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Center for Microfinance

The microfinance sector in Bangladesh: Innovation or Stagnation.

BA Thesis in Banking and Finance

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Bangladesh has been known as the birthplace of microfinance, and competition has markedly increased during the last decade. However, the microfinance industry is only just now beginning to put mechanisms in place that will advance commercialization and innovation. As the MFI-sector's apex wholesaler played an important role with regard to the rapid growth of the sector during the 1990’s, it will now be necessary to reduce these cheap, subsidized funds.

The "Microcredit Regulatory Act", enacted in 2006, could help prepare large and middle-sized MFIs to transform into formal financial institutions and to integrate into the formal financial sector, but at present, it is still nascent and the newly established Microcredit Regulatory Authority will need to build its own capacity before the law can be extended. In addition, the MRA must further the interests of *both large and small* microfinance institutions - which were virtually unregulated during the last three decades - in order to gain their universal acceptance.

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Full Text Version

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List of Acronyms

ASA	Association for Social Advancement
BIDS	Bangladesh Institute for Development Studies
BRAC	Bangladesh Rural Action Committee
BRDB	Bangladesh Rural Development Board
CDF	Credit and Development Forum
CGAP	Consultative Group to assist the Poor
CIB	Credit Information Bureau
G8	Group of Eight
GNI	Gross National Income
GOB	Government of Bangladesh
IGA	Income Generating Activities
MFI	Microfinance Institution
MIX	Microfinance Information eXchange
MRA	Microcredit Regulatory Authority
NGO	Non-Government-Organization
NGOAB	NGO Affairs Bureau
PKSF	Palli Karma Sahayak Foundation
PO	Partner Organization
RLF	Revolving Loan Fund
SME	Small Medium Enterprise
USAID	United States Agency for International Development

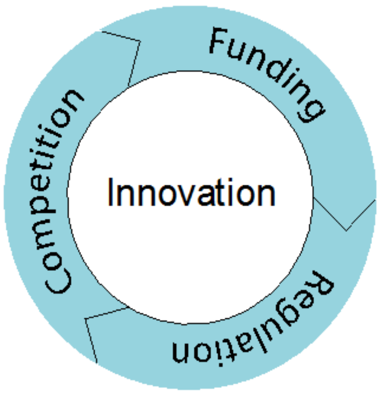
1. Introduction

This paper assesses the state of the microfinance sector of Bangladesh. The question this paper deals with is if the microfinance industry of Bangladesh is innovative, or if there are obstacles in the way that inhibit the development of innovative products.

In order to approach this complex issue, this paper examines the basic prerequisites for innovative product development in the microfinance industry of Bangladesh. Therefore it focuses on the state of the three cornerstones of innovation, i.e. funding of microfinance, regulation & supervision and competition and their implications on innovative microfinance product development.

From the literature the following context can be derived:
Commercialization of microfinance includes the application of market-based principles to microfinance (Rahman / Charitonenko, 2002). It is widely believed that only through achievements in sustainability are MFIs able to reach great levels of outreach and accommodate demand through innovative product development. Financial sustainability implies turning away from donor grants and making use of commercial funding sources, such as retained earnings, equity investments, bank loans or clients' deposits. Without proper regulation, MFIs are not allowed to collect deposits from the general public, and banks will only lend to financial institutions which are subject to financial monitoring and reporting using standardized accounting (Conroy / McGuire, 2000). As the market matures and is more and more saturated, competition among MFIs intensifies, resulting again in the development of innovative microfinance products (Mahmoud, C. et al, 2009).

Fig. 1: Funding, Regulation & Supervision and Competition in the Context of Innovation



Source: Author

The first section provides a brief overview of the microfinance sector of Bangladesh. Second, it introduces the main microfinance players in the industry and their microfinance products. Third, it deals with funding issues of microfinance and looks at the funding sources for MFIs in Bangladesh. Fourth, it looks into the regulatory environment of microfinance. Fifth, it analyzes the competitive environment in the microfinance sector and the sixth section concludes.

2. Introduction to the Microfinance Industry of Bangladesh

2.1 Country Indicators

Bangladesh, with a total population of almost 160 million, is one of the world's most densely populated countries'. In 2006, nearly half of the population was living under the national poverty line, i.e. earning less than $1 per day. The GNI per capita (Atlas method, US$) for 2008 was at $520, compared with $986 for South Asia (Bangladesh at a glance, 2009). The literacy rate for Bangladeshi adults was 47%, compared with 58% for South Asia, and life expectancy at birth was 64 years in 2007. The country's poverty has various dimensions which are apparent in terms of inequality in income distribution, dramatic increases in the cost of living, malnutrition by the vast majority of the population and unemployment and internal migration. The United Nations Human Development Programme (UNDP) ranked Bangladesh 139th out of 177 countries in 2005 measured by the Programme's Human Development Index (Bangladesh Microfinance Country Profile, 2006).

2.2 The Microfinance Sector in Bangladesh

The Author divides the development of the microfinance sector in Bangladesh into four phases since the mid-70's on the basis of Zaman (2004):

1) Action research phase in the 1970's
2) Microcredit development phase in the 1980's
3) Expansion phase in the 1990's
4) Increased competition and formalization from 2000 onwards.

Action research phase in the 1970's

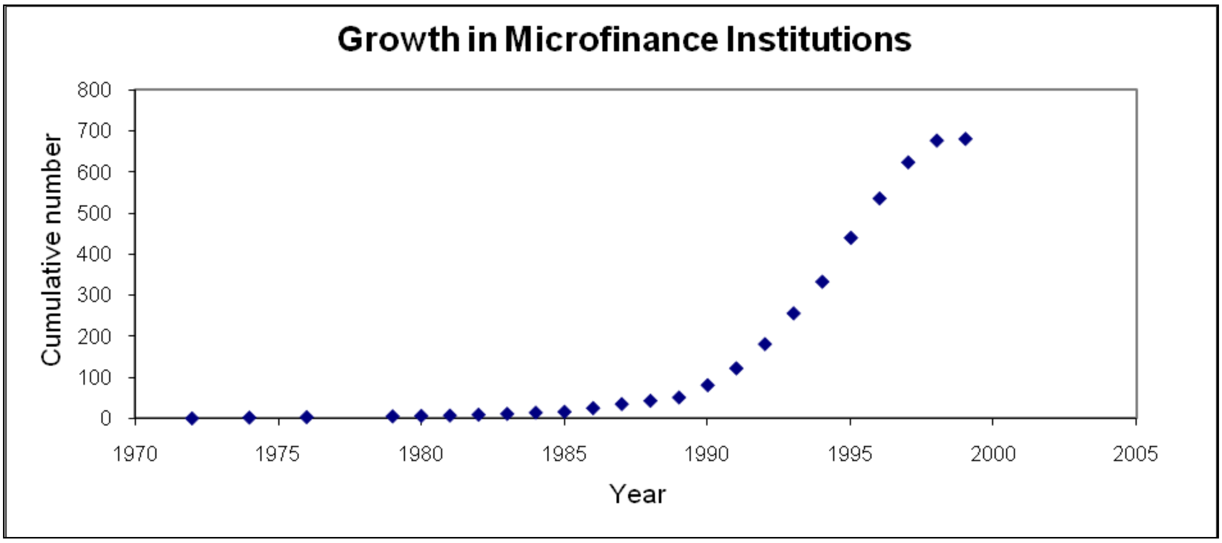
Right after Bangladesh's independence war in 1971 the country was in a condition of devastation. Since the new government was unable to cope with the scale of destitution, a number of NGOs emerged to confront the challenges (Zaman, 2004). The independence movement led to a new generation of young activists who were devoted to the reconstruction of war-ravaged Bangladesh. Hence, the early years of NGO activities focused on relief and rehabilitation, with an emphasis on community development (Microfinance industry report: Bangladesh, 2009). Besides that, the main emphasis was on health, literacy, agricultural development programs and food relief programs. The focus was not yet particularly on microcredit. The mid 1970's though can be seen as the hour of birth of microcredit in Bangladesh, when a team of researchers at Chittagong University, led by Prof Yunus, began an action-research program, known as the 'Jobra' experiment, which provided loans to poor households in a few villages (Zaman, 2004). The team used a solidarity group-based delivery system using peer pressure and group guarantee to ensure timely repayment. After some trial and error the 'Grameen Project' proved highly successful and its success eventually paved the way for the establishment of the Grameen bank under a special ordinance in 1983. To this day the Grameen Bank remains the only bank with a poverty alleviation bank license (Microfinance industry report: Bangladesh, 2009). This full-fledged banking license allows Grameen to collect deposits not only from its members but also from the general public. Grameens microcredit activities also inspired other NGOs to try out different kinds of microcredit schemes, and soon microcredit became a part of almost every social development NGO (Ahmed, 2004).

Microcredit development phase in the 1980's

This trend of active NGO development continued, and in the 1980's, NGOs began to put a much greater emphasis on the development of their microcredit programs (Microfinance industry report: Bangladesh, 2009). Donor grants were available on a grand scale contributing to the creation of Revolving Loan Funds (RLF), i.e. funds to lend out to MFI members for income generating activities. The orientation towards microcredit was remarkable and some NGOs, ASA the most prominent, decided to turn away from their social and community development work and to concentrate solely on microfinance (ASA 2009a).

Expansion phase in the 1990's

Figure 2: Expansion of MFIs in the 1990's



Source: Ahmed (2003)

The 1990's was characterized by an extremely fast-paced and large-scale expansion of microfinance activities by MFIs, using the Grameen-style microcredit approach (Ahmed, 2003). Figure 2 depicts this trend. As Stuart Rutherford pointed out to the author (Interview Rutherford, 2009), originally, the microfinance pioneers at Grameen and BRAC believed that their loans would be assigned to small businesses run by women, so that these women could use these loans to get out of poverty. In fact, their micro credit had a much wider appeal than that: the debtors could repay these loans with very small weekly installments, so that most households could afford to make the payments, irrespective of how the borrowed money was spent. Thus, those households which had businesses and which reinvested the loans into their businesses were doing quite well, but also lots of other families who didnt run own businesses could use these loans for all kind of investment (marrying, housing, etc). As a result the Grameen-style credit approach (small loans with very small weekly repayment amounts) became very popular, and families all over the country took advantage of the idea.

Considering the size of the country and the percentage of population living under the poverty line, there was a huge market to serve. That's why the MFI's growth strategy was based on a 'franchising approach', where new branches replicated the procedures of existing branches and offered primarily a standardized microcredit product to all clients, making it easier to recruit new staff and train them quickly in a simple product, thus enabling the MFIs to open new branches at a rapid rate (Zaman, 2004).

In 1990, the Palli Karma-Sahayak Foundation (PKSF) was established (PKSF, 2009a). The PKSF is financed by the government and the World Bank and acts as apex wholesaler. Its inception stimulated the even faster growth of MFIs, since now they had the benefit of relatively low cost refinancing. Additionally, the PKSF provides NGOs with technical assistance to enhance their institutional infrastructure and management information systems – a prerequisite for expanding outreach, improving efficiency, increasing self-sufficiency and reducing dependence on grants other than PKSF (Microfinance industry report: Bangladesh, 2009).

This rush towards winning new clients led to approximately ten million new microfinance clients becoming members of a microfinance program (Armendariz / Murdoch, 2005). The microfinance sector was well established with the “Big Four” namely, Grameen Bank, ASA, BRAC and Proshika and a multiplicity of small and very small NGO-MFIs, most of them pursuing the standard Bangladeshi plan: group credits, with an emphasis on women, and weekly group meetings and repayment modalities.

Increased competition and formalization from 2000 onwards

By the end of the 1990’s the microfinance sector plunged into a repayment crisis that took Grameen Bank’s reported repayment rates from above 98% to below 90% (Armendariz / Murdoch, 2005). This crisis was due to the explosive growth of the Big Four which led to overlending and multiple memberships (“overlapping”) of their clients with more than one MFI, and it was aggravated by the nationwide floods in 1998 and by the tailing off of donor grants. As Rutherford (Interview, 2009) stated, this led Grameen to rethink its position and was a key moment in product development in Bangladesh. Not only did Grameen get rid of some inflexibility, but other MFIs began offering a wider array of services and products.
NGO-MFIs in Bangladesh were barely regulated from the time of their emergence until recently. When competition within the microfinance sector intensified in the late 1990’s and donor funds became less available to the MFIs, many MFIs started offering voluntary and open access savings accounts to their clients. This led to a growing concern among most policy makers and stakeholders of the industry and it became clear, that under these circumstances the sector would have to be regulated in some way (Conroy / McGuire, 2000). As a result, in 2006 the Government of Bangladesh established the Microcredit Regulatory Authority (MRA) under the newly passed “Microcredit Regulation Authority Act”, a

regulatory framework that all Bangladeshi MFIs have to follow which have with microcredit operations (MRA, 2009a). The MRA will be responsible for the enforcement of the act and will have the power to prepare detailed rules related to the operations of MFIs. The possible implications of the MRA Act on the microfinance sector are discussed later in this paper.

3. Suppliers and Microfinance Products

The principal microfinance service providers (MFIs) in Bangladesh are usually categorized into four major groups: MF-NGOs, specialized institutions, commercial banks with microfinance programs and administrative ministries or divisions (Bangladesh Microfinance Country Profile, 2006). Since the enactment of the "Microcredit Regulatory Act 2006", 4236 MF-NGOs which had microcredit operations before the enactment of the Law applied for licensing by the Authority (An Overview of NGO-MFIs in Bangladesh, 2009). Although there are thousands of MF-NGOs throughout the country offering micro credits, many of them are very small in loan portfolio or number of borrowers, and the majority of micro credit clients are being served by four huge MFIs, namely Grameen Bank, BRAC, ASA and Proshika. The World Bank estimates that in 2005 the four institutions combined account for 86% of all active borrowers and over 90% of all outstanding loans in the Bangladesh Microfinance sector (Bangladesh Microfinance Country Profile, 2006).

Credit Products

Microcredit in Bangladesh is used for individual and group activities. Borrowers are not required to provide any collateral. There is a range of different types of loans including general loans, program loans, housing loans, etc. General loans are used for different kind of income generating activities, such as rural trading, transport, paddy husking, food processing, small shops, and much more. Loans usually range between $15 and $160. If borrowers repay their loan on time, they can usually take a larger follow-up loan (Bangladesh Microfinance Country Profile, 2006).

Program loans are available for group members who take up activities in poultry, livestock, agriculture, sericulture or fisheries. MFIs provide these groups with training, technical assistance and inputs. There is a variety of credit, such as micro enterprise credit services, emergency credit, disaster credit, sanitary latrine credit, etc.

Savings

Savings have been introduced around the turn of the century by a growing number of MFIs (Wright, G. A. N. et al, 2001). Meanwhile, client savings contribute increasingly to MFIs

RLF. According to the CDF, a national networking organization working with a multitude of MFIs, in 2006 member savings made up 29% of the MFIs RLF (Awal, 2006).

Savings products available in the microfinance sector of Bangladesh consist of mandatory savings as quasi-collateral against member's default when they take a loan, special savings, contractual savings, time deposits, and daily savings. As de Aghion and Morduch (2004) point out, there is a trend to shift from an emphasis on the compensatory savings toward voluntary and open access savings.

MFIs in Bangladesh mostly offer 5-6% interest on deposits from members, and only a few offer more than 7%, the most prominent being Grameen Bank who offers interest rates between 8.5% and 12% (Bangladesh Microfinance Country Profile, 2006).

Insurance

Bangladeshi MFIs have become increasingly interested in insurance products. There are various kinds of products offered, i.e. health insurance, credit insurance, property insurance, crop insurance, etc. The most essential to poor borrowers though is loan/life insurance. For poor borrowers in Bangladesh it is particularly important that they don't burden their relatives with outstanding loans in the case of their death. Loan/life insurance covers the outstanding loan amount of a client in case of the client's death. This provision makes the insurance very popular among poor borrowers (Rutherford, 2004).

Group-based lending

The main feature of Bangladeshi microfinance is the provision of loans without demanding traditional collateral as security. This has been successfully dealt with through the application of group-based lending technologies (Microfinance industry report: Bangladesh, 2009). Morduch looks into basic mechanisms of group lending technology and asserts that group lending can not only help micro lenders overcome adverse selection problems, but that it can also potentially mitigate ex ante and ex post moral hazard problems as well, through peer monitoring by fellow group members (de Aghion / Morduch, 2004).

3.1 Grameen Bank

The Grameen Bank was established in 1983 under a special law with the initial support from the Bangladesh Bank. It is the only MFI that has been awarded a license to operate as a special bank for microfinance. All the other MFIs are NGOs that are registered with the NGO Affairs Bureau (NGOAB) and now with the MRA (Microfinance industry report: Bangladesh, 2009).

Grameen's poor borrowers own 95% of the bank's total equity (Grameen Bank, 2009a). The remaining 5% is owned by the government. According to the MIX Market, a leading microfinance platform[1], as of December 2008 Grameen Bank was the second largest MFI in Bangladesh with an outstanding loan portfolio of 642 million Dollars and 6.2 million active borrowers, of which almost all of them (97%) are women (Mix Market, 2009a). Grameen claims to be fully financially sustainable. It takes no donor funds, nor does it take any loans from local or external sources, and finances its credit program solely through its clients deposits, which amount to 142% of its outstanding loans. The bank, which operates with 2'560 Branches in nearly 85'000 villages, has a loan recovery rate of 98%. The bank's net income after taxes amounted to 19 million Dollars in 2008. In 2006 Grameen Bank and its founder, Dr Mohammed Yunus, were awarded the Nobel Peace Prize "[…] for their efforts to create economic and social development from below." (The Nobel Prize, 2009).

With regard to Grameen Bank's stated recovery rate, it must be taken into consideration that due to its regulatory status, which is similar to those of banks, it is subject to standard portfolio risk classification for loan losses and write offs that are weak and not appropriate for microfinance operations (Rahman / Charitonenko, 2002). For example, provisioning is made for 100% for loans overdue more than two years, and they are only wholly written off once they are three years past due (Rutherford, 2004). Microfinance loans usually are shorter-term loans than those of commercial banks, and if Grameen Bank would adapt its provisioning policy to microfinance standards, its recovery rate would most likely be lower than the stated 98%. This issue not only affects Grameen Bank but also all other MFIs, because up until the enactment of the MRA Act, the MFIs had not stood under any regulatory regime. It will be interesting to see if the MRA will impose binging standards with respect to the provisioning of overdue loans and how this would affect provisionary costs of MFIs.

1 See http://www.mixmarket.org

Another prevailing issue is the number of borrowers in Bangladeshi MFIs. As Rutherford (2006) lays out, many MFIs don't distinguish clearly between active borrowers, members or even lapsed members. This leads to the exaggeration of reported microfinance clients by MFIs.

Group membership

In order to become a member of Grameen and be eligible for a loan, potential borrowers need to join a group. Loan contracts are made in the name of individuals, but the group is an essential mechanism in the delivery and recovery process. Grameens group based lending methodology was copied all over the country by the majority of MFIs and is still the predominant credit delivery method in the Bangladesh microfinance sector (Microfinance industry report: Bangladesh, 2009), although in recent years a growing number of MFIs have started to offer individual loans without the requirement of joining a group (Interview Rutherford, 2009).

As Prof Yunus, founder of Grameen Bank, once explained to Morduch and Rutherford in 2002, Grameen never practiced joint liability in a way that would make group members responsible for paying on behalf of a defaulting member. However, he acknowledges that field staff may nevertheless use these practices occasionally (Rutherford, 2004). Today, on its website, Grameen states that, although there is no group-guaranty or joint liability, its loan conditionalities include "[…] stress on credit discipline and collective borrower responsibility or peer pressure." (Grameen Bank, 2009a).

Product delivery - the Kendra

Typically, six to ten groups, each consisting of five members, meet weekly at the *kendra* (Centre) at the village. The Kendra is the forum for discussing all matters related to the clients' membership, financial or non-financial, and most bank transactions take place at the kendra meeting, which is attended by a bank worker. Weekly meetings are mandatory for all clients, and if a client frequently fails to attend the meeting or to pay his loan, this can not only have an impact on the timely issue or value of his loans, but also on those of his fellow group members (Rutherford, 2004).

Products

The following section is based on Rutherford (2004), who lays out the main product features of the Grameen Bank.

Grameen Bank offers a *basic loan* with flexible terms regarding duration, timing of the loan, scheduling and size of installments. It offers a *flexi loan* which is a rescheduled basic loan with special conditionalities, *bridge loans* for borrowing beyond the normal loan ceiling if the client has a high enough savings balance, *loan/life insurance* which pays for the entire outstanding amount in case of the client's death as well as several other loan types, such as *housing loans*, *special investment loans* and *education loans* for its members' children. It also offers loans to *beggars* with no interest rate.

Grameen Bank has three types of savings accounts. When clients take a loan, part of the loan goes into the clients' *personal savings account* and part into its *special savings account*. Clients may withdraw from their personal savings account, but are only allowed to withdraw from their special savings account under certain conditions.

Grameen Bank offers a *pension deposit account* to its members. After ten years, clients receive a guaranteed amount that is roughly double the amount they put into the account over the years. In addition, every borrower with loans above Tk 8'000 must make obligatory deposits in their pension deposit account. Grameen also offers savings devices for non-members, such as fixed deposits, the "Doubling in 7 years" product and a "Monthly income Deposit". The exact products and terms can be found in Appendix 1 at the end of this paper.

3.2 ASA

ASA was founded in 1978 and received formal registration from the government in 1979. Its primary objective was to help the poor organize & empower themselves so that they would establish their political and social rights for a just society. During this time, the members of ASA conducted a series of social actions to fight against social injustices, gain their rightful access to institutional and public resources, obtain just wages, enter into the local power structures and have access to land (ASA, 2009b). In the mid-80's ASA realized that in order to be able to assist the poor more effectively, it would have to get into the business of microcredit. By 1992 it focused solely on microfinance. ASA is registered as a non-profit social-welfare organization under the Societies Act and remained an NGO throughout its existence (Rutherford, S. et al, 2008). ASA has built a reputation as a cost effective and super efficient microfinance institution (Wright, G. A. N. et al, 2001). It claims to be self-reliant since 2001 when it moved away from depending on donor funding and grants. According to the MIX Market (Mix Market, 2009b), ASA is the third biggest MFI in Bangladesh, with an outstanding loan portfolio of 454 million Dollars and 5.9 million active borrowers in 2008. It works in 71'200 Villages throughout 3'300 Branches in all Districts of Bangladesh with a total of nearly 25'000 employees. For 2008, ASA reported its net income after tax to be almost US$ 43 million.

Product delivery

ASA operates a credit delivery and recovery system that is similar to the version of the Grameen Bank's group-based lending methodology. ASA's members form and join groups as well and meet weekly at the Branch office, the center of providing financial services. Loan terms and repayment schedules are fixed and non-negotiable (Rutherford, S. et al, 2008). Unlike Grameen Bank, ASA does not have an option for overdue clients to reschedule their loans. As Rutherford, S. et al (2008) point out, ASA puts pressure on recovering outstanding loans on time from each member, and it can occur that loan officers use techniques that come close to social collateral, similar to what we have seen at Grameen Bank.

Products

ASA's core product has been its small standardized loan since ASA began operating microfinance in 1992 (Rutherford, S. et al., 2008). It offers a wider range of other loan products, including loan/life insurance. Alike Grameen Bank, ASA offers voluntary, mandatory and long term savings. The exact products and product terms are listed in Appendix 2 at the end of this paper.

3.3 BRAC

BRAC was founded as a relief organization in 1972 after the liberation of Bangladesh (BRAC 2009a). It initially helped refugees returning from India and soon broadened its focus to long term sustainable poverty reduction. Its holistic approach to poverty alleviation and empowerment of the poor include a range of core programs in economic and social development, health, education, and human rights and legal services. Today, BRAC employs more than 115,000 people, the majority of which are women, and reaches more than 110 million people with its development interventions in Asia and Africa. BRAC had 6.3 million active borrowers and an outstanding loan portfolio of 648 million Dollars in 2008 and was listed as the biggest MFI at the Mix Market both in terms of borrowers as of loan portfolio size. It operates in 69'500 villages throughout 2705 branch offices and the average net income after taxes from 2004 to 2007 was US$ 14.6 million (Mix Market, 2009c).
BRAC's major development programs comprise its Economic Development Program, Health Program, Education Program, Social Development Program, Human Rights & Legal Services, Disaster Management and Environment & Climate Change (BRAC, 2009b). The paper focuses on its microfinance operations within the Economic Development Program.

Product delivery

Like Grameen Bank and ASA, BRAC uses the group-based lending-methodology as well. According to its website, BRACs approach differs from that of other institutions in the way that they utilize a "[…] credit-plus approach where loans are accompanied by various forms of assistance for the borrowers, such as skills-training, provision of higher quality inputs and technical assistance as well as marketing for finished goods." (BRAC, 2009c).

There are two different microfinance products: microloans (group-based, exclusively for women) and microenterprise loans (individual loans for both men and women). For each of these products there are three different schemes: Dabi, Unnoti, and Progoti. Group based small loans are particularly designed for the lower end poor. Microenterprise loans are aimed at small entrepreneurs for expanding their businesses.

BRAC organizes its members into so-called “village organizations” (VO) of 30- 40 women. These VO’s gather regularly for meetings and address their financial or non-financial matters. BRAC encourages its members to use its credit facilities to start new enterprises or expand existing ones and as they increase their business, they become eligible for larger loans.

Products

- Dabi

Dabi is BRACs core microfinance product. It is aimed at poor landless women and provides access to microloans and savings schemes. As of 2008, a vast majority of BRACs microfinance clients were Dabi members. The average loan size in 2007 was $121, and interest rates have remained at 15% flat (BRAC, 2009c).

- Unnoti

Unnoti provides financial services to small and marginal farmers who own more than one acre of land. Loan sizes range between US$ 147-735 and interest rates are 15% flat (BRAC, 2009c).

- Progoti

Progoti provides financial services to the “missing middles”. These are small entrepreneurs who won’t get a loan from commercial banks and at the same time aren’t targeted by microfinance programs because they do not fall into the category of landless poor. Progoti provides larger loans to BRAC and non-BRAC micro entrepreneurs. Interest rates are 15% flat.

3.3.1 BRAC Bank

BRAC holds a share in a number of related institutions, among others in BRAC Bank Limited. BRAC Bank is a full-scale commercial bank and was constituted in 2001. It focuses on perusing market niches in the Small and Medium Enterprise (SME) sector of Bangladesh, where it offers collateral-free loans to its clients (Brac Bank, 2009a). Alike Grameen Bank, ASA and BRAC, repayment rates at BRAC Bank are very high as well, with reported 98% (The Financial Express, 2009a). BRAC bank is owned by BRAC, International Finance Corporation (IFC) and Shorecap International and is listed in the Dhaka and Chittagong Stock Exchange (Brac Bank 2009b).

At the end of 2007, BRAC bank's outstanding loan portfolio amounted to approximately US$ 470 million (Brac Bank 2009c). Its net profit for the year was about US$ 5.4 million. According to different definitions of microfinance services, BRAC Banks' products cannot be viewed as microfinance products. The Mix Market employs a functional definition of microfinance and draws the line where the average balance of microfinance services doesn't exceed 250% of the average GNI per capita (The Mix 2009a). As stated by the World Bank, the GNI per capita in Bangladesh is $470 (Bangladesh at a glance, 2009). Mahmoud, C. et al. (2009) too, state that microloans above Tk 30'000 (approximately $440) differ from income generating activities (IGA) and fall into the category of microenterprise loans. Since the collateral free loans offered to SME's throughout the country range between $4'500-$15'000, and also retail products require clients to receive relatively high salaries (see Apendix 3), BRAC bank's products are not regarded as microfinance products. Rather, BRAC Bank's operations are aimed to the "smaller end" of the small enterprise sector (Zaman, 2004). As Rutherford pointed out to the author though, BRAC Bank has been lending funds to MFIs, acting as a microfinance wholesaler (Interview, 2009).

BRAC Bank's network has grown to 26 branches, 376 SME unit offices, more than 1,000 remittance delivery points, 28 ATMs and 5 Cash Deposit Machines across the country (Brac Bank, 2009a). The bank's customer base also expanded to 300,000 deposit accounts and 75,000 advance accounts in 2006.

Because BRAC Bank Limited is not an MFI, this paper won't go into any more details at this point. Appendix 3 provides an overview of the banks' banking products.

3.4 Proshika

Proshika is listed the fourth biggest Bangladeshi NGO-MFI at the Mix Market, with a bit over 1.7 million active borrowers and an outstanding loan portfolio of US$ 58 million (Mix Market, 2009d). It was founded 1975 and received formal registration one year later (Proshika, 2009a). Like Grameen, and BRAC, Proshika is active in various fields, such as Peoples Organization Building, Education, Training, Health, Legal and Aid Services, Environmental Protection and Microfinance with the objective of human development and empowerment of the poor (Proshika, 2009b). Up to December 2007, Proshika covered over 24'000 villages, providing loans to over 4.2 million borrowers. Proshika is not financially sustainable. According to the information provided the Mix Market, donor funds at the end of the 1990's amounted to an average US$21 million per year and Proshika was earning an average of US$19 million (including donations) (Mix Market, 2009e). In recent years, Proshika had to scale-down its microcredit operations due to continued blockage of donor funds by the government, after the government accused Proshika of alleged political alignment with the opposition party (Bangladesh Microfinance Country Profile, 2006). In 2007 it received a little more than US$ 2 million in donations and was running its microfinance activities with a deficit of over US$ 4 million (Mix Market, 2009f).

3.5 SafeSave

In Chapter 3.1- 3.4 we have viewed the four largest MFI's in Bangladesh in terms of number of clients and gross loan portfolio. These four, and most other Bangladeshi MFI's, are characterized by the strict conditions imposed upon their clients. For example, if clients of Grameen Bank take out a loan, they are required to deposit a percentage of that loan in an obligatory savings account (Rutherford, S. et al, 2004). ASAs product terms and repayment schedules are fixed and non-negotiable (Rutherford, S. et al, 2008). As mentioned before, with Grameen Bank as well as ASA and BRAC and most other Bangladeshi MFIs, the group based lending methodology as well as an emphasis on women borrowers remains the predominant credit delivery method in Bangladesh.

Safesave's approach to microfinance product delivery however is fundamentally different. Its success makes a closer look at its products and product delivery system all the more indispensible.

SafeSave was co-founded in 1996 by Stuart Rutherford, a microfinance enthusiast and Rabeya Islam, a Dhaka housewife with years of experience of running savings-and-loan clubs among her neighbors (Safesave, 2009a). The MFI was registered as a cooperative in 1997 (Staehle, 2005).

Compared with the Big Four, which have millions of clients, SafeSave is very small. As of August 2009, *Safe*Save's was serving 13’600 clients through 8 branches and had 8’000 active loans with outstanding balances averaging $65. Yet, the MFI is has been financially sustainable since 2005, when it stopped accepting donor grants, and began borrowing at commercial rates.

Product delivery

Other than the big majority of Bangladeshi MFIs which mostly follow the Grameen-style group-lending methodology with weekly group meetings, weekly repayments and an emphasis on woman borrowers, SafeSave’s approach to microfinance product delivery is fundamentally different. SafeSave’s field workers visit their clients door-to-door at their home or workplace every day. There are no groups, nor are there group meetings. There is no fixed-term and no fixed repayment schedule for loans, except for the interest payment, which is due every month. Clients are able to save or repay any amount they wish at the door-step and only need to visit the branch to open an account, take loans, or make withdrawals larger than $8. There is no minimum loan size and clients are not required to borrow at all (Staehle, 2005).

Products

SafeSave offers loans, passbook savings and long term savings. The exact product terms can be viewed in appendix 5.

3.6 Government Agencies and the BRDB

Bangladesh Rural Development Board (BRDB) is the largest microcredit provider of the government. It works in rural areas and provides microfinance services mostly to cooperatives with the support the financial and technical support of the Government of Bangladesh and its development partners. The BRDB also provides non-financial services, such as family planning, health and education (Bangladesh Microfinance Country Profile, 2006).

As noted by Wright and Alamgir (2004), the interest rates charged by the BRDB and other government programs are too low because they don’t have to meet the full costs of their operations. Nevertheless, BRDB has disbursed US$ 520 million to cooperative societies and groups and reached about 3.6 million members by 2004 (Bangladesh Microfinance Country Profile, 2006).

4. Funding of Microfinance

This Chapter examines the different internal and external funding sources available to MFIs in Bangladesh and their potential implications on commercialization and innovation. It gives a brief overview of a theoretical debate with regard to subsidized and sustainable MFIs and analyzes the different sources of capital for MFIs in light of that sustainability debate.

4.1 Resource mobilization of MFIs

According to Awal (2006) and Rahman and Charitonenko (2002), MFIs finance their loan portfolio through the following cash flows:

Table 1: Sources of fund for loan portfolio of MFIs

Share in loan portfolio (in %)	2004	2003	2000	1999	1998	1997	1996
Donor grants	11	13	18	19	26	30	48
Member savings	29	29	25	25	20	17	20
Service charges	24	24	16	12	13	14	n/a
NGOs' own fund	4	4	4	4	5	5	n/a
PKSF	17	21	23	24	21	17	10
Local banks	13	8	n/a	n/a	n/a	n/a	n/a
Others	3	2	n/a	n/a	n/a	n/a	n/a

Source: CDF Statistics, different volumes, compiled from Awal (2006) and Rahman and Charitonenko (2002)

The following sections examine these sources of capital for MFIs in more detail and deal with specific related issues which are dealt with in the literature.

4.1.1 Donor funding

In Bangladesh, foreign donation was traditionally the major source of funding for NGO-MFIs, contributing almost 50% of the MFIs RLF until 1996. As we can see in table 1, from then on, the share of donations in the RLF declined dramatically by almost 40 percent points to 11% in 2004. Contrary to popular opinion, only the relative share of donor funds in total RLF of MFIs has been declining, while in absolute terms donor funding has actually been rising over time (Rahman / Charitonenko, 2002). The microfinance sector of Bangladesh has been growing rapidly over the last two decades and continues to do so.

How should this decline of the relative share to MFIs RLF be considered? In order to answer this question, this paper first looks at the debate that takes places within the literature, concerning the sustainability of MFIs. There is a theoretical debate about sustainable and charitable MFIs within the literature when it comes to sustainability of microfinance (Schicks, 2007) and it makes sense at this point to examine the basic positions in order to better understand the funding issues related to Bangladeshi MFIs.

According to the *institutionist approach*, MFIs are to become financially sustainable in order to attract private capital and achieve broad outreach to the poor. Looking at the amount of donor funds available for microfinance, it becomes clear that the means that donors provide is by far not enough to reach all those in need of microfinance. But if MFIs would attract private funds in capital markets, everybody could be served (Schicks, 2007). The Consultative Group to Assist the Poor (CGAP)[2] stated that in 2006, $4 billion in foreign capital was invested in microfinance (Reddy, 2007) and Cull, Demirguc-Kunt and Morduch suggest even higher numbers in light of the highly successful initial public offering of Banco Compartamos in Mexico in 2007 (Cull, R. et al, 2009). Finally, market pressures on sustainable MFIs are considered to be conducive to *innovation* in MFIs (Schicks, 2007). This is the institutionist approach and it is followed by leading organizations like the World Bank, the CGAP and USAID (Conning, 1999).

On the other side, the *welfarist approach* believes, that fully subsidized, charitable MFIs are able to reach the less profitable clients because they don't have to turn down poor borrowers for commercial reasons, as do sustainable MFIs. Otero (2005) even goes so far to suggest that charitable MFIs which are fully subsidized can even be *more innovative* than for-profit MFIs, because they can focus on developmental impact without having to worry about financial tradeoffs. Therefore, if charitable MFIs surpass the developmental impact of sustainable institutions, their subsidies would be justified (Schicks 2007).

There are arguments for and against the two mind-sets.

[2] CGAP is an independent policy and research center supported by over 30 development agencies and private foundations and is housed at the World Bank. CGAP provides market intelligence, promotes standards, develops innovative solutions and offers advisory services to governments, microfinance providers, donors, and investors. Website: http://www.cgap.org

On the one hand, it is not obvious that sustainable MFIs really have the greatest possibility for reaching out to very poor people, while non-for-profit organizations take such outreach for their explicit mission. Then again, as Armendáriz and Morduch point out, sustainable MFIs competing with subsidized MFIs can force the sustainable one to lower its interest rates until it isn't viable any more. This could even prevent a sustainable MFI sector from emerging in the first place in local markets (Armendáriz / Morduch, 2005).

The 'Good Practice Guidelines for Funders of Microfinance', published by the CGAP and endorsed by the G8 in 2004, promotes the idea that donor funding should complement private capital, not compete with it, meaning donor funds should be used on a temporary basis to build the institutional capacity of financial providers in its earliest stages. Zaman too, suggests that donor funds can help expand the capital base of MFIs at the beginning, as long as there is a viable route to institutional sustainability (Zaman, 2004).

This paper takes an institutionist approach to examine the nature of innovation in Bangladesh. As shown in Chapter 2.2, the time when the NGO community initially emerged and started experimenting with different means of providing credit to the poor was in the 1980's and that's when they needed help and assistance in building their institutional capacity. According to Rahman and Charitonenko, continued availability of donor's grants would partly remove incentives for MFIs to access commercial sources of capital which in turn could have an inhibitive effect on innovation (Rahman / Charitonenko, 2002). Grameen Bank brought forth a wave of innovations after donor funds had diminished; for example, it cut some inflexibility of its loan terms (Rutherford S. et al. 2004) and a number of MFIs started to offer voluntary and open access savings accounts (Zaman, 2004).

Haque and Rashid from the Bangladesh Bank suggest that one way for many MFIs to face the challenge of declining donor funds is to reduce their administrative and transaction costs, which in 2002 still appeared to be quite high (Haque / Rashid, 2002). This could be approached by improving bookkeeping and accounting policies in order to identify weak points of operation. In this context it would be interesting to see in what way the accounting standards imposed by the newly established MRA on MFIs in Bangladesh affect their operational results and if MFIs manage to improve efficiency. This could leave more funds available for innovative experimentation.

4.1.2 Deposits and interest income

With the declining trend of foreign donation, the MF-NGOs have concentrated on accumulating funds from internal sources such as saving mobilization from their members (Haque / Rashid, 2000). Therefore, it has been seen that members' saving has increased over time and in 2004 it has contributed 29% of total loan portfolio. The contribution of service charge to loan portfolio has also increased with the decreasing rate of foreign donation. Now the contribution of service charge in Revolving Loan Fund in terms of percentage is more than double of that of foreign donation.

MFIs can mobilize deposits in three different forms: Through compulsory deposits, voluntary deposits from MFI clients and voluntary deposits from other private sources (Awal, 2006). Client savings is a cheap way for MFIs to refinance their operations. Savings mobilization represents lower cost capital compared to other private sources. However, offering savings accounts and deposits requires careful designing of bookkeeping, monitoring and supervision systems on the part of the MFIs (Awal, 2006) and it is not clear if the smaller MF-NGOs have the institutional capacity to manage these funds.

4.1.3 Retained earnings

According to the 2005 Bangladesh Microfinance Highlight Report (2005 Bangladesh Microfinance Highlights Report), produced by the Microfinance Information Exchange (MIX), a global business information provider for the microfinance industry[3], leading Bangladeshi institutions achieved net operating income of over 20 per cent. Awal (2006) notes that operational surplus contributed 14 per cent to the MFI's RLF by the end of 2003.

4.1.4 PKSF wholesale funds

As the microfinance industry in Bangladesh continues to grow and the MFIs loan portfolios increase rapidly, raising capital to lend out to the poor is an essential task for many MFIs. In order to face this challenge accordingly, the Government of Bangladesh created a national wholesale fund, managed by the Palli Karma-Sahayak Foundation (PKSF). The Foundation is

[3] See http://www.themix.org

a 'company not-for-profit' registered under the Companies Act of 1913 and acts as an apex organization involved in the long-run financing of organizations with microfinance services since its inception in 1990 (PKSF, 2009a).

PKSF receives funds in the forms of grants, loans and contributions from a wide variety of sources which include the Government of Bangladesh (GOB), private individuals and organizations, foreign governments, international donors and lending agencies and capital markets (Bangladesh Microfinance Country Profile, 2006). So far PKSF has received funds from the GOB, the IDA/World Bank, the USAID, the Asian Development Bank (ADB) and the International Fund for Agricultural Development (IFAD) (Rahman / Charitonenko, 2002).

PKSF does not only provide its Member-MFIs (Partner Organizations, POs) with funds, but emphasizes both their financial and institutional sustainability. Therefore, it provides debt financing to its POs, develops best practices for the microcredit sector, provides institution and capacity building support to POs and calls for appropriate policies and regulations for the microfinance industry (PKSF, 2009a).

PKSFs Credit Program

PKSF's mainstream credit program consists of five components (PKSF 2009a): a) Rural Microcredit, b) Urban Microcredit, c) Micro-enterprise credit, d) Ultra-poor Credit and e) Seasonal Credit.

Loan Terms

PKSF provides loans to three categories of POs – Organisations Operating in Small Areas (OOSA); Big Partner Organisations Operating in Large Areas (BIPOOL); and Pre-PKSF POs[4] (PKSF, 2009a).

PKSF charges 4.5% service charge per year from its OOSA and Pre-PKSF category POs and 7% service charge per year from its BIPOOL category POs.

Loans received by OOSA and Pre-PKSF category POs from PKSF are repayable within a

[4] PKSF established a Pre-PKSF program to fund and develop small locally based NGOs, which do not yet qualify as PKSF partners, but have the potential to do so (Squillace, 2004).

period of 3 years. The first 6 months are considered a grace period, and loans along with service charge are to be repaid in 10 quarterly installments within the following 30 months.

Loans received by BIPOOL category POs are payable in 4 years in 12 equal installments with a grace period of 12 months.

4.1.4.1 Selection of Partner Organizations

As can be seen from the previous description of loan products, PKSF onlends funds to its POs only on highly concessional terms. In order to receive funds from PKSF, MFIs must meet certain performance criteria (Meagher, 2002). In 1998, PKSF introduced a rating system to categorize its Pos (PKSF 2009b). The rating system is a weighted scoring system to categorize POs and determine their capacity to take up loans from PKSF. Various aspects, like the viability of microcredit borrowers, institutional viability (Program placement, Program implementation, Human resource development program, Monitoring and Evaluation, Institutional Culture, Financial Management and Internal Control, Status of physical assets) and financial and economic viability of the POs are evaluated by PKSF and weighted according to PKSF's practice. Then the POs are organized into five different groups, of which each group comprises a different credit limit.
Table 2 shows the different criteria for assessing the credit capacity of PKSF's POs.

Table 2: Rating Criteria for PKSF POs

Nr.		Weight	Acquired Score
1	Viability of micro Credit Borrowers	2	
2	Program placement	2	
3	Group management	2	
4	Loan disbursement and recovery system	2	
5	Level of skills of field workers	2	
6	Efficiency of accountant	1	
7	Quality of chief executive	2	
8	Skill of mid and top level Managers	2	
9	Human resource development programme	2	
10	Monitoring & Evaluation	1	

11	Sound governance	2	
12	Incentive base for management staff & employees	1	
13	MIS	2	
14	Accounting system	1	
15	Internal audit	2	
16	Regular internal supervision	1	
17	Budgetary practice	1	
18	Status of physical assets	1	
19	Financial sustainability	2	
20	Quality of portfolio	2	
21	Productivity ratios	1	
22	Status of micro credit fund of the PO	1	
23	Financial ratio analysis	1	
	Total	36	

Source: Compiled from PKSF website (PKSF, 2009b)

At present PKSF provides loans to 233 POs for onlending under its mainstream credit program as well as under some other projects. 11 of the POs are considered big and 222 are small and medium MFIs. Among the partner organizations, big NGOs are taking more than 72 per cent loan from PKSF while the rest goes to the small partner organizations (PKSF, 2009c).

PKSF's loans are not considered typical commercial loans, but Soft Loans. Soft Loans is a form of financing that offers "[…] flexible or lenient terms for repayment, usually at lower than market rates." (Business Directory, 2009a). As shown before, the interest rate charged on PKSF loans to various MFIs (4.5% - 7.0%) is significantly below market rates, which ranged between 10-12 per cent in 2004 (Wright / Alamgir, 2004). These low interest rates were set by the World Bank as a direct result of the low, subsidy-dependent rates charged by Grameen Bank, back when Grameen was still receiving large amounts of subsidies (Rahman / Charitonenko, 2002). The bank used part of these subsidies to fund its operation but at the same time passed on the other part to its clients through low interest rates. It is not clear to what extent it was really necessary for the World Bank to set the interest rates charged on PKSF loans to its POs so low. Mahmoud, C. et al. (2009) and Schicks (2007) both state that having access to finance at all is more important for poor borrowers than interest rates, and as Rutherford (Interview, 2009) points out, in the 1990's MFIs did not yet use interest rates as a weapon for competition.

After Grameen received its last donor fund in 1998 (Grameen Bank, 2009a), PKSF's soft loan interest rates remained at the same level until today. This gives rise to the question, whether or not in continuing to provide these subsidies, funding agencies are hindering natural market mechanisms and impeding microfinance commercialization.

From the view of poor borrowers, the PKSF played an essential role in expanding access to microcredit in the 1990's (Zaman, 2004) and the criteria PKSF's POs have to meet in order to get a loan ensured certain accounting and reporting standards, which were the only regulatory means until the establishment of the "Microcredit Regulatory Act" in 2006.

Zaman (2004) notes that one important factor behind the success or failure of a microfinance wholesaler is the capacity of its Partner Organizations to absorb the funds assigned to them. In 1996 and 2001 the World Bank provided the PKSF with a $105 million and $151 million credit, respectively (Rahman / Charitonenko, 2002). These are considerably large amounts when compared with the CDF Statistics of 1999, which revealed that the total outstanding loan amount of all reported 533MF-NGOs (including BRAC, ASA, Proshika, etc.) was Tk. 18'692 (approximatly $367 million 1999 Dollars)[5] (Hossain / Ahmed, 2000). Zaman (2004) believes that thanks to the good retail capacity of Bangladeshi MFIs, PKSF's played a successful role as an apex wholesaler, whereas Rutherford (Interview, 2009) suggests, that these large cash provisions through the World Bank may have led to a bloated sector, leaving some MFIs with too much money.

4.1.5 Bank loans

According to Awal (2006), commercial banks had lots of excess liquidity by the end of 2005. Part of this liquidity could be used to onlend to MFIs who lack funds to conduct their microfinance operations, i.e. banks could act as wholesalers as well. Table 3 shows the amount of excess liquidity lying idle with commercial banks in Bangladesh.

[5] See http://www.oanda.com/convert/classic for 12/31/1999, accessed on 09/16/2009

Table 3: Excess liquidity with banks in June, 2005

Type of formal institution	**Million US$**
Nationalized commercial banks	911.43
Private commercial banks	405.08
Foreign commercial banks	258.10
Specialized commercial banks	119.37
Total	1693.97

Source: Awal (2006)

The CDF is very actively involved in the process of linking its partner microfinance NGOs with commercial bank credit. It was established in 1992 and works with 1’500 partner MF-NGOs (CDF, 2009a). It also provides referral services by sending the names of capable NGO-MFIs to PKSF for financial assistance. With the aim of commercialization, it focuses on capacity building, stresses operational and financial sustainability, product pricing/costing, cost efficiency, productivity, and eventually links its partners with commercial sources of funds (Rahman / Charitonenko, 2002). In 2006, the CDF set a target for the next three years to link at least 150 of its 1’500 network members to commercial funds in order to meet the huge demand for linkage service (Awal, 2006). This goal appears reasonable, given the growing interest of commercial banks to participate in the microfinance business, since they have seen that MFIs can be very profitable (Schicks, 2007). Meanwhile, linkages to the formal sector have been established with all types of commercial banks (Rahman / Charitonenko, 2002).

It must be noted though that not all reservations on the side of the banks concerning wholesaling to MFIs have been shaken off yet. According to Awal (2006), there are no policy guidelines for funding the MFIs by the banks in Bangladesh and the interest rates charged by banks to MFIs, which are considerably higher than PKSF’s Soft Loans, still make it hard for banks to lend out funds to microfinance institutions.

Awal (2006) suggests that to facilitate growing partnership between financially viable MFIs and the banks, the relevant financial authority could act as guarantor on behalf of MFIs or establish Guarantee funds. He mentions one example of such a guarantor - the Swiss Agency for Development and Cooperation (SDC), which guaranteed a loan from Sonali Bank, the largest bank in Bangladesh. The repayment to the bank was excellent, and the guarantee from the SDC was reduced annually until the next loan was approved by Sonali Bank without any guarantee necessary.

Another fact that should be considered is that according to the CDF (Awal, 2006), the recovery rate from wholesaling is higher for commercial banks compared to their recovery rates in direct microfinance involvement. As Schicks (2007) points out, in recent times there have been commercial banks around the world entering the microfinance business, which see serving the poor as an investment in access to lucrative markets. In Bangladesh, this "downscaling" has taken place as well, but due to obstacles for these banks in microfinance such as regulation and prudential norms, the mindset and commitment level of staff or in general a lack of understanding for the microfinance industry, these banks have not had much success so far in trying it out on their own (Awal, 2006). For example, the recovery rate for Sonali Bank was only 76% in 2006. At the same time its wholesaling activities to reputable NGO-MFIs were by far more successful and resulted in an overall recovery rate of 97% (see Table 4).

Table 4: Involvement of commercial banks in wholesaling (in million US$)

Name of Bank	No. of MFIs financed	Cumulative disbursement	Outstanding	% of recovery
Sonali Bank	60	12.47	5.19	97%
Janata Bank	07	2.04	0.03	98%
Agrani Bank	31	20.60	14.57	95%
Basic Bank	29	-	3.20	100%

Source: Awal (2006)

Awal (2006) sees the main reason for this in their respective comparative and competitive advantages which lead to synergy in linkage between the banks and NGO-MFIs. By wholesaling to a NGO-MFI, a commercial bank can rely on the MFI's experience, capacity and understanding of the market while the NGO-MFI on its part is backed by the commercial bank's resources.

The data seems to confirm a trend towards increased involvement of commercial banks in wholesaling. According to the 2005 Bangladesh Microfinance Highlight Report (2005 Bangladesh Microfinance Highlights Report), produced by the Mix Market, commercial funding made up 20% of the loan portfolio of MFIs in Bangladesh in 2005, an increase of 45% since 2004.

5. Regulation and Supervision

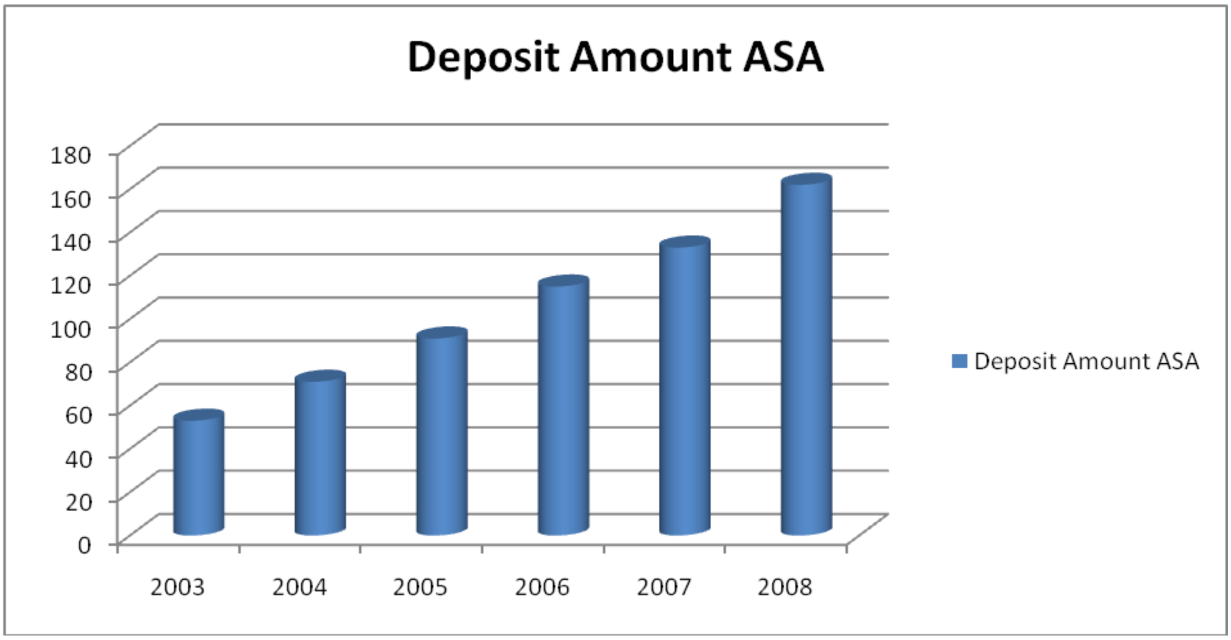
Bangladesh is considered one of the Birthplaces of microfinance. However, from the emergence of microfinance in the 70's until recently, no NGOs offering microfinance in Bangladesh were regulated or supervised either by the central bank, the Bangladesh Bank or any regulatory agency, except in the case of Grameen Bank (Bangladesh Microfinance Country Profile). NGO-MFIs merely needed to report to the government NGO Affairs Bureau (NGOAB) for certification. This consisted of legal identity, budget approvals, audits and evaluations (Mac Abbey, 2008). Mc Guire & Conroy (2000) state that huge microfinance institutions grew because of lack of formal regulation, which allowed innovative services, and they quote Carpenter, who suggests that it was, among other factors, thanks to the absence of regulatory oversight that the microfinance sector of Bangladesh resulted in "[…] the ad hoc evolution of sophisticated and innovative MFIs" (Carpenter 1997, quoted in Mc Guire & Conroy 2000).

There are various reasons why the microfinance market of Bangladesh was marked by regulatory freedom all this time: On the one hand the country was in a terrible state in the late 70's after the war of independence, when microfinance emerged. The government of Bangladesh was - and still is - not well organized, and for many years of its history Bangladesh was dependent on foreign donations to run its development Program (Rutherford, interview, 2009). Since both the government and central bank didn't have the capacity or the machinery to regulate the multitude of NGOs and MFIs and at the same time donor's influence was great, the Bangladesh Bank has taken a fairly "hands-off" approach to the development of the microfinance industry (Rahman / Charitonenko, 2002). On the other hand, until recently the largest and most powerful MFIs resisted any kind of regulation, apparently because they anticipate bureaucracy and imposition of control where they have operated with considerable autonomy to date (Conroy / McGuire, 2000).

As both Abbey (2006) and Rutherford (interview, 2009) point out, from the late 1970's to the end 1990's most clients were net borrowers, and would not have been hurt in case of a collapse of the system. Hence, the Bangladesh Bank decided to do an informal agreement with the MFIs, letting them take deposits only from their members.

This has changed rapidly over the past decade. As microfinance products became more flexible after the turn of the century and MFIs were not only requiring their borrowers to make compulsory savings but were also offering voluntary savings accounts, this became an increasing concern among policy makers in Bangladesh. Already in 2000, Conroy and McGuire (2000) were concerned about an increasing number of NGO-MFIs attracting voluntary deposits and there has been a general consensus between stakeholders that eventually there had to be some kind of regulation put in place (Conroy / McGuire, 2000). Figure 3-5 show the deposit amounts of the three biggest Bangladeshi MFIs ASA, BRAC and Grameen Bank. As suggested before, since the introduction of voluntary and open access savings accounts after the turn of the century, there has been an increasing trend in this domain.

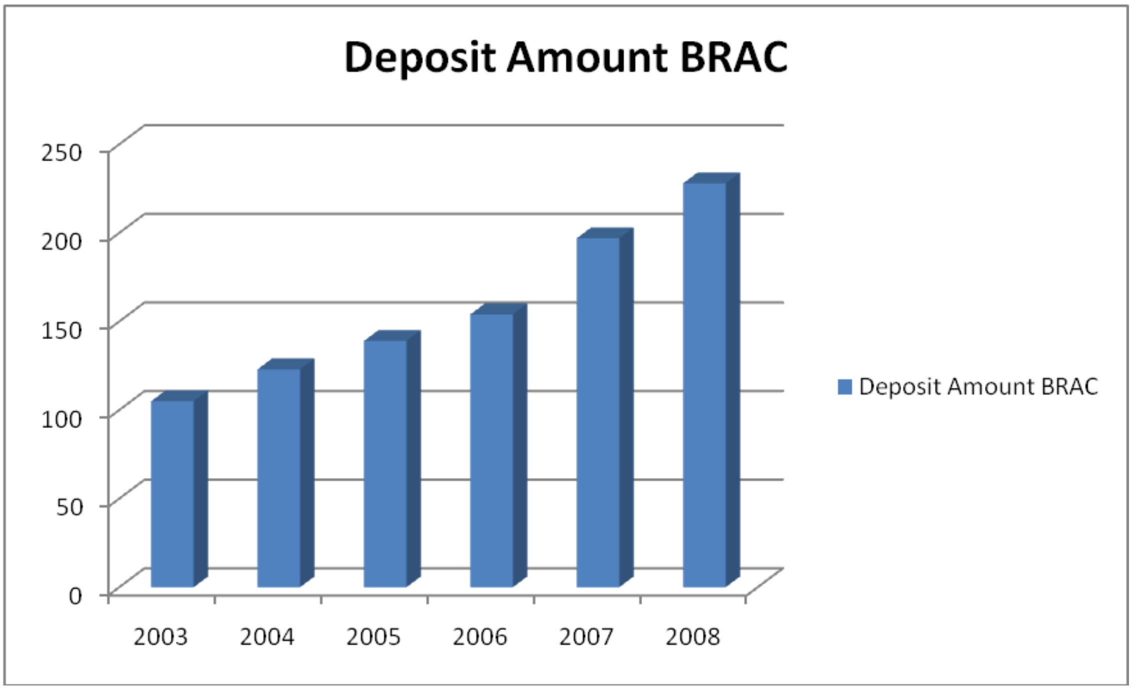
Figure 3: Deposit Amount ASA, 2003-2008



Source: Own research, compiled from the MixMarket at http://www.mixmarket.org[6]

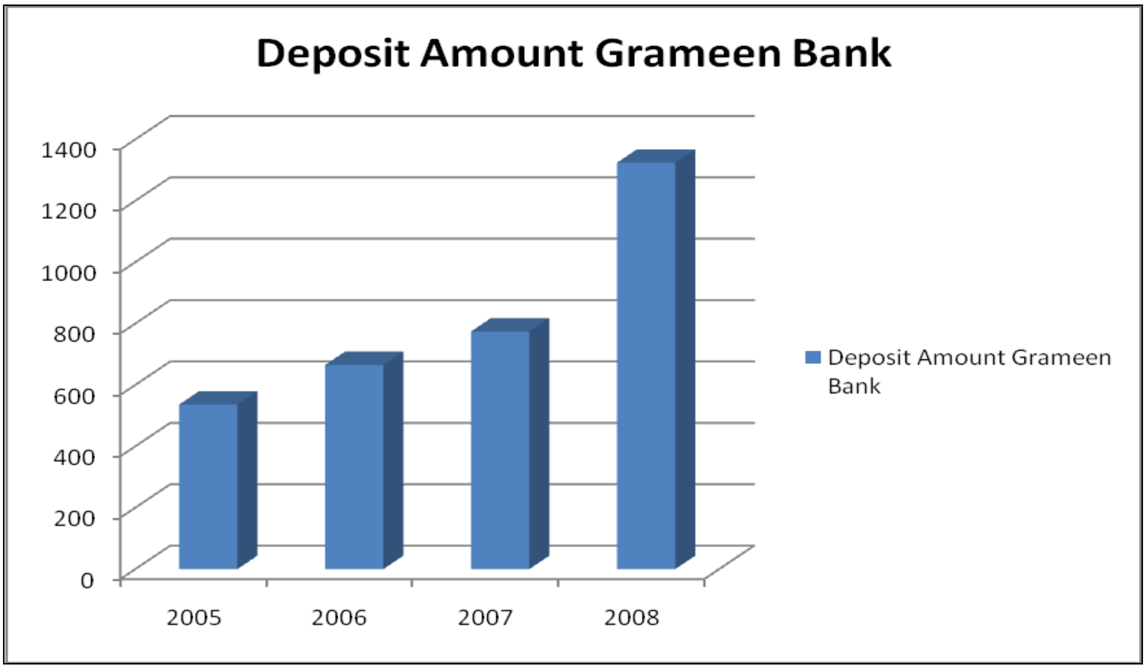
[6] Accessed on 10/10/2009

Fig. 4: Deposit Amount BRAC, 2003-2008



Source: Own research, compiled from the MixMarket at http://www.mixmarket.org[7]

Fig. 5: Deposit Amount Grameen Bank, 2005-2008



Source: Own research, compiled from the MixMarket at http://www.mixmarket.org[8]

[7] Accessed on 10/10/2009

5.1 The Microcredit Regulatory Authority

The government of Bangladesh has been dealing with the issue of regulating the microfinance sector since the late 1990's. Since then, it has commissioned studies examining regulatory aspects of MFIs and linking them to the formal financial sector (MRA, 2009a). In 2000 a committee was established which consisted of members of the Ministry of Finance, the Social Welfare Ministry, NGO Affairs Bureau, PKSF, Grameen Bank, ADAB[9], BRAC, and others. It provided the government with recommendations related to a regulatory framework for microfinance in Bangladesh. The government passed the "Microcredit Regulatory Authority Act 2006" in July 2006 on the basis of the suggestions given by the Committee.

In 2006, the government of Bangladesh established the Microcredit Regulation Authority (MRA) under the "Microcredit Regulatory Authority Act" with eight members of its board of directors and with the governor of the Bangladesh Bank as its chairperson. The Authority is to ensure transparency and accountability of microcredit activities of the NGO-MFIs in the country and has been given power to issue and cancel licenses for micro finance operators and oversee, supervise and facilitate the entire range of activities of MFIs. It is empowered and responsible for implementing the act and bringing the microcredit sector of the country under a full-fledged regulatory framework.

5.2 The MRA Act 2006

The basic contents of the MRA Act 2006 are the following (MRA, 2009a):

- No NGO-MFI may act as microfinance institution without the license of the MRA (including credit-only MFIs).
- MFIs may not collect deposits from persons other than their members, i.e. they may not collect deposits from the general public.

[8] Accessed on 10/10/2009

[9] Association of Development Agencies in Bangladesh [ADAB] is the national apex organization of the local, national and international non-government organizations [NGOs] working in Bangladesh. It was founded in January 1974 as a loose coalition of some foreign aided NGOs that were engaged in relief and rehabilitation activities. Its members concentrate their activities in the field of agriculture and food production.

- All institutions with microcredit operations must separate their financial operations from other development works and keep their accounts separate.

- The Authority also has the power to prepare detailed rules related to the operations of microcredit including conditions for spending any income, area of operations, guideline of internal and external audit and accounts, collection of deposits, and use of earned profit, governance structure of MFIs, reporting requirements etc.

- Only MFIs who meet the threshold of either a minimum of 1000 borrowers or minimum loan outstanding of Tk 4’000’000 (approximately $58’000) may apply for a license by the MRA (Microcapital, 2009a).

- The MRA will take punitive measures if any institution does not comply with these rules. Persons who are convicted are punishable with imprisonment of not more than one year, or a fine of not more than Tk. 500’000 (approx. $7’300), or both.

In May, 2009, the MRA announced that MFIs will have to limit interest rates they charge clients to a flat 15% or an effective rate of 30%. In addition, it announced that MFIs cannot collect deposits totaling more than 80% of their total outstanding loan portfolio, in order to prevent fraud (Microcapital, 2009a).

5.2.1 Evaluation of the MRA Act

How should this new regulatory act be judged? Since it has only been in effect since August 2006 and MFIs are given time to fulfill minimum licensing criteria until the end of 2009, it is difficult to draw any conclusions right now. It will still take some time for all stakeholders to adapt to the new act and its implications and to identify limitations or weaknesses of the system. Yet, we can take a closer look at the existing facts:

Interest rate ceilings

In 2009, The MRA announced that it will impose an interest rate ceiling of 15% flat[10] or 30% effective interest rate on its MFIs. There is a general consensus within the literature which opposes such rate ceilings. The CGAP Microfinance Consensus Guidelines on regulation, representing the standpoint of the microfinance industry in many countries, maintains: "Interest rate caps, where they are enforced, almost always hurt the poor – by limiting services – far more than they help the poor by lowering rates" (Christen, R. et al., 2003, 13).

Conroy and McGuire too, emphasize that interest rate restriction "[…] impedes the development of sustainable microfinance" (Conroy / McGuire, 2000, 50).

These restrictions could possibly confront the less efficient NGO-MFIs in Bangladesh with problems. It must be seen though that by the end of June, 2007, from 425 MFIs reporting to the MRA and representing nearly 90% of the sector, only 4.7% were charging interest rates above 15% by flat method (An Overview of NGO-MFIs in Bangladesh, 2009). Additionally, as we will see in the next chapter, PKSF has capped the onlending interest rates of its clients at even 12.5% (flat) in 2004, so many middle-size NGO-MFIs receiving funds from PKSF are already operating under the MRA interest rate limit.

Yet, as the average loan size per borrower provided by NGO-MFIs offering microcredit to the very poor tends to be smaller than that of MFIs who serve higher productive clients, the costs per borrower of these MFIs tend to be higher. In order to cover these costs, MFIs most likely have to charge higher interest rates. As Cull, R. et al. (2009) or (Shicks, (2007) point out, having access to credit remains a more important thing to borrowers who otherwise wouldn't have access and therefore, price is not a priority. Thus the question remains, whether or not the MRA possibly hinders innovation and excludes the very poor segment from access to microcredit with its policy of capping interest rates.

[10] For details on the flat interest rate calculation method, see chapter 6.3.1 Interest rates in Bangladesh

Restriction of deposit amount

In May 2009, the MRA announced that MFIs are not going to be allowed to collect deposits that exceed 80% of their total outstanding loan portfolio. Data of the 425 members selected by the MRA for its yearly publication show that the average savings-to-outstanding-ratio for these MFIs was 32% in 2007 (An Overview of NGO-MFIs in Bangladesh, 2009). Yet there are members with an amount of savings close to or above total loan outstanding and it is not clear if this restriction is conducive to commercialization of the microfinance market, being that clients' deposits contribute increasingly to the loan portfolio of MFIs and therefore provide a cheap source of funds for them to refinance their operations. For example, according to the Mixmarket, Grameen Bank, which has its own regulatory status and is not regulated by the MRA, had a savings-to-outstanding-ratio of 145% (Mix Market, 2009g) . The bank requires its new Branches to operate with their own money collected from deposits and come to break-even point within the first year of work (Yunus, 2006). Thus it manages to grow at a rapid rate.

The MRA has announced this restriction on deposits with the objective of preventing fraud. In order to advance the commercialization of microfinance in Bangladesh, it will be essential for the MRA to strengthen its own capacity to monitor its MFIs adequately rather than restricting their potential source of funds.

No legal channel for MFIs to convert into formal banks

The MRA Act does not provide a regulatory corridor for MFIs to transform into fully commercial banks (Act no 32 of 2006). Other than in Peru, whose regulatory framework was ranked one of the most conducive to microfinance development by the American Development Bank (Pait, 2009), there are no intermediate regulatory stages for MFIs at which they could offer a wider range of products or operate under other premises. This could have an inhibiting effect on the development of innovative products. It might also be too early to expect the MRA to have the capacity to oversee and control such transitional banks at present.

Exclusion of Micro insurance

As we have seen in Chapter 3, micro-insurance became a very popular issue over the past decade. Insurance as a specialized product is treated neither by the Central Bank nor by the MRA (Act no 32 of 2006).

Exclusion of foreign MFIs

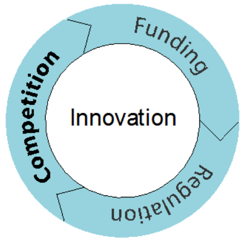
The MRA Act does not include foreign MFIs (Act no 32 of 2006). This could result in negative competition, since domestic MFIs are bound to the MRA's rules, whereas foreign MFIs aren't.

Table 5 provides an overview of the current regulation of financial institutions of Bangladesh, the regulators and the regulated activities.

Table 5: Regulation in Bangladesh

Bangladesh	Legal basis for regulating	Regulator(s) and role of regulator(s)	Regulated activity
Banks Any business conducting banking business, meaning accepting deposits from the public for the purpose of lending or investments (Bank Companies Act 1991 (as amended), Section 5(o-p)).	Bank Companies Act 1991 (as amended) Prudential Regulations for Banks	Bangladesh Bank (BB)	Accepting deposits for the purpose of lending or investments, with the strictest prudential requirements and highest minimum capital requirements.
Non-bank Financial Institutions Leasing and financing companies (Financial Sector Review, Chap. 1, Bangladesh Bank).	Financial Institutions Act, 1993	Bangladesh Bank (BB) (Financial Institutions Act, 1993, Sections 4-5)	Leasing, merchant banking, and other financing services to commercial entities, with lower capital requirements and without the ability to accept demand deposits.
Cooperatives/Credit Unions Cooperative societies are societies established to promote the common interests of their members using cooperative principles. Credit cooperative societies create funds to be on-lent to members (Ordinance 8(1); Rule 2(2) (vi), cited in WOCCU 2005).	Cooperative Societies Ordinance, 1984 (cited as "Ordinance."); Cooperative Societies Rules 1987 [cited as "Rule"]; Micro Credit Regulatory Authority Act; Micro Credit Regulatory Authority Rules (rules forthcoming in 2007)	Registrar of Cooperative Societies and Micro Credit Regulatory Authority (MCRA). MCRA issues and cancels registration certificates, audits MFI accounts, etc. (Ordinance 6, cited in WOCCU 2005) (MCRA Act 2006, Section 9).	Deposit and lending services offered by a membership-based cooperative society.
Non-profit institutions Nonprofit societies or trusts engaged in microfinance activities.	Micro Credit Regulatory Authority Act;	Micro Credit Regulatory Authority (MCRA). MCRA issues and cancels registration certificates, audits MFI accounts, etc. (MCRA Act 2006, Section 9).	Microfinance services offered by a nonprofit society or trust.

Source: http://www.microfinanceregulationcenter.org, accessed on 09/09/2009



6. Competitive environment within the Microfinance Industry

6.1 Market Share and Overlapping

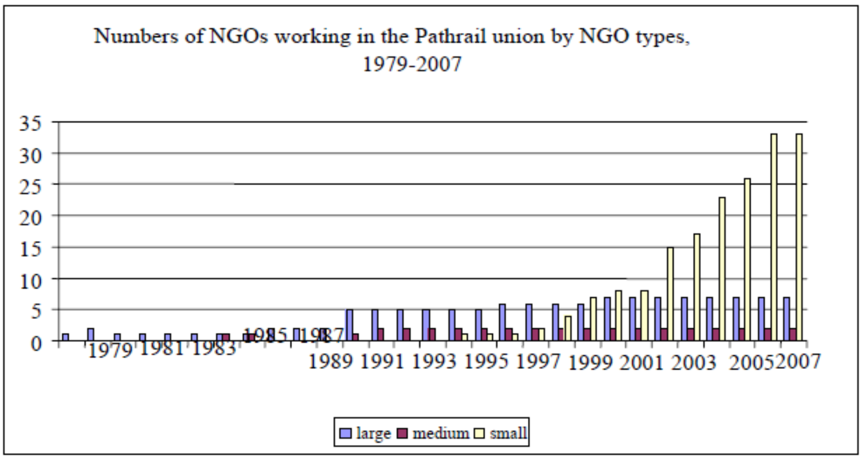
The micro-finance sector in Bangladesh is one of the worlds largest (Bangladesh Microfinance Country Profile, 2006). In most of Bangladesh, there is a very high density of MFIs and now MFIs are largely in competition with each other, instead of exclusively with banks or other financial institutions, in attracting borrowers (Mahmoud, C. et al., 2009).

As Rutherford (Interview, 2009) pointed out to the author, a typical middle-size village will have a branch of Grameen, BRAC, ASA, three or four middle-size NGO-MFIs and three or four local ones. How did the microfinance industry in Bangladesh get so crowded? On the one hand there was a lot of funding pressure. As mentioned already in section 4.1.4, PKSF as wholesaler has provided many MFIs with much funding, with the effect of many MFIs expanding rapidly, sometimes forced to meet preset targets and ignore any information they might have about the household's existing MFI debt obligations (Matin, 2001). On the other hand, Rutherford (Interview, 2009) indicated that, especially since the turn of the century, natural competition between MFIs became increasingly intense. If BRAC saw, for example, that ASA opened a branch in one village, they would go to that village as well, not wanting to miss out on that market. As soon as one MFI pushed into a new village all the others would follow instantly. There was a rush to go everywhere, since the microfinance market was and is still huge and MFIs would not only try to win new clients but also to allure existing clients away from the other competing MFIs (Mahmoud, C. et al., 2009).
The newly established MRA publishes information of its registered NGO-MFIs on a frequent basis. For 2007, it included 425 institutions' reports in its statistics (An Overview of NGO-MFIs in Bangladesh). Although there were over 2500 tiny MFIs that didn't meet the threshold of getting a license by the MRA, it estimates that these 425 institutions actually represent nearly 90% of operations of the sector. According to the data provided by the MRA, among these 425 MFIs the largest two (BRAC and ASA) have a 65.93% share of the total outstanding loan and 57.17% share of total savings. Grameen Bank as a specialized bank is not included in the sample.

There has not been much research conducted on how MFIs in Bangladesh compete with each other. Imram Matin describes in a CGAP Note how smaller MFIs complain about their more mature clients being taken by larger MFIs, whereas larger MFIs are annoyed by the fact that smaller MFIs give credit to *their* clients and thereby endanger their repayment performance (Matin, 2001).

Mahmoud, C. et al. (2009) conducted a recent study about the nature of competition in the microfinance market in Bangladesh over time. Using data of a census of microcredit borrowers at Pathrail union[11] in the Tangail district of Bangladesh, they found that there was a marked emergence of small and middle-sized NGO-MFIs throughout time and that smaller MFIs are now successfully competing side by side with bigger ones in most of the places. The means with which they compete with other MFIs are through large loans, higher deposit interest rates, special loans such as housing or micro enterprise loans, and loans adapted to local conditions. Another finding of Mahmoud, C. et al was that a high market share comes with higher credit sums which necessitates having greater capital reserves. This makes it more likely that large MFIs will win greater market shares because of their greater refinancing capability.

Figure 6: Emergence of NGO-MFIs in Pathrail Union 1979-2007



Source: Mahmoud, C. et al. (2009)

Figure 6 illustrates the rapid emergence of NGO-MFIs in Pantrail union. The small and mid-sized NGO-MFIs have made inroads to the market shares of the larger MFIs. Despite this, the

[11]The rationale behind this was that the union has one of the longest microfinance histories in Bangladesh and any development that would be observed here would most likely be able to indicate the future direction of the microfinance in the rest of the country (Mahmoud, C. et al., 2009).

volume of credit distribution in all classes of MFIs – from small to large – has continued to grow, as the total market has continually expanded, and now practically all MFIs are faced with the phenomenon of client-overlapping.

Overlapping occurs when an individual or a household holds multiple memberships with different MFIs. Generally speaking, one can speak of “household overlapping” and “membership overlapping”. Overlapping has been a major concern to industry leaders over the last decade. Overlapping can lead to over-indebtedness, undermine the primary incentive to repay and therefore be a threat to the financial system through interrelated portfolio risk (Rahman / Charitonenko, 2002). Over-indebtedness, also caused by overlapping, was a considerable problem around the turn of the century in Bangladesh. People today are worried that the microfinance industry is building up a bubble, similar to the subprime bubble in the developed countries. ASA, for instance, which has been expanding at a rate of one hundred branches a year, has stopped expanding about a year ago (Interview Rutherford, 2009). At the same time, overlapping can also be necessary for households, whose net worth is increasing on a sustainable basis. Those households can use multiple memberships with different MFIs to take higher productive activity by enlarging investments (Mahmoud, C. et al., 2009). Mahmoud, C. et al. (2009) found that in some cases overlapping at household or membership level is even used deliberately as one instrument of competition. This has also led PKSF to change its definition of overlapping. Today, Jashim Uddin, Deputy General Manager at PKSF, defines overlapping as the incidence of an individual taking loans from more than one MFI as against to the earlier definition of different MFIs giving loans to one household (Uddin, 1999). Rutherford (Interview, 2009), as a student of how poor people manage their money, mentions that poor people are always in multiple debt and from his side of perspective it is still better to be in debt with an MFI than with a moneylender, since the MFI will always let the client pay back at least a token amount. For these reasons, overlapping must be regarded in a wider range of context, although most observers believe that it represents a considerable risk (i.e. de Aghion / Morduch, (2004), Kassmin / Rahman (2008), Mahmoud, C. et al. (2009), Uddin (1999)).

Causes of overlapping

Uddin lays out that the causes of overlapping can be found at loan receiver's level as well as at managerial level of MFIs (Uddin, 1999).

At loan receiver's level overlapping can occur, when supply doesn't meet demand, either with respect to the amount needed by the borrower or to loan terms. It can be that an existing client has an immediate need for a loan and is has no other choice than to get it from another MFI which will provide it to him immediately (1999).

At managerial level overlapping can be caused by expanding the MFI's loan program and forming incompatible number of groups compared with the availability of loan portfolio, or by fixing up targets on behalf of the organization – for example by keeping their loan programs concentrated in a specific geographical area (1999).

Measurement of overlapping

Measurement of overlapping at both household and individual membership level is difficult and cannot be achieved only by exchanging membership lists of MFIs - as these do not typically include membership at the household level - but only of individual clients (de Aghion / Morduch, 2004). This is what makes estimating multiple memberships in MFIs so problematic. Matin (2001) describes, how staff members of the same MFI would give him figures ranging from 10% to 50% and that the perception of the extent of overlapping diverges greatly. The Bangladesh Institut of Development Studies (BIDS) conducted a large-scale study in 2001 and concluded the rate of households with multiple MFI memberships to be at 15% in 2001 (Bangladesh Institute of Development Studies, 2001). Since individual overlapping is always a subset of household overlapping, this seems rather low compared with the PKSF estimates of 15% in 1999, 33% in 2003 and 40% in 2005 at individual level (PKSF, 2009d). Nevertheless, Sajjad Zohir estimates overlapping intensity at individual membership level as high as 40% in 2007 (Zohir, 2007).

6.2 Microfinance Credit Bureaus

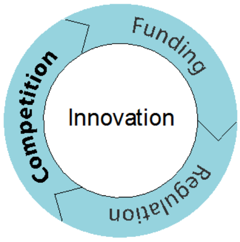
The need for collaborative effort among the MFIs and the government to establish a common database for all microfinance clients in order to avoid the possibility of poor borrowers taking up multiple loans with different MFIs is widely advocated (de Aghion / Morduch, (2004), Rutherford (2006), Kassmin / Rahman (2008), Mahmoud, C. et al. (2009)). While there already is a credit information bureau (CIB) in Bangladesh for providing reports to commercial banks and in certain cases banks are even required to collect data from the CIB, there is no information on microfinance borrowers in the CIB or any other centralized system (Rahman / Charitonenko, 2002). In the 1980's there were already efforts in this direction, as local MFIs met each weak and tried to exchange membership lists. This proved unsuccessful at that time because of competitive pressures and problems of administration. Since the majority of poor Bangladeshis are illiterate and until recently were lacking identification cards, it was very difficult for MFIs to exchange member lists and identify multiple membership (Interview Rutherford, 2009). Moreover, such information sharing could, in fact, increase overlapping, because MFIs would have access to the names of borrowers of competing MFIs (Rahman / Charitonenko, 2002).

Nevertheless, according to the PKSF website, it has started to build up a Credit Bureau Database containing selected information of all microcredit institutions of the country. The database will have information up to the borrower's level (PKSF, 2009a).

6.3 Competition and microfinance interest rates

Since most donors are no longer willing to finance operational expenses of Bangladeshi MFIs, it is essential for almost all NGO-MFIs to cover the costs of funds, management, etc. through interest income. In order to make their programs financially viable, they are required to manage microfinance like a business (Wright / Alamgir, 2004).

Any lender has costs comprising four basic components which (should) determine the interest rate charged (Wright / Alamgir, 2004). The cost-side for MFIs therefore consists of a) cost of funds, b) operating or processing costs, c) cost of risk or loan losses and d) net income.



Interest rates charged on loans by MFIs should ensure their long term financial sustainability. The CGAP, representing the consensus in the microfinance industry, believes that only financially sustainable MFIs can ultimately increase outreach through innovative products. This means, among other things, charging interest rates consistent with full cost recovery to ensure profitability and growth (Good Practice Guidelines for Funders of Microfinance, 2006).

To determine the appropriate rate, MFIs need to look at both the cost and the income side of their operations.

- The Cost-side

Cost of funds

In 2004 NGO-MFIs paid 5-8% on the savings, borrowed money from PKSF at the rate of 4.5-7% and, occasionally, borrowed from commercial banks at the rate of 10-12% per annum. Wright and Alamgir (2004) determine the average cost of capital at around 6%.

Operating costs

Determining the right operating costs is very difficult, since key factors can vary widely. A PKSF study of 18 POs of different scale and geographical location reveals a significant range in operational expenses (Uddin, 2003). The operating costs as a percentage of average performing assets vary from 12-20%, and, contrary to the suggestion of Mahmoud, C. et al. (2009), there were no economies of scale evident: The five largest POs in the sample of 18 have costs varying between 14-21%. According to the PKSF study, some of the lowest costs are for POs with borrowers less than 7,500.

Loan loss

Loan losses reported by the 18 POs of the PKSF study were less than 2%, indicating that there is not much more room for improvement in this area.

- The Income-side

On the income side, the key factors are the interest rate charged and the actual borrowings by members.

6.3.1 Interest rates in Bangladesh

Generally there are two methods in calculating loan interest: flat method and declining balance method. Out of 535 MFIs covered by the Microfinance Statistics 2007[12], 18 follow both flat and declining methods, nine MFIs follow only declining balance method, and the rest follow flat method (Mahmud / Khalily, 2007).

Table (6) shows the distribution of interest rates on loans under the Flat method in 2007. It becomes apparent that most MFIs chose a rate of 15% flat, which corresponds with 29% APR. Considering the above mentioned figures relating to the costs of Bangladeshi microfinance operations, it appears to provide an adequate net income for these MFIs. But there has been increasing political pressure to reduce rates, and in 2004, PKSF capped the onlending rate of all its clients at 12.5% flat beginning in 2005. ASA and BRAC kept their interest rates high so that now there are three main interest rate categories for microcredit in Bangladesh: Grameen Bank has the lowest rate at 10% flat. PKSF partners charge 12.5% and ASA and BRAC along with over 300 other MFIs remain at 15% (Porteous, 2006). This distribution of interest rates on loans is mostly consistent with the information published by the MRA (An Overview of NGO-MFIs in Bangladesh, 2009).

[12] Provided by the CDF and the Institute of Microfinance

Table 6: Distribution of Interest Rate on Loan under Flat Method, Dec. 2007

Interest Rates	No. of MFIs	% of Total MFIs
2-5	0	0
5-8	3	0.56
8-11	3	0.56
11-12.5	18	3.36
12.5	180	33.64
12.5-15	3	0.56
15	309	57.76
15-20	2	0.37
20	5	0.93
Above 20	0	0
Total	508	100

Source: Mahmud / Khalily (2007)

The approximate equivalent annual percentage rate (APR) charged on the outstanding balance amount of a loan is called the "declining method" of interest rate calculation. Table (Y) compares the "Flat rate" with the "APR".

Table 7: Comparison of Interest Rates: 'Flat' v APR (Loan size Taka 1,000)

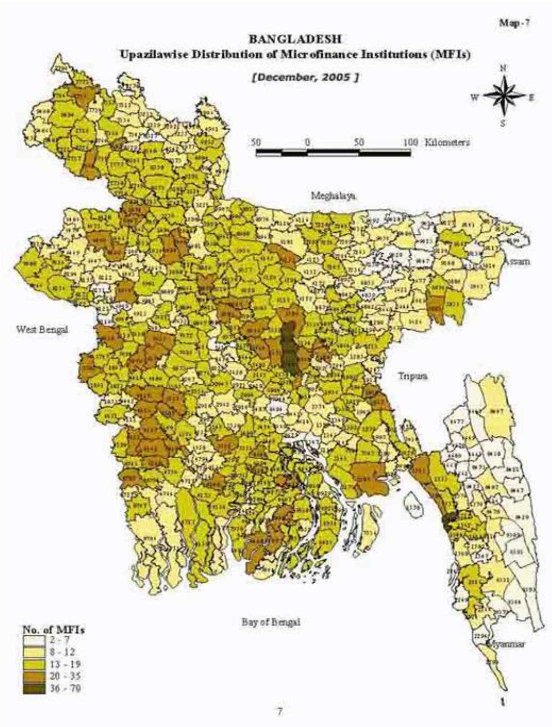
'Flat' Rate (%)	Total Interest Payment (Taka)	Annual Percentage Rate (%)
10	100	19
12.5	125	24
15	150	29
18	180	35
20	200	38

Source: Wright / Alamgir (2004)

Interest rate capping

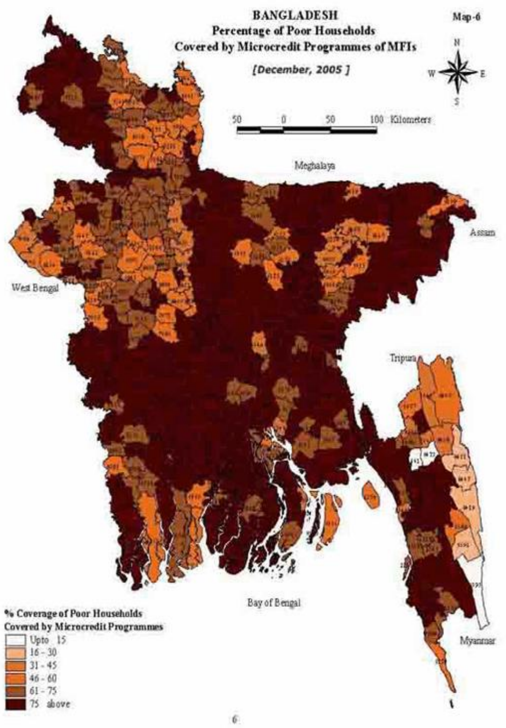
As we already discussed in Chapter 5.1.3, the capping of interest rates by the central bank, the government, a regulatory authority or a microfinance wholesaler can ultimately result in the limiting of access of the very poor to financial services. Also, operating in more remote areas tends to be more costly for MFIs (Mahmoud, C. et al., 2009). In order to determine whether interest rate capping results in lesser coverage of microfinance services, one would need to analyze which region is covered by what kind of MFIs and whether drop outs would have an effect on the borrowers or if other, financially more viable MFIs would step into the breach. PKSF published its last map on microcredit coverage in upazilas (subdistricts) of Bangladesh in 2006. Figure 7 shows the distribution of MFIs for each subdistrict and Figure 8 the percentage of poor households covered by MFI programs in 2005. Figure 7 reveals very thin coverage of MFIs especially in the east and south-east. If only a few MFIs would have to shut down their operations because they couldn't cover their costs at such low interest rates, the poorer population's access to microfinance would most likely be constrained.

Fig. 7 : Upazilawise distribution of MFIs, 2005



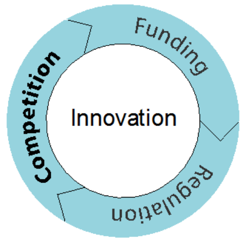
Source: PKSF (PKSF, 2009e)

Fig.8: Percentage of poor households covered by MFI programs, 2005



Source: PKSF (PKSF, 2009e)

Yet another, perhaps even more profound area of research would be to investigate how microfinance coverage is affected if a multitude of very small MFIs fail to meet the minimum requirements of the MRA. 2'749 MFIs are considered as very small and are given time until the end of 2009 to expand their operations. Many of these MFIs are not in touch with the MRA and it is likely that a majority of them will not be able to obtain license (An Overview of NGO-MFIs in Bangladesh, 2009).



Government programs

Government programs involved in microfinance in Bangladesh charge artificially low interest rates (between 10-20% APR), since they do not have to pay for the full costs of their operations, such as cost of fund or loan loss provision (Bangladesh Microfinance Country Profile, 2006).

Commercial banks in microfinance

As described in chapter 4.1.5, commercial bank's involvement in lending to NGO-MFIs is still relatively modest and at rates between 10-12%, they find it hard to compete with the rates charged by PKSF (Wright / Alamgir, 2004). In the past years though there has been growing interest both on the side of MFIs as well as with commercial banks to establish linkages between the formal and semi-formal sector (Awal, 2006), and since not all MFIs are satisfied with the conditions PKSF imposes in exchange for loans and the need for funding is high, these MFIs are willing to take loans from commercial banks at higher rates.

6.3.2 Interest Rates and Competition

In fully commercialized, competitive environments, price usually becomes one of the main weapons for competition. Competition often results in a price war, and the winner captures a bigger market share. In the 1990's, when expansion was especially widespread and hasty, the products were mainly the same across all the NGOs, which made competition between MFIs unnecessary, since an almost endless market was being exploited. When competitive pressure started to build up in the 1990's, and then, increasingly, at the turn of the century, the first thing NGO-MFIs competed over was not interest rates, because there were many other ways they could make their programs more attractive, for example by cutting some of the inflexibilities in the microfinance industry. Wright and Alamgir (2004) noticed that large MFIs tend to attract poor borrowers with larger loan sizes, resource rich MFIs have the possibility to disburse loans quicker than their competitors, and flexibility in terms and conditions of loans is used as a means to differentiate from other MFIs. For example, poor borrowers can now join a NGO instantly. They don't have to wait to join a group, and they can take a loan immediately. Easy access to savings have evolved as a direct result of competition, and additional services such as education, training and health services can provide one MFI with a competitive advantage over another.

Rutherford (Interview, 2009) pointed out to the Author, that during the period of product evolution in Bangladesh, evolution itself took care of the competitive matters, like dropping group modalities, or offering higher loans, etc. With the current maturing of the industry, interest rates will become more important and probably continue to drop. He believes that, especially the big NGO-MFIs that make considerable profits would have room to reduce rates even further and points out the case of Grameen, which is doing very well *because* it charges less than its competitors.

It is difficult to assess the impact on smaller NGO-MFIs if interest rates drop further. One main reason is that most NGOs provide nonfinancial services or so-called ‘credit plus’ activities as well and rarely publish or allow access to any separate accounting of their microfinance operations (Rahman / Charitonenko, 2002). CDF Statistics though imply that a majority of small and medium sized MFIs are not sustainable (2002) and as mentioned before, donors are becoming less willing to finance operational expenses of MFIs.

7. Conclusion

Funding

PKSF as a source of funds for MFI is in good part responsible for the rapid growth of the MFI sector from the 1990's onwards. Yet its role as wholesaler must be regarded critically. It is not clear to what extent it was really necessary for the World Bank to set the interest rates charged on PKSF loans to its member MFIs so low, thereby fueling MFIs with Soft Loans. Up until recently, having access to finance *at all* was more important for poor borrowers than what the interest rates may be, and in the 1990's MFIs did not yet have to compete with the banks' interest rates. Therefore the question remains: is it possible that PKSF, by fueling MFIs with cheap money, may have actually hindered commercialization – although it generated rapid growth – in the sense that the MFIs did not have to learn to apply market-based principles to microfinance?

There seems to be a tendency towards increased linkage of MFIs to the formal sector. Although the share of bank loans to the loan portfolio of MFIs has been increasing, this does not imply that this source of funding will be available to all MFIs. Although banks are becoming more and more interested in wholesaling to MFIs, there are still certain reservations on the side of the banks. If the industry wants to build real confidence between the two parties, it would have to provide certain regulations for the banks' funding of MFIs. As of this writing, such formal, binding regulations do not exist.

Finally, although financially viable MFIs which can afford taking a loan through a bank are increasingly willing to do so in order to be freed of the conditions imposed by the PKSF, banks still find it relatively hard to compete with PKSF's Soft Loans, since the rates charged by banks are considerably higher.

Regulation

In MFI's earlier days, MFI clients were primarily net borrowers. However, this has changed since the turn of the century, when donor funds began to tail off. At that point, many MFIs started to introduce voluntary savings and open access accounts as additional sources of funds. Therefore there was a growing need to regulate these activities, since poor borrowers could ill afford to lose their hard-earned savings.

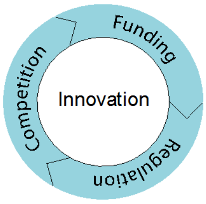
It is still too early to draw any all-encompassing conclusions about the new regulatory framework for the country's MFIs. There will certainly be some changes made to the framework over time, and the future issue will be about which MFIs – the many smaller, ore the fewer larger – will exercise their influence on the regulatory structure.

Whereas the big and powerful MFIs rather oppose to a rigid regulatory framework, the small MFIs that had previously functioned in a legal grey area could benefit from and be protected by such a framework. On the other hand, it will be interesting to see how politically independent the MRA will really be. The introduction of an interest rate ceiling could lead to the MFIs becoming even more dependent on the PKSF's soft loans and could thereby impede commercialization and ultimately the process of innovative product development.

Nevertheless, the fact that all MFIs will be subject to reporting and accounting standards – and therefore be more transparent in their operations – might improve the banks' confidence in these institutions, resulting in increased linking activities between the formal and the semi-formal sector. This could help alleviate funding problems for some of the MFIs and give them more room for innovative experimentation.

Competition

Competition has increased rapidly since the end of the 1990's. Today, small MFIs represent serious competition for the larger ones. This competition has led to massive client overlapping and increased arrears. Although reasons for overlapping lie at loan receiver level as well as at managerial level of MFIs, the fact that estimates for overlapping in Bangladesh are so high could be a sign that the mass of products offered by the MFIs maybe aren't attuned to the customer's individual needs after all. Yet, measuring of overlapping remains a difficult matter. In any case overlapping is a great concern for most Bangladeshi stakeholders and it is not clear, whether or not it might become a big bubble that will damage the industry or if it's a passing phase. ASA has already decided to stop expanding, and others may follow its example.



As competition increases, the importance of interest rates will increase as well. The larger MFIs will be able to withstand periods of lower interest rates more easily than the smaller ones. Lower interest rates are welcome when effected through competition, because competition as a rule leads to innovative product development. However, when interest rates are artificially held low because of political motives, the small MFIs operating in rural regions and also those MFIs which in general serve the very poor could be forced out of business, thus causing the poorest of the poor to be excluded from the finance system.

Although Bangladesh is the birthplace of microfinance, it is only now taking measures that will eventually lead to real commercialization. In Latin American countries commercialization of the microfinance sector is far more advanced thanks to regulatory frameworks which further fully commercial microfinance banks such as Mibanco in Peru or Banco Compartamos in Mexico.

The traditionally hands-off policy of the government of Bangladesh in the microfinance sector led to the rapid growth of the sector, and only now are the MFIs getting involved with regulation and its related implications for commercialization. For this new era to be successful, all involved parties with their respective interests - the big MFIs as well as the small ones, and the government -will have to cooperate with each other.

Innovation or stagnation

Let us recall our scheme in chapter 1, where we established a relation between regulation, funding, competition and – ultimately – innovation:

We stated that through achievements in sustainability MFIs are able to reach great levels of outreach and accommodate demand through innovative product development. Financial sustainability means turning away from donor grants and soft loans and making use of commercial funding sources. These commercial funding sources will only be available to properly regulated and supervised MFIs. Increasing competition as a result of market saturation will then in turn lead to the development of innovative microfinance products.

Although Bangladesh is the birthplace of microfinance, it is only now taking measures that will eventually lead to increased commercialization and therefore to competition, ultimately leading to real innovation of microfinance products that suit the needs of the individual borrower. In Latin American countries commercialization of the microfinance sector is far more advanced thanks to regulatory frameworks which further fully commercial microfinance banks such as Mibanco in Peru or Banco Compartamos in Mexico.

The traditionally hands-off policy of the government of Bangladesh in the microfinance sector led to the rapid growth of the sector, and only now are the MFIs getting involved with regulation and its related implications for commercialization, competition and innovation. For this new era to be successful, all involved parties with their respective interests - the big MFIs as well as the small ones, and the government -will have to cooperate with each other.

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Appendix I: Product List of Grameen Bank

These product characteristics have been derived from Rutherford, S. et al. (2004).

Product	Description	Terms	Interest rates
Group membership and Kendra	Groups formed of five people (one sex), with revolving chairman. After Grameen Staff recognizes group, borrower is member. 6-10 Groups, meet weekly, in a Kendra (with Chairman). Most bank transaction take place in Kendra.		
Savings			
Personal Savings	**Depositing**: Should be weekly at Kendra meeting. With loan minimum deposit per week. **Obligatory Deposits**: Obligatory deposit of 2.5% of loan if loan is taken (except flexi loan). **Withdrawing**: At any time and any amount. No withdrawal when flexi- or bridge loan.		8.5% Paid annually
Special Savings	**Obligatory Deposits**: If loan obligatory deposit of 2.5% of loan in Special Account (5% with flexi loan). **Withdrawing**: First 3 Years blocked. After that may withdraw balance of account each 3 Years (except 2000 taka). **Share purchase**: May be done with Special Savings Money.		8.5% Paid annually
Other savings products			
Grameen Pension Savings	**Eligibility**: Obligatory for all borrowers with 8’000 taka and more in loans. Optional for other members. **Term**: 5 or 10 years **Maturity**: At maturity can be taken as lump sum or monthly income.		10% for 5 year term, 12% for 10 year term
Fixed deposits	Lump sum deposits, attract high interest for members.		8.75-9.5%
“Double in 7 years” fixed deposit	Double the amount deposited after 7 years.		10%
Monthly Income Scheme	Pays monthly income starting just after the sum is deposited, in stead of term-end interest.	10.04% for 5 year term 10.67% for 10 year term	
Loan Products			
Basic Loan	**Eligibility**: Any member older than 1 week. Group and Kendra leaders decide. **Security**: No collateral. Fellow members agree to help struggling member as good as possible (not obligated). **Obligatory savings**: 5% of loan in Personal % Special Savings account. If loan > 8’000 taka then must open a GPS with		20% p.a.

	monthly deposit of min. 50 taka. **First Loan Value**: Normally 5’000 taka (for starters). Subsequent loan value: Determined by 1)individual and group repayment / meeting attendance and 2)Savings balances. **Term**: 3-36 months **Loan ‘top-up’**: If loan > 12 months, you may top-up after 6 Months the amount repaid. **Repayment**: Weekly, amount may vary. **Flexi-Loan:** Obligatory if borrower can’t repay basic loan for ten consecutive weeks or can’t make GPS deposits for four months. No fixed term and schedule for Flexi Loan. Flexi Loan can also be top-up’d. After repayment of Flexi Loan, member is eligible for further basic loans. Members with Flexi Loan may not withdraw any savings from any savings accounts.	
Other Loan Products		
Housing Loan	**Term**: 1-10 years **Loan Size**: 5’000-25’000 taka. A loan > 25’000 taka can be taken as a Special Investment Loan with 20% p.a. **Repayment**: Weekly. Prepayments accepted. Disbursement of loan to members against certain **priority criteria**: need, quality and age of membership, since amount available is limited by Zone.	8% per year
Bridge Loan	**Eligibility**: If savings exceed 2/3 of total outstanding loan balance. **Loan Size**: up to the amount where savings balance is 2/3 of outstanding loan. **Term**: max. 6 months **Repayment**: any amount at any time.	20% p.a.
Special investment loan	**Eligibility**: Proof of viable larger enterprise capable of absorbing extra loan capital. **Loan Size**: higher than basic loan. **Terms**: Same as basic loan. Need to make higher weekly deposits into personal savings account.	
Education loan	Loan for higher education of Grameen members students. Student begins to pay back as soon as starts to earn.	
Loan/life insurance savings	Optional insurance coverage for all loans. **Premium**: 3% of outstanding value of current loan on the last day of the calendar year.	
Other services and features		
High-school scholarships	High-school scholarships for clients’ children	
Destitute and ‘struggling’ members	Zero interest rate loans for beggars without any fixed loan terms.	0%

Appendix II: Product List of ASA

These product characteristics are quoted from the ASA Website (ASA, 2009c)

Product	Description	Terms	Interest rates
Basic Loan Products			
Small Loan for Female Clients (78%)	Economically active poor to undertake or strengthen income generating activities.	Init. Max Loan size: BDT 10,000-20,000 or US$ 150-300 depending on the economic potential of area and client's capacity as well Loan Term: 45 weeks Repayment: 37 equal weekly installments Incremental increase of loan size: BDT 4,000 or US$ 60 (maximum) in each loan cycle	12.5% (flat)
Hardcore Poor Loan (1%)	A flexible loan product for hardcore/ultra poor to match their irregular pattern of income generating activities.	Init. Max Loan size: BDT 5,000 or US$ 75 Loan Term: Flexible; 4, 6 or 12 months Repayment: Flexible; Monthly, quarterly and half-yearly installments or at a time Incremental increase of loan size: BDT 2,000 or US$ 30 (maximum); annual	12.5% (flat)
Small Business loan (12%)	A loan product for informal or formal micro enterprises to promote production/enhance business activity and employment generation.	Init. Max Loan size: BDT 50,000 or US$ 735 Loan Term: One Year Repayment: Flexible; Weekly or Monthly Incremental increase of loan size: BDT 7,000 or US$ 100 (maximum); in each loan cycle	12.5% (flat)
Small Entrepreneur Lending (SEL)	A loan product for informal or formal small/micro enterprises to promote production/enhance business activity and employment	Init. Max Loan size: BDT 400,000 or US$ 5,900	12.5% (flat)

(6.5%)	generation. This product also caters to Information Technology related activities.	Loan Term: 12/18/24 months Repayment: Monthly Incremental increase of loan size: Not fixed; depends on projects	
Agri-business Loan (1.5%)	A loan product for supporting agribusiness related activities.	Init. Max Loan size: BDT 400,000 or US$ 5,900 Loan Term: 12/18/24 months Repayment: Monthly Incremental increase of loan size: Not fixed; depends on projects	12.5% (flat)
Special Loan Products			
Small Loan for Male Client	A special loan product designed for the spouse or family head of ASA's female client to cater to the need for strengthening supplementary/main income generating activities of the family by injecting some working capital. It also intends to support rural households for their agricultural activities during seasons.	Init. Max Loan size: BDT 4,000 or US$ 60 Loan Term: One Year Repayment: Monthly (12 equal monthly installments) Incremental increase of loan size: BDT 1,000 or US$ 15 (maximum); annual	12.5% (flat)
Business Development Loan	Defaulters who lost projects due to factors beyond their control and have willingness to pay. Mainly to cater to the need of small and small business loan clients'.	Init. Max Loan size: BDT 5,000 or US$ 75 Loan Term: One Year Repayment: Flexible; Weekly or Monthly Incremental increase of loan size: Not fixed; depends on progress and capacity	12.5% (flat)
Rehabilitation Loan	A loan product for clients' affected by natural disasters e.g., flood, cyclone etc.	Init. Max Loan size: BDT 1,000 or US$ 15 Loan Term: 12 months Repayment: Flexible; Weekly or Monthly Incremental increase of loan size: NA	No interest
Short Term Loan	A loan product of short duration for clients' having business activities in need during seasons.	Init. Max Loan size: BDT 100,000 or US$ 1,470	12.5% (flat)

		Loan Term: Flexible; 3 months Repayment: Flexible; Monthly or at a time Incremental increase of loan size: NA	
Scarcity Loan	A loan product for clients' in scarcity during lean season; Loan can be used for both asset building before the lean season and consumption during the lean season.	Init. Max Loan size: BDT 3,000 or US$ 45 Loan Term: 3 months Repayment: Flexible; Monthly or at a time Incremental increase of loan size: NA	12.5% (flat)
Education Loan	A loan product to support clients' children studying in 8th grade and above.	Init. Max Loan size: BDT 3,000 or US$ 45 Loan Term: One Year Repayment: Weekly Incremental increase of loan size: NA	10.0% (flat)
Savings Products (equal to 19% of total portfolio)			
Mandatory Savings	Clients belonging to basic loan category except SEL and BDS loan are required to deposit a fixed amoun	**Deposit rate (minimum):** BDT 10 or US$ 0.15. **Term:** Continue throughout the membership. **Deposition mode:** Depends on Loan repayment mode. **Withdrawal provision:** Clients can withdraw anytime but need to keep 5% equivalent of loan (principal) as balance.	4% (flat)
Voluntary Savings	Clients who participate in mandatory savings is optional	**Deposit rate (minimum):** Any amount above mandatory deposit. **Term:** Continue throughout the membership. **Deposition mode:** Depends on Loan repayment mode. **Withdrawal provision:** Clients can draw anytime but need to keep 5% equivalent of loan (principal) as balance.	4% (flat)

Long Term Savings	Any client can participate in this product; an installment based deposit with fixed return usually higher than regular savings but close to fixed rate of return	**Deposit rate (minimum):** 50/ 100/ 200/ 300/ 400/ 500. **Term:** 5 or 10 years. **Deposition mode:** Monthly. **Withdrawal provision:** Clients can draw any time before maturity but with lower rate of return.	9% at maturity
Insurance/Security Fund Product (equal to 21% of total portfolio)			
Loan Insurance	Any client can participate in this product; an installment based deposit with fixed return usually higher than regular savings but close to fixed rate of return.	**Premium in each loan cycle:** 0.1% except Small (male) loan which is 0.05% **Insurance Payment:** Non-refundable but in case of death of Borrower or Borrower's spouse, the total outstanding is written off **Term:** Continue throughout life as borrower **Deposition Mode:** Cash before disbursement **Management of Insurance Fund:** ASA	
Member's Security Fund (Mini Life Insurance)	All Basic Loan Clients' must contribute and participate in this product.	**Premium in each loan cycle:** BDT 10 or US$ 0.15 per week, BDT 50 or US$ 0.72 per month but BDT 10 or US$ 0.15 per month for Hardcore Poor Loan **Insurance Payment:** Refundable with 4% interest but 6 times the amount of balance paid in case of client's death **Term:** Eight Years **Deposition Mode:** Cash with loan installment **Management of Insurance Fund:** ASA	4%
Male Member's Security Fund (Mini	Spouse or Family Head of Female clients' may participate in this product.	**Premium in each loan cycle:** BDT 10 or US$ 0.15 per week	2%

Life Insurance)		**Insurance Payment:** Refundable with 2% interest but 3 times the amount of balance paid in case of client's death **Term:** Four Years **Deposition Mode:** Cash with loan installment **Management of Insurance Fund:** ASA	

Appendix III: Product List of BRAC Bank

These product characteristics are quoted from the Brac Bank Website (Brac Bank, 2009d).

Product	Description	Terms	Interest rates
SME Banking			
Anonno Rin business loan	business loan designed to finance small scale trading, manufacturing and service ventures, especially to to help small and medium entrepreneurs to meet their short-term cash flow shortages and bridge the fund-flow gaps. Loan for Working Capital Finance and/or fixed assets purchase	Loan without mortgage. Installments: monthly or single. Discount rates for borrowers who pay in due times.	17-17.8%
Apurbo Rin business loan (rel. bigger)	Loan for Small and Medium business. Targets relatively bigger business units requiring loan above tk. 8 lacs to 30 lacs.	Req.: minimum of 3 years of some business activities. Business must be a going concern for 3 years. Disbursement in 1 or 2 installments. Flexible monthly repayment plan.	17%
Pathshala Rin Educational institutions loan	Loan for purchasing fixed assets. Loan meets the needs of small and medium sized private educational institutions, such as kindergartens, schools and colleges etc.	Req.: The educational institution must be in operation for minimum 3 years. The educational institute must be a profit making concern. Minimum BDT 3 lac to maximum BDT 30 lac Loan up to 9.5 lacs without Mortgage Easy monthly installment	17-17.25%
Aroggo Rin Health service Provider loan	Loan meets the needs of various Health service Providers like private clinics, diagnostics centers and doctors' chambers.	Req: Minimum 2(two) years in operation Health center must be located in the same address for at least 6 months Health center must be a profit making concern Minimum of 3 lac to maximum of 30 lac	17-17.25%

		Repayment within 3 years	
Digoon Rin Double loan on deposit	Double loan on deposit. Enables to take double amount of loan on the deposit for business expansion.	Req: Entrepreneur having minimum 2 years of business activities The business which must be a going concern for 2 years Cash security (BRAC Bank FDR) 50% of the loan amount. Minimum of 5 lac to maximum of 30 lac BDT. Installments: monthly or single	17-17.8%
Prothoma Rin Fixed Asset loan for women entrepreneurs	Loan for women entrepreneurs. Loan for working capital finance and/or fixed assets purchase.	Req: Entrepreneurs with minimum 2 years experience in the same line of business Minimum 1(One) year of continuous business history. Minimum BDT 3 lac up to maximum of BDT 9.5 lac. Loan without Mortgage. Discount rates for borrowers who pay in due times.	15%
Prapti Current Account Interest bearing current account	Interest bearing current account. Any institution can open this account in the name of the Institution Opening balance only BDT. 10,000.00 & BDT. 5000	Interest bearing current account. FREE Smart ATM Card with BDT-100,000 withdrawn facility (per day) from ATM & BDT- 300,000 from POS. No upfront relationship fees. No inter-city or intra-city online transaction charges. No Relationship fee will be charged if	Up to 4% interest on daily balance.

		half yearly average is BDT 25,000, along with free cheque book.	
Cash Secured Loan	Loan for starting new business. Loan against FDR 2 types of loan facility in the product i.e. **Secured Loan** and **Secured Overdraft**. These facilities are fully secured by fixed deposit of BRAC Bank.	Req: 6 (Six) months experience in the same line of business. BRAC Bank FDR minimum 100% of loan amount. From minimum BDT 3 lac up to maximum of BDT30 lac.	2-3% spread over FDR rate
Bizness loan	Equated monthly loan facility for all types of business who have healthy bank transactions for the purpose of working capital finance and/or fixed assets purchase.		17.8%
Proshar BL for manufacturing businesses	loan for small & medium sized manufacturing business. Loan for working capital finance and/or fixed assets purchase.	Req: Entrepreneur must have minimum 2 years experience in the same line of business. Minimum 2 (Two) years of continuous business history of the enterprise. From minimum BDT 3 lac up to maximum of BDT 30 lac. Without Mortgage up to Taka 9.50 Lacs.	17-17.25%
Trade plus Import Businesses	Loan for import-oriented businesses to meet their trade finance requirements.	Req: Import oriented business with valid trade license, Import registration certificate, V.A.T. Registration certificate & T.I.N. Certificate. Features: Two types of Letter of Credit Facilities – One Off LC and Revolving LC Two types of post import finance facility –LATR & Revolving loan Overdraft facility for day to day working expenses Loan tenure of Letter of Credit – 180	17-17.8%

		days Flexible repayment system Limit: LC (One-Off): BDT 3.00 Lac – BDT 30.00 Lac LC (Revolving): BDT 5.00 Lac – BDT 30.00 Lac LATR: BDT 3.00 Lac – BDT 30.00 Lac Revolving Loan: BDT 5.00 Lac – BDT 30.00 Lac Overdraft: BDT 5.00 Lac – BDT 30.00 Lac	
Super Supply Loan	Loan for Suppliers of various large retailers, marketing companies, manufacturing companies and various corporate houses.	Req: Entrepreneur having 2 (two) year's experience in the same line of business. Operating the current business for last 1 (one) year. From minimum BDT 4 lac up to maximum of BDT 30 lac. Installments: Monthly or Single	16-17.8%
Retail Banking	***Loans***		
Salary Loan Loan against salary	Loan against your salary.	Req: Employed as a regular salaried staff. Have minimum age of 25 years, max - 53 years (at the time of application). If you earn a gross monthly salary of Tk. 10,000. Anywhere between 1.5 lac to 10 lac (maximum) Features: • Loan up to 15 times of your Salary	19% Person with salary account with BRAC Bank will enjoy 1% less than the prevailing

		• No collateral of cash securities • Loan processed just within 24 hours • Flexible repayment Equal Monthly Installments (EMIs) over a period of 12 months to 60 months • minimum 2 years at the current organization	interest rate
Car Loan	Car Loan	Req: Both salaried executives and business persons. Both salaried executives and business persons. Age between 21 at the time of application to 60 at the time of maturity. Minimum monthly income BDT 25,000. Length of service/Age of business: Minimum 2 years.	16.5-18.5%
Retail Banking	***Deposit Products***		
Fixed Deposit	General Features » A term deposit with a guaranteed monthly return on investment. » Competitive interest rates. » Early encashment flexibility. » Secured Loan and/or Secured Overdraft eligibility.	Req: A Current Account or Savings Account	Competitive interest rates
InterestFirst Fixed Deposit	Interest gets paid **in advance**.	Instant interest on fixed Deposit Interest reinvestment opportunity Attractive rate of return Loan facility against the IFFD	
Abiram' Account	Fixed Deposit scheme with a guaranteed monthly return on investment. Features Monthly interest on your depositAttractive rate of return.		

	95% loan against your deposit.		
Deposit Premium Scheme (DPS)	General Features Monthly installments can be as low as Tk. 500 or any multiples of it. On-line banking facilities.		
EZee Account	A non-cheque interest bearing account for small savers who are in frequent need of transaction.	24 hour access to ATMs and POS Interest on daily balance No minimum balance No ledger (Buch) fees	4%
Savings account	Regular savings account with interest on deposit amount. Features 8 transactions Cash withdrawal and deposit of 5 lac and above need clearification No requirement for notices to be given before making a withdrawal Use our network of ATMs for easy cash withdrawal		Interest rate of 5.5% on avarage monthly balance
Current Account	Current Account, deposit and withdrawal		0-4%
Salary Account	Payroll account for Employers and Employees.	Req: The organization needs to have a minimum of 10 employees and a payout of Tk. 1 lac per month and an average salary per employee of Tk. 10,000 per month. No minimum balance required. No Cheque book. ATM Debit Cards. The account also accrues interest on deposits.	4%
Probashi Banking			
Probashi Current Account	For Probashi Bangladeshis / Returning Bangladeshis who do not wish to earn interest due to religious or other reasons. This account also comes with cheque book and ATM card and is ideal for regular transaction		No interest
Probashi Savings Account	A regular savings account in local currency for the NRBs who is residing abroad and want to save their hard-earned money to utilize in	Any NRB over 18 Years with legal / resident work permit	

	future after coming back to Bangladesh. Interest bearing Taka account in which interest is paid twice a year.		
Probashi Fixed Deposit	Fixed Deposit for expatriates.	The NRBs' can choice and pick any of the Fixed Deposit maturity period among from different set period of time like: 3 months, 6 months, 12 months, 24 months, 36 months.	

Appendix IV: Product List of Proshika

These product characteristics are quoted from the Proshika Webiste (Proshika, 2009c).

Product	Description
Credit From the Revolving Loan Fund	PROSHIKA's approach to credit is 'credit plus plus'—a system under which not only credit is given but proper training, technical assistance, marketing facilities, as well as social and other development supports are also provided. Through this unique peer group lending system, a total of Tk. 36,642 million has been disbursed against 904,703 projects, creating 10.19 million employment/self-employment opportunities for the poor. The management of credit is highly participatory.
PROSHIKA Savings Scheme (PSS)	The PSS has been introduced on the basis of certain principles like security of group savings, life insurance, risk coverage for damages caused by natural disasters, accessibility, etc. The life and property risk coverage aspects of PSS are unique in Bangladesh. The number of PSS groups presently is 114,864 while the number of members is 1.81 million. The savings balance stands at Tk. 1,854.02 million. The total compensation paid from the PSS so far on account of death and damage is Tk. 58.16 million.
Economic-Social Security Programme (ESSP)	Established in July 1999, the ESSP has gained much popularity among the PROSHIKA group members for its uniqueness. The programme is meant to provide them with medical facilities, stipend to their children, loans at low rates of interest for constructing houses and purchasing land, and legal support, if needed. The ESSP savings balance stands at Tk. 104,82 million today. An amount of Tk.1.44 million has so far been paid to 282 students as stipend and Tk. 982,182 paid as medical bill.
PROSHIKA Fixed Deposit Scheme (PFDS)	PROSHIKA introduced this new savings product in 2005, for the group members who are interested in depositing their savings individually. This scheme is also very conducive to boosting poor people's savings and the process of their capital formation.
Practical Skill Development Training Programme (PSDTP)	This training largely contributes to the effective implementation of Employment and Income Generating (EIG) activities through providing relevant information about the management of projects implemented through environmentally sound technology. In skill development training, the number of courses offered so far reached 49,407. A total of 1.13 million participants have attended these courses.
Small Enterprise Development Programme (SEED)	The aim of this programme is to provide the graduated groups of PROSHIKA with entrepreneurial support loans along with technical assistance, formal training, business counselling and marketing support. The programme is operated by PROSHIKA SEED Trust. Up to December 2006, a total of 13,441 entrepreneurs (40% female) have been organized at 76 PROSHIKA ADCs and Tk. 742 million loans have been disbursed among them. A total of 43,095 new employments (54% full-time and 46% casual) have already been created. Both formal and non-formal training has been imparted to around two thousand entrepreneurs. Business counseling and technological and marketing extension supports have also been provided to them.

Livestock Development Programme (LDP)	Under this programme 5,014, 1,157 and 195 group members have so far been trained as vaccinators, paravets and artificial insemination technicians respectively. They are working as resource persons in various livestock-related group training courses and earn Tk. 1000-2000 per month on an average. So far, a total of Tk. 2,305.39 million has been disbursed to the group members through 50,066 livestock projects.
Fisheries Development Programme (FDP)	The programme facilitates the access of poor fishers and poor fish farmers to the public and private water resources and contributes to the overall fish production of the country. Credit, again, plays the most important role here in income generation. So far, a total of 680 ponds have been re-excavated by the group members and thousands of members received help on getting license for fish farming in 183 water-bodies. A total of Tk. 1,304.91 million has been disbursed to date through 25,093 fishery projects.
Apiculture Development Programme (ADP)	PROSHIKA has undertaken the Apiculture Development Programme as one of the most promising, and environment-friendly income generating activities for its group members. Apiculture involves less investment of capital and time yet yields high returns. PROSHIKA has also innovated and introduced a number of new technologies to modernize apiculture practices in Bangladesh. Along with credit, PROSHIKA provides training and also marketing facilities to those group members who produce honey.
Sericulture Development Programme (SDP)	The SDP is one of the most attractive and successful programmes of PROSHIKA and an alternative income generation option for its group members as well as a means to promote the country's rich heritage of silk fabric. More than 2.14 million mulberry saplings have been planted by the group members under this programme. The group members have implemented a total of 2,915 projects with Tk. 29.60 million over the years.
Organic Agriculture Programme (OAP)	The programme promotes uses of organic methods in cropland and vegetable production. A total of 769,234 farmers have adopted organic agriculture in 228,411 acres of land so far. A total of Tk. 299.31 and Tk. 336.22 million have been disbursed against 5,496 organic agriculture and 9,393 homestead gardening projects respectively.
Irrigation and Farm Power Technology Services Programme (IFPTSP)	The main objectives of the IFPTSP are to enable the landless and marginal farmers to become owners of the irrigation and farming equipment like pumps, threshers, and shellers, and to increase their income by selling water for irrigation and providing farming services. Since the inception of this programme, 590,502 acres of land has been irrigated and ploughed by 203,651 group members. They have so far successfully implemented 7,214 irrigation and power tiller projects with Tk. 185.32 million.

Appendix V: Product List of SafeSave

These product characteristics are quoted from the SafeSave Website (Safesave, 2009a).

Passbook Savings	Clients may deposit as little as one taka ($0.015) when the collector calls at their house each day. Accounts with balances above 1,000 taka ($15) earn 6% interest. Clients may withdraw up to 500 taka per day ($7.50) at their doorstep, or up to 5,000 taka per day ($75) at the branch office within a guaranteed maximum of 10 minutes (larger amounts within 24 hours).
Long Term Savings	In two of our eight branches a longer-term 'commitment savings' account is available. It is not linked to loans, and savers deposit regularly for a defined term and receive higher rates of interest.
Loans	are not mandatory, and there is no minimum amount. All borrowers start with a credit limit of 3,000 taka ($45). One loan may be taken per household at a time. Loan interest is 3% per month on the declining balance (36% per year in nominal terms, or about 30% in real (inflation adjusted) terms). A minimum passbook savings balance equal to 1/3 of the loan balance is required as collateral at all times. No other collateral is required, nor does SafeSave require personal guarantors. Loans are taken and repaid flexibly, with no minimum nor maximum duration. Each month the minimum payment is the interest due, but principal repayment is left entirely flexible, to give clients the maximum flexibility in their use of loans. However, steady repayment progress is required to earn increases to the credit limit, and this provides an indirect incentive (along with avoiding future interest) to repay as quickly as possible. Roughly 2/3 of all clients hold a loan, with outstanding balances averaging 4000 taka ($57).