

**Channeling Commercial Fund to NGO-MFIs: A Case Study of Bank-NGO  
Linkage Programme of Sonali Bank.**

**A Dissertation**

**By**

**Md. Mukhlesur Rahman**

**Submitted to the Department of Economics and Social Science, BRAC University, in partial  
fulfillment of the requirements for the degree of Master of Development Studies.**

**July 2004.**

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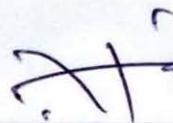
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## GLOSSARY OF TERMS

ADAB	:	Association of Development Agencies in Bangladesh
BRAC	:	An NGO, formerly known as Bangladesh Rural Advancement Committee
BURO	:	Bangladesh Unemployment Rehabilitation Organization
BRDB	:	Bangladesh Rural Development Board
CDF	:	Credit and Development Forum.
BT	:	BURO- Tangail, an NGO-MFI
CIB	:	Credit Information Bureau
GOs	:	Governmental Organizations
GKF	:	Grameen Krishi Foundation
GDP	:	Gross Domestic Product
IFAD	:	International Fund for Agricultural Development
MFI	:	Micro Finance Institutions
MFM	:	Micro Finance Markets
MCD	:	Micro Credit Division
MOU	:	Memorandum of Understanding
NABARD	:	National Bank for Agricultural and Rural Development
PAGE	:	Poverty Alleviation and Gender Equity
PKSF	:	Palli Karma Sahayak Foundation
PA	:	Per Annum
RLF	:	Revolving Loan Fund
SB	:	Sonali Bank
SHGs	:	Self Help Groups
SMEs	:	Small and Medium Enterprises
SDC	:	Swiss Agency for Development and Cooperation
UCCA	:	Upazila Central Cooperative Association



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## **Abstract**

Bangladesh has the largest and most vibrant micro finance industry in the world, which is greatly appreciated for its contribution in the reduction of poverty in the country. This industry, however, is encountering funding problem, because low cost funds and donations from abroad are declining. In this situation, strong suggestions have been made to finance this operation on commercial basis through statutory banks.

Sonali Bank has such a programme called SB-NGO Linkage programme for several years. This study analyzes the performance of this programme and concludes that by using comparative advantages, both the bank and the NGO-MFI can benefit through forging an effective linkage programme. Commercial banks can substantially increase their profitability through this kind of linkage, because the cost of lending is very low while the rate of recovery is very high. On the other hand, such programme significantly increases the sustainability and outreach of NGO-MFIs.

Therefore, the study strongly recommends to formulate a workable mechanism, which would facilitate mutual trust between commercial banks and NGO-MFIs, working towards an effective and sustainable linkage with necessary government and NGO collaboration. Under such a framework, both GO and NGO can work together on the basis of their comparative advantages through coordination and cooperation to effectively serve the cause of poverty reduction.

## CHAPTER 1

### 1.1 Introduction

Micro-credit or in its wider dimension, micro-finance has been accepted globally today as an approach to poverty alleviation and as a tool for development. It has been suggested that access to micro finance should be recognized as a right for the poor (Yunus, 2003).

The idea of micro-finance is something for which Bangladesh can deservedly claim the intellectual property right (Mahmud, 2003). Not only Bangladesh's model of micro-finance is now replicated worldwide, it has also found its place of pride in standard economic textbooks. Micro-credit has now reached half of all rural households in Bangladesh. Perhaps, no single poverty intervention programme ever reached such a wide coverage anywhere in the world. The success of micro-finance has been mainly due to effective targeting and addressing the credit needs of the poor people.

Micro-finance in Bangladesh has passed through three phases: experimentation phase in the seventies, formalization phase in the eighties and expansion phase in the nineties. Currently it is passing through consolidation and institutional phase. The most imminent challenges of micro finance sector is to formulate strategies to help achieve the Millennium Development Goals (reduce by half the proportion of people living in extreme income poverty: living on less than \$1 a day).

Micro Finance Markets (MFMs) in Bangladesh can be classified into three sectors: formal, semi-formal and informal. The formal sector includes regulated Financial Institutions (FIs). The semi-formal sector includes Micro Finance Institutions (MFIs) and programmes, mostly organized by Non-Governmental Organizations (NGOs) and some by Governmental Organizations (GOs), e.g., Swanirvar Bangladesh (a Government-floated organization) and Bangladesh Rural Development Board (an apex organization implementing the formal cooperative credit programme). The informal sector includes private transactions falling outside the formal and semiformal sources. Informal sources include traders and dealers, shopkeepers, landlords, friends and relatives.

So, one of the main challenges for the MFIs is to source sufficient capital to fund their expanding loan portfolio and the sustainability of both the institutions and the beneficiaries.



MFIs in Bangladesh, the majority of which are NGOs have over the last thirty years created demand for enormous funds in this field to flourish and sustain their activities. In course of time, sustainability has become a big issue in the operation of micro-finance globally and Bangladesh in particular. Cash flow in the form of low cost funds/grants/ donations which used to be generated for this sector, has been declining over the years, consequently, advocacy for mobilizing domestic resources has been becoming stronger both from the donor side and for the national authorities. For sustainability reason, there is no alternative to the commercialization of portfolio investment.

As a result, there has been a long- felt need for a mutually beneficial business linkage between commercial banks and NGO-MFIs, whereby the commercial banks' wholesale finance which the borrowing NGOs retail to their clients. India experimented with the linkage-approach first in this region. A couple of years ago the National Bank for Agricultural and Rural Development (NABARD), a subsidiary of Reserve Bank of India, has issued policy guidelines to the state-owned banks for establishing linkage with and leveraging fund to the NGO-MFIs and Self Help Groups (SHGs) of the country. The Philippines, Kenya, Srilanka and some Latin American countries have also adopted the linkage model as an alternative source of funding to the NGO-MFIs of their respective countries.

In Bangladesh, Sonali Bank (SB), the largest state-owned commercial bank has initiated a similar programme. SB stepped into micro credit operations as early as in 1974. Over time, it has earned valuable experiences from operating 20 rural/micro credit products. As a part of its ongoing efforts, SB adopted NGO-Linkage credit programme in 1997. A significant departure from the conventional lending system, the programme provides NGOs/MFIs access to SB finance for onlending to their clients. This dissertation makes an attempt to evaluate this important initiative.

## **1.2 Hypothesis**

Our hypothesis is that the NGO-linkage programme enhances the profitability of the bank compared to its traditional micro-credit operations and at the same time improves the sustainability of NGO-MFIs.

To examine the hypothesis that NGO-linkage programme enhances profitability of banks, linkage programme of SB has been compared with direct micro-credit operations. The indicators used to test the hypothesis are: investment, recovery rate, non-performing assets, and operational cost.

NGO-linkage programme of SB seems better than direct micro-credit operations because of (a) it is wholesale lending so, the operational cost is lower than direct micro-credit operations, (b) in NGO-linkage programme there is hardly any political interference/ government dictations. As a result the programme may run smoothly with consistently higher recovery rate (95%-100%) compared to direct micro-credit operations; (c) corruption, procrastination and bureaucracy are less as the loan proposal is processed and sanctioned by Head Office through one-stop service.

To examine the hypothesis that linkage programme improves the sustainable performance of NGO-MFIs on managerial, operational and financial aspects over the years. The indicators used to test the hypothesis are: growth in assets, growth in savings, growth in income, cost per unit money lent, operational and financial self-sufficiency and access to commercial fund.

The NGO-MFIs are expanding their programme by way of (a) deepening of financing among existing borrowers; and (b) increasing outreach by including new areas and new borrowers. The NGO-MFIs are not only expanding their programme, they are also diversifying their products based on the needs of the clients. As there are a huge number of players in the micro-credit business, micro-credit market is becoming competitive.

Against this backdrop, if MFIs fail to deliver the financial services, the interest of the poor will suffer; second, the MFIs will lose the confidence of the donors and the national government. Further, failure of MFIs will have serious implications for financial sector and development efforts of the government. Therefore, for long term sustainability both for institutions and beneficiaries MFIs require more to access fund from market and commercial source. At the same time capacity building is vitally important for MFIs and concerned stakeholders.

### **1.3 Methodology**

This research has been based on both qualitative and quantitative methods. Primary data supported by secondary data were collected mainly from SB and BURO Tangail (BT), an NGO-MFI. BT has been a partner of SB over the last three years. It has already utilized first credit line of TK one crore which was collateral free, and a second credit line has been opened for TK two crore for four years. In selecting this particular NGO-MFI, three factors were considered-namely, outreach, efficiency and networking.

**Quantitative Method:** To achieve the objective of this study both primary and secondary data were collected and analyzed. Quantitative data include bank statements of yearwise disbursement, recovery, rate of recovery, number of beneficiaries, etc. To assess the



performance of this programme in terms of cost of fund, rate of recovery, non-performing assets/classification status and growth information on NGO linkage and other micro-credit operations were compared.

Statements from NGO-MFI include disbursement, recovery, recovery rate, number of beneficiaries, growth in assets, portfolio investment, Revolving Loan Fund (RLF), savings, beneficiaries, etc. Other sources of data include statements from SB Head Office, NGO-Head Office/field office, and CDF book of statistics and PKSF annual report. For case study, field visits were made to collect necessary data.

**Qualitative Method:** The quantitative analysis was complemented by a qualitative study of two borrowers, of whom one was a success story and the other a non-success story. Data were collected from the field of the concerned NGO-MFI. Then the collected data were processed and analyzed to see the impact of micro credit on borrowers in terms of their socio-economic development. The two borrowers were selected purposively from the command area of BT. Information was collected on access to resources, housing, sanitation, education, and health and gender issues.

**Limitations of the Study:** This study can not be generalized because; only two borrowers were selected as case studies. While testing the hypotheses some interrelated variables were ignore. Besides time constraint was also a limitation during field visit.

#### 1.4 Organization of the Study

After the Introduction, Chapter 2 discusses the framework of micro finance system in Bangladesh, which includes a brief introduction to micro-credit and micro-finance, NGO and NGO-MFI, financial institutions, status of micro finance and commercialization of micro finance in Bangladesh. It is argued here that micro-finance must increasingly embrace commercialization to survive and expand. Chapter 3 provides an assessment of one particular case of commercialization of micro-finance, namely the Sonali Bank-NGO linkage Programme. It includes basic information on Sonali Bank and its micro-credit operations, evolving views on Bank-NGO Linkage programme and analysis of the statements of bank and NGO-MFI. Bank statements analysis include profitability and out-reach and NGO-MFI statements analysis include sustainability and outreach. Chapter 4 assesses the socio-economic impact of SB-NGO Linkage Programme through two case studies--one success story and a story of failure. Chapter 5 offers some concluding observation.

## CHAPTER 2

### The Framework of Micro Finance System in Bangladesh.

#### 2.1 Micro-credit and Micro-finance:

Micro-credit and micro-finance are very popular terms in the current development discourse. However, because these terms are often used synonymously, huge confusions and misunderstandings are being created in the development discourse as well as policy making. Muhammad Yunus (2004a), founder of the legendary Grameen Bank, underlined the problem in a recent micro-credit seminar: "The word 'micro-credit' did not exist before the seventies. Now it has become a buzz-word among the development practitioners. In the process the word has been imputed to mean every thing to everybody."

Micro-credit idea evolved as a part of paradigm shift in the Third World development thinking. Western interests in the TW development were inspired after WW II, when most of these countries gained political independence. To help improve socio-economic conditions of these decolonized countries, national and international agencies were created to transfer Western monies and materials (Harcourt, 1997).

Micro-credit has been defined by the Micro credit summit as "programs that provide credit for self-employment and other financial and business services (including savings and technical assistance) to very poor persons" (Micro credit summit 1997, Draft declaration and Plan of Action). Micro-finance is defined as a development approach that provides the financial as well as social intermediation (Ledgerwood, 1999; Robinson, 2002). Financial intermediation includes the provision of savings, credit and insurance services, while social intermediation involves organizing citizens' groups to voice their aspirations and concerns for consideration by policy makers, development of self-confidence etc.

The main features of micro finance are: delivery of credit and related services at commercial rates of interest in a convenient and user friendly way, quick disbursement of small and short term loans with no collateral, clear recovery procedures and strategies, maintaining high repayment rates, incentives of access to large loans immediately following successful repayment of first loan, guarantee mechanism and peer pressure and group lending.



Three types of lenders provide these services: formal institutions, such as rural banks and cooperatives; semiformal institutions, such as NGO-MFIs; and informal sources such as moneylenders and shopkeepers. Institutional micro-finance includes micro-finance services provided by both formal and semiformal institutions called Micro-finance Institutions (Asian Development Bank, 2004).

Apparently, the basic functional difference between micro-credit and micro-finance programmes concerns the type of services provided by them. Micro-credit programmes, such as Grameen Bank, provide mainly one kind of service-loan disbursement and recovery that are inseparably attached with group formation and compulsory savings mobilization. Micro-finance programmes, on the other hand, provide several financial and organizational services including credit, savings, insurance and community development. Thus, micro-credit is just one, albeit the most important, element of the current micro-finance movement. To paraphrase the popular methodological maxim of economics, micro-credit is a necessary, but not sufficient, element of the new financial sector that is emerging to cater to the credit needs of the poor who do not have access to formal sources.

From functional perspective, the differences between the two ideas appear more semantic than substantive. However, from conceptual perspective, the differences are very fundamental because they involve both motives and means of operating these functional ventures. Thus, the two programmes need to be treated separately for framing appropriate poverty- alleviating policies and institutions for the Third World.

## **2.2 Micro Finance Markets (MFMs) in Bangladesh**

MFM in Bangladesh can be classified into three sectors: formal, semi-formal and informal. The formal sector includes regulated financial institutions. The semi-formal sector includes MFIs and programmes, mostly organized by NGOs and some by GOs e.g., Swanirvar Bangladesh a government floated organization, and Bangladesh Rural Development Board (BRDB) implementing the formal cooperative credit programme and the informal sector includes private transactions falling outside the regulated banking framework. Informal sources include moneylenders, traders and dealers in agricultural markets, shopkeepers, friends and relatives.

After liberation in 1971, the banks operating in Bangladesh were brought under state ownership. These banks were merged and clustered into 6 commercial banks. Later in 1985, two were returned to private ownership. Among the other four, one has been privatized recently. The two state-run specialized banks are Bangladesh Krishi Bank (Bangladesh Agricultural Bank) and



Bangladesh Shilpa Bank (Bangladesh Industrial Bank). At present, there are four state-run commercial banks, five specialized banks, 30 privately-owned commercial banks (including BRAC bank), 11 foreign private banks and 36 financial institutions-privately and publicly-owned in Bangladesh (Ministry of Finance, 2003).

The main motivation behind nationalization or state ownership of the banks was to curtail the monopoly power of rural moneylender and expand network of formal financial institutions. But over time, formal sector institutions miserably failed to fulfil their objectives. So, NGO-MFIs emerged in Bangladesh to fill up a big gap in the area of rural development and poverty alleviation. The public sector development infrastructure could not be extended to the grassroots level, may be due to resource constraints and other policy shortcomings. Whatever facilities were created, service provision was poor and scanty. Inefficient and corrupt bureaucracy is an important constraint in service delivery. Absence of accountability and lack of transparency also inhibit efficient delivery of output.

### ***NGO-MFIs***

Literally, the term Non-Governmental Organization (NGO) may be used to include any institution or organization outside the government, and as such, may include political parties, private and commercial enterprises, academic institution, youth organization, even sports club, etc. But, these are not the institutions, which would be referred to by the terminology NGO. In fact, the terminology includes all those non- government organizations, which are involved in various development activities with the objective of alleviating poverty of the rural and urban poor. Such organizations are often termed as development NGOs (Task force Report 1990).

An NGO is a non-profit, non-partisan private body that comes into being as a result of personal initiative of an individual or a group of individuals to voluntarily undertake development work at grassroots level to improve the lives of the poor (Khan, 2003). In Bangladesh this terminology is used to refer to all such organizations and institutions that are registered with the Government under the voluntary Social Welfare Agencies (Registration and Control) Ordinance of 1961 and the Foreign Donation (Voluntary Activities) Regulation Ordinance of 1978. Some are also registered under the Companies Act 1869. In Bangladesh, the NGO-MFIs are involved in various social, economic and educational activities, more intensively in the rural areas.

In Bangladesh, NGOs have proved their superiority in providing quick and efficient delivery of development services. They have developed their service infrastructure at grassroots level. Target oriented organized group approach, awareness and motivation building, micro-finance,

health and education, promotion of income generating activities, providing skill training, input and marketing services- all have contributed positively in improving the well-being of the poor and in empowering them to have easier access to services and realizing their legal and human rights. The successful micro-finance programme developed in Bangladesh has become a model for the rest of the world.

In short the following are the advantages of NGO-MFIs over public agency (Khan, 2003):

- Capacity to reach the poor and work with them in remote areas
- Capacity to effectively encourage and promote local participation
- Capacity to work quickly and with other relevant agencies in a flexible manner
- Capacity to experiment, innovates and adapt.
- Capacity to facilitate local resource mobilization and ensure local development
- Advocacy capability.

An NGO having micro credit/ micro finance programme (at least 80% of its portfolio investment) is called NGO-MFI. In other words it is called credit plus NGO which deals with micro finance, and also with other socio-economic programmes like health, education, etc.

The informal sector includes private transactions falling outside the formal and semiformal sources. Informal sources include moneylenders, traders and dealers, shopkeepers, landlords, friends and relatives. This sector is widely perceived to function efficiently with low defaults and loan transaction cost. Personalized transactions alleviate information problems (for screening and monitoring borrowers); geographical proximity makes lenders more accessible; flexibility in terms and conditions allows customizing loans to borrowers' needs and the threat of monetary and social sanction creates strong disincentives to default.

The poor have less access to formal sectors because of the collateral obligation, traditional attitude and mindset, corruption, bureaucracy, etc. On the other hand, the semiformal sector having committed and skilled manpower, well organized network, accountability, flexibility and transparency cannot expand their loan portfolio and outreach due to funds constraint. Therefore, the poor having no other alternative go to the moneylenders to borrow though they charge usurious interest rate compared to the formal and semiformal sectors.



### 2.3 Status of Micro Finance in Bangladesh

Today, Bangladesh has the largest and most vibrant micro finance industry in the world. Its eventual proliferation has added a new dimension to the poverty reduction process of the country. In Bangladesh there are four main types of MFIs involved in small lending activities. These include Grameen Bank, NGOs and Government Agencies. CDF (2002) statistics reveal that about 1000 micro finance NGOs are carrying out micro finance operations. These micro finance NGOs have become more responsive to the demand for loan facilities. Over time, loan products have been diversified. Now there are more than 15 loan products including general loan, emergency loan, disaster loan, leasing loan, housing loan, loan for old aged people and community-based loan (e.g. for fisherman). Loan is given mostly for undertaking income-generating activities, which the customers perceive as a pure financial service. Normally, the loan ranges from TK. 1000 to 20,000 for one year. There is also a wide array of savings products available in the market. Some NGO-MFIs are introducing flexible rules for savings products. Though the micro finance sector, over time, has developed innovations and various credit and savings products yet it is confronted with many internal and external challenges. These include, among others, how to reach more poor people through micro-credit particularly the hard core poor, how to deliver micro-credit services in a sustainable way while serving the poor and how to balance the social objectives with the financial objectives of micro-credit. These are hampering the growth of the industry and creating hindrance to serve the customers effectively.

**Table-2.1 Performance of Micro Finance Sector.**

(Figures in million taka)

Sectors	Disbursement	Outstanding	Recovery (%)	No of beneficiaries
NCBs and other specialized banks including GB	252759.29	48976.02	86%	9704162
Different departments of GOB	55326.37	14804.31	94.58%	8476046
656-NGO-MFIs	208619.05	299888.12	97.93%	12860615
Total	525573.68	365011.06	94.5%	31598134

Source: CDF Micro Finance Statistics, Volume 15, December 2002.

## Sources of funds for NGO-MFI

The main sources of fund for NGO-MFIs in Bangladesh include the following:

- ◆ Savings.
- ◆ Donations (internal & external).
- ◆ PKSF and Commercial Banks.
- ◆ Accumulated surplus.

**Table-2.2 Revolving Loan Fund Position of NGO-MFIs in Bangladesh (December 2002)**

(Figures in million taka)

Sources	Amount	Percentage
Members Savings	10530.23	26.87
PKSF	8601.12	21.95
Local Bank Loan	3548.40	9.05
International NGO	211.75	0.54
International Donor	5815.36	14.84
Service charge	6979.78	17.81
BRAC	33.12	0.08
ASA	48.39	0.12
Proshika	70.48	0.18
Own fund of NGO-MFIs	2314.68	5.91
Others	1040.41	2.65
Total	39193.74	100

Source: CDF Micro Finance Statistics, Volume 15, December 2002

## 2.4 Commercialization of Micro finance

The emergence of the micro finance industry in Bangladesh presents a tremendous opportunity to extend financial services to the vast majority of the poor people, who constitutes about half the population. Commercial banks in the country typically serve no more than ten percent of the population. Rest of the poor does not have access to formal financial services.

In the last twenty years or so, the NGO-MFIs have devised appropriate financial service instruments to serve the poor people. Among them, a few organizations have demonstrated



splendid success and have become known worldwide. The country is now teeming with more than 1200 micro-finance NGOs. Most NGOs have taken up micro finance as core activity.

As micro-finance industry in the country is growing fast, new issues are constantly coming to the forefront. The role of market in micro finance institutions is one such vital issue that had been ignored hitherto. NGO-MFIs in Bangladesh have both social mission and commercial objectives. For a micro-finance programme each complements the other. Social mission assumes that more and more poor people should be covered and continuity of the service should be maintained through ploughback of the recovered fund.

The commercial sector has also socio-economic mission (in terms of employment generation, contribution to GDP and export earnings) as well as commercial objectives. They too are working for the welfare of the people satisfying their needs regardless of who are rich or who are poor. Social mission of NGO-MFIs also mean that they will go to the doorstep of the poor people with appropriate financial services with a view to eradicating poverty. While doing these, they will have to pursue commercial strategy meaning covering full cost recovery with a desired capitalization. Indeed, the NGO-MFIs should try to strike a balance between the two objectives in order to have the desired outreach and sustainability. However, unless there is adequate supply of funds and fair competition, delivery of financial services will not improve and the needs of the poor clients will remain unmet. In this context there is no alternative to commercialization as it is the crux of competition.

The term "commercialization" in the context of micro finance industry of Bangladesh is a relatively nascent idea and has understandably wide ramifications. This concept is also gradually gaining ground in some other developing countries of the world. Chiefly, it tends to treat the poor as clients rather than as beneficiaries. It conceives the micro finance market not as segmented markets but as an integral part of the country's total monetary system. It takes into view of healthy competition through product differentiation that encompasses the practice of marketing by launching new products. On the other hand, grant money that has zero cost is not perceived favourably by many small potential organizations in the country as it distorts market competition. On the whole, micro finance is considered as a business and there is every justification to look at it from the commercial angle. Notably, forty percent of a large sample of 618 NGO-MFIs surveyed recently shows that they have received 17% (CDF: 2002) grants from various foreign NGOs and donors for operating micro finance programmes. Of the aforesaid figure, about thirty five percent has also received concessionary loans. There may be a commonality, however, between the grants and soft loans recipients. This advantage of grants and soft loans received by a segment of organizations may put the majority NGOs in a difficult situation in pricing their loans. As a result, maximum number of NGOs will enjoy a very thin spread, if the grants and soft loan culture



continues. Under the circumstances, the donors should ponder to review their policy of providing grants. The donors may rather come up with alternative ways of financing. This will consequently invigorate commercialization and help expand the micro finance market. The commercial approach also argues for the delivery of services at a scale and cost commensurate with the needs and ability of the market for which it is intended.

The foregoing points suggest that real customer service through commercialization should be the basis for moving forward. In a competitive environment, customer satisfaction and commercialization should be the driving force for survival and growth. The micro-finance regulation in the country is now underway, which will provide a legal basis and streamline the current and future MFI activities. To reap the benefits of commercialization, the clients should be allowed to exercise free choices. They should be granted liberty to do their own financial management in order to increase their net worth. It is expected that the ensuing regulation will promote good governance and prudential management of NGO-MFIs, help protect depositors, improve access to finance, preserve the innovations and variety, integrate micro -finance with formal financial system and pave the way for commercialization of micro-finance sector.

Bank-NGO linkage provides one channel of commercializing micro-finance. Sonali Bank has taken important initiatives in this regard. The present dissertation will examine one such initiative.

## **2.5 Review of literature and Justification of the study.**

India experimented with the linkage-approach first in this region. National Bank for Agricultural and Rural Development (NABARD), a subsidiary of Reserve Bank of India (RBI), introduced in 1992, a pilot project for linking banks with the NGO-MFIs and Self Help Groups (SHGs) of the country to encourage thrift and savings amongst the rural poor and to supplement their credit needs through the banking system. With a view to studying the functioning of SHGs and NGOs and for expanding their activities and deepening their role in rural sector, RBI constituted a working group in November 1994, comprising of eminent NGO functionaries, academicians, consultants and bankers under the chairmanship of the Managing Director, NABARD. The working group has since submitted its report recommending for treating the linkage programme as a business opportunity for reaching rural poor. Based on the recommendation of the working group the RBI decided to extend SHG linkage programme beyond the pilot phase and advised the banks to make it a part of their mainstream banking function. As an extension to the project for linking SHGs, NABARD decided on pilot basis to extend refinance to banks for providing credit support to NGOs. The scheme envisages provisions of bulk loan to NGOs by banks duly



supported by NABARD refinance for on lending to the rural poor. NABARD has taken upon itself the task of training, orienting and information sharing among the participants in SHG-Bank linkage programme in a comprehensive manner. Banking with the poor, through SHGs and NGOs have gained acceptance among formal credit institutions in India. Several studies by NABARD and experience of banks have proved that this linkage programme has contributed significantly in reduction of transaction costs, besides reducing the financial risk.

The Philippines, Kenya, Sri Lanka and some Latin American countries have also adopted the linkage model as an alternative source of funding to the NGO-MFIs of their respective countries and being benefited significantly both in terms of profitability of banks and sustainability and outreach of NGO-MFIs.

There is a growing literature on the evaluation of linkage—based micro-credit programmes in Bangladesh. Hakim (1996) in a study of Janata Bank and PAGE (Poverty Alleviation and Gender Equality), a NGO Linkage programme identified some problem areas. From the NGO perspectives, the main problems were long time in loan processing, under amount of loan, fluctuation of interest rate with high transaction cost and collateral bias. On the other hand, subsidized rate of interest, shortage of trained manpower and absence of legal vis-a-vis regulatory frame work were some of the problems from the bank perspective. The study concluded that both the NGO and the bank should create national consultative mechanism to help each other in the sphere of exchanging ideas, views, information and evaluate the credit activities.

Roy, et.al (2000) tried to trace the origin and evolution of linkage approach in rural credit management, and to analyze the socio-economic aspects of some linkage schemes between GOs and NGOs to bring about effective rural development in Bangladesh.

The review of past studies on linkage issue have analyzed various models and micro aspects of rural lending from their own view point and the results of the studies conveyed many ideas in the operation and effectiveness of linkage approach on poverty alleviation. However, these studies do not touch on the question of achievements of different linkage programmes in terms of investment and profitability of banks and the sustainability and outreach of NGO-MFIs.

**Justification of the study:** After the liberation war in 1971 banks operating in Bangladesh were brought under state ownership and government directed all the formal sector institutions to get involved in poverty alleviation programmes.

The main motivation behind such policy was to:

- ◆ Curtail the so called " monopoly power " of rural money lenders
- ◆ Expand network of formal rural financial institutions
- ◆ To increase volume and out-reach
- ◆ To achieve financial viability

The informal sector in Bangladesh is still supplying as much as one-third of rural credit while the formal sector institutions have failed to achieve their objectives in terms of financial viability, out-reach and deposit mobilization.

The main stumbling blocks on the part of formal sector institutions are; high transaction cost, lack of information (asymmetric information) and enforcement, attitude and mind-set, screening problem, incentive problem, default culture, politicization, etc.

On the other hand, MFIs, the majority of which are NGOs, have skilled and committed manpower, transparency in accounting, accountability, a congenial credit culture and a track record of good disbursement and repayment as well as a network. Unlike the formal sector, the players in this sector work at the doorstep of and in close proximity with their members/clients. But in Bangladesh, most of NGO-MFIs run their micro credit operation with zero or low cost funds. Their Revolving Loan Funds (RLF) consist of director's contribution, savings of the members, and donor fund. More recently, MFIs have had the opportunity to access soft loans (interest rate ranges from 4.5-7%) from the PKSF. But sustainability, which has been a most talked about issue in micro finance shall remain simply far away with the zero or low cost fund. So, for long term sustainability, it is essential to pump in commercially borrowed funds in the micro finance sector. As the formal sector banks have huge idle funds and the MFIs have funds constraint, as such, by forging a link, the commercial banks and the MFIs can both benefit from their respective comparative advantages.

In this context, the study on Bank-NGO Linkage in terms of mutual benefit will not only help to diagnose the problems of effective linkage but also help to explore the new cost-effective investment avenue for commercial bank and at the same time ensure the long-term sustainability of the NGO-MFIs.



## **2.6 Objectives of the Study**

The general objective of the study is to analyze the SB-NGO linkage programme and evaluate its socio-economic achievements. The specific objectives are:

- i) To document policies, procedures and methods of the SB-NGO linkage programme.
- ii) To examine and analyze the programme/ achievements of
  - a) SB in terms of investment, profitability and social objectives and
  - b) NGO-MFI in terms of out-reach, profitability and sustainability
- iii) To determine the impact of the programme on socio-economic development of the poor (through two case studies).

## CHAPTER 3

### **Sonali Bank-NGO Linkage Programme: An Assessment.**

#### **3.1 Basic Information on Sonali Bank**

Sonali Bank (SB) is the largest state-owned commercial bank in Bangladesh. At the same time, it is the largest of all the Private and Public Sector banks. Fully state-owned, this bank came into being under a Government Ordinance in the year 1972 through merger of branches of three banks, the then National Bank of Pakistan, Bank of Bahawalpur and Premier Bank Ltd. which are functioning within the geographical territory of the erstwhile East Pakistan

SB is managed by a Board of Directors comprising seven members including a Managing Director (MD) nominated by the government. A non-executive chairman appointed from among the directors by the government heads the board. The board is responsible for setting the overall policy of the Bank.

#### **Sonali Bank's Micro-credit Programme**

SB has been with 'old paradigm' micro credits for the last 28 years. At the inception, it concentrated on financing for enhancing crop production including cereal crops, tubers, pulses, etc. But, as time went by, the poverty reduction efforts both in the formal and the semi-formal sector cumulated and both the on-farm and off-farm activities were considered to be the potential sectors for self-employment generation. So, came the poverty alleviation credit, now-a-days popularly called 'micro credit'.

Back in 1974, SB stepped into micro credit operations. Over time, it has earned valuable experiences from operating 20 rural/micro credit products. As time goes by, SB has to innovate new products to address the changed clientele's need.

As a part of its ongoing process, SB has adopted the NGO-Linkage credit programme in 1997, a significant departure from the conventional lending system. The programme provides NGOs/MFIs access to SB's finance for on lending to their clients.

The SB's micro-credit operations/programmes breaks-up into:

- A. Direct micro-credit operations/programmes: These are own financed programmes. The overall performances of these micro-credit operations are not satisfactory.



B. Linkage with NGO which breaks up as:

- i) Linkage with Credit and Development Forum (CDF) and Association of Development Agencies in Bangladesh (ADAB) -Federated NGO-MFIs.
- ii) Linkage with lead NGO-MFI with the funds provided by International Fund for Agricultural Development (IFAD).

In all linkage programmes SB provides wholesale funds to the institutions/NGOs, who in turn retail the funds to their clients. Experience reveals that programmes having government involvement run smoothly initially but with the passage of time the performance becomes unsatisfactory due to the political interference of the government and other factors. Similarly, donor funded projects run well as long as the project people stay with the programmes. Performance declines with the phase-out of the projects. In bank-NGO Linkage, IFAD-funded projects are time consuming, as it has to pass through different tiers. Government has to sign loan agreement with IFAD and also with the concerned bank. The bank subsequently signs a Memorandum of Understanding with the borrowing NGO to run the programme.

The NGO-linkage programme seems to be a comparatively better programme of Sonali Bank both in terms of profitability and better quality assets. SB wholesales fund to NGO-MFIs based on their own assessment. Though it is bulk lending (limit ranges from 2.00 lakh to 20.00 crore) the bank does not insist on any collateral. Collateral is substituted through confidence built-up and close monitoring. Rate of interest ranges from 5% to 10 %, simple and reducing balance method. Repayment terms and conditions are flexible-quarterly installment, loan period being 3 years with 6-12 months grace period. SB's mission is as under:

- To provide performance-based credit support to the qualified NGO-MFIs for on lending to their clients.
- To supplement as well as complement the government's efforts for poverty reduction and socio- economic development of the poor men and women.
- To develop an effective and mutually beneficial business partnership with NGO-MFIs.

### **3.2 Evolution of Bank-NGO Linkage Programme in Bangladesh**

Back in 1997, the Sonali Bank opened a credit line for an amount of TK.50 million to Grameen Krishi Foundation (GKF), a spin-off of Grameen Bank, almost emotionally in responding to Dr. Muhammad Yunus, the founder Managing Director of the Grameen Bank.

The Bank opened a second line of credit for an amount of TK.50 million to SHAKTI Foundation for disadvantaged Women under a partial repayment guarantee of Swiss Agency for Development and Cooperation (SDC). Actually, SDC encouraged Sonali Bank to get into this business. In fact, SDC offered two-fold services to Sonali Bank: (i) Partial guarantee of Sonali Bank- finance to a women-led NGO working for overall development of disadvantaged women in city slums and (ii) Building capacity of Sonali Bank's concerned department, staff and branches in micro-finance.

The Sonali-SDC-Shakti linkage significantly inspired Sonali Bank to embark on its next endeavour in developing a lending framework for ADAB-federated NGO-MFIs under direct intervention. This massive linkage outfit is well organized, pragmatic, experience-based and more practical. The track record and reputation of the MFIs, rating report and ADAB-recommendations overcome the collateral obligation, which the conventional banking system is historically used to insist upon. Being inspired by the success of the above two linkage programmes Sonali Bank Board of Directors approved a lending framework in its 633<sup>rd</sup> meeting held on 24 June, 1999 for financing the ADAB -federated NGO- MFIs. Under this linkage outfit, Sonali Bank wholesales credit at an interest rate of 2% over bank rate, with a minimum rate of 10% against an undertaking by ADAB with regard to on- time repayment of Sonali Bank loans/dues which the borrowing NGO-MFI on-lends to their clients, poor men and women. Under this outfit, mostly large size NGO-MFIs have access to Sonali Bank finance.

To cater to the credit needs of medium and small size NGO-MFIs Sonali Bank signed a Memorandum of Understanding (MOU) with Credit and Development Forum (CDF) on February 18, 2000. Under this outfit CDF selects and appraises/rates the member/partner-MFIs before recommending to Sonali Bank. It further continuously provides liaison between the borrowing MFIs and the Bank and feed back/report at regular interval to the bank.

Moreover, it undertakes and ensures on-time repayment by the MFI of the bank-dues (principal + interest) and as cost of monitoring and follow-up, CDF shares interest @ 2% with Sonali Bank,



which charges 12% on declining balance method basis on the MFI. Out of this 2%, 1% is kept aside as Bad Debt Reserve fund to minimize the risk of Sonali Bank.

### **3.3 The mission of SB-NGO Linkage programme.**

SB provides performance-based credit support to the qualified MFIs for on lending by them to their clients to supplement and complement the government's efforts for poverty-reduction and socio-economic empowerment of the poor men and women. Secondly, it provides collateral free fund to develop an effective and mutually beneficial long term business partnership with the NGO-MFIs.

To be eligible for the SB-NGO Linkage Programme, an NGO-MFI must have commendable reputation, registration with appropriate Government body (ies), adequate experience, good track records, clear mission etc, satisfactory network, volume and outreach, minimum 95% recovery rate on demand basis, Revolving Loan Fund (RLF) having sizeable equity, transparent and systematic accounting and MIS system and an executive committee having experienced, non-partisan and socially reputed persons.

The loan is given for maximum 5 years with negotiable moratorium at the beginning. Rate of interest ranges from 5% - 10% (depending on products) per annum simple rate on reducing balance method basis. It is a collateral free loan and close monitoring and confidence built-up substitute the collateral.

### **3.4 Sustainability and outreach of NGO-MFIs.**

To evaluate the sustainability and outreach of NGO-MFIs the BURO-Tangail (BT), a partner NGO-MFI of SB has been studied. BT has been a partner of SB since 1999. SB opened its' first line of credit for TK. one crore in 2001. The repayment was on time. SB opened the second line of credit for TK. two crore based on the performance and confidence already built due to an effective and mutually business relationship. To examine the sustainability of BT an introduction with its core programmes has been illustrated. Also year wise disbursement, recovery rate, growth in assets, savings, composition and volume of Revolving Loan Fund (RLF) and some financial key ratios have been analyzed.

## **An introduction to BT**

BT is an independent, sustainable micro finance institution that provides diverse, appropriate and market responsive quality financial and business development services at competitive prices to very poor and vulnerable non-poor customers. Born in 1992 it started micro credit programme back in 1996 and over time has expanded its micro-finance operation in 18 districts. BT is registered with (i) Dept. of Social Welfare (ii) NGO – Affairs Bureau and (iii) Registrar, Joint Stock Companies. BT has 22-member General Body that appoints a 7-member Executive Body.

Its mission is to establish an independent, sustainable organization dedicated to providing effective flexible and responsive quality financial services to promote self-reliance among the rural poor with a vision is to establish a happy and prosperous society through the overall development of the people of Bangladesh.

Programme Area: BT demonstrates a unique blend of its experience in piloting its model and promoting the same in its different operational areas. BT's sustainable, self- financing model has four dimensions reflected in the four core and two supplementary programmes that it implements.

### **Core Programmes**

**Flexible financial services:** The organization offers flexible savings and credit services.

**Domestic resources mobilization:** The present source of funding is primarily the donors followed by customers' savings and service charges from flexible financial services. Low cost funds from PKSF and commercial fund from SB are the other two sources.

**Institutional capacity building:** Since its inception, the organization has been providing equal importance to build institutional capacity of its customers and its own. The abilities of the organization to ensure proper service delivery meeting the demands of the customers consistently enhanced because of the continuously increased skill of the staff.



**Human resource development:** This began since 1995 to increase the productivity of the staff with the customer and capital growth of the organization. The efficiency of the staff that will lower the cost of the services to the organization is directly proportional to the skill of the staff and availability of the physical and infra-structural facilities to apply the skill into practice.

**Supplementary programme:** A support programme of the organization is intended to reduce economic erosion of the customers through provision of two services: disaster preparedness service and the responses from the customers to the services of disaster management by the organization.

**Operations research:** BURO, Tangail continues to conduct operations research to enhance the flexibility and responsiveness of its financial services. The outcome is used to design and improve the quality of services.

### **3.5 Assessment of the SB-NGO Linkage Programme.**

The main objectives of this research are to evaluate the economic viability/profitability and outreach of SB and the sustainability and outreach of the NGO-MFIs. To assess profitability of SB information on year wise loan disbursement, recovery rate, non-performing assets and operational cost in NGO linkage programme has been compared with direct micro-credit operations; and to assess the sustainability of the NGO-MFI managerial, operational and financial performance over the years have been compared. For this purpose we want to test the following hypotheses:

- i) The NGO-linkage programme is more profitable for the Sonali Bank than the other micro-credit operations.
- ii) Linkage with Bank enhances the sustainability of NGO-MFIs.

Here in this chapter section 3.5.1 examines profitability of bank in terms of investment, recovery rate, classified loans and operational cost. Section 3.5.2 examines sustainability of the selected NGO-MFI in terms of growth in assets, growth in savings, growth in income, operational and financial self-sufficiency, cost per unit money lent and access to commercial fund.

#### **3.5.1 Profitability**

Profitability means the profit making ability of the enterprise. It indicates the ability of a given investment to earn a return from its use. Profitability is measured in terms of different

components of income statement and balance sheet.

Profit = Income – Expenditure (both operational and non-operational). Here, in banking term expenditure includes mainly cost of fund and administrative/operational costs and income includes interest earned from loans and advances, discounts, commission, exchange and brokerage, foreign remittance, other receipts, etc.

Profitability depends on a number of factors, which are mutually interdependent. In banking system, as the profitability mainly depends on more and more safe investment, higher recovery rate, less classified loans/non-performing assets so, the other minor factors have been ignored. Therefore, profitability has causal relationship with the following explanatory variables: investment, rate of recovery, non-performing assets/classified loan, and operational cost etc. This relationship may be expressed in the functional form, which is as follows:

Profitability (P) = f (growth in investment (+), rate of recovery (+), non-performing assets/classified loans (--), operational cost (--)).

In the functional form (+) sign indicates positive relationship and the (–) sign indicates negative relationship.

The above functional form suggests that:

- The profitability increases with the increase of investment.
- Higher the recovery rates higher the profit.
- Lower the classified loan higher the profit.
- Lower the operational cost higher the profit.

### **Investment**

Bank receives deposit from the depositors and provides interest on deposit. From this deposit bank invest funds as loans to the potential borrowers and charge interest on it at higher rate. The margin they earn is simply the profit. So, more investment means more profit. Thus, profitability has positive correlation with investment.

### **Recovery rate**

Banks invest funds as loans for a particular period and ask the borrower to repay the installments on time as per repayment schedule. If the repayment is not on time the recovery falls which reduces the profit. So, recovery rate has a positive correlation with profit.



## **Classification of loans**

If a borrower continues to be a defaulter of loans for more than one-year, the bank has to classify the loans and make 100% provision for bad loans, which affects its profit. Here classification has negative correlation with profit.

## **Administrative/Operational cost**

Profit mainly depends on cost of deposits and administrative cost. Cost of deposits can hardly be reduced as it depends on government dictation/policy. But operational cost can be reduced through efficient use of resources in a cost-effective way. Therefore, by reducing operational cost bank can maximize its profit.

## **Findings**

Tables-3.1 and 3.2 provide information on year wise loan disbursement, recovery rate of direct micro-credit operations/programmes and SB-NGO linkage programme. The tables show huge difference in disbursement and outreach between the two programmes. This is because the direct micro-credit operations/ programmes are very old and has grown over time. On the other hand rate of recovery of SB-NGO Linkage programme is much higher than the direct micro-credit operations/ programme (Table-3.1).

While comparing the two programmes in terms of recovery we see NGO-linkage has the consistently higher recovery rates (Table-3.2). Table-3.3 shows that NGO- linkage programme has a lower rate of classified loan ranging from 0% to 4% only where direct micro-credit programmes has the higher rate of classified loans ranging from 32.02% to 38.85%. Year wise overall cost of fund of NGO-linkage is less than that of direct micro-credit operations (Table-3.4).

For more perfection and to get credible and more accurate results we have calculated operational cost and rate of earnings for a single credit line at branch level. The study reveals that operational cost/administrative cost of SB-NGO linkage programme is much less than that of the direct micro-credit programmes (Table-3.5 and 3.6).

These results confirm that Bank-NGO linkage has shown better performance in terms of investment, recovery rate and in minimizing the operational/administrative cost. The growth of investment and outreach is increasing over time which indicates a positive trend.

As the classified loan is only 1-4% compared to the direct micro-credit operations/ programmes (32-39%) it has hardly any cost from society's point of view. As SB- NGO linkage is wholesale lending programme, its administrative cost is minimum. So, cost of fund is lower than that of the direct micro-credit operations/ programmes.

**Table-3.1 Year wise disbursement, out reach and recovery (Direct micro-credit operations/programmes)**

Figures In lakh taka

Year	Disbursement	Out-reach	Rate of recovery( %)
1999	24391	290311	63%
2000	18007	361282	64%
2001	30486	232645	64%
2002	29497	123805	66%
2003	29869	672818	74%

Source: Annual Reports of SB bank and further analysis of bank statements

**Table-3.2 Year wise disbursement, out reach and recovery (NGO-Linkage)**

Figures in lakh taka

Year	Disbursement	Out-reach	Rate of recovery( %)
1999	16	8940	100%
2000	508	28300	100%
2001	3218	41379	100%
2002	842	3269	99.5%
2003	1541	16337	96%

Source: Annual Reports of SB bank and further analysis of bank statements



**Table 3.3-Year wise/ Intervention wise position of classified loans of direct micro-credit operations/programmes and NGO-linkage.**

Programmes	1999	2000	2001	2002	2003
Direct micro-credit operations/programmes	38.85%	38.69%	38.32%	33.47%	32.02%
Bank-NGO linkage	0%	0%	0.62%	0.4%	4%

Source: Annual Reports of SB, bank statements and further analysis of bank statements

**Table-3.4 Year wise/ Intervention wise cost of Fund.**

Programmes	1999	2000	2001	2002	2003
Direct micro-credit operations/programmes	8.08%	8.00%	8.00%	7.65%	7.21%
Bank-NGO linkage	6.45%	6.25%	6.12%	6.05%	6.01%

Source: Annual Reports of SB bank and further analysis of bank statements

**Table-3.5 Comparative analysis of cost of fund for this single credit line under NGO-linkage programme at branch level.**

Programs	2001	2002	2003
Direct micro-credit operations/programmes	8.00%	8.00%	7.21%
Bank-NGO linkage	6.12%	6.05%	5.49%

Source: Statements collected from Sonali Bank, Tangail branch.

**Table-3.6 Comparative analysis of rate of earnings for single credit line under NGO-linkage programme at branch level.**

Programmes	2001	2002	2003
Direct micro-credit operations/programmes	8.00%	8.00%	7.21%
Bank-NGO linkage	9.85%	10.00%	10.00%

Source: Statements collected from Sonali Bank, Tangail branch.

### **3.5.2 Sustainability and Outreach of BT.**

Sustainability of an NGO-MFI requires that in addition to covering all costs, without the help of donors, it is able to generate income to grow. In fact, an NGO-MFI is sustainable only when it is able to cover the costs of administration, loan losses, savings account interest, and cost of other capital from funds generated through receipts of service charges and other fees.

Sustainability depends on disbursement, recovery rate, growth in assets, savings, composition and volume of Revolving Loan Fund (RLF) and some key financial ratios. Sustainability has the causal relationship with growth in asset, financial self sufficiency, operational self sufficiency, cost per unit money lent, growth in net income, composition and volume of RLF, access to commercial fund and the management of funds in cost-effective way which are explanatory variables.

Therefore, the relationship between sustainability of NGO-MFIs and other explanatory variables may be expressed in a functional form which is as follows:

Sustainability (S) = f (growth in asset (+), growth in savings (+), growth in net income (+), financial self-sufficiency (+), operational self-sufficiency (+), cost of per unit money lent (--), composition and volume of RLF (+), and access to commercial fund (+) etc).

In the functional form (+) sign indicates positive relationship and the (–) sign indicates the negative relationship.



The above functional form indicates that:

- Sustainability increases with the growth in assets, savings and income.
- Sustainability increases with the increase of financial and operational self-sufficiency.
- Lower the cost of per unit money lent higher the sustainability.
- Access to commercial fund increases sustainability.

### **Growth in assets**

Assets structure such as fixed assets, loan portfolio, investment, other current assets, cash and bank balance, etc. indicates the financial health of an organization. Steady growth in assets of an NGO-MFI indicates institutional sustainability and sustainability of its programmes/activities.

### **Growth in savings**

Savings is the major source of fund for NGO-MFIs and playing a considerable role in augmenting the volume of credit. Savings mobilization and its management is an important factor for institutional sustainability and also for the sustainability of the activities.

### **Growth in net income**

NGO-MFIs are non-profit organizations that generate income by selling goods, commercializing services, or leveraging assets (tangible and intangible) to support its social service activities without continued reliance on donor funding.

NGO-MFIs are the best known examples of social enterprises and are committed to achieving a double bottom line- their social mission and their financial objectives. Therefore, for long term sustainability both for institutions and activities growth in income is essential.

### **Financial self-sufficiency**

It measures how well an NGO-MFI can cover its costs taking into account a number of adjustments to operating revenues and expenses. The purpose of most of the adjustments is to model how well the MFI could cover its costs if its operations were unsubsidized and it were funding its expansion with commercial cost liabilities. So, higher the financial self-sufficiency higher the sustainability.

### **Operational self-sufficiency**

It measures how well an MFI can cover its cost through operating revenues. In addition to operating expenses, it is recommended that financial expenses and loan loss provision expenses be included in this calculation as they are normal and significant costs of operation. So, operational self-sufficiency has positive correlation with the sustainability.

### **Cost per unit of money lent**

It provides a meaningful measure of efficiency for an MFI, allowing them to determine the average cost for per unit money lent. It also indicates cost-effective fund management. So, cost per unit of money lent has inverse relationship with sustainability.

### **Access to commercial fund**

Access to commercial fund helps an NGO-MFI to expand its loan portfolio, borrowing components of RLF and outreach, which further helps in attainment of institutional sustainability. More access to commercial fund and its efficient management indicates institutional sustainability and has a positive correlation.

### **Findings**

Table-3.8 shows that the growth in loan portfolio and growth in borrowers are accelerating. The prime assets have significantly increased during the year 2003 (Table-3.8). Growth in savings has increased 61% in 2003 compared to 55% in 2002 (Table-3.8). BT has attained operational self-sufficiency of 149% in 2003 compared to 139% in 2002, which is accelerating (Table-3.10). BT has also attained financial self-sufficiency of 123% in 2003 compared to 114% in 2002 (Table-3.10). Recovery rate of micro-credit programme over the last five years is impressive (Table 3.7)

Cost per unit of money lent declined to TK.0.082 in 2003 from TK. 0.095 in 2002, which decreased by 13.68%. The indicator implies attainment of high productivity and efficiency in operations (Table-3.10). Growth in income is impressive from 2001 to 2003 which is increasing (Table-3.8). Table 3.9 shows that access to commercial fund in the year 2001 increased due to the access to SB's fund and reached 2300 clients, which is an important sign of institutional sustainability.



The study of BT, a partner NGO-MFI of SB reveals that growth in assets, growths in savings, operational self-sufficiency and financial self-sufficiency have positive relation with sustainability and negative relation with cost per unit money lent.

Access of BT to SB's fund has positive correlation and helped BT expand its loan portfolio, product diversification and larger amount of loan for graduated borrowers which eventually helped BT attain sustainability both for the institution and the borrowers.

As the micro-finance industry in Bangladesh is growing the main challenges for NGO-MFIs is to source sufficient capital because, savings, accumulated surplus, donor's fund and little borrowing from financial institutions are not enough to meet the growing demand of the clients.

Micro-finance programme should have to be pro-poor and growth oriented to attain the goal of poverty alleviation at sustainable level. So, for product diversification, scaling up of programmes and targeting the missing middle and for long term sustainability both for institutions and activities NGO-MFIs need hug funds.

Given the situation, there should be provision for NGO-MFIs to have access to commercial fund. By channeling commercial fund to NGO-MFIs through effective linkage both bank an MFI can be benefited.

**Table-3.7 Year wise disbursement and rate of recovery of micro credit programme of BT.**

Figures in crore taka

Particulars	1999	2000	2001	2002	2003
Disbursement	26.99	30.11	46.64	69.56	108.26
Rate of recovery	98.87%	99%	99.04%	98.08%	99%

Source: Annual Reports of BT and further analysis of Balance Sheets.

**Table-3.8 Year wise growths in assets, savings, borrowers, loan portfolio and net income.**

Figures in crore taka

Particulars	1999	2000	2001	2002	2003
Growth in Assets	27.67	29.02	38.02	48.67	66.77
Growth in Savings	4.51	5.83	8.93	13.82	22.36
Growth in borrowers	49282	54189	69256	91866	128112
Growth in Loan Portfolio	17.02	21.31	28.97	40.29	54.77
Growth in net income	.73	-.63	1.34	2.80	5.04

Source: Annual Reports of BT and further analysis of Balance Sheets.

(-) indicates negative growth of income

**Table-3.9 Year wise Revolving Loan Fund (RLF) composition of BT.**

Figures in crore taka

Year	Equity/own fund		Member savings		Borrowing		Total
	Amount	%	Amount	%	Amount	%	%
1999	17.01	63	5.73	21	4.35	16	100
2000	16.53	58	7.36	26	4.56	16	100
2001	19.58	52	11.05	30	6.80	18	100
2002	24.22	51	16.72	35	6.55	14	100
2003	29.66	48	24.40	40	7.45	12	100

Source: Annual Reports of BT and further analysis of Balance Sheets.



**Table-3.10 Some key ratios of BT.**

Ratios	1999	2000	2001	2002	2003
Return on equity Net operating income+taxes/Average equity	7%	-4%	7%	13%	19%
Operating self sufficiency Operating income/Financial expences+loan loss provision expences+operating expences	125%	102%	128%	139%	149%
Financial self sufficiency Adjusted operating revenue/ Financial expences+Loan loss provision expences+Adjustedoperating expences	101%	85%	104%	114%	123%
Financial spread Net operating income/operating revenue	28%	22%	27%	28%	30%
Port-folio at risk Port-folio at risk x days/gross loan portfolio	3.79%	3.83%	3.59%	3.50%	1.89%
Risk coverage ratio Loan loss reserve/ Portfolio at risk> x days	145%	134%	130%	118%	107%
Loan officer productivity Number of active borrowers/number of loan officers	603862	602129	752703	877854	872272
Cost per client Operating expense/Average number of clients	.002	.001	.002	.002	0.002
Cost of per unit money lent	0.144	0.157	.116	.095	0.082
Profit margin (Net Profit/Total Cost)	23%	-120%	20%	33%	43%
Loan loss reserve ratio	5.75%	5.30%	4.80%	4.27%	2.02%

Source: Annual Reports of BT and further analysis of Balance Sheets.

(-) Indicates negative growth of income

## Chapter-4

### **Socio-economic impact of SB-NGO linkage programme: Two Case Studies.**

To supplement the quantitative analysis of the preceding chapter, two borrowers of BT were selected as case studies of which one is a success story and the other is a non-success story.

#### **SUMOLA BEGUM: A success story**

Sumola Begum is a member of the 26th centre of BT. Her family is a happy-nest comprising her spouse Aziz Mia and two sons, Faruqe and Israfil. Her family never was a happy family though it was defined so for its size.

In 1988, during the devastating flood they migrated from Rangpur to Tangail travelling a long distance in quest of job. Aziz Mia learned that here, in the farming families, there is scope for year long jobs. Losing everything in the flood, this couple passed their lives in inhuman conditions, they had to even live on dishes of only rice and greens, when they had no job. Arriving in Tangail Aziz Mia found a job in a farming family at Tetulia. He was paid three hundred taka per month, but it was insufficient for their living. He then changed the job and managed a job at the residence of a UP-member. But he was not only deceived by the member, but also subjected to torture by him.

Lastly Aziz Mia started as a labour for earth work. And at this time he met a man sympathetic to him. He advised him to be a member of BT. The couple exchanged their views and Sumola Begum started savings with the BT. But they had another problem. When they applied for loan, they were suspected by somebody that receiving money they would go back to Rangpur. Sumola Begum gave assurance to everyone, "I will not be back to Rangpur until I die." She promised to be on the soil of Tangail at any cost. She received the first loan amount of Tk. 2000. She bought hens and goats with the money. Some of that was spent for the purpose of urgent health care, but she didn't fail to repay installments in time. Afterwards she received a loan of Tk. 4000, which she spent for buying CI sheet to build her house. She repaid that amount and received another amount of Tk. 5000. This time she bought some land. Afterwards she received a general loan of Tk.12000 with which she bought more lands, started cropping paddy, jute, vegetables, etc.



Her spouse assisted Sumola Begum, time to time, in repaying 'Kisties'. She was also facilitated by the size of her family as it is not a large one -- now the days of misery were over. Her spouse Aziz Mia acknowledged that, their's was a life sunk in poverty, he had nothing to sell. He managed the communication-fair selling two boxes he inherited from his father.

They didn't return to Rangpur from Tangail, but they visited their birthplace two times -- once they went to Rangpur receiving the news of death of Sumola Begum's father. That time Sumola Begum narrated to her village men, her present days of well-being. She said about BT, how BT supported her to fight the struggle for standing on her own feet.

She inspired her village people to make savings and to organize them around a 'samiti'. Sumola Begum, in transcendence, sketched her future -- "I will design a home for me, will expand my land area and will make more income." While talking to Sumola in her own house she informed that two years ago she had to drink pond water. Now she has her own tube well. Not only that she has now sanitary latrine. Being the member of BT, they are now aware about health care, nutrition and environment.

Diligence realizes the dream if there is support with cordial assistance, which she received from BT. She wishes to educate her sons as long as she can. Now her elder son is a student of class nine and the younger one is a student of class six. Sumola Begum gestures," they could not have any land if BT were not with them." Days are running and everything runs, Sumola is now totally adopted in the new neighbourhood. She seems to be habituated in the village of Narinda. Her accent is also changed. Sumola explains her condition as 'Allah the almighty is the keeper of my days, I am living well.

All the information stated above have been summarized in the following tables and attempts have been made to determine the impact of the micro credit programme in socio-economic development of Sumola. To do this before and after affects of micro credit on household has been studied.

**Table 4.1 Information about micro-credit of Sumola Begum.**

Number loan	Amount	Activities	Utilization	Repayment	Outstanding	Arrears
1 <sup>st</sup> time	TK.2000	Poultry and goat rearing.	80%.20% for health care	100%	Nil	Nil
2 <sup>nd</sup> time	TK.4000	Housing	100%	100%	Nil	Nil
3 <sup>rd</sup> time	TK.5000	Land purchase	100%	100%	nil	nil
4 <sup>th</sup> time	TK.12000	Growing vegetable, paddy etc.	100%	100%	5550	nil

**Table 4.2 Impact of micro-credit on Sumola Begum.**

Indicators	Before	After	Change
Access to land	Nil	Purchased some land	Increased
Cattle	Nil	nil	No change
Small stock	Domestic birds	Small poultry farm.	Increased
Income sources	Only husband	Both husband and wife	Increased
Food security	Less	More than before	Increased
Drinking water	Pond water	Tube well water	Positive
Sanitation	Katcha latrine	Sanitary latrine	Positive
House hold quality a) katcha b) tin/brick	Katcha	Tin shed	Positive
Social mobility	No	Now participate	Increased
Literacy and school enrollment of children.	Primary	Secondary. Expectation raised	Improved.
Health and Nutrition	Less	More aware	Improved



**Factors responsible for her success:** Sumola has clear vision and mission. She is regular in attending weekly meeting and depositing savings and installment of loans. She is an opportunity seeker and diversifies her loan portfolio. She is sincere, committed and puts her best efforts to expand her business. Her husband helps her if and when needed. She utilizes loan amount in proper ways and hardly diverts fund for unnecessary consumptions and luxurious purposes.

Table-4.2 shows that access to micro-credit has increased her access to resources, housing, health and sanitation, food security and nutrition, literacy and school enrollment of children, and social mobility, which are the main elements of her success.

### **Saleha Begum: A non-success story**

On arriving her house, we saw a woman on the courtyard stirring paddy on either side a loom-house and knitting yarn on her 'charka' (loom). This woman is Saleha Begum. Near her hands there was a long bamboo stick, sometimes she uses it to drive out naughty little chickens.

In an afternoon just at 2 P.M we appeared on her courtyard accompanied and guided by, Khandokar Dilruba Maya- the kendra prodhan of centre 11 of BT. Saleha Begum marked us and fell in hurry to arrange to receive us. We sat on 'Pidies' and requested her to narrate her story of ups and downs. Meanwhile she arranged for some refreshment.

'I am busy twenty-four hours," said Saleha Begum. It may sound empty but there is not even a little lie in her statement. Saleha Begum was coordinating her jobs- Knitting, drying paddy, driving out chickens, stirring paddy to dry, and watching on the loom-house- lastly taking to us was added. She didn't stop her work while talking to us.

Her days actually start at mid-night. "I set the pots on the ovens and knit", said Saleha. She prepares meal for labourers after giving food to her cattle and poultry farm early in the morning, supplies all materials, for the looms, and in this time she takes care of her children and husband.. She is busy twenty-four hours in governing her family.

She even does not like to lose an hour while she goes to weekly meetings to deposit TK. 10. For this she hands over fixation to kendra prodhan Maya Apa if she fails to attend the meeting.

We intended to know about her days of sorrow as she spoke to us. Grameen Bank employed her husband, as a field worker. He quit his job when he was posted to Potuakhali, almost a remote area to him. But his father was disappointed with him, he compelled him to be separated.

His father gave him only a loom. Saleha had to start a new family but they had no shed or livelihood for them. She was then pregnant. Her mother-in-law was sympathetic to them and she sometimes tried to send food to them. But Saleha didn't let her decline, her indomitable mental will and immeasurable diligence kept her stand unbending. She faced audacity and in struggling for life.

BURO stepped forward to assist her. She started savings as a member of the 11th center of BT. She received Tk 2,500 from BT, gave it to her husband. Her husband Badal Mia started his loom.

Repaying the first term she received the 2nd term loan. "I received assistance provided by BT," she commented when she was asked what sort of particulars BURO has, " we can make our savings being at home."

But, she has been unfortunate as whenever she is little well off some uncertainty hits her and make her vulnerable again.

While she was passing a happy life one-day she felt pain at her lower abdomen and under went a major operation. She had to spend TK.15, 000.00 to meet the medical expenses and had to sell a piece of land. During her distress BT came forward with a disaster loan.

Afterwards, she received her 3<sup>rd</sup> loan –a general loan of TK.12000 and increased the number of looms. Their dual income from the IGA run by the loan was more than expectation. When their business was growing, at one mid night their two looms were stolen and again they fell into distress.

As she has been a good saver as well as the good borrower BT again gave her another emergency loan. She is optimistic, her hard days will be changed, as Allah is merciful, she said to us. Allah always helps his honest banda but at times test their iman. So, in near future we shall be able to overcome our hard day's inshallah.

All the information stated above have been summarized in the following tables and attempts have been made to determine the impact of the micro credit programme in socio-economic development of Saleha Begum. To do this before and after affects of micro credit on household has been studied.



**Table 4.3 Information about micro credit of Saleha Begum.**

Times	Amount	Activities	Utilization	Repayment	Outstanding	Arrears	Profit
1st loan	2500	loom	100%	100%	nil	nil	Satisfactory
2 <sup>nd</sup> loan	5000	loom	100%	100%	nil	nil	Satisfactory
3 <sup>rd</sup> loan	12000	loom	100%	Rescheduled			Satisfactory
4 <sup>th</sup> loan	4000	loom	100%	100%	11000	nil	Satisfactory

**Table 4.4 Impact of micro-credit on Saleha Begum.**

Indicators	Before	After	Change
Access to land	130 decimal	100 decimal	Decreased
Cattle	2 cows	2 cows	No changed
Small stock	5 hens	7 hens	Increased
Income sources	Husband	Both husband and wife	Increased
Food security	Less	More	improved
Drinking water	Pond water	Tube well	Improved
Sanitation	Kutchra latrine	Sanitary latrine	Improved
House hold quality	Kutchra	Tin	Improved
Social mobility	Less	Improved	Improved
Literacy and school enrollment of children.	Less	More	Increased
Health and Nutrition	Less access	More access	Improved

**Factors responsible for her non-success:** Though Saleha is a hard working, sincere, committed and put her best efforts to expand her business, due to repeated misfortunes she could not expand her business. To face the different shocks she had to sell even a piece of land. But, she is optimistic and trying to overcome the financial crisis with the help of BT and themselves by hard work and perseverance.

**Lessons learnt from the two case studies:**

- 1) Access to commercial funds help NGO-MFIs to expand their loan port-folio and out-reach, diversification of credit products and provision of larger amount of loan for graduated borrowers which in turn;
- 2) Helps borrowers to avail different types of loan such as general, supplementary, disaster etc and larger amount of loans to expand their business from micro-credit to micro-enterprise.
- 3) Hard working, tenacity of purpose and entrepreneurship qualities positively affect success of MFI members. However, external shocks- whether manmade or natural negatively affect success.



## Chapter-v

### Conclusion and Recommendations.

Poverty poses a serious socio-economic problem in Bangladesh, and micro-finance programmes have been proved to be very effective economic measures to redress the severity of the problem. Micro finance programmes have traditionally been funded through foreign donations. Recently this source has been declining. If we look at the demand side we see that micro credit has got huge potentials. Credit need is constantly increasing due to the expansion of loan portfolio. If we critically look at the supply side we see donors' grant money is decreasing; 17.36 in 2001 and 14.84 in 2002 (CDF 2002). So, one of the major challenges for growing MFIs is to source sufficient capital to fund the expanding loan portfolio and to attain sustainability both for institutions and beneficiaries. Against this backdrop advocacy and suggestions have been made to channel funds from commercial banks to NGO-MFIs.

As we know PKSF, NGO -MFIs and the commercial Banks are the major players in the field of micro-finance and all of them have the same social and commercial mission. But banks, despite having huge idle fund, can not expand their loan portfolio in this sector due to collateral obligation, traditional mindset and attitude, lack of commitment, institutional weakness, default culture, interest exemption, and government dictation, among others.

On the other hand NGO-MFIs having strong leadership, committed and skilled manpower, well designed/organized net work, accountability, flexibility, transparency, and enticing incentive package cannot expand their loan portfolio and outreach due to fund constraints.

So, using their comparative advantages, both bank and NGO-MFI can be benefited through such linkage programmes.

But the problems, particularly in the developing countries, stem mainly from attitudes and mindset. Historically, a poor country like Bangladesh is used to prioritize the poverty alleviation agenda and provide utmost thrust on poverty reduction. Some governments do it almost as charity or an act of social obligation, which have been the main reasons for their micro finances not coming out successful. Over the last two decades, things have changed a lot and there has been growing interest in the governmental tiers about micro finance and its long-term validity. But, for moving forward in an objectively oriented manner, a conducive policy environment has been a long-felt need.

An MFI – friendly regulatory framework will be instrumental, which will watch over the saver's stake. But, the regulatory framework should not be over enthusiastic about the micro-credits, which should be left to the interaction and relations between MFIs and their clients. The government's role should concentrate here on policy formulation and regulation. Donor's role will be to buildup the capacity and confidence. MFIs should progressively move towards self-sustainability. Apex organizations' role is networking between their members and facilitate inter organization linkage and institutional building through skill promotion, leadership creation and efficiency of NGO-MFIs.

As micro-credit has proved to be an effective tool for poverty alleviation, there must be a reasonable budgetary allocation. Micro credit should be brought under the mainstream of the economy by establishing backward and forward linkages. It is essential to ensure the access of all the poor, including the hard-core to micro-credit as well as create better investment opportunity for the graduated micro credit clients and the enterprising poor. Therefore, macro policies (fiscal and monetary) should be reoriented to achieve these goals.

There should be some standard criteria for good governance and self-regulation to ensure transparency and accountability for NGOs, and also user-friendly policy and regulatory framework to ensure smooth operation of micro finance. A common code of cooperation and coordination may be developed and practiced by both GO and NGO.

It is established that micro credit is a specialized financial service which demands grass roots organizations, people centered methodology and commitment. NGO-MFIs have already demonstrated their efficiency, effectiveness and appropriateness in delivering micro credit to the poor in a flexible manner. So, both GO and NGO can work together on the basis of their comparative advantages through coordination and cooperation.

NGOs can never be the alternative to the government. NGO can supplement/compliment the government development efforts. Government should create an enabling legal and administrative environment for these institutions.

For several years SB has been funding such a programme called SB-NGO Linkage. This linkage initially had been a pilot programme. As a programme over time, it has proved to be very successful in terms of investment, profitability and outreach. It should now become a regular programme and may be replicated across the country.



This study analyzed the performance of SB-NGO linkage. The research findings reveal that linkage programme benefits: 1) bank in terms of profitability and outreach 2) NGO-MFI in terms of sustainability of both institution and activities through access to commercial funds and 3) positive impact on borrower in terms of household income, vulnerability and non-income dimensions of poverty.

Therefore, to improve linkage benefits, government can instruct all commercial banks through Bangladesh Bank to provide wholesale funds to NGO-MFIs and to make budgetary provision at least 5% of their annual profit to meet the growing demand of NGO-MFIs. Government can also take the linkage programme as a priority programme for poverty alleviation in national development agenda.

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