

ACCELERATING MSME CREDIT PENETRATION IN THE PHILIPPINES: A DIGITAL TRANSFORMATION IMPERATIVE

by Paramdeep Singh

According to the Philippine Statistics Authority, MSMEs make up over 99% of registered businesses in the country, contributing to 65.10% of the country's total employment.

Sheela Dantes*, a resident of Manilla has a small tailoring factory which employs 17 people. She sells these clothes to small distributors around the town and gets paid partly in cash and partly in her bank account. Sheela suddenly gets a huge order and needs working capital to buy the materials. She goes to a nearby bank for a loan.

Unfortunately, she does not have a credit history and cash flow projection documents. Without them, it would be impossible for the bank to decide her creditworthiness and approve a loan. Her only resort now is to go to a loan shark. The Philippines has an estimated 15 million informal entrepreneurs and self-employed workers like Sheela, consisting of a massive pool of would-be borrowers with little access to traditional finance.

According to the Philippine Statistics Authority, MSMEs make up over 99% of registered businesses in the country, contributing to 65.10% of the country's total employment. Their significant presence underscores the potential for financial institutions to tap into a vast market and support the diverse needs of MSMEs.

Challenges Faced by Banks in Providing MSME Loans

While the MSME sector presents a lucrative opportunity, banks encounter several challenges in extending credit to these businesses:



Credit Risk Assessment: MSMEs often lack a robust credit history, making it challenging for banks to assess their creditworthiness. Traditional credit scoring models which rely on the underwriter’s knowledge of the firm, the industrial sector, the market and/or the economy may not adequately capture the risk associated with these enterprises



Limited Financial Documentation: MSMEs, especially micro and small enterprises, may need more financial documentation to be able to qualify for the traditional lending process that heavily relies on comprehensive paperwork



Collateral Requirements: Banks typically require collateral to mitigate risk. MSMEs, especially startups, may struggle to provide the necessary collateral, limiting their access to credit



Higher Reject Rate: Incomplete collateral, information or missing credit history can lead to higher rejection rates



High Operational Costs: The manual processing of loan applications contributes to high operational costs for banks. This cost factor can be prohibitive, particularly when dealing with smaller loan amounts

An MSME in the Philippines has to typically provide 10 to 15 documents and then wait for anywhere from 3 days to a week for a credit decision. On the bank side, an underwriter faces challenges like access to qualified and complete data, repetitive manual processing of the loan, human error and more.

Digital Onboarding and Loan Origination for Enhanced Inclusion

Account opening for MSMEs in the Philippines can take anywhere from a few days to a few weeks and involve at least 10 unique documents. This can be quite overwhelming for someone starting a new business or applying for a loan for the first time. From a bank’s perspective, it also creates a barrier to entry. Advanced Digital Engagement Platform makes the entire onboarding process hassle-free and seamless.

MSMEs can upload their documents on the bank’s app or net banking, start, pause and restart anytime. The back-end engines perform KYC, liveness check, risk Digital Onboarding and Loan Origination for Enhanced Inclusion categorisation, and partner and member validation, all in real time. The entire process can be shortened from days to minutes. What’s unique is that banks can modify the onboarding process to suit their requirements without any coding knowledge in a few hours. This is made possible due to the no-code enterprise integration technology driving the platform.

Further, the loan origination process can be simplified as well to introduce seamless processes, guided workflows and reduced paperwork. Below is a checklist of must-have features in a Loan Origination Platform.

FEATURE CHECKLIST FOR A LOAN ORIGINATION PLATFORM



OMNI-CHANNEL ORIGINATION

- Customer Initiated/ RM Assisted journeys
- Drop-in drop-off alternating across channels



DIGITAL DATA AGGREGATION

- Interface-led data aggregation
- Structured and unstructured data sources



DOCUMENT MANAGEMENT

- End-to-end document lifecycle management
- Customised template generation
- Zero-touch Documentation enabled by digital signatures



API-BASED ORIGINATION

- Collaborate with Fintechs
- Scale-up volumes with zero-touch processing



AUTO ADJUDICATION

- Integrate and fetch risk scores from existing risk models
- Automated scoring, deviations, affordability computation



AUDITABLE CONVERSATIONS

- Ad-hoc deviation & exception approvals
- Consultative decision-making Single source of referral and decision trails

Leveraging Alternate Data for Informed Decision-making

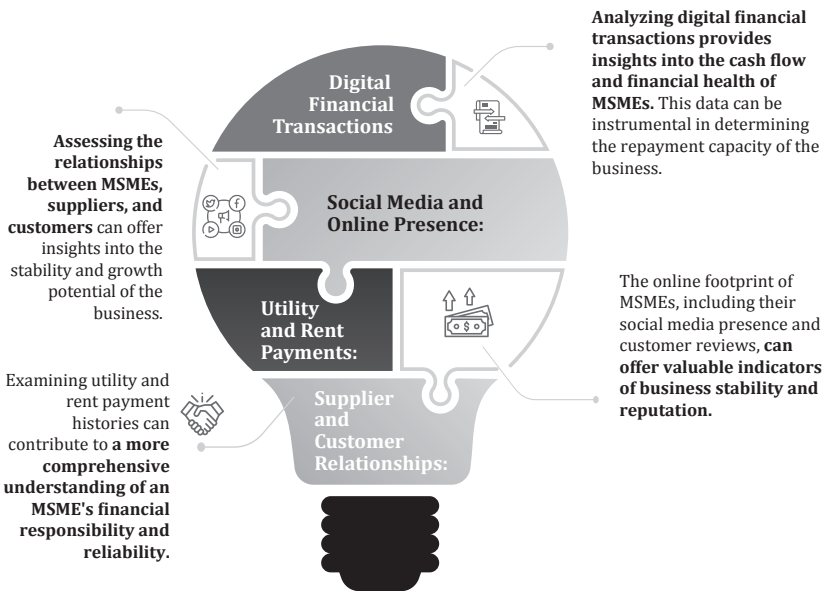
For a bank to ascertain creditworthiness, they need data which is recent, harmonised and validated. Most MSMEs in the Philippines don't have extensive credit histories and traditional documentation. In such cases, banks can turn to alternate data sources to assess the creditworthiness of MSMEs.

Alternate data includes non-traditional information such as online transactions, social media activity, telecom data and payment behaviours. Leveraging alternate

data broadens the scope of information available to banks, enabling a more holistic assessment of MSMEs.

Open Finance for Enhanced Credit Disbursal

Open finance involves the sharing of financial data between different financial institutions through secure application programming interfaces (APIs). This concept empowers MSMEs by giving them control over their financial data and allows banks to make more informed lending decisions based on a comprehensive financial picture.



ADVANTAGES OF OPEN FINANCE FOR MSMEs



HOLISTIC FINANCIAL ASSESSMENT: Open finance enables banks to access a broader set of financial data, providing a more holistic view of an MSME's financial health. This includes data from various banking and financial accounts



FASTER DECISION-MAKING: With real-time access to financial data, banks can make quicker and more informed credit decisions. This is especially valuable for MSMEs that require timely access to funds for business operations



CUSTOMISED FINANCIAL PRODUCTS: Open finance facilitates the development of personalised financial products based on the unique needs and financial behaviours of MSMEs. This can lead to more tailored and accessible credit solutions



IMPROVED RISK MANAGEMENT: The comprehensive financial data available through open finance allows for more accurate risk assessment, reducing the likelihood of defaults and improving overall risk management for banks

While banks in the Philippines are not fully convinced about the benefits of Open Finance, a leading banker in the Philippines says “ When Credit Bureaus came in the Philippines 15-20 years ago, banks were apprehensive about them. We are now realising that even large banks are benefitting from sharing data with these credit bureaus. The same is the case with Open Finance”.

Generative AI in Credit Disbursal

Generative AI, a subset of artificial intelligence, plays a transformative role in credit disbursal for MSMEs. By utilising advanced algorithms, generative AI can analyse vast datasets, identify patterns, and make predictions, enhancing the efficiency and accuracy of credit decision processes.

GENERATIVE AI-BASED CHATBOT USE CASES IN LENDING



Loan Servicing

- Assist borrowers with account management, billing questions and payment reminders etc.
- Generate personalised loan servicing strategies to improve customer satisfaction



Debt Management

- Real-time monitoring and proactive debt management
- Personalise the customer collection experience through behavioural science
- Improve agent efficiency with intelligent workload distribution



Underwriting

- Auto-generate sections of credit memos such as the executive summary, business description, and sector analysis to speed up the underwriting process

- Allow customers to access their e-files and pose questions on underwriting results (correct any inaccurate data or offer additional relevant information)



Credit Decisioning

- Analyse consumer credit ratings and financial histories to determine creditworthiness
- Assess data from a variety of sources to gauge the riskiness of a loan application
- Sentiment analysis and financial scenario generation

Conclusion

Accelerating MSME credit penetration in the Philippines is not merely a financial imperative; it is a catalyst for economic growth and empowerment. The convergence of digital onboarding & loan origination, alternate data utilisation, streamlined credit checks, open finance, and generative AI offers a transformative pathway for banks to tap into the vast potential of the MSME sector. By embracing these technological advancements, financial institutions can not only overcome the challenges associated with MSME lending but also foster a more inclusive and dynamic financial landscape for the businesses that form the backbone of the Philippine economy.

Banks can leverage a powerful combination of iGCB's award-winning Digital Engagement Platform and iKredit360 to offer an end-to-end digital credit experience to SMEs. The combination can help banks reduce onboarding and loan disbursement time, make faster and more informed credit decisions, reduce operational costs, manage risks proactively and collaborate with multiple fintech partners to originate loans from multiple channels.

Built on eMACH.ai (Events, Microservices, API, Cloud, Headless & AI) and both these platforms come with a country-ready marketplace, giving banks the capability to create and curate SME credit experiences for their unique set of customers.