bendigo Bank) offers citizen groups access to its banking license under a strict set of conditions as to capital commitment, community involvement and operational standards.

The responses also include initiatives by the Australian credit union movement to fill financial service gaps in some communities. The Australian credit unions are, quite apart from their responses to these more recent changes in the Australian financial landscape, an interesting and instructive study of alternative approaches, given their progressive modernization and embrace of technology and

¹⁸ C. Connolly and K. Hajaj, *Financial Services and Social Exclusion*, Financial Services Consumer Policy Centre, University of New South Wales, Sydney, 2001, available online at <http://www.fscpc.org.au/publ/publications.htm>.

FINANCIAL EXCLUSION IN AUSTRALIA

Connolly and Hajaj have studied the consequences for households and communities of financial exclusion, defined as “the processes that prevent poor and disadvantaged social groups from gaining access to the financial system.” They focused particularly on the effects of the closure of bank branches and agencies.

Community consequences of financial exclusion

In urban areas

- Increased travel requirements
- Higher incidence of crime
- General decline in investment
- Difficulties gaining access to credit
- Decreased choice in local shops and businesses
- Increased unemployment

In regional and remote areas

- Financial drain from the community, as people travelled to larger centres to do their banking and shopping, with 88 per cent of respondents reporting that their expenditure locally had decreased
- Loss of financial investment, with 30 per cent of respondents indicating that the new financial environment had persuaded them not to proceed with undertaking a loan
- Loss of confidence in the community, with 90 per cent of respondents indicating they were now more pessimistic about the future of their community and 39 per cent reporting that they would leave if they could

Business consequences of financial exclusion

In urban areas

- General decline in passing trade
- Loss of access to middle class and higher-income consumers
- Higher retail tenancy vacancy rates
- Less investment
- Difficulties in gaining access to banking staff with local knowledge, especially regarding lending

- Higher cash handling costs
- Higher insurance premiums
- Increased risk of crime

In regional and remote areas

Consequences for small businesses seem to be exacerbated. Research suggests that small businesses were the first to feel the effects of any withdrawal of financial services. These consequences included:

- Increase in cheque cashing
- Loss of cash sales
- Accumulation of excess cash
- Delay in deposit of cheques
- Increase in bad debts

Another study cited by Connolly and Hajaj added the following consequences:

- Increased security concerns owing to the lack of secure facilities to deposit takings and the need to transport large amounts of cash to and from the nearest bank branches in an unsuitable vehicle such as a private car
- Difficulties in obtaining small change
- Farming businesses being particularly disadvantaged by the loss of bank staff with intimate knowledge and experience in rural banking

Connolly and Hajaj cite British research findings that a lack of local knowledge among financial institutions can perpetuate a cycle of urban degeneration. They note also that loss of local knowledge is a significant issue in both urban and regional areas, as it tends to make financial institutions more cautious in local lending, falling back on national lending models which may not be appropriate in the local area.

Source: C. Connolly and K. Hajaj, Financial Services and Social Exclusion, Financial Services Consumer Policy Centre, University of New South Wales, Sydney, 2001, available online at <http://www.fscpc.org.au>.

their efforts to reach out to new communities, including Aboriginal people and migrants.

There is also some evidence of the reinvigoration of a nineteenth century social institution, the “Friendly Society”, as a base for providing access to financial services to the long-term unemployed and low-income families. Efforts are being made to associate friendly societies and credit unions with rotating savings and credit associations (RoSCAs), which operate along traditional lines among the recently-arrived in some migrant communities. Other initiatives are being taken by voluntary welfare agencies to free low-income earners (the working poor) who do not have access to bank credit from dependence on so-called ‘payday lenders’ who operate at the factory gate. Such schemes have often started as low- or no-interest lending, but experience has convinced some agencies to attempt a greater degree of cost recovery.

It is obvious that most of the Australian microbanking services described above are directed to households rather than to enterprises, and to financing consumption rather than investment. This serves to remind us of an important difference, discussed above. This difference is between the developed economies, in which there is usually a clear distinction between household and enterprise, and where relatively few enterprises are household-based, and the developing economies where, typically, the household *is* the enterprise.

IX. THAILAND’S PROMOTION OF SPECIALIZED FINANCIAL INSTITUTIONS

In 2003, Thailand became Chair of APEC and, among other initiatives, introduced the topic of specialized financial institutions (SFIs) to the agenda of APEC’s Economic Committee. SFIs were described as institutions underwritten by Governments and designed to fulfil specific social purposes, filling gaps in financial service provision left unfilled by commercial entities. Thailand proposed this theme as an extension of initiatives taken by Mexico in 2002 to focus attention on financial exclusion in APEC economies.

In fact, there are grounds for questioning the degree to which emphasis on SFIs could be regarded as supportive of a financially-inclusive financial sector. This is because in the developing APEC economies there remain significant elements of financial repression, supported in many cases by the activities of SFIs. In these economies vestiges of earlier approaches to financial institutions and markets continue to exist. These include credit guarantees and insurance, state participation in the capital and management of financial institutions, differential interest rates and cross-subsidies, and preferential rediscount rates and facilities furnished by

monetary authorities at the behest of Governments. Such activities lessen the capacity of financial systems to achieve financial inclusion in a sustainable fashion.

Among the financial sector measures is a wholesale moratorium on farm debt and the injection of some US\$ 1.5 billion of spending power across the rural sector through a village development fund. Each of these initiatives was implemented by a state SFI. These and other stimulatory measures are credited with contributing to the boom in consumer spending that supported economic growth in Thailand over the period 2001-2004.

Thailand's farm debt moratorium expired during 2004. The Bank for Agriculture and Agricultural Cooperatives is an SFI with an international reputation as an effective and efficient rural development bank. It was required by the Government to carry the outstanding farm debt, although its management had reservations about eventual repayment and anticipated damage to the bank's balance sheet.¹⁹ As for the other initiative, the village development fund, there is a dearth of data concerning their loan collection performance. The possibilities of politicized lending and damage to the rural credit culture cannot be excluded. Both the debt and village banking initiatives have implications for the sustainability, and hence capacity for inclusiveness, of Thailand's rural financial system.

The Thai study of SFIs, published by the Economic Committee towards the end of 2003, appeared to endorse the provision of subsidized credit by SFIs to low-income households and microenterprises despite the implications of such lending for rural credit culture and financial sector development.²⁰ That APEC members passed this report through the Economic Committee does not mean they had committed themselves to such policies.

¹⁹ M.-L. Haberberger, L. Wajananawat and N. Kuasakul, "Case Study: Bank for Agriculture and Agricultural Cooperatives, Thailand" in *The Challenge of Sustainable Outreach. How can Public Banks Contribute to Outreach in Rural Areas? 5 Case Studies from Asia* (Eschborn, Deutsche Gesellschaft für, 2003), pp. 249-288, available online at <http://193.97.170.92/themen/economic-development/download/COSO-5CaseStudiesfromAsia.pdf>. This study of BAAC notes that "[i]n the past...BAAC ha[d] managed to sustain pressures from political interest groups and to resist interference from local government in borrower selection and lending decisions." However, as a result of the 1997 financial crisis and international debt exposure, about half of the bank's equity was lost. With the advent of the Thaksin government in 2001, the study judges that the government-directed farm debt suspension was "...affecting the autonomy of the BAAC's operations." Further, "the outcome of the debt suspension program is uncertain. It certainly interrupted BAAC's struggle for viability and presents a potential threat to its long-term sustainability and [seems likely to] support the spread of moral hazard of BAAC borrowers. Therefore, BAAC should be well prepared for a very challenging time ahead from 2004 onwards."

²⁰ APEC, chapter 2, "Role and Development of Specialized Financial Institutions" in *2003 APEC Economic Outlook*, (Singapore, APEC, 2003), available online at http://www.apecsec.org.sg/apec/publications/free_downloads/2003.html.

X. MORE RECENT DEVELOPMENTS

Among the outcomes of the APEC process for 2003 was a call in the APEC Leaders' Declaration for action to "mainstream the informal sector".²¹ This appeared to recognize the importance of the informal sectors of APEC economies and to legitimate efforts to bring household production units in those informal sectors within reach of formal financial services. This positive development was coupled with an endorsement, by SME Ministers, of microfinance as "an instrument to reduce the 'financial exclusion' often experienced by micro-enterprises in the APEC economies". The Ministers declared that "...there should be a clear policy framework and development plan for a micro-finance system in APEC economies where the need exists for the extension of the financial system to incorporate the financially excluded".²² These statements represented explicit acceptance of the concept and language of financial exclusion into the APEC lexicon and provided a basis for further progress should APEC members be disposed to pursue the issue in future. Recognition of these principles at the political level, however, may not be enough to overcome inertia at other levels, as discussed below.

During 2002 (under Mexican leadership) and 2003 (under Thai leadership), issues of relevance to financial exclusion were discussed within the Economic Committee process of APEC. This was strategically sound, in that the Committee was established to conduct policy-relevant economic analysis and dialogue as well as to advance structural reform within APEC economies. However, under Chilean guidance in 2004, the Economic Committee was redirected to consider other issues. The locus of activities concerned with microfinance and microenterprise financing switched to the SME Ministerial process and the newly created Sub-Group on Micro-enterprises. The new Subgroup arose with the realization that the SME Working Group was not an ideal forum for discussion of the quite distinct problems of microenterprise. However, the Subgroup is required to report to the annual APEC Ministerial Meeting via the SME Working Group and the SME Ministers.

Given a close identification between microenterprises and households in the developing APEC economies where financial exclusion is most extreme, the Subgroup might seem to be an appropriate forum to progress an agenda of financial inclusion. It also appears well-placed to work on the Leaders' instruction, from

²¹ APEC 2003 Economic Leaders' Declaration: Bangkok Declaration on Partnership for the Future, Bangkok, 21 October 2003, available online at http://www.apecsec.org.sg/apec/leaders_declarations/2003.html.

²² Joint Ministerial Statement at the tenth APEC Small and Medium Enterprise Ministerial Meeting, Chiang Mai, Thailand, 7-8 August 2003, available online at http://www.apecsec.org.sg/apec/ministerial_statements/sectoral_ministerial/small_medium_enterprises/2003_small_and_medium.html.

2003, to mainstream the informal sector. However, there seems still to be some ambivalence within the SME Working Group concerning initiatives to incorporate the informal sector into policy frameworks. This is despite the Working Group having taken up the challenge in its work programme from 2004. Conceptual issues also pose a barrier to progress, notably the difficulty of agreeing upon operationally-useful definitions of microenterprise among so diverse a group of economies. Where issues of microenterprise financing are discussed, there is some tendency to consider them outside a financial sector development framework. For these reasons, progress has been uneven. Definitional difficulties lead to the introduction of inappropriate small and medium enterprise issues into the Subgroup discussions, and relatively few economies have fielded experts on micro issues at the Subgroup meetings.²³ Potentially useful initiatives by developing member economies (for example, a Peruvian proposal to consider micro- and small enterprise financing as a tool for mainstreaming the informal sector) are to be progressed in 2005. A proposal by Viet Nam to secure endorsement for an APEC Fund for Microenterprises, with a special concern for microenterprise financing and participation by international financial institutions active in the region, appears to have stalled.

These considerations raise a question, whether the SME Working Group and the Subgroup are the most appropriate forums in which to progress an essentially financial sector issue, that of financial exclusion. The SME process may yield benefits, in terms of more appropriate policies for increasing the productivity of microenterprises and their incorporation into the formal sector. However, the financial inclusion of households, in their dual roles as units of consumption and production, might be better addressed through an APEC forum concerned with issues of financial sector development. For this purpose, the APEC Finance Ministers' process may be more suitable. Finance Ministers already have work in progress on SME financing within APEC economies, suggesting that they are prepared to consider lower-level issues of financial sector "architecture". Also, China has proposed the creation of an Asia-Pacific Finance and Development Centre within the Finance Ministers' process. This could offer a platform for the exploration of financial exclusion, if its charter were made sufficiently broad. Without expert assistance from a financial sector forum, the SME process is unlikely to achieve the "clear policy framework and development plan for a micro-finance

²³ In recognition of this, SME Ministers noted that "In recognizing ME as a unique sector of the economy, Ministers noted the need for better participation by ME specialists in the Subgroup". Joint Ministerial Statement at the eleventh APEC Small and Medium Enterprise Ministerial Meeting, Santiago, Chile, 6-7 October 2004, available online at http://www.apec.org/apec/ministerial_statements/sectoral_ministerial/small_medium_enterprises/2004_small_and_medium_html.html.

system in APEC economies ... to incorporate the financially excluded", for which the SME Ministers called in 2003, as noted above.²⁴

XI. CONCLUSION

After explaining the circumstances under which microbanking and microenterprise development issues were introduced into the APEC agenda over the period 2002-2003, this paper has argued the case for the continuing relevance of the concept of financial exclusion to all of the APEC economies, whether advanced industrial, developing or transitional. It pointed to evidence that, in all APEC economies, significant population subgroups are excluded from access to the services of formal financial institutions. It argued that providing such access would bring economic benefits, both in terms of aggregate economic efficiency and in terms of interpersonal equity and equity between households. The paper examined the distinction between microbanking and microfinance, concluding that the latter is a subset of the former and primarily applicable to the developing economies, rather than representing a solution to the generalized problem of financial exclusion.

The paper then discussed the different forms that microfinance has taken in a wide range of institutional settings in developing economies within the APEC region. After this it examined alternative financial service delivery systems that have developed in a representative advanced APEC economy, Australia, and which are likely to have analogues in other such industrial economies in which financial exclusion persists.

This paper has argued that Mexico made a promising beginning by introducing issues of microbanking and microenterprise development to the APEC agenda in 2002. Mexico secured the endorsement of the APEC Ministerial Meeting for a comprehensive statement of principles on microbanking development, regulation and supervision, which was paralleled by a comprehensive endorsement of microfinance as a measure for microenterprise development by the APEC Ministers responsible for SMEs. It also introduced the concept of financial exclusion into the APEC vocabulary. These advances signaled the acceptance by APEC economies of the need for financially-inclusive policies.

Thailand's championing of specialized financial institutions in APEC the following year may have reduced the momentum for reform. However, the process continues, with other APEC forums, including the SME process and

²⁴ See footnote 22.

a specially-constituted Sub-Group on Micro-enterprises, currently providing the locus of activities for the reduction of financial exclusion as it affects the populations of APEC economies. However, these forums suffer from impediments, in terms of their capacity to address the issues effectively. Among these is their lack of a comprehensive financial sector development philosophy. Further progress within APEC towards the elimination of financial exclusion would be assisted by cross-sectoral cooperation, to which the resources of the APEC Finance Ministers' process should be committed.