

Microcredit Delivery in Bangladesh A Strategy for Poverty Eradication

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To my parents

Mrs Hamida Begum
Professor Aka Firowz Ahmad

Preface

In recent years, microcredit, in its wider dimension known as microfinance, has become a much favored intervention for poverty alleviation in the developing countries and least development countries. Although Bangladesh has huge potential for development, it is, for various socio-economic reasons, among the poorest countries in the world. Therefore, poverty alleviation and creation of rural employment are top priorities in the development agenda of the government of Bangladesh (GOB) which has adopted a broad-based approach to poverty alleviation, emphasizing macroeconomic stability, economic liberalization, and support for a number of government agencies and non-government organizations (NGOs). Substantial progress has been made in implementing the microcredit disbursement by MF-NGOs, administrative ministries, banks and specialized institutions. The main objectives of micro credit programs are to increase employment opportunities and to enhance income adequate to lift the poor above the poverty line on a sustainable basis.

This book is the modified version of my research paper prepared for the partial fulfillment of my masters' courses in the Department of Banking, University of Dhaka, Bangladesh. Here I make an attempt to summarize the impact of the microcredit delivery in Bangladesh on poverty alleviation. It focuses on three major aspects related to the field i.e. financial structure, economic structure and condition of micro credit delivery of Bangladesh. To analyze the impact of microcredit disbursement cumulative credit disbursement is taken into account along with the trend analysis, comparison of the trends with poverty and regression analysis of per capita GDP at current price with credit disbursement.

Because of lack of time, experience and expertise I can not cover all information related to micro credit delivery in Bangladesh. However, I am alone responsible for the shortcoming of this work. This book can at least be taken as a first step towards a more meaning full work.

First and foremost, I am grateful to almighty Allah, the omniscient and omnipotent, who bestowed me the capability of successful completion of my research paper. I must offer my heartfelt thank and gratitude to my internship advisor Dr. A. R. Khan. His constructive advice and guidance have emerged as stepping-stone in conducting the research work. Thanks are also due to a number of individuals for their unprecedented support, cordial co-operation, objective direction and endless encouragement that have significantly helped me in writing the book.

My pleasure turns blooming to offer thanks to Mr. Md. Yunus Ali Miah, the Administrative Manager of the Credit and Development Forum (CDF), for allowing me to show my practicability in an organizational area under his supervision. I like to convey something more than thanks and usual gratitude to Mr. Md. Mamtaz Uddin, the Senior Officer and Sub-Manager. I am very grateful to Mr Md Rokonuzzaman, officer of CDF.

And last but not the least; I would like to thank Mr. Shahjahan Kazi to compose this book and Osder Publications to publish this book. I am very grateful to my family to cooperate to by providing various supports without which I could not concentrate to this research. Again, thank to all the personnel helped me by providing information, without their assistance and co-operation, this book might not have seen the light of day.

Fahim Muntaha

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Chapter 1

Introduction

Background

In recent years, microcredit, in its wider dimension known as microfinance, has become a much favored intervention for poverty alleviation in the developing countries and least development countries. Although Bangladesh has huge potential for development, it is, for various socio-economic reasons, among the poorest countries in the world. About half of the country's population lives below the poverty line with 80% in the rural areas. The burden of poverty falls disproportionately on women, who constitute half of the total population. Logically, therefore, poverty alleviation and creation of rural employment are top priorities in the development agenda of the government of Bangladesh (GOB) which has adopted a broad-based approach to poverty alleviation, emphasizing macroeconomic stability, economic liberalization, and support for a number of government agencies and non-government organizations (NGOs). Substantial progress has been made in implementing the microcredit program (MCP), and the scope for its efficient expansion is enormous.

This book is based on a research study conducted with a view to exploring the practical situation of the economy and implementation of the theoretical knowledge in practical and realistic work environment with special reference to micro credit delivery of Bangladesh. It is divided into 3 sections i.e. financial structure, economic structure & condition of. Delivery of micro credit plays an important role to conduct different financial services. So this report focuses on the impacts of micro credit on eradication poverty.

Objective of the Study

The General Objectives include (1) to get practical exposure to economic condition, (2) to understand the financial system and its trend and (3) to observe the micro credit delivery in Bangladesh from the year 1971 to 2007; while the Specific Objectives are : (1) to get an overall idea of micro credit delivery by various institutions, (2) to evaluation the impact of micro credit on poverty alleviation, (3) to search the drawbacks related to micro

credit to eradicate poverty and (4) to recommend some guidelines to improve the effectiveness of micro credit to alleviate poverty.

Methodology Used

To meet the objectives of the study instead of a single method multiple methods such as formal & oral discussion, direct observation, questionnaire survey, consultation with expert and study of related publications of various institutions were followed for collecting information.

Data have been collected from both primary and secondary sources. Information from the Primary Sources are collected using the following methods:

- **Interview:** Face to face conversation with the respective officers and staffs of various institutions help me by giving important information through interview.
- **Case Study:** In depth-study of selected cases helps me to collect information.
- **Group Discussion:** Group discussion with other student of the branch and my classmates is another way to make me informative.

The Secondary Sources of data include:

- Micro-credit Statistics of Credit and Development Forum
- Reports of Ministry of Finance
- Statistical Year Book of BOS
- Economic Review
- Several books and periodicals related to the micro credit.
- Bangladesh Bank's report
- Various documentary file and prior research report related to micro credit.
- Various website
www.mincom.gov.bd
www.bangladeshbank.com
www.mof.gov.bd
www.statisticalbureau.com
www.mdgbangla.org
www.southasiananalysis.org.

Secondary Data have been collected from the related office, continuous search on published websites and library, and interview with related officers. It has been tried to make the report informative and handy. The data collected are significantly reliable in the sense that all data generated in the report are used by the renowned websites and reports.

Sample size: Primary data have been collected through interview from a sample size of 30 from which, assigning quota, 15 respondents are rural poor and 15 respondents are urban poor. Judgment was used to select respondent who have used micro credit and their economic benefit of micro credit was surveyed through interview.

Aspect of Analysis

Micro credit disbursement by various institutions like Ministry of GOB, Non bank Financing Institutions, Banks and Non-Governmental Organizations (NGOs) etc. have been analyzed using the following criteria:

- To find out whether the amount of all indicators or variables to micro credit show any increasing or decreasing trend.
- To evaluate impact of disbursement of micro credit to eradicate poverty
- A regression analysis of delivery of micro credit with per capita GDP at current price from the year 2002 to 2006

Both independent and dependent variables have been taken into consideration at the time of data analysis

Independent Variables: In correlation analysis of poverty and micro credit delivery the total micro credit delivery of the country is the independent variable considering the following things.

- Specialized Institutions,
- MF-NGOs,
- Banks, and
- Administrative Ministries.

Dependent variable: In correlation analysis of poverty and micro credit delivery the dependent variable is poverty considering per capita income and expenditure, GDP, housing & Socio Demographic practice, land and asset ownership, consumption of food item, nutrition and welfare, credit and crisis management, savings etc.

Methodology of Data Analysis

- **Trend analysis:** In this section effort is to find out whether the delivery of micro credit by different institutions are increasing or decreasing from year to year.
- **Impact analysis:** Through this section, the impact economic data such as, Total revenue, total expenditure, investment, consumption, savings, CPI (consumer price index), poverty etc from the year 2002 to 2006 have been analyzed.
- **Regression Analysis:** The relationship between dependent variable (per capita GDP at current price for eradicating of poverty) and independent variables (micro credit disbursement by MF-NGOs, Banks and Specialized institutions and ministries) has been statistically analyzed.

Limitations of the Study

The present study was not out of limitations. Some constraints are appended bellow:

- **Lack of Information or Data:** In-depth and well-organized information is not available for access. Though the officials tried to assist, sometimes their working pressure couldn't give proper assistance what was needed. There is some information which need special permission from top level is not always achievable. Again lack of specific data by different institutions like ministries and specialized institutions, specific data of MF-NGOs was used as that was specific and available.
- **Inconsistent Information:** Some information is available for year end and some information available for July to June. So for comparison it creates some complexity and had to take some assumptions.
- **Time Constraint:** It is something like impossible to cover the entire impacts of micro credit on eradication poverty within the very short period of study.
- **Secrecy of Information:** Some of the information needed to explore the current marker scenario of the company was not disclosed.

Chapter Design of the Book

The book consists of seven chapters. The first chapter of the report describes the introductory words of the report and methodology used in the preparation of the report. In chapter two deals with the economic structure of Bangladesh and its trend. The third chapter describes the financial structure of Bangladesh and its trend. Chapter four consist of the dimensions of poverty in Bangladesh. In chapter five the microcredit delivery in Bangladesh through various institutions, its flows and utilization have been presented. Critically analysis of related to the trend of micro credit delivery, its impacts on economy and eradication of poverty has been done in the chapter six. The chapter seven contains the critics of microcredit delivery and findings and recommendations of the problems. This seventh chapter makes some concluding remarks about the impact of the delivery of microcredit in Bangladesh to eradication poverty.

Chapter 2

Macroeconomic Situation

Introduction

Macro economy is the most important indicator to observe any country. The Bangladesh economy has experienced both macro-economic stability and robust economic growth following the transition to a democratic rule in the early of 1990s. In the backdrop of the deep macro-economic crisis of the late 1980s, a series of stabilization measures were introduced in the Bangladesh economy which largely restored macro-economic stability in the early 1990s.

The macroeconomic developments in the first half of the 1990's were demonstrated the high degree high degree of the economic stabilization process in Bangladesh. The macroeconomic developments in Bangladesh since the beginning of the 1990s, until middle of the decade, were characterized by a record-low rate of inflation, an unprecedented build-up of external reserves and an improved resource position of the government. These developments have been interpreted in part as evidence of successful macroeconomic stabilization, but also in part as symptoms of economic stagnation. The changes in the macroeconomic trends in the early 1990s came in the wake of a transition to a democratic rule along with the launching of a comprehensive program of market-oriented liberalizing policy reforms. After that period there was an evident in a build-up of inflationary pressures, deterioration in the government's budgetary balances and a rapid draw-down on foreign exchange reserves. (Mahmud: 1997)

Since the beginning of the new decade after 1990s, the Bangladesh Economy was facing possibly the most severe exigency after the macroeconomic crisis of the late 1980s. The enormous achievements of the 1990s have fallen under threat because of the twin shocks emanating from large fiscal deficit and deteriorating balance of payment position that have exposed the entrenched vulnerabilities of the Bangladesh. It appeared that both the pillars of success of the macro-economy, *viz.* stability and growth, were in peril. But the pressure has been accentuated by a benign neglect in undertaking necessary reform measures to improve the competitiveness of the economy. However, the obtaining situation has been aggravated further by a confluence of external factors ranging from global recession and practices of

discriminatory trade preferences to terrorist attacks in the USA on September 11, 2001 (Bhattacharaya 2003).

Some macroeconomic indicators of Bangladesh are reviewed below as

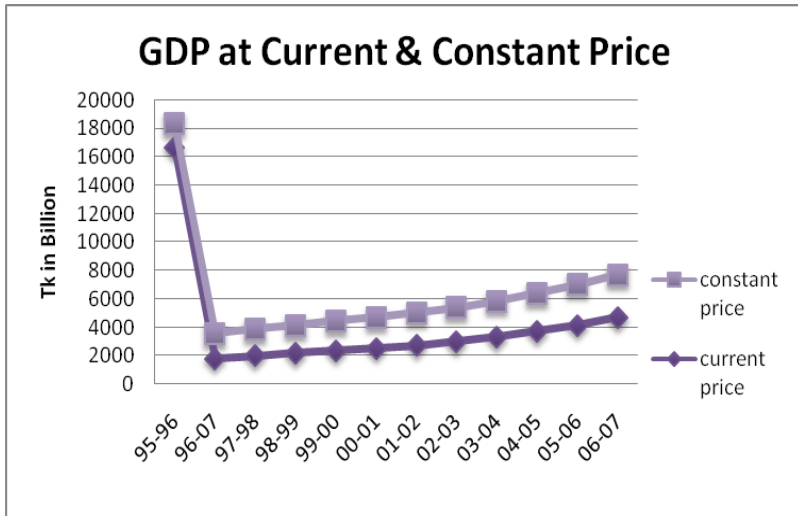
- Growth, savings & investment
- Public finance
- Monetary Sector
- Real economy
- External sector

GDP, Growth, Savings & Investment

GDP

GDP of both current and constant price after 1995 had fallen drastically because of the twin shocks emanating from large fiscal deficit and deteriorating balance of payment position that have exposed the entrenched vulnerabilities of the Bangladesh. After 1996 to 2007 both of these GDP was increasing at a steady rate.

Fig: 2.1 GDP at current and constant price

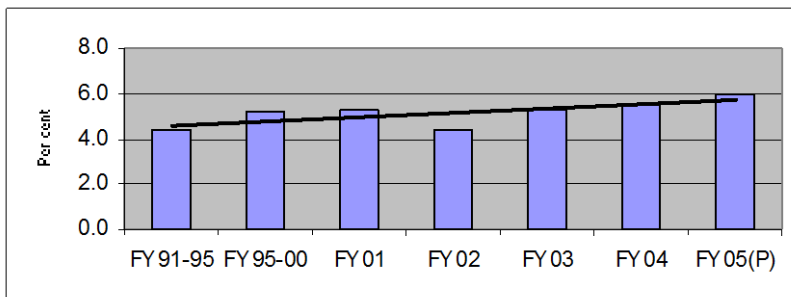


Growth

The Bangladesh Economy has experienced acceleration during the 1990s in comparison to the 1980s. The economic growth of Bangladesh has routinely registered 4 per cent plus growth in the 1990s (Figure 2.1). In the 1990s, the growth momentum was higher during the second half

of the decade in comparison to the first half: average growth rates were 4.4 per cent (FY91-95) and 5.2 per cent (FY96-05)

Fig: 2.2 Trend of GDP growth

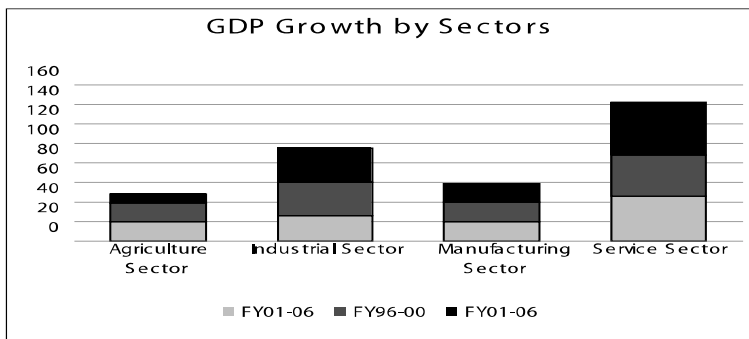


According to the BBS, the Bangladesh economy posted a growth of 5.5 per cent during FY04 as against 5.3 per cent in FY03 and 4.4 per cent in FY02. And I-PRSP projections indicate that GDP growth rate will grow at 6.0 per cent in FY05 and reach to 6.5 per cent in FY06.

Sector-wise Contribution to Incremental Growth

Analysis of the sector-wise growth figures show that within the real economy sectors such as *Industry* demonstrated stronger growth during the first half of the 1990s as against the impressive performance of the *Agriculture* in the subsequent period. It should be noted that during the second half of the 1990s, the *Agriculture* and *Industry* emerged as the major source of GDP growth in comparison to more pronounced role of the *Service Sector* in the earlier half of the decade. But in the recent time *Service Sector* again dominates as the major source of GDP growth and accounted an average of more than 50 per cent from FY01-FY06 (Fig 2.3).

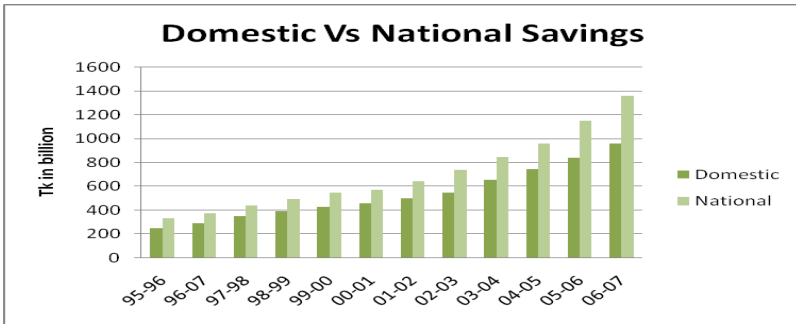
Fig: 2.3 GDP growths by sectors



Savings

Bangladesh has one of the lowest domestic savings rates among the developing countries in general and South Asian countries in particular. Bangladesh's domestic savings performance in the early 1990s was in fact paralleled the budgetary performance. The national savings rate was more or less stagnated in the first period of 1990s, which represents a reversal of the macroeconomic gains of that period.

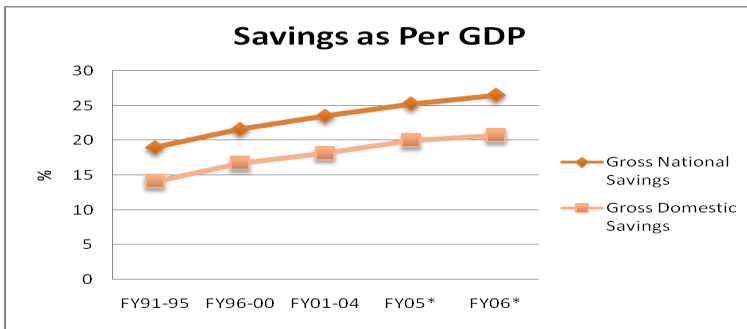
Figure 2.4: Trends in Savings Rate (FY91-FY07)



Notes: Economic Review 2007

But the domestic savings rates were more remarkable in that period. In FY91, the domestic savings rate was 18.23 per cent of GDP which was much higher than the average growth rate of the same period (14.12 per cent). The possible reasons responsible for that scenario were weakening efforts for mobilization of public sector resources and import liberalization, in the absence of a strengthening of domestic tax efforts after FY91.

Fig: 2.5 Savings as per cent of GDP (FY91-06)



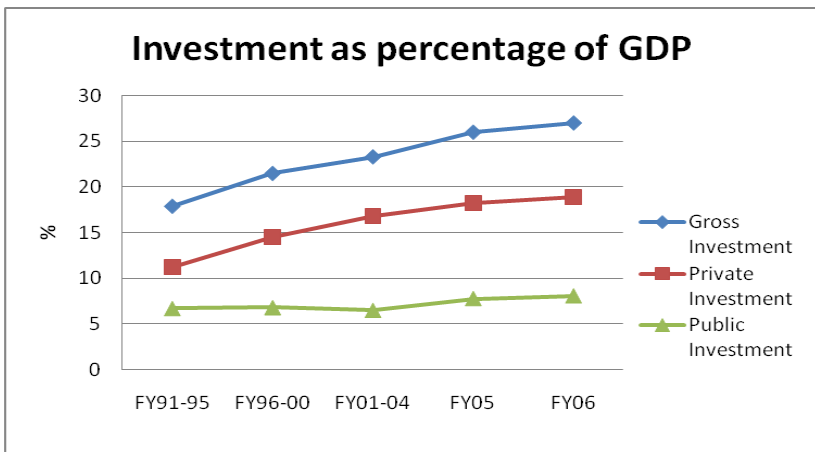
Source: Computed from CPD-IRBD Database and Finance Division

The savings rate both domestic and national showed an increasing trend in the latter period of 1990s compared to its previous period, although it did not show any drastic change. The domestic savings rate is stagnated for last couple of years. In FY01 it was 18.00 per cent, stagnates at 18.27 per cent in FY06. On the other hand, the national savings rate also increased marginally from 22.41 per cent in FY01 to 22.49 per cent in FY04. The marginal increase of the latter is underpinned by increasing flow of foreign remittances from the expatriate Bangladeshi workers. The prolonged stagnation of the domestic savings may be largely explained by the deteriorating income distribution scenario in the Bangladesh economy as the poor who demonstrate higher propensity to save are being deprived of their proportionate share in incremental national income.

Investment

The official estimates show that the gross investment-GDP ratio increased steadily by more than 4 percentage points between FY91 and FY95. The import boom witnessed in this period can be perhaps attributed to short-lived investment dynamism, coupled with large cuts in import duty rates undertaken as part of import liberalization program.

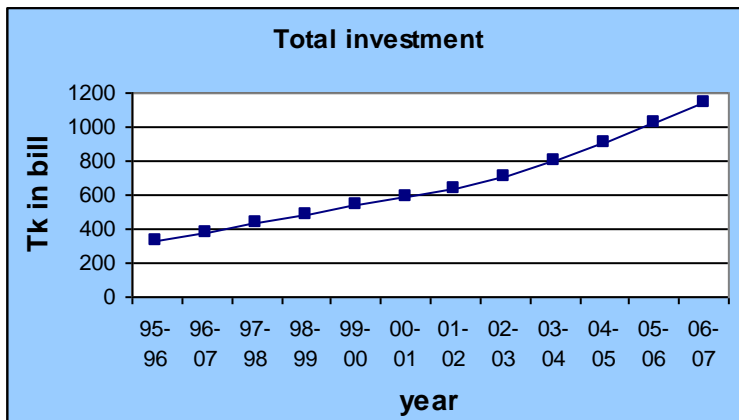
Fig: 2.6 Investment as percentage of GDP (FY91-FY04)



Gross investment as a share of GDP reached 23.02 in FY00 from 19.99 per cent in FY96, recording an average growth of about 21.51 per cent during that period. In average, the public investment rate has increased marginally from 6.69 per cent during FY91-FY95 to 6.79 per cent during FY96-FY00. The time series data shows that a virtual stagnation

was prevailing in the rate of private investment as it is hovering at an average less than 15 per cent of GDP during the period.

Figure 2.7: Investment Trend (FY91-FY07)



Note: Economic Review 2007

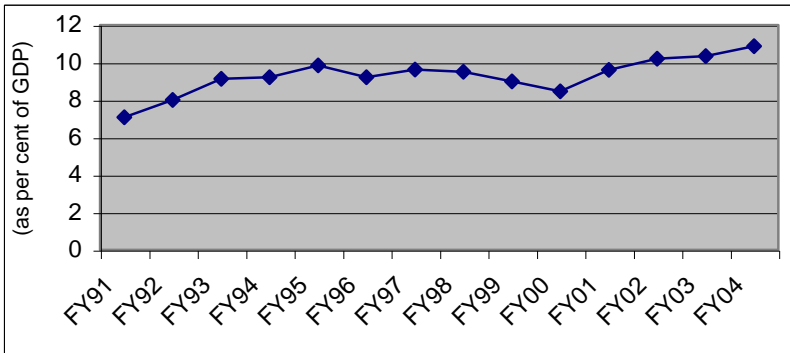
The gross investment rate was 23.09 per cent and 23.58 per cent of GDP in FY01 and FY04, respectively, indicating a less than 0.50 per cent growth during this period. The public investment rate has declined from 7.25 per cent in FY01 to 6.12 per cent of GDP in FY04. The private investment rate private investment has increased from 15.86 per cent in FY01 to 17.47 per cent of GDP in FY04. However, data shows that private investment is more or less stagnated during the period. So, it is obvious that without the sustained increase of the public investment rate during the corresponding period, the gross investment scenario would have been much more depressing.

Public Finance

Revenue Receipts

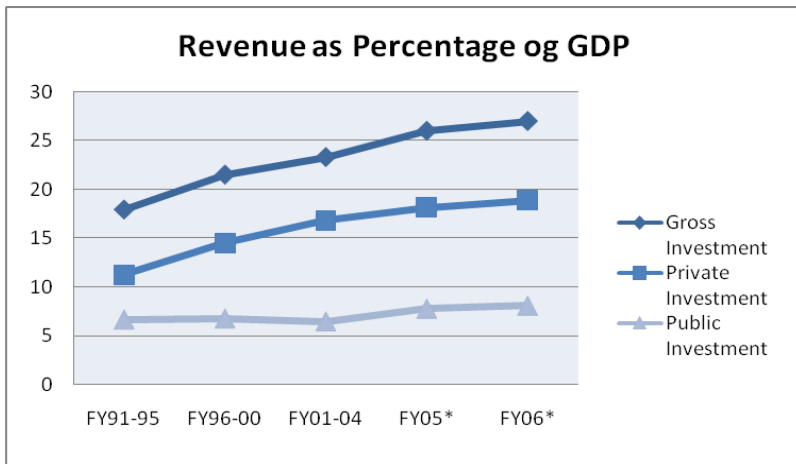
Weaknesses in the domestic resource mobilization effort have emerged as one of the major structural constraints facing the Bangladesh economy in the 1990s. Though the share of revenue (tax and non-tax together) in the GDP has increased from 7.08 per cent in FY91 to 10.87 per cent in FY06, nonetheless one observes a plateauing of the revenue-GDP ratio since the mid-1990s (Figure 2.8). Thus the revenue receipts in Bangladesh, as a share of GDP, is still lower than many developing countries.

Figure 2.8: Total Revenue as percentage of GDP



After the success of the early 1990s in revenue earnings, the revenue mobilization process started to show signs of exhaustion. The success of the early 1990s was greatly triggered by the introduction of VAT. The VAT provided a bigger source of revenue compared to the taxes it replaced, mainly in respect of taxation of domestic production. The dip

Fig: 2.9 Revenue as percentage of GDP (FY91-FY06)



*Notes: * indicates I-PRSP Projections*

Source: Computed from CPD-IRBD Database and Finance Division (2004)

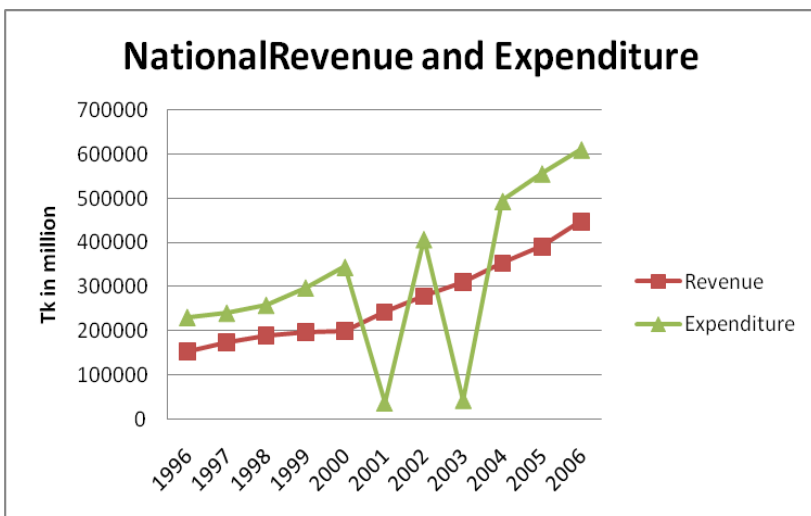
in the second half of 1990s was largely predicated by the devastating floods of 1998. Some recovery was observed in FY01, when the total revenue collection recorded 9.60 per cent of GDP and increased to

10.87 per cent in FY04. Such a feat was possible thanks to spectacular success in meeting the revenue collection target by the NBR. The I-PRSP projections show that the total revenue as percentage of GDP will reach to 11.9 per cent in FY06.

Public Expenditure

Two distinctive phases in the trend of total public expenditure growth may be discerned in the Bangladesh economy during the 1990s. Public expenditures as a share of GDP experienced a rise in the early 1990s from the benchmark level of 12.91 per cent in FY91 and had hovered above 14 per cent during the mid-1990s. The said share once again started to increase in the second half of the 1990s, recording its peak in FY01 (14.8 per cent). And in FY04, public expenditure stagnates to 14.8 per cent of GDP and anticipates reaching 15.47 per cent in FY05. One important thing is to note that public expenditure-GDP ratio in Bangladesh remains quite low compare to other neighboring countries where the said share is around 20 per cent of GDP. For example, in India and Pakistan central government expenditure as a share of GDP (2002) are 30 per cent and 20 per cent respectively.

Fig: 2.10 National revenue and expenditure

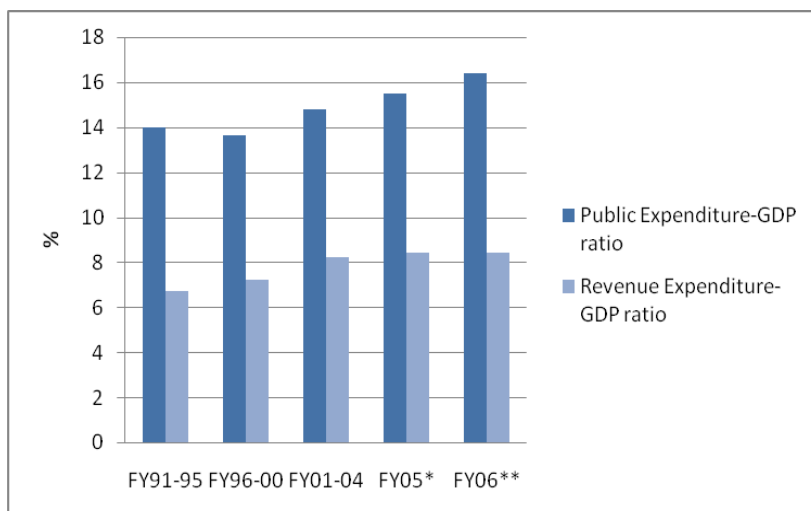


Revenue Expenditure

The revenue expenditures as a share of GDP had experienced a secular rise throughout the 1990s. But it has observed from the estimates that the average growth of revenue expenditure was lower during the first

half of the 1990s compare to the second half. For instance, the revenue expenditure as a per cent of GDP was, on average, 6.7 per cent during the FY91-FY95 period; whereas the comparable figure for the next period (FY96-FY00) was 7.2 per cent. The said ratio was increased to 8.2 per cent on average for the last four fiscal years (FY01-FY06). According to the I-PRSP projections the revenue expenditure will increase by 8.4 percentage of GDP for the next two years.

Fig:2.11 Public Expenditure and Revenue Expenditure as percentage of GDP



*Notes: * indicates I-PRSP Projections*

Source: Computed from CPD-IRBD Database and Finance Division (2004)

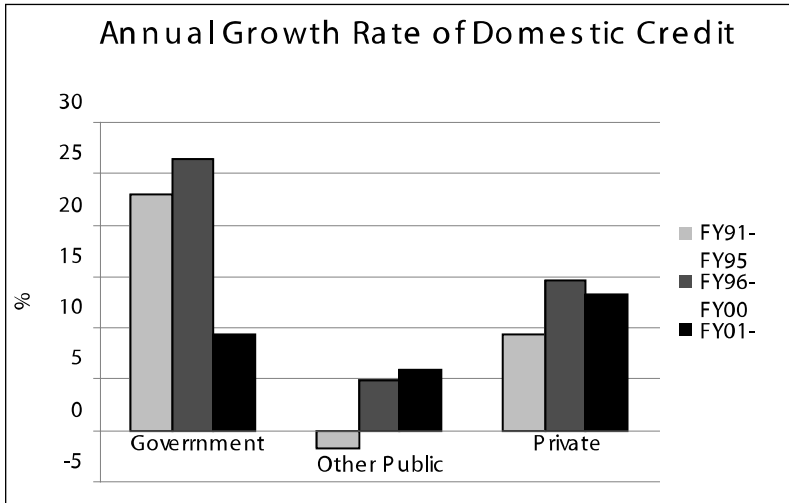
Monetary Sector

Domestic Credit Expansion

Domestic credit expansion has been observed a rapid growth during the first half of 1990s with an average of 9.31 per cent (from 7.25 per cent in FY01 to 17.56 per cent in FY95) except 4.86 per cent growth rate recorded in FY94. It has been arrested after the mid-1990s and brought down to 13.64 per cent at the end of the second half of 1990s, although a 14.69 per cent growth rate has registered in that period which is much higher than the first half. A moderate expansionary monetary policy was responsible for that higher average growth rate of aggregate credit during the later part of the 1990s. It is also essential to be noted that the growth rates of aggregate credit in the second half were consistently

higher compare to the first half. Domestic credit expansion has once again picked up in FY01 registering a growth rate of 17.65 per cent and brought down drastically to 9.48 per cent in FY03 which decreased the average growth rate to 13.35 during FY05-FY06 compare to the previous period.

Fig: 2.12 Annual growth rate domestic credits



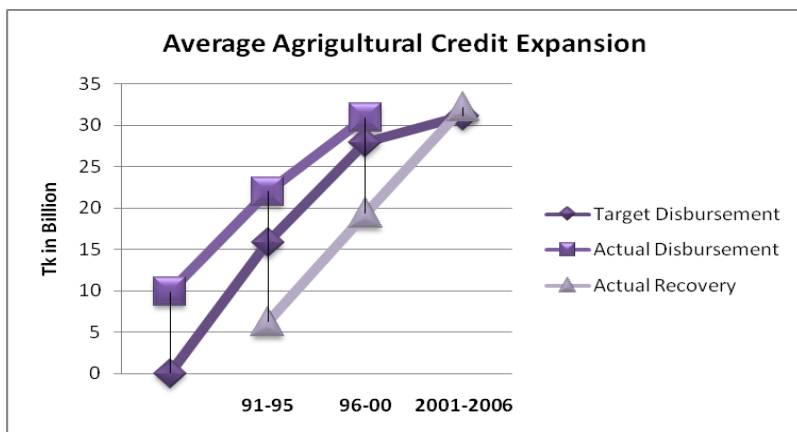
Source: Computed from CPD-IRBD Database and Bangladesh Bank data

However, it is important to note that the annual growth rate of domestic credit expansion in the government sector had been systematically higher throughout the 1990s than that of the private sector. For example, the average rate of growth in the government sector during FY91-FY95 was 22.95 per cent as against about 10.89 per cent in the private sector. During the second half of 1990s, the respective rates were 26.52 per cent and 13.77 per cent correspondingly. The differential between the two sets of credit expansion rate shows an opposite picture after 1990s registering, on average, a growth rate of 9.42 per cent in the government sector and 15.40 per cent in the private sector respectively during FY01-FY06. A negative growth rate (5.46 per cent) in the government sector in FY03 was responsible for that remarkable change in the composition of domestic credit expansion. In spite of the differential rates of growth, the private sector is maintaining its major share in the total credit expansion, from 68.82 per cent, on average, during FY91-FY95 to 72.02 per cent during FY01-FY06.

Agricultural Credit

One of the weak links of Bangladesh's rural economy is the flow of agricultural credit from institutional sources. Financial institutions have rather emerged as a guide for rural-urban resource transfers. Throughout the 1990s a little net inflow of resources from the rural areas had been observed as the annual disbursement figure exceeds the corresponding recovery figure. For example, during FY91-FY95 and FY96-FY00 on average, such net outflows registered Tk. 13.6 billion and Tk. 2.63 billion respectively.

Fig: 2.13 Averages Agricultural Credit Expansion



Source: Computed from CPD-IRBD Database and Bangladesh Bank data

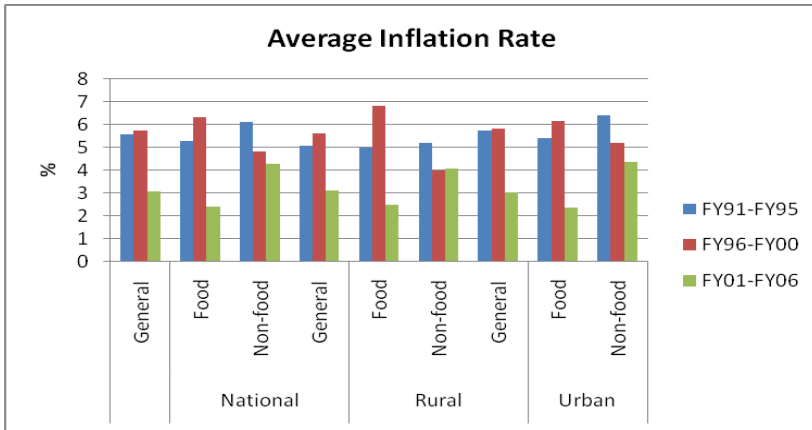
After a long time, the government went for an extraordinary agricultural expansion with a view to both reviving rural economic activity and sustaining aggregate demand in the post-flood situation in FY99. As against a recovery of Tk. 19.2 billion, Tk. 30.2 billion was disbursed resulting in a net inflow of Tk. 11.03 billion of agricultural credit. That large amount of agricultural credit played a significant role in boosting the record *boro* crop of FY99, which played such an important part in helping the rural economy to recover from the effects of the floods. At the end of the 1990s and the beginning of the new decade, a net outflow of resources from rural areas was observed, registered, on average, Tk. (-) 1.27 billion during FY05-FY06.

Inflation

A low rate of inflation is one of the cornerstones of macroeconomic stability of an economy. The country has experienced a moderate rate of

inflation under double digit throughout the 1990s. At the first half of the 1990s, the national inflation rate (moving average) was, on average, 5.55 per cent, while the inflation rates for the abovementioned period for the urban and rural areas were 5.05 per cent and 5.71 per cent respectively. The average inflation rate in the latter half of the 1990s was somewhat high but under double-digit level. Even during the flood year (FY99) the national inflation rate did not rise to double-digit level.

Fig: 2.14 Average Inflation Rate (Moving Average) (FY91-FY06)



Source: CPD-IRBD Database and BBS data. (Base: FY86=100)

Although the rate remained under double-digit level, the inflation rate indicates an upward trend after FY97 just for two years. But the rising trend in inflation during FY99 was corrected during FY00 as the moving average rate came down to 3.41 per cent in June 2000 compare to 8.90 per cent in June 1999 because of a record *aman* harvest in FY00. As we observe that the average inflation rate for the said period was 5.70 per cent in the national level. For the rural and urban areas, the rates were 6.79 per cent and 6.11 per cent respectively. The increasing trend of inflation rate had been corrected since the beginning of new decade after 1990s. Such sustained low level of inflation was dictated by lower food grain prices ensured by successive good harvests. During the first three years of the new decade the average national inflation rate observed 3.03 per cent with very low level of food inflation rate at 2.38 per cent.

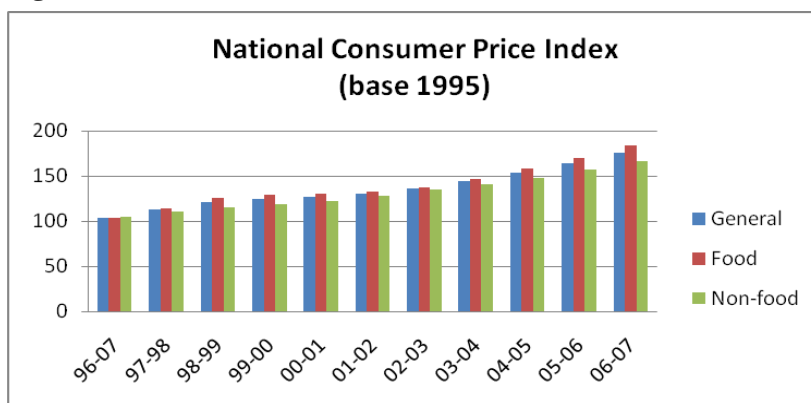
The recent trend in inflation rate (moving average) demonstrates an increasing trend. The inflation rate has increased from 2.36 per cent in the end June of FY02 to 5.14 per cent in the end June of FY05. Two

disturbing features of the recent rise in the price level may be noted. *First*, the inflation rate during the period FY03 had been higher in the rural area in comparison to its urban counter part. *Second*, curiously, increase in food price during above mentioned period had been again higher in the rural area along with non-food price.

National Consumer Price Index

The national consumer price index from 1996 to 2007 shows an upward trend. In fig 2.15 a comparative trend of food and non food consumer price index indicates that both of them had a increasing trend.

Fig: 2.15 National Consumer Price Index



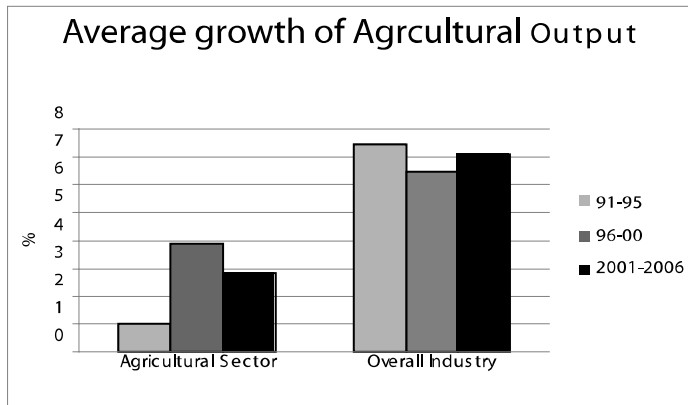
Real Economy

Agricultural & Industrial Production

In spite of diminishing share in GDP, almost all the components of the agricultural sector have been demonstrating robust growth during the 1990s. The agricultural sector in general and the crop sector in particular still define the threshold performance of the Bangladesh economy. In the first half of the 1990s, the fisheries sub-sector had recorded the highest average growth of 7.78 per cent as against of 0.98 per cent average growth in the whole agriculture sector. A negative average growth rate (-) 0.34 per cent of the crop sector was responsible for that tiny growth in the agricultural sector during FY91-FY95. However, the agricultural sector received an excellent support from the sustained impressive growth of the crop sector during the second half of the 1990s. After the devastating shock imparted by the 1998 floods, the agricultural sector came back sharply and has maintained an outstanding growth performance through the consecutive record harvest of food

grains. The sector has achieved an average growth rate of 3.88 per cent with the outstanding growth rate of 3.86 per cent in the crop sector during the second half. The fisheries sub-sector continued its highest performance (7.78 per cent on average) during that period. The agricultural sector continued to perform well in the first three years after 1990s although the average growth rate (2.83 per cent) during these years was lower compare to the second half of 1990s.

Fig: 2.16 Average Growth of Agricultural Output



Source: Computed from CPD-IRBD Database and BBS Data

During the early 1990s, the high growth in the manufacturing industries was accompanied by a rapid reduction in protection through the lowering of the import tariff. The industrial sector in the first half of the 1990s grew at an average annual rate 7.47 per cent which was largely possible for a robust growth in the manufacturing sector with on average growth rate 8.20 per cent. The robust performance of the manufacturing sector has decelerated during the second half of the 1990s recorded an average growth rate of 6.52 per cent. As a result, the growth of overall industry declined to 6.44 per cent, on average. The prolonged and devastating flood of 1998 was basis for the severe losses of the industrial sector at the end of the second half 1990s. For example, the overall industrial sector grew at annual rate of 4.90 per cent while the growth rate of the manufacturing sector was 3.19 per cent in FY99.

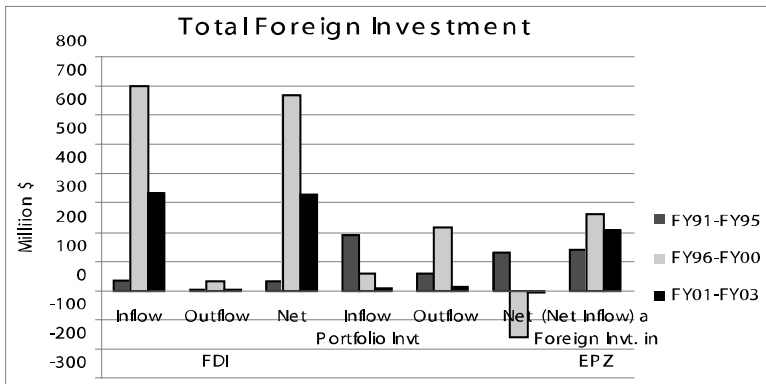
The industrial sector has recovered gradually in the successive years after 1990s posting, on average, 7.12 per cent growth rate during FY01-FY04. The recovery was visible mainly in the large and medium scale industries as well as in small industries as 6.26 per cent and 7.39 per

cent growth rate, on average, during FY01-FY06 against 5.49 per cent and 5.87 per cent during the second half of the 1990s.

Foreign Investment

Bangladesh received a net amount of \$304.40 million as foreign investment (including foreign direct investment, portfolio investment and foreign investment in the EPZs) in the first half of the 1990s, of which, about \$141.10 million (46.4 per cent) came as foreign direct investment (FDI) in the EPZ and \$ 130.66 million (42.9 per cent) as portfolio investment. During the second half of the decade, a drastic change has observed in the composition of the total foreign investment as FDI played the key role in boosting the total inflow of foreign investment. Net flow of FDI sharply increased from \$32.64 million during FY91-FY95 to \$667.72 million in the second half, which is about 87 per cent in total inflow of foreign investment (\$770.05 million). Portfolio investment recorded a net outflow of \$ 157.57 million in that period while foreign investment in EPZ recorded a 84.2 per cent growth rate over the first half.

Fig. 2.17 Totals Foreign Investment



Source: Computed from CPD-IRBD Database, Bangladesh Bank Data and BEPZA.

During the first three years after 1990s Bangladesh witnessed an inflow of foreign investment of \$534.30 million, of which \$330.98 million (61.94 per cent) came as net inflow of FDI and another \$207.24 million in the EPZ. It is expected that the figure may rise further in FY04 – but largely in the EPZs. However, the resurgence of the controversy regarding trade union rights in the EPZs, reflecting the concerns of Bangladesh's largest export market, the USA, vis-a-vis the concerns of some of Bangladesh's largest sources is investment in the

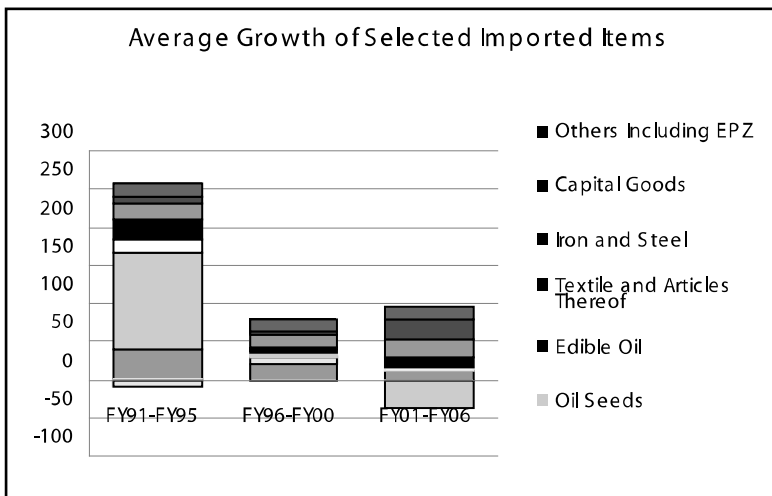
EPZ, drawn from Japan and the Republic of Korea needs to be reserved without prejudice either to Bangladesh’s export or investment prospects.

External Sector

Export & Import

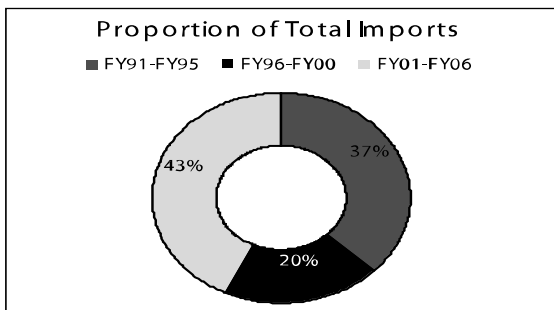
Throughout the 1990s, Bangladesh's import sector registered an average growth rate of about 11 per cent. During the first half of the decade, liberalization policy taken by the governments for swelling imports gave support to the flow of inputs for export-oriented and domestic industries, and led to a surge in consumer and non-production related imports (Rahman: 2002). As a result, the total imports recorded an average growth rate of 14.53 per cent in the said period. Among the sub-sectors, the average growth rates of food grain, textile & dairy seeds and iron & steel were 39.17 per cent, 25.78 per cent and 23.04 per cent respectively. Imports of oil seeds showed a robust average growth of 127.55 per cent.

Fig: 2.18 Average Growths of Selected Imported Items (FY91-FY06)



Source: Various Issues of Economic Trends, Statistics Department, Bangladesh Bank

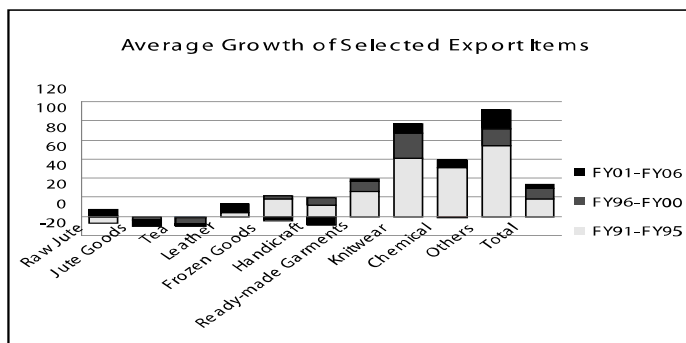
During the second half of 1990s, almost every imported items registered lower average growth compared to the previous period. Imports of food grain (20.32 per cent), oil seeds (5.66 per cent), textile and articles thereof (2.76 per cent) showed a drastic fall in the average growth rate. As a result, the average growth rate of total imports in the said period slowed down to 7.63 per cent.

Fig: 2.19 Proportion of Total Import

The import growth arrested a positive tone during the first three fiscal years of the new decade after 1990s. The average import growth was 16.84 per cent which is the highest average growth rate among the three compared periods. This modest growth rate of imports has been achieved due to the robust growth of textile and articles thereof (11.51 per cent), iron and steel (23.79 per cent) and capital goods (25.76 per cent). The growth rate of oil seeds continued to decline registering average growth rate of (-) 37.94 per cent during this period.

Exports

One of the major achievements of Bangladesh economy during the 1990s was the robust growth of exports, which put the country in the league of top 20 countries demonstrating fastest export expansion. At the same time, Bangladesh was in the process of graduating from a predominantly aid-dependent economy to a trading economy in this decade. Bangladesh's export sector registered an average growth rate of 14.53 per cent per annum throughout the 1990s.

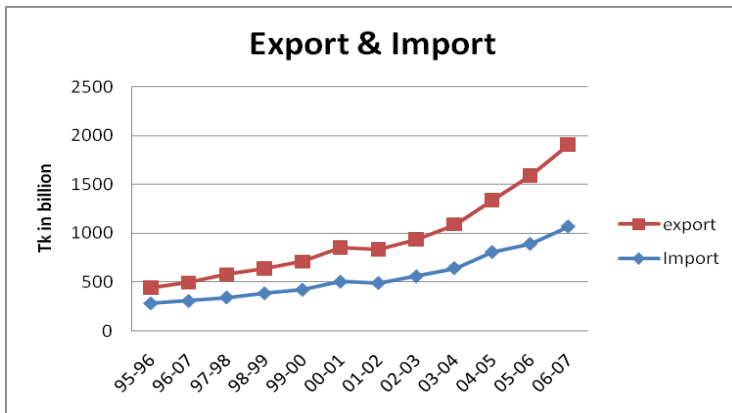
Fig: 2.20 Average Growths of Selected Export Items (FY91-FY06)

Source: Computed from CPD-IRBD Database and EPB Data

Table 16 indicates that the average growth rate of export (18.34 per cent) sector during the first half of the 1990s was much more higher comparing to the second half (10.73 per cent). Almost all export items experienced a robust average growth rate in the first half. More specifically, such a moderate growth rate of the export sector was possible due to the robust growth of frozen goods (18.80 per cent), ready-made garments (25.64 per cent), knitwear (60.55 per cent), chemical (50.92 per cent). During the second half of 1990s, the average growth rate of some of these items had drastically fallen. For example, a negative growth rate (1.08 per cent) registered in the chemical item and very lower growth rate in the frozen goods (3.03 per cent) and in the ready-made garments (11.27 per cent).

Most encouraging point of the beginning in the new decade (after 1990s) is positive and considerable growth rate (6.40 per cent) of raw jute items although the average growth rate have fallen to 4.77 per cent during the last three years. Again, very low growth rate of ready-made garments (2.10 per cent), knitwear (9.55 per cent) was observed in the said period.

Figure: 2.21 Total Imports (FY91-FY07)



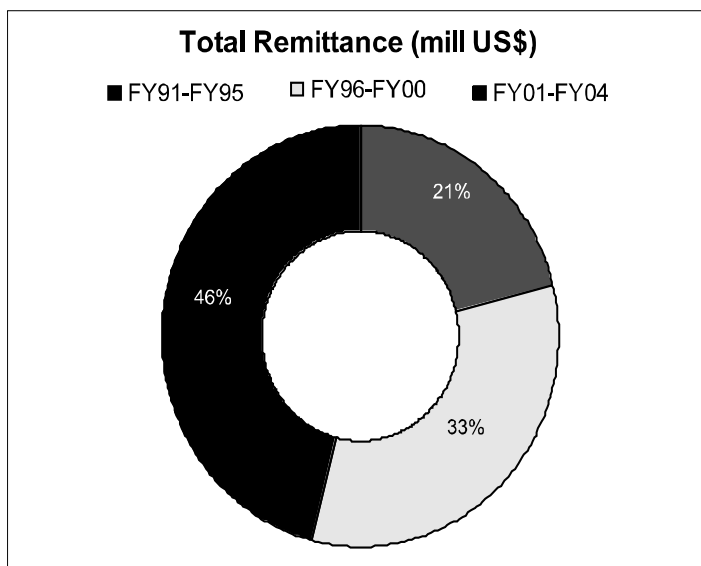
Foreign Remittance

The annual flow of remittances received from Bangladeshi migrant workers has been quite robust throughout the 1990s rising from US\$ 764.0 million in FY1991 to US\$ 1949.32 million by FY2000. At the beginning of the new decade after 1990s flow of remittances has been continuing its robust growth and reached to US\$ 3367.0 million in FY06.

At the first half of the 1990s Bangladesh received a total US\$ 4844.49 million as foreign remittances with an average growth rate of 9.62 per cent per annum. Likewise, the annual average growth rate of the number of persons going abroad was 18.48 in the said period.

Throughout the latter half of 1990s, the increase in the number of persons going abroad was, on average, 5.20 per cent indicating a fall in the flow of Bangladeshi migrant workers. On the other hand, the annual average growth rate of remittances was 10.46 per cent with the total remittances US\$ 7872.95 million, implying higher earning by Bangladeshi migrant workers during this period compare to the previous.

Figure: 2.22 Proportion of Total Remittance (FY91-FY07)



Source: Economic Trends, Bangladesh Bank & Bangladesh Economic Survey, Ministry of Finance, GOB.

During the first four years (FY01-FY04) after 1990s, Bangladesh received US\$ 10812.99 million, which was as high as 15.5 per cent more annually, on average, than the comparable figure for second half of the 1990s. However for the first time in recent history, there was a fall in remittances in FY01 with a negative growth of 3.4 per cent (Figure XII). In FY02, the country received the record inflow of more \$2.5 billion registering a record annual growth of about 33 per cent since 1990.

Foreign Aid

During the decade of the 1990s Bangladesh has undergone a historical structural transformation from being an aid dependent to a trade driven country as a consequence of a sharp rise in the importance of international trade relative to the flow of aid to the country. In 1990 export was 0.8 times that of aid disbursed; in the 2000 this has raised to 3.6 and it has reached to 4.13 in FY05.

Figure: 2.23 Total Foreign Aid (FY91-FY07)

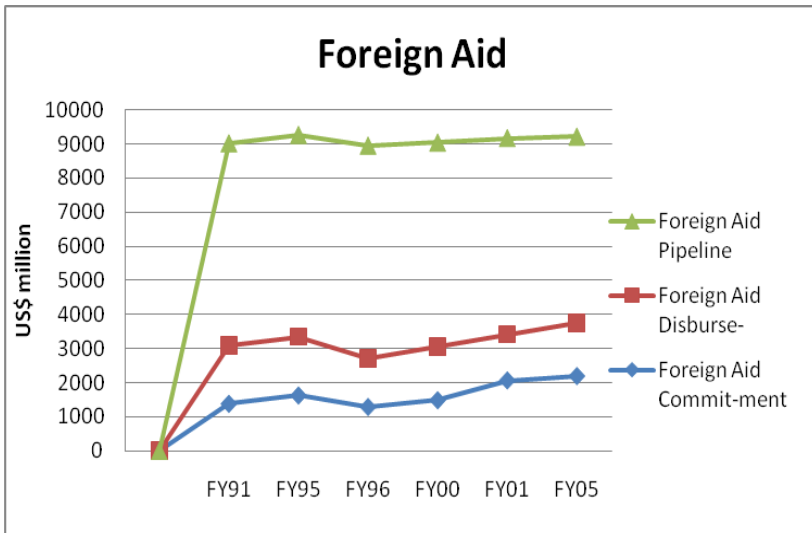
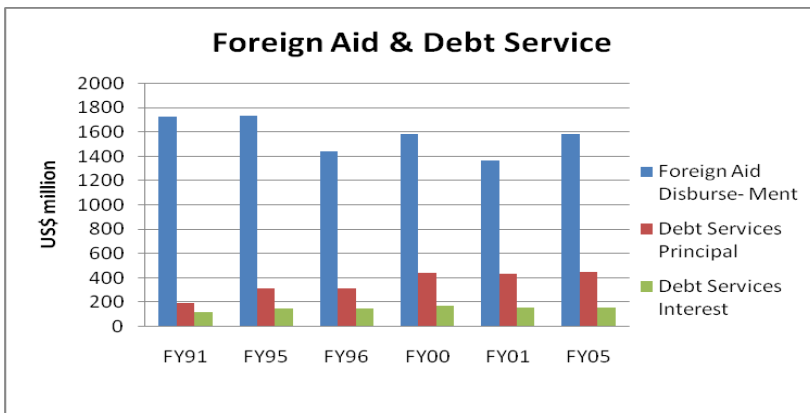
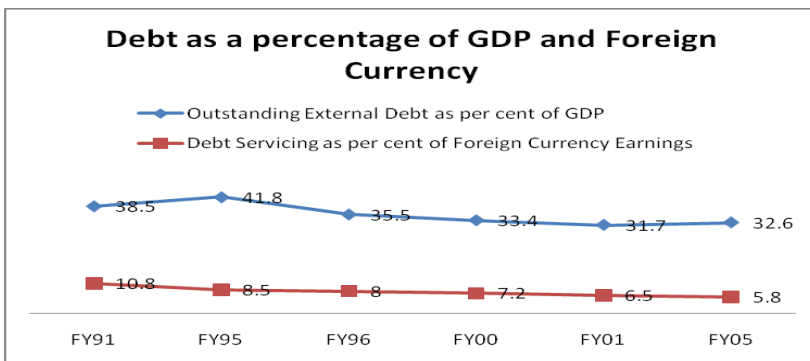


Table 18 provides information about the foreign aid and debt services for three consecutive phases since FY91. Foreign aid commitment and disbursement in FY91 were \$1715.2 million and \$1663.4 million, respectively. At the end of the first half of 1990s (FY95), although commitment was 17.66 per cent higher than FY91, the growth rate of disbursement was very low (only 0.3 per cent). The beginning of the second half was more depressing for overall foreign aid situation. Both foreign aid commitment and disbursement showed a negative growth rate of 20.6 per cent and 17 per cent, respectively. But they bounced back with positive growth rate of 15.23 per cent and 9.9 per cent respectively at the end of the second half. The positive growth rate of commitments and disbursement has continued in FY03 when they were \$2179 million and 1585 million respectively.

Figure: 2.24 Total foreign aid and debt services (FY91-FY07)

The total outstanding external debt of Bangladesh as of June 1995 was about \$15.95 billion (41.8 per cent of GDP) which has decreased by 1.4 per cent at the end of the 1990s. In FY03 7.8 per cent higher total outstanding debt has observed compare to FY00.

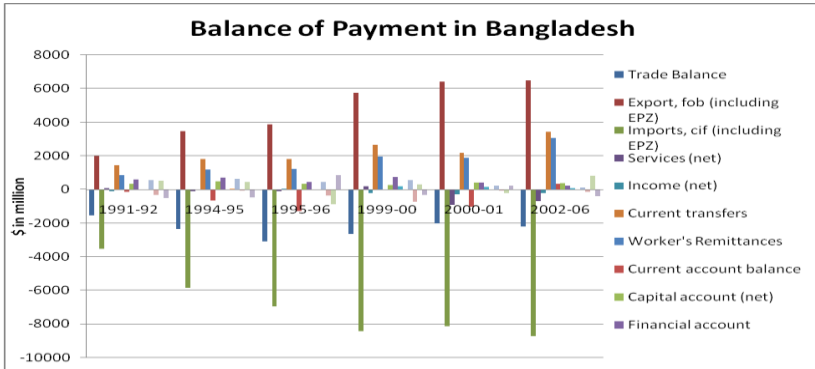
Figure: 2.25 Debt as a percentage of GDP and foreign currency

Balance of Payment

Bangladesh's overall balance of payments (BOP) position demonstrated a positive trend between FY91-FY94. But in the middle of the 1990s, the BOP situation has reversed due to a significant increase in imports and the outflow for invisible payments. After that some improvements have been witnessing to the end of 1990s due to high export growth, modest import expansion, huge flow of workers remittances, reasonable flow of official transfer and steady net income from sale of services abroad (Bhattacharaya, 2003).

The current account balance have some diverse experienced throughout the 1990s. At the beginning of the decade (FY92), Bangladesh had a negative current account balance of (-) \$118 million which has reached to (-) \$1291 million in the beginning of the second half (FY96) due to a huge negative trade balance of (-) \$3063 million arise from the large volume of imports from abroad.

Fig: 2.26 Balance of Payments Scenario of Bangladesh (FY91-FY06)



Source: Computed from CPD-IRBD Database and Bangladesh Bank Data

It is notable to mention that in FY96 Bangladesh observed the highest negative trade balance during the last one and half decade. The current account balance has witnessed some improvements by the end of 1990s and enjoyed, albeit small, positive balance of \$2 million. On the other hand, in FY01, Bangladesh experienced a negative balance of (-) \$1019 million in its current account. In FY06, the current account balance amounted to a positive sum of \$328 million which facilitated the overall balance of payments to reach a positive amount of \$815 million by the end of the said fiscal year. These are the overall scenario of economic performance of Bangladesh.

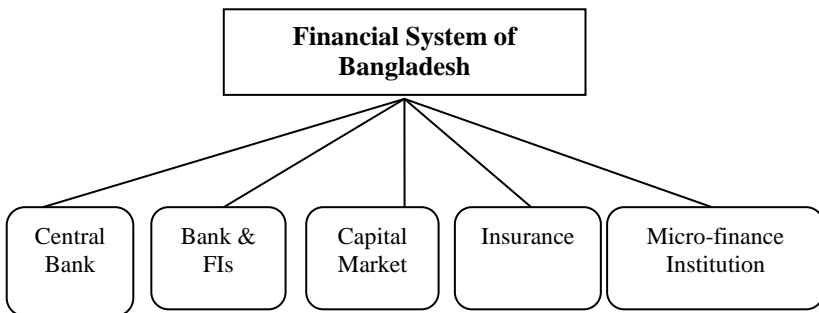
Chapter 3

Financial System of Bangladesh

Introduction

The financial system of Bangladesh consists of Bangladesh Bank (BB) as the central bank, 4 State Owned Commercial Banks (SCB), 5 government owned specialized banks, 30 domestic private banks, 9 foreign banks and 29 non-bank financial institutions. Moreover, license has given to 298 Microcredit Organizations. The financial system also embraces insurance companies, stock exchanges and co-operative banks. But the overall financial system of Bangladesh comprises the following institutions:

- Central Bank
- Bank & FIs
- Capital Market
- Insurance
- Microfinance Institution (MFIs)



Central Bank

Central Bank and Its Policies

Bangladesh Bank (BB), as the central bank, has legal authority to supervise and regulate all banks and non-bank financial institutions. It performs the traditional central banking roles of note issuance and of being the banker to the government and banks. Given some broad policy goals and objectives, it formulates and implements monetary policy manages foreign exchange reserves and lays down prudential regulations and conduct monitoring thereof as they apply to the entire

banking system. Its prudential regulations include, among others: minimum capital requirements, limits on loan concentration and insider borrowing and guidelines for asset classification and income recognition. The Bangladesh Bank has the power to impose penalties for non-compliance and also to intervene in the management of a bank if serious problem arise. It also has the delegated authority of issuing policy directives regarding the foreign exchange regime.

Interest Rate Policy

Under the financial sector reform program, banks are free to charge/fix their deposit (Bank /Financial Institutes) and Lending (Bank /Financial Institutes) rates other than Export Credit. At present, Loans at reduced rates are provided for all sorts of export credit since January 2006. With a view to controlling the price hike and ensuring adequate supply of essential commodities, the rate of interest on loan for import financing of rice, wheat, sugar, edible oil (crude and refined), chickpeas, beans, lentils, onions, spices, dates and powder milk has been temporarily fixed to a maximum of 12%. Now, banks can differentiate interest rate up to 3% considering comparative risk elements involved among borrowers in same lending category. With progressive deregulation of interest rates, banks have been advised to announce the mid-rate of the limit (if any) for different sectors and the banks may change interest 1.5% more or less than the announced mid-rate on the basis of the comparative credit risk. Recently Banks have been advised to upload their deposit and lending interest rate in their respective website.

Capital Adequacy of the Banks

With a view to strengthening the capital base of banks and making them prepare for the implementation of Basel-II Accord, banks are required to maintain Capital to Risk-Weighted Assets ratio 10% at the minimum with core capital not less than 5% effective from December 31, 2007. However, minimum capital requirement (paid up capital and statutory reserve) for all banks will be Tk.200 crore as per Bank Company (Amendment) Ordinance, 2007. Banks having capital shortfall will have to meet at least 50% of the shortfall by June, 2008 and the rest by June, 2009.

Revaluation reserves of held to maturity (HTM) securities (up to 50% of the revaluation reserves) has been added to the components of supplementary capital. Besides, 'Hedging the price risk of commodity transactions' has been included in Short-term self liquidating trade related contingencies.

Loan Classification and Provisioning

In order to strengthen credit discipline and bring classification and provisioning regulation in line with international standard, Bangladesh Bank issued a master circular on loan classification and provisioning through BRPD circular no 5 dated June 5, 2006. The revised policy covers an independent assessment of each loan on the basis of objective criteria and qualitative factors which is appended below:

- Any **Continuous Loan/Demand Loan** if not repaid/renewed within the fixed expiry date for repayment will be treated as past due/overdue from the following day of the expiry date. A **Continuous Loan/Demand loan/Term Loan** which will remain overdue for a period of 90 days or more will be put into the "Special Mention Account (SMA)". Interest accrued on "**Special Mention Account (SMA)**" will be credited to Interest Suspense Account, instead of crediting the same to Income Account.
- A **Continuous Loan/Demand loan** is classified as '**Sub-standard**' if it is past due/over due for 6 months or beyond but less than 9 months, classified as '**Doubtful**' if it is past due/over due for 9 months or beyond but less than 12 months and classified as '**Bad/Loss**' if it is past due/over due for 12 months or beyond.
- If any installment(s) or part of installment(s) of a **Fixed Term Loan** is not repaid within the due date, the amount of unpaid installment(s) will be termed as 'defaulted installment'. In case of **Fixed Term Loans**, which are repayable within **maximum five years of time**- If the amount of '**defaulted installment**' is equal to or more than the amount of installment(s) due within 6 (six) months, the entire loan will be classified as "**Sub-standard**", if the amount is equal to or more than the amount of installment(s) due within 12 (twelve) months, the entire loan will be classified as "**Doubtful**" and if the amount is equal to or more than the amount of installment(s) due within 18 (eighteen) months, the entire loan will be classified as "**Bad/Loss**".
- In case of **Fixed Term Loans**, which are repayable in **more than five years** of time and if the amount of 'defaulted installment' is equal to or more than the amount of installment(s) due within 12 (twelve) months, the entire loan will be classified as "**Sub-standard**". If the amount is due within 18 (eighteen) months, the entire loan will be classified as "**Doubtful**" and if the amount is due within 24 (twenty four) months, the entire loan will be classified as "**Bad/Loss**".

- The **Short-term Agricultural and Microcredit** will be considered irregular if not repaid within the due date as stipulated in the loan agreement. If the said irregular status continues, the credit will be classified as 'Substandard' after a period of 12 months, as 'Doubtful' after a period of 36 months and as 'Bad/Loss' after a period of 60 months from the stipulated due date as per loan agreement.

Besides, if any situational changes occur in the stipulations in terms of which the loan was extended or if the capital of the borrower is impaired due to adverse conditions or if the value of the securities decreases or if the recovery of the loan becomes uncertain due to any other unfavorable situation, the loan will have to be classified on the basis of qualitative judgment.

As regards the provision, banks are required to maintain General Provision against all categories of loans along with off-balance sheet items in the following manner:

Particulars		Short Term Agri. Credit and micro credit	Consumer Financing			Small Enterprise Financing	All other Credit
			Other than Housing Finance & Loans for Professionals to set up business	Housing Finance	Loans for Professionals to set up business		
UC	Standard	5%	5%	2%	2%	1%	1%
	SMA	-	5%	5%	5%	5%	5%
Classified	SS	5%	20%	20%	20%	20%	20%
	DF	5%	50%	50%	50%	50%	50%
	B/L	100%	100%	100%	100%	100%	100%

Source: BRPD circular no: 05, dated June 5, 2006.

BRPD circular no: 08, dated August 07, 2007

BRPD circular no: 10, dated September 18, 2007

BRPD circular no: 05, dated April 29, 2008

Besides, banks are required to maintain general provision against Off-balance sheet exposures in the following manner:

- @ 0.5% provision effective from December 31, 2007 and
- @ 1% provision effective from December 31, 2008

Other instructions such as Eligible securities in determining base for provision along with a revised format for submitting the report on classification of loans and advances are also provided in the respective circulars.

Foreign Exchange System

On March 24, 1994 Bangladesh Taka (domestic currency) was declared convertible for current transactions in terms of Article VIII of the **IMF** Articles of Agreement. Consequent to this, current external settlements for trade in goods and services and for amortization payments on foreign borrowings can be made through banks authorized to deal in foreign exchange, without prior central bank authorization. However, because resident owned capital is not freely transferable abroad (Taka is not yet convertible on capital account), some current settlements beyond certain indicative limits are subject to confides checks. Direct investments of non-residents in the industrial sector and portfolio investments of non-residents through stock exchanges are repairable abroad, as also are capital gains and profits/dividends thereon. Investment abroad of resident-owned capital is subject to prior Bangladesh Bank approval, which is allowed only sparingly.

Exchange Rate Policy

The exchange rate policy of Bangladesh Bank aims at maintaining the competitiveness of Bangladeshi products in the international markets, encouraging inflow of wage earners' remittances, maintaining internal price stability, and maintaining a viable external account position. Prior to the inception of floating exchange rate regime, adjustments in exchange rates were made while keeping in view the trends of Real Effective Exchange Rate (REER) index based on a trade weighted basket of currencies of major trading partners of Bangladesh and the trends of other important internal and external sector indicators. Under the existing floating exchange rate regime (that started from 31/05/2003), the inter-bank foreign exchange market sets the exchange rates for customer transactions and inter-bank transactions based on demand-supply interplay; while the exchange rates for the Bangladesh Bank's spot purchase and sales transactions of US Dollars with ADs is decided on a case to case basis. Bangladesh Bank does not undertake any forward transaction with ADs. The ADs are free to quote their own spot and forward exchange rates for inter-bank transactions and for transactions with non-bank customers. However, along with intervention in the taka money market, the US dollar purchase or sale transactions take place by the Bangladesh Bank as needed, to maintain orderly market conditions.

Banks and FIs

Bank Licensing

Bank Company Act, 1991, empowers BB to issue licenses to carry out banking business in Bangladesh. Pursuant to section 31 of the Act, before granting a license, BB needs to be satisfied that the following conditions are fulfilled: "that the company is or will be in a position to pay its present or future depositors in full as their claims accrue; that the affairs of the company are not being or are not likely to be conducted in a manner detrimental to the interest of its present and future depositors; that, in the case of a company incorporated outside Bangladesh, the Government or law of the country in which it is incorporated Bangladesh as the Government or law of Bangladesh grants to banking companies incorporated outside Bangladesh and that the company complies with all applicable provisions of Bank Companies Act, 1991."

Licenses may be cancelled if the bank fails to comply with above provisions or ceases to carry on banking business in Bangladesh.

Commercial Banks

The commercial banking system dominates the financial sector with limited role of Non-Bank Financial Institutions and the capital market. The Banking sector alone accounts for a substantial share of assets of the financial system. The banking system is dominated by the 4 State Owned Commercial Banks, which together controlled more than 30% of deposits and operates 3383 branches (50% of the total) as of June 30, 2008.

A. Four State Owned Commercial banks

1. Agrani Bank
2. Janata Bank
3. Rupali Bank Limited*
4. Sonali Bank

B. List of the private banks operating in Bangladesh:

1. Al-Arafah Islami Bank Limited
2. Arab Bangladesh Bank Limited
3. Bangladesh Commerce Bank Limited
4. Bank Asia Limited
5. BRAC Bank Limited

6. Dhaka Bank Limited
7. Dutch Bangla Bank Limited
8. Eastern Bank Limited
9. Export Import Bank of Bangladesh Limited
10. First Security Bank Limited
11. International Finance Investment and
12. Commerce Bank Limited
13. Islami Bank Bangladesh Limited
14. Jamuna Bank Limited
15. Mercantile Bank Limited
16. Mutual Trust Bank Limited
17. National Bank Limited
18. National Credit and Commerce Bank Limited
19. One Bank Limited
20. Prime Bank Limited
21. Pubali Bank Limited
22. Shahjalal Islami Bank Limited
23. Social Investment Bank Limited
24. South East Bank Limited
25. Standard Bank Limited
26. The City Bank Limited
27. The Oriental Bank Bangladesh Limited
28. The Premier Bank Limited
29. The Trust Bank Limited
30. United Commercial Bank Limited
31. Uttara Bank Limited

Foreign commercial banks (10)

1. American Express Bank Limited
2. Bank Alfalah Limited
3. Citibank N.A
4. Commercial Bank of Ceylon Limited
5. Habib Bank Limited
6. National Bank of Pakistan
7. Standard Chartered Bank
8. State Bank of India
9. The Hongkong and Shanghai Banking Corporation Limited
10. Woori Bank Limited

Specialized Banks

Out of the 5 specialized banks, 2(Bangladesh Krishi Bank and Rajshahi Krishi Unnayan Bank) were created to meet the credit need of the agricultural sector while the other two (Bangladesh Shilpa Bank (**BSB**) & Bangladesh Shilpa Rin Sangtha (**BSRS**)) are for extending term loans to the industrial sector of Bangladesh.

1. Bangladesh Krishi Bank
2. Bangladesh Shilpa Bank
3. Bangladesh Shilpa Rin Sangtha
4. Commerce (BASIC) Bank Limited
5. Rajshahi Krishi Unnayan Bank

Financial Institutions

Twenty-nine financial institutions are now operating in Bangladesh. Of these institutions, 1 (one) is govt. owned, 15 (fifteen) are local (private) and the other 13(thirteen) are established under joint venture with foreign participation. The total amount of loan & lease of these institutions is Tk. 99,091.80 million as on 31 December, 2007. Bangladesh Bank has introduced a policy for loan & lease classification and provisioning for FIs from December 2000 on half-yearly basis. To enable the financial institutions to mobilize medium and long-term resources, Government of Bangladesh (GOB) signed a project loan with IDA, and a project known as “Financial Institutions Development Project (FIDP)” has started its operation from February 2000. Bangladesh Bank is administering the project. The project has established “Credit, Bridge and Standby Facility (CBSF)” to implement the financing program with a cost of US\$ 57.00 million.

The Capital Market

The Capital market, an important ingredient of the financial system, plays a significant role in the economy of the country.

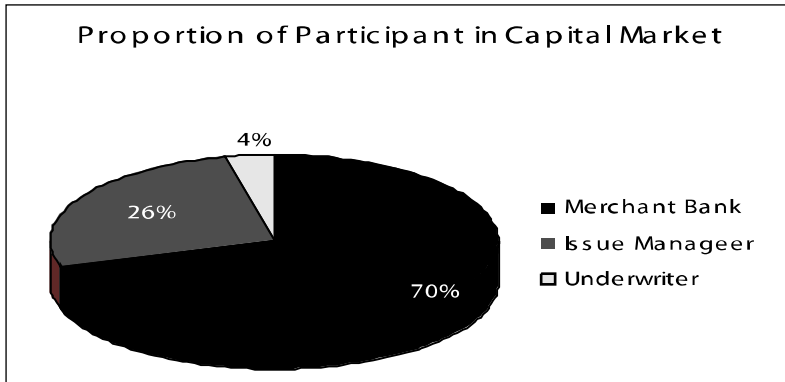
Regulatory Bodies

The Securities and Exchange Commission exercises powers under the Securities and Exchange Commission Act 1993. It regulates institutions engaged in capital market activities. Bangladesh Bank exercises powers under the Financial Institutions Act 1993 and regulates institutions engaged in financing activities including leasing companies and venture capital companies.

Participant in the Capital Market

The SEC has issued licenses to 27 institutions to act in the capital market. Of these, 19 institutions are Merchant Banker & Portfolio Manager while 7 are Issue Managers and 1(one) acts as Issue Manager and Underwriter.

Fig: 3.1 Proportion of Participant of Capital Market



- i) **Stock Exchanges** There are two stock exchanges (the Dhaka Stock Exchange (**DSE**) and the Chittagong Stock Exchange (**CSE**) deal in the secondary capital market. DSE was established as a public Limited Company in April 1954 while CSE in April 1995. As of 30 June 2000 the total number of enlisted securities with DSE and CSE were 239 and 169 respectively. Out of 239 listed securities with the DSE, 219 were listed companies, 10 mutual funds and 10 debentures.
- ii) **Investment Corporation of Bangladesh (ICB)** The Investment Corporation of Bangladesh was established in 1976 with the objective of encouraging and broadening the base of industrial investment. ICB underwrites issues of securities, provides substantial bridge financing programs, and maintains investment accounts, floats and manages closed-end & open-end mutual funds & closed-end unit funds to ensure supply of securities as well as generate demand for securities. ICB also operates in the DSE and CSE as dealers.
- iii) **Specialized Banks** Bangladesh Shilpa Bank (**BSB**), Bangladesh Shilpa Rin Sangstha (**BSRS**), BASIC Bank Ltd., some Foreign Banks and NCBs are engaged in long term industrial financing.

Insurance

The insurance Sector is regulated by the Insurance Act, 1938 with regulatory oversight provided by the controller of Insurance on authority under the ministry of commerce. General insurance is provided by 21 companies and life insurance is provided by 6 companies. The industry is dominated by the two large, state-owned companies--SBC for general insurance and JBC for life insurance--which together command most of the total assets of the insurance sector.

MFIs

The member-based Microfinance Institutions (MFIs) constitute a rapidly growing segment of the Rural Financial Market (RFM) in Bangladesh. Micro credit programs (MCP) in Bangladesh are implemented by various formal financial institutions (nationalized commercial banks and specialized banks), specialized government organizations and Non-Government Organizations (NGOs). The growth in the MFI sector, in terms of the number of MFI as well as total membership, was phenomenal during the 1990s and continues till today. Over the period of June 2003 to June 2006 the growth rate was over 70% in terms of horizontal expansion of micro credit borrower. The total coverage of MCP in Bangladesh is approximately 30.09 million borrowers without considering overlapping figures. Table-1 shows the coverage of major institutions in the formal and semi-formal sectors.

It is estimated that after considering the overlapping problem, which is expected to be over 40%, the effective coverage would be around 18.05 million borrowers. Out of 18.05 million borrowers covered by micro credit program, about 62% are below poverty line and so over 11.19 million poor borrowers are covered by micro credit program by 2006.

Micro credit programs of NGOs (known as NGO-Microfinance Institutions or NGO-MFIs) and Grameen Bank play dominant role in this financial market, NGO-MFIs serve more than 61 percent and Grameen Bank alone serves 24 percent of the total borrowers. Among NGO-MFIs more than 80 percent of the outstanding loan disbursed by the top 20 NGOs, three of them are very large and have coverage all over the country. Service charge on credit varies from 10% to 20% at flat method of collection, all partners of Palli Karma-Sahayak Foundation (PKSF) charge 12.5%. Average interest offered by NGO-MFIs on savings to the members is 5%. Near about 90% of the clients of this sector are female. Loan recovery rate is generally very high compare to the banking sector, which is over 90%. Average loan size of NGO-MFIs was found around Taka 4,000.

Micro credit Regulatory Authority

Microfinance is now a nation-wide activity in Bangladesh. The issue of a regulatory framework has come to the forefront because NGO-MFIs, the major provider of this service, are providing financial services to the poor outside the formal banking system. The government of Bangladesh enacted 'Microcredit Regulatory Authority Act 2006' (act number 32 of the year 2006) on July 16, 2006 with effect from August 27, 2006 with a view to ensuring transparency and accountability of micro credit activities of the Microfinance Institutions (MFIs) in the country. Micro credit Regulatory Authority (MRA) has been established under the act which is now empowered and responsible to implement the said act and to bring the micro credit sector of the country under a full-fledged regulatory framework. According to the Act, no MFI can carry out micro credit activities without obtaining license from MRA. Section 15(2) of 'Micro credit Regulatory Authority Act 2006' has made it mandatory for MFIs who had micro credit activities before the effective date (August 27, 2006) of the act to apply for license to MRA within six months (February 26, 2007) from the effective date of the act.

Accordingly 4236 NGO-MFIs have applied to MRA for license by February 26, 2007. It was decided by the Authority that among these organizations, only those organizations will be considered for license that can fulfill minimum criteria (have equal to or more than 1000 borrowers or equal to or more than taka 40 lakhs loan outstanding). Rest of the organizations already applied to the Authority will be allowed time till June 2009 to reach the above mentioned minimum criteria. If they are unable to meet those criteria within specified time they will have to close their microcredit operation after that given time. Accordingly applications from 705 institutions are being considered for license. After evaluating their application and real operations at field level they are being considered finally as eligible to get license. Up to May 20, 2008 the authority has issued 250 licenses to different NGO-MFIs and licensing procedure of other selected NGO-MFIs are under process.

MRA is also working to prepare details rules and policies to monitor and supervise licensed NGO-MFIs that will cover governance issues, financial transparency, mode of operations and other related issues to ensure transparency and accountability in operation.

These are an overview of financial system of Bangladesh. Next chapter will describe the literature review part of micro credit and poverty picture of Bangladesh.

Chapter 4

Dimensions of Poverty in Bangladesh

Introduction

There is no universally acceptable definition of poverty, although there are several connotations and definitions in vogue. Poverty implies a condition of life characterized by deprivation some sort or the other and perceived as undesirable by the persons concerned or others. It is multidimensional concept and phenomenon. Generally, there is a consensus among scholars about poverty being conceived and defined as absolute or relative. There are following types of poverty:

- **Absolute poverty** implies a person's lack of access to objectively determined, reasonably adequate quantities of goods and services, to satisfy his/her material and non-material basic needs.
- **Relative poverty**, on the other hand, means that person's access to the basic needs of life is relatively lower, as compared to some reference group of people. Between two household or two persons, one may be considered as poor, while the other in comparison may not be so, even though both may be in a position to fulfill their basic material needs.

Measurement of the Incidence of Poverty in Bangladesh

Household Expenditure Survey (HES) was carried out first in Bangladesh in FY1973-74. In subsequent years, a number of HESs were undertaken; the latest one was conducted by BBS in 2005. HESs carried out up to FY1991-92 were based on Food Energy Intake (FEI) and Direct Calorie Intake (DCI) methods in order to measure the incidence of income poverty. FEI method computes poverty lines by finding the value of per capita consumption at which a household can be expected to fulfill its calorie requirement. DCI method is used to calculate the incidence of absolute poverty where population or households fall below a threshold calorie intake (2122 kilocalories per person on a daily basis). Similarly, a person having daily calorie intake of less than 1805 kilocalories is considered to be in hard-core poverty. In Household Expenditure Survey (HES) conducted in FY1995-96, the BBS for the first time adopted the Cost of Basic Needs (CBN) method for constructing poverty lines. Similarly, in the Household Income and Expenditure Surveys (HIES) of 2000 and 2006, CBN method was used.

With this method, an absolute poverty line is defined as the value of consumption needed to satisfy minimum subsistence needs (food as well as non-food consumption). These three methods are summarised in Table 13.1.

Table 1.a: Alternative Methods for Measuring Absolute Income Poverty in Bangladesh

	Direct Calorie Intake	Food Energy Intake	Cost of Basic Needs
Indicator	Calorie Intake	Expenditure (or income)	Expenditure (or income)
Threshold	2,122 kilocalories/person day	Expenditure level at which household members are expected to reach calorie intake threshold	Expenditure level at which household members are expected to meet basic needs (food and non-food)
Measure	Head-count or other	Head-count or other	Head-count or other
Strengths and weaknesses	Indicator not representative; threshold consistent (for monitoring calorie intake)	Indicator representative; threshold not consistent (for real expenditures)	Indicator representative; threshold consistent (for real expenditures)

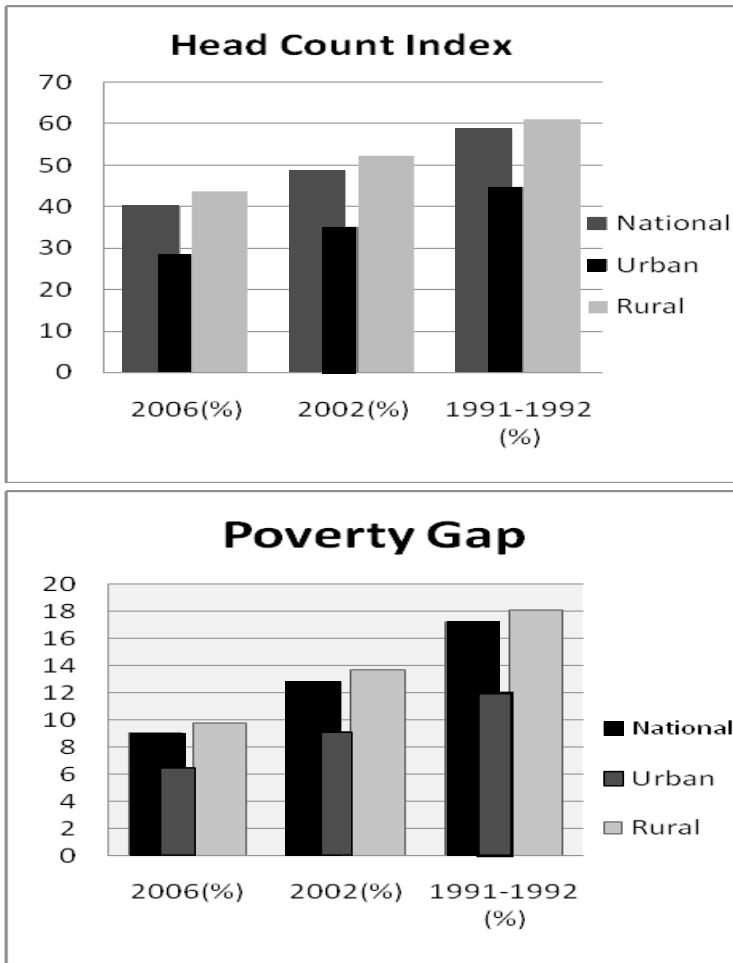
Source: World Bank 2002, A Source Book for Poverty Reduction Strategy (vol. 1)

Poverty Picture of Bangladesh

Poverty is divided into two categories, such as (1) income poverty and (2) human poverty.

Poverty Picture based on CBN Method

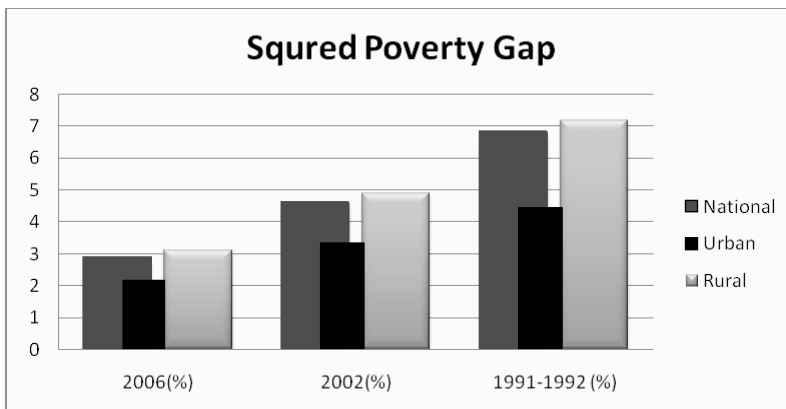
The incidence of poverty at the national level declined from 58.8 percent in 1991-92 to 40.0 percent in 2006 based on the upper poverty line (fig 4.1). During this period, the compound poverty reduction rate per year is recorded at 1.8%. But the rate of reduction in urban area (yearly compound rate 2.2 percent) is faster than that of the rural area.

Fig: 4.1 Head Count Index and poverty gap

On the other hand, during 2000 to 2006, income poverty also reduced from 48.9 percent to 40.0 percent and the compound reduction rate is 3.9 percent. This time also reduction rate is faster in the urban area (yearly 4.2percent) than that of the rural area (3.5 percent).Between 2000 and 2006, the depth (measured by poverty gap) and severity (measured by squared poverty gap) of poverty declined simultaneously both in urban and rural areas. It is notable that between 1991-92 to

2000, reduction rate of poverty was faster in the rural area than that of the urban area. Sources: BBS,

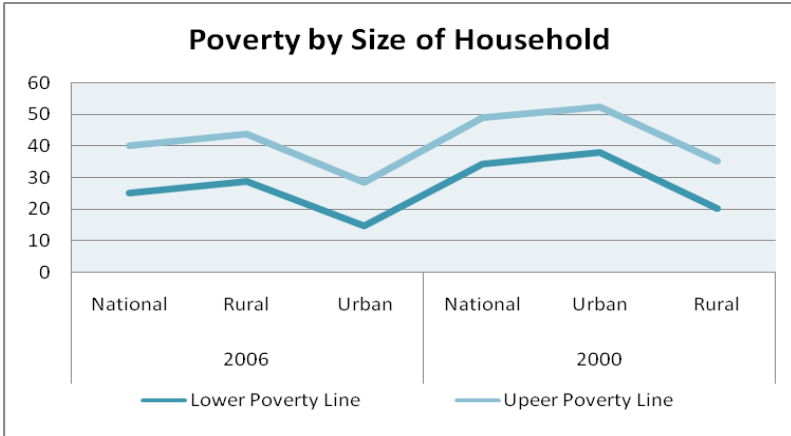
Fig: 4.2 Squared poverty gap



Incidence of Poverty (CBN) by Size of Household

The estimates of Head Count Ratio of incidence of poverty using the lower poverty line by household size (number of members) showed that households having 1-2 household members had the lowest HCR. It is estimated at 8.8 percent in 2006 against 15.0 percent in 2000. On the other hand, it appears from Table 13.4 that the HCR increases with the increase of household size up to 9-10 members. It falls down for the household size 11+. The estimates using the upper poverty line show the similar correlation of HCR with household size as shown by HCR estimates using the lower poverty line.

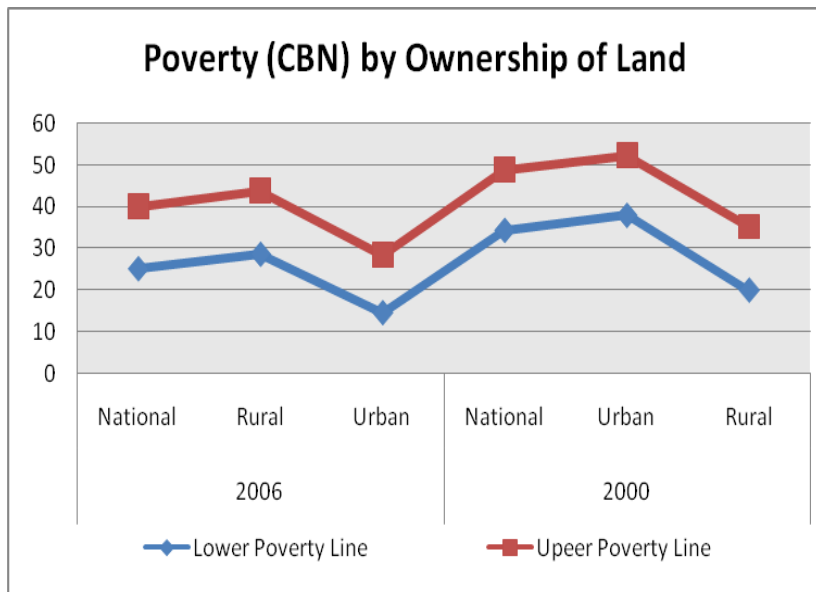
Fig: 4.3 Poverty picture by size of household



Poverty on the basis of Land Ownership

In 2006, the estimates of incidence of poverty by ownership of land using the upper poverty line, were found to be 46.3 percent for landless households, 56.4 percent for owners of less than 0.05 acre land, 44.9 percent for owners of 0.05-0.49 acre land, 22.9 percent for 1.5-2.49 acre land, 15.4 percent for 2.50-7.49 acre land and 3.1 percent for owners of 7.5 acre or more land. In 2006, the estimates of HCR by ownership of land using the lower poverty line were found to be 39.2 percent for land size less than 0.05 acre, 28.2 percent for 0.05 to 0.49 acre, 20.8 percent for 0.05-.49 acre, 11.2 percent for 1.5-2.49 acre, 7.0 percent for 2.50-7.49 acre and 1.7 percent for 7.5 acre or more land. Estimates of incidence of poverty (CBN) by ownership of land using both lower and upper poverty lines have been presented through the following figure.

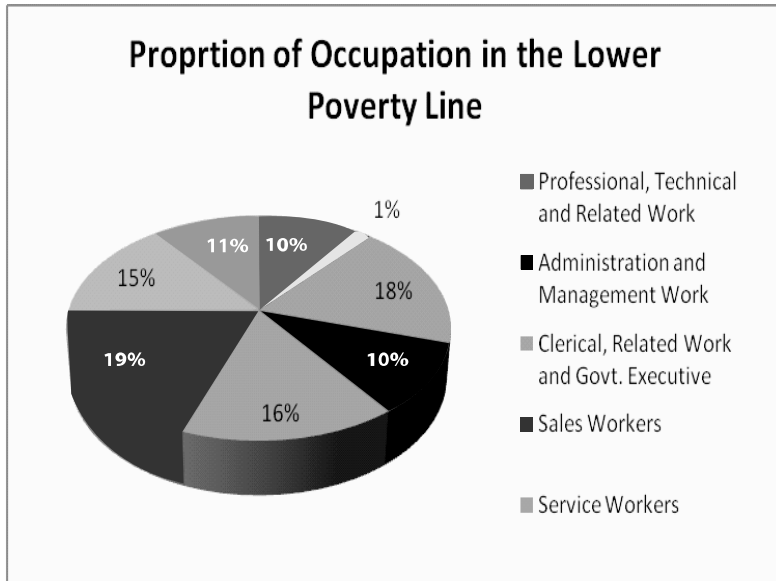
Fig: 4.4 Poverty picture by ownership of land



Incidence of Poverty (CBN) by Main Occupation of Head of Household

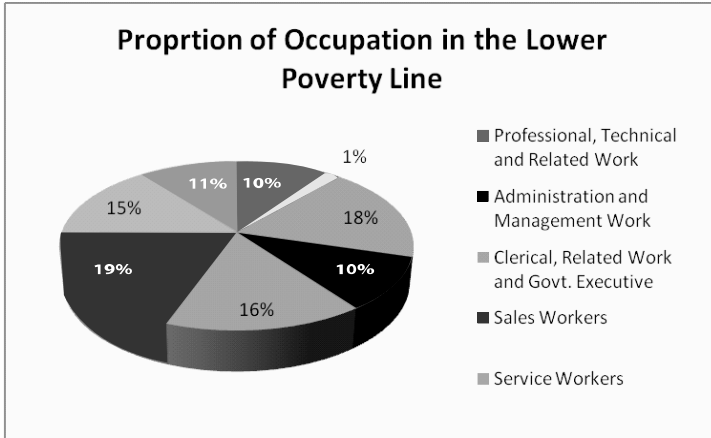
Estimates of incidence of poverty (CBN) by occupation of head of household using both lower and upper poverty lines have been presented in Table 4.5.

Fig: 4.5 Proportion of occupation in the lower poverty line



It is observed from Table 4.5 that at the national level, by using the lower poverty line, the highest incidence of poverty (31.5 percent) exists in the households where the occupation of the head relates to agriculture, forestry and fisheries. On the other hand, the lowest incidence of poverty (2.4 percent) was observed in the households with head in administrative and managerial work. Using the upper poverty line, the highest incidence (48.2 percent) of poverty was observed in the case of heads of households with their occupation relating to agriculture, forestry and the fisheries and the lowest (9.8 percent) for the households with head in administrative and managerial work. There also exists rural and urban variation in incidence of poverty by occupation. In the rural area (using the upper poverty line), the highest incidence of poverty (51.8 percent) was observed in the households with heads belonging to clerical, related work and government executive and the lowest in the households with head in professional, technical and related work (28.0 percent). On the other hand, using the same poverty line, the highest incidence of poverty was observed in the case of households with head in agriculture, forestry and fisheries (44.8 percent) and the lowest for households with head in administrative and managerial work (3.0 percent) in the urban area.

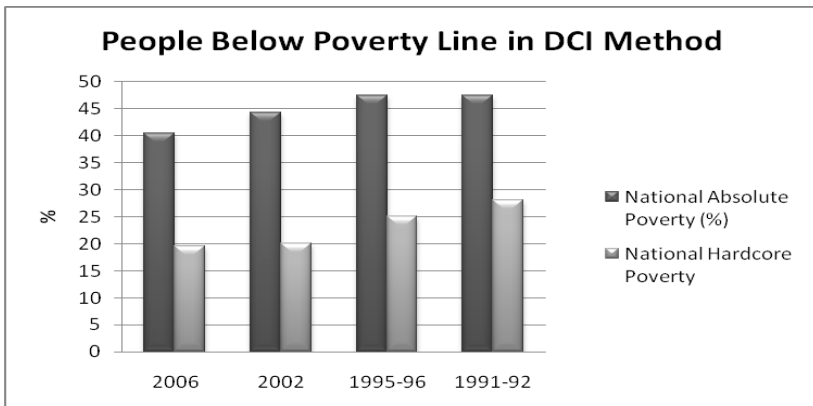
Fig: 4.6 Proportion of occupation in the upper poverty line



Poverty Picture based on Head Count Ratio and DCI Method

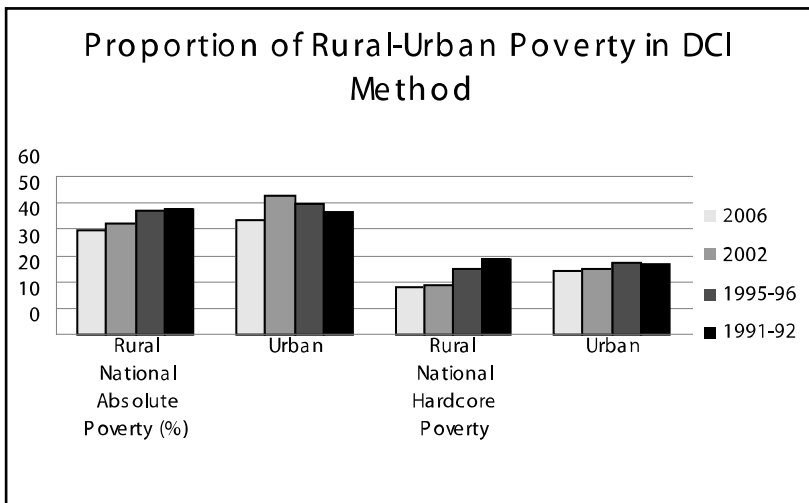
According to Head Count Ratio using DCI method, in 2006, the incidences of absolute poverty were 40.4, 39.5 and 43.2 percent in national, rural and urban areas respectively. Under this method, a reduction of absolute poverty is recorded at 4.1 percent from 2000 to 2006. People living below poverty line in 2000 were 55.8 million, which increased to 56 million in 2005. Though the number of poor people increased by 0.2 million during this period, it increased at a slower rate than that of the previous period. The trends of poverty on the basis of Head Count Ratio and DCI method is presented by the figure.

Fig: 4.7 Trends of Poverty based on Head Count Ratio and DCI Method



According to Head Count Ratio, using DCI method, the incidences of hardcore poverty were 19.5, 17.9 and 24.4 percent in national, rural and urban areas respectively in 2006. Under this method a reduction of hardcore poverty is recorded 0.5 percent at the national level, 0.8 percent in the rural area and 0.6 percent in the urban area. People living below hardcore poverty line in 2000 were 24.9 million, which increased to 27 million in 2006. Though the poor people increased during this period, it decreased as compared to 1991-92.

Fig: 4.8 Proportion rural-urban poverty in DCI method



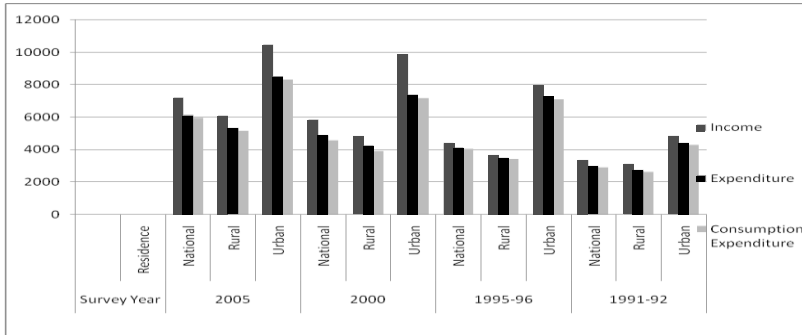
Household Income, Expenditure and Consumption

Monthly household nominal income, expenditure and consumption expenditure from the surveys 1991-92 to 2005 have been presented in figure 4.9. The difference between expenditure and consumption expenditure is that expenditure includes purchase of durable goods which is not included in consumption expenditure.

It appears from the above table that household nominal income; expenditure and consumption expenditure have increased gradually over the years. The monthly household nominal income was estimated at Tk.7203 at the national level, whereas it was estimated at Tk. 6096 in the rural area and Tk. 10463 in the urban area. Monthly household income was Tk. 5842 at the national level in 2000. It increased by 23.3 percent in 2006 over the year 2000 and by 115.59 percent over 1991-92 in nominal terms. The average monthly household expenditure was

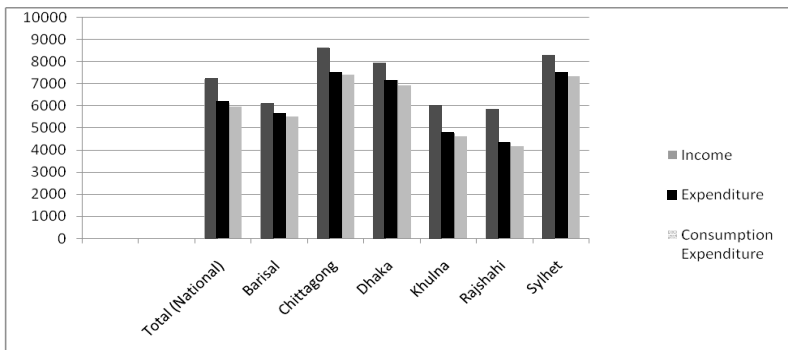
estimated at Tk. 6134 in 2006 at the national level, where as it was Tk. 5319 in the rural area and Tk. 8533 in the urban area. In 2000, it was Tk. 4886, Tk. 4257 and Tk. 7360 at the national, rural and urban levels respectively.

Fig: 4.9 Monthly Household Nominal Income, Expenditure and Consumption Expenditure by Residence



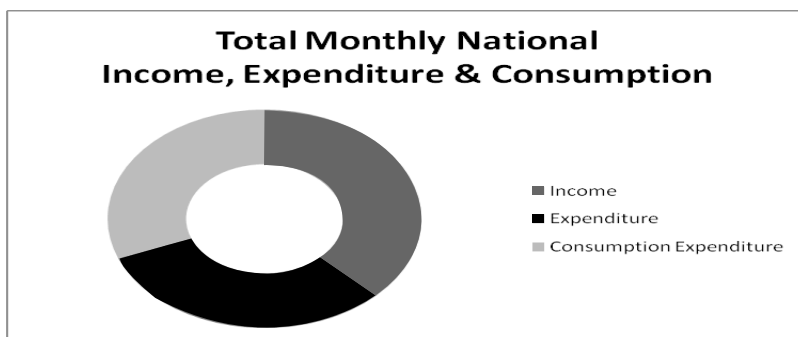
The monthly average expenditure increased by 25.54 percent in 2006 over the year 2000 and increased by 108.36 percent over the year 1991-92. The monthly 178 average household consumption expenditure was estimated at Tk. 5964 in 2006 at the national level, while it was Tk. 5165 in the rural area and Tk. 8315 in the urban area. In 2000, it was Tk. 4542, Tk. 3879 and Tk. 7149 at the national, rural and urban levels respectively. The monthly average consumption expenditure increased by 31.3 percent over the year 2000 and by 105.37 percent over 1991-92. Table 4.10 provides monthly household income, expenditure and consumption expenditure by administrative divisions.

Fig: 4.10 Monthly Household Nominal Income, Expenditure and Consumption Expenditure by Divisions



The highest average monthly household nominal income was recorded at Tk. 8654 in Chittagong Division followed by Sylhet Division at Tk. 8315 and Dhaka Division at Tk. 7949 and all of these exceed the national average of Tk. 7203. Three divisions which recorded monthly household income below the national average are Barisal Division Tk. 6094, Khulna Division Tk. 6006 and Rajshahi Division Tk. 5864. The highest average monthly nominal expenditure was recorded in Chittagong Division at Tk.7526 followed by Sylhet Division at Tk. 7503 and Dhaka Division at Tk. 7159 and all of these exceed the national average of monthly household expenditure at Tk. 6134. On the other hand, the average monthly household expenditures of Barisal Division, Khulna Division and Rajshahi Division fell well below the national average and were estimated at Tk. 5653, Tk. 4749 and Tk. 4353 respectively.

Fig: 4.11 Proportion of monthly income, expenditure and consumption



Source: BBS

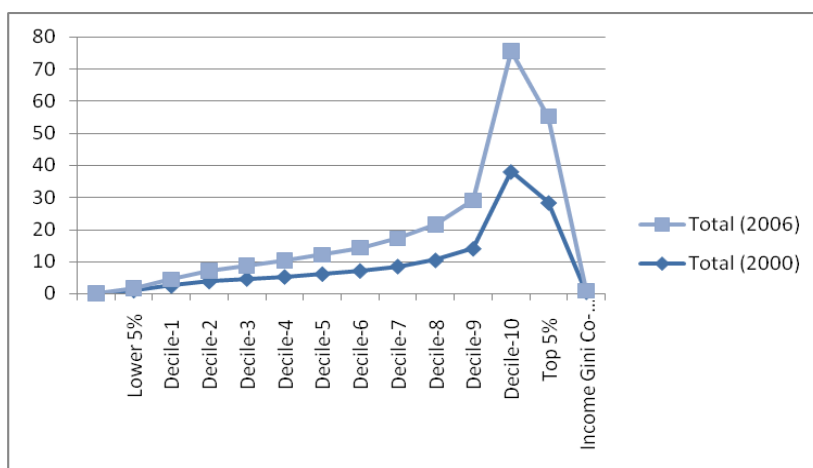
The highest monthly household nominal consumption expenditure was recorded at Tk. 7412 in Chittagong Division followed by Tk. 7329 in Sylhet Division and Tk. 6931 in Dhaka Division and all of these exceed the national average of monthly household consumption expenditure at Tk. 5964. The monthly household consumption expenditure of Rajshahi Division, Khulna Division and Barisal Division fell well below the national average and recorded at Tk. 4186, Tk. 4637 and Tk. 5511 respectively.

Decile Distribution of Income and Gini Coefficient

The percentage shares of income by decile groups and Gini coefficient with rural and urban break-down for the surveys conducted during 2000 and 2006 are presented in figure 4.12.

It is evident from figure 13.10 that income shares accruing to households belonging to Decile-1 to Decile-5 were recorded at 2.00 percent, 3.26 percent, 4.10 percent, 5.00 percent and 5.96 percent respectively at the national level. All these declined with respect to 2000 survey findings, which were 2.41 percent, 3.76 percent, 4.57 percent, 5.22 percent and 6.10 percent respectively. These five deciles jointly share only 20.32 percent of total income, although they comprise 50 percent of the population.

Figure:4.12 Percentage Distribution of Income Accruing to Households in Groups (Deciles) and Gini Co-Efficient 2006 & 2000



Source: BBS

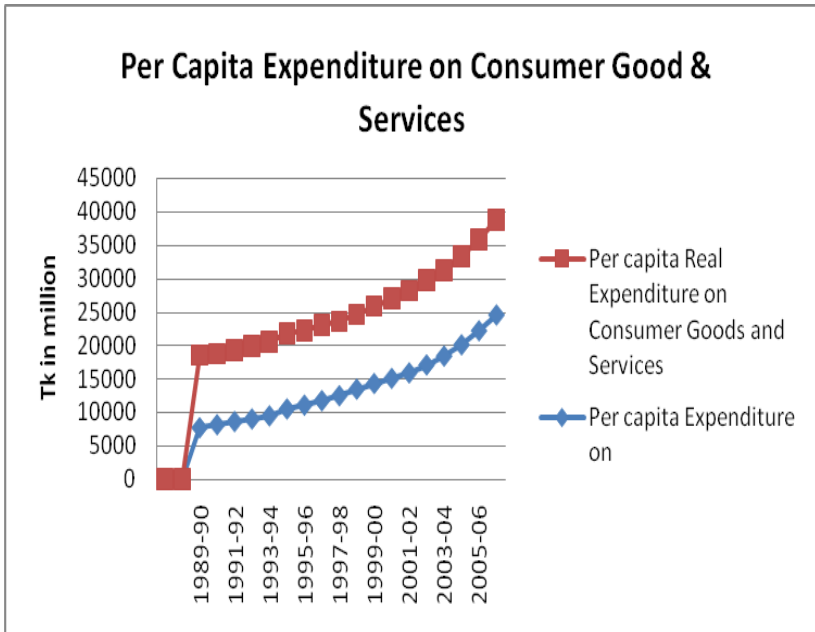
The percentage share of income of the lowest 5 percent household decreased from 0.93 percent in 2000 to 0.77 percent in 2006. On the other hand, in 2006, the income share of the households belonging to Decile-6 to Decile-9 increased but that of Decile-10 decreased compared to that of 2000. The top 5 percent households were significantly losing their share of income and recorded at 26.93 in 2006, whereas the same was 28.34 percent in 2000. It may be mentioned that in the past surveys, the Decile-10 including top 5 percent households sharply gained their share of income but in 2006, their shares declined. This may be attributed to gain by Decile-6 to Decile-9 in 2006.

Per Capita Expenditure on Consumer Goods and Services

Per capita expenditure on consumer goods and services covering the period from FY1989-90 to FY2006-07 has been presented in Fig. 4.13

13.11. Per capita expenditure on consumer goods and services at market prices increased to Tk. 24600 in FY 2006-07 from Tk. 7,740 in FY 1989-90. The compound growth is 7.04 percent during 1990-2007. On the other hand, per capita expenditure on consumer goods and services (at 1995-96 prices) increased to Tk. 14231 from Tk. 10,800 during FY1989-90 through FY 2006-07. The compound growth rate is 1.64 percent.

Figure: 4.13 Per capita expenditure on consumer goods and services

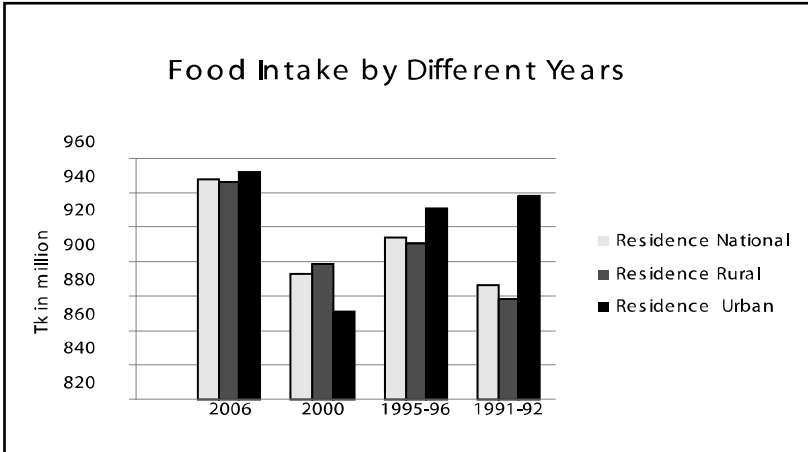


Note: * Calculated from private consumption data under GDP new series.

Source: BBS, Statistical Yearbooks (Various issues) and calculated by Finance Division.

Consumption of Food

In 2005, the average quantity of food items consumed was estimated at 947.8 grams per capita per day. It was 893.1, 913.8 and 886.2 grams in the year 2000, 1995-96 and 1991-92 respectively. In the urban area, food intake shows more fluctuating trend during the period 1991-92 to 2006. The quantity of food intake per capita per day increased by 6.12 percent in 2006 over 2000. The average quantity (grams) per capita per day intake of food is presented in Graph 4.14.

Fig: 4.14 Food intakes (grams) in different survey years

Source: BBS

The government of Bangladesh faces an enormous challenge in reducing poverty. However, the government can not act alone as it can not command all the resources, personnel, administrative outreach or expertise necessary to maintain progress in poverty alleviation. The MFIs have taken a key role in poverty alleviation efforts and they have been providing credit to these poor people who lack savings and capital but want jobs in the farm and non-farm sectors. In next chapter impact of microcredit disbursement by different institution on eradication of poverty will be analyzed.

Chapter 5

Microcredit Situation in Bangladesh

Introduction

Microcredit is the extension of very small loans (micro loans) to the unemployed, to poor entrepreneurs and to others living in poverty that is not considered *bankable*. These individuals lack collateral, steady employment and a verifiable credit history and therefore cannot meet even the most minimal qualifications to gain access to traditional credit. Micro credit is a part of microfinance, which is the provision of a wider range of financial services to the very poor.

Microcredit is financial innovations which originated in Bangladesh where it has successfully enabled extremely impoverished people to engage in self-employment projects that allow them to generate an income and, in many cases, begin to build wealth and exit poverty. Due to the success of microcredit, many in the traditional banking industry have begun to realize that these microcredit borrowers should more correctly be categorized as *pre-bankable*; thus, microcredit is increasingly gaining credibility in the mainstream finance industry and many traditional large finance organizations are contemplating microcredit projects as a source of future growth. Although almost everyone in larger development organizations discounted the likelihood of success of micro credit when it was begun. The United Nations declared 2005 the International Year of Micro credit.

Microcredit has been practiced at various times in modern history; Jonathan Swift inspired the Irish Loan Funds of the 18th and 19th centuries, in the mid-1800s abolitionist/legal theorist Lysander Spooner wrote about the benefits of numerous small loans for entrepreneurial activities to the poor as a way to alleviate poverty, and microcredit was included in portions of the Marshall Plan at the end of World War II. However, in its most recent incarnation, with attention paid by economists and politicians worldwide, it can be linked to several organizations starting in Bangladesh in the 1970s and onward.

Evolution of Microfinance Institutions in Bangladesh:

During the late 1970s, when the 'Jobra' experiment was underway under Professor M. Yunus, the Dheki Rin Prokolpa was initiated by the

Bangladesh Bank in collaboration with the Swanirvar Bangladesh, and several other pilot schemes were initiated by a handful of the NGOs which were active then. At that time, it was difficult to conceive that these initiatives would lead to a major micro-credit movement, which would make Bangladesh known to the rest of the world. Even during the 1980s, in spite of Grameen Bank's success, the main discourse amongst development practitioners in Bangladesh centered on the desirability of micro credit program as opposed to conscientization. By 1990, unhindered experimentation in the fields led to a quiet resolution of the debate and the country experienced a massive expansion of microfinance activities during the 1990s. PKSF contributed significantly to the expansion of microcredit programs in Bangladesh. This is borne out by the figures on the time path of NGO-microfinance institutions (NGO-MFIs) expansion as well as, by the expansion in membership in these MFIs.

This rapid expansion drew attention from all important quarters—policymakers, academia and development practitioners—each trying to grapple with the unfolding stream of issues and trying to shape the course of the social and economic dynamics initiated due to introduction of microcredit. With a view to meet the demand for fund for re-lending by the development partners (NGO-MFIs), and due to an urge to coordinate the flow of such funds to appropriate use, the Palli Karma-Sahayak Foundation (acronym PKSF and the full Bengali name can be translated in English as "Rural Employment Support Foundation") came into being in late 1990. Over the years, its share in the revolving loan fund of the MFIs increased— from 9 percent in 1996 to 24 percent in 2002 (Table 2 in appendix A). In recent years MFIs have moved from the margins of the financial system towards the mainstream. It is now more widely accepted that populations traditionally excluded by the formal financial sector can, in fact, be a profitable market niche for innovative banking services. The 1997 Microcredit Summit held in Washington D.C., launched a global movement to reach 100 million of the world's poorest families with credit for self-employment and other financial and business services by the year 2005. Much remains to be done, however, to integrate micro financial systems, and for orthodox financial institutions, notably commercial banks, to recognize its full potential.

There are a total of 19.3 million members, of which the big four MFIs counts 13.7 million (71 percent) members. But the total number of active members is only 14.3 million (See World Bank 2005).

For the last two decades, Bangladesh has been drawing attention of the world for its poor-focused microcredit initiatives. In Bangladesh, there are four main types of institutions involved in microcredit activities. These are

1. Specialized Banks,
2. Non-Government Organizations (NGOs),
3. Commercial Banks, and
4. Government Agencies.

Principles of Microcredit Program

Microcredit is based on a separate set of principles, which are distinguished from general financing or credit. Microcredit emphasizes building capacity of a micro entrepreneur, employment generation, trust building and help to the micro entrepreneur on initiation and during difficult times. Microcredit is a tool for socioeconomic development. The mission of microcredit has been guided by four core themes:

- Reaching the poorest
- Reaching and empowering poor
- Building financially self-sufficient institution
- Ensuring a positive measurable impact on the lives of the clients and their families.

Modus Operandi of Microcredit Program

It requires borrowers to organize into small groups that meet and make repayments weekly. A group of about 5 is made. At first only 2 members are allowed to apply for a loan depending on their performance in repayment, the next apply, hence loans are extended gradually to the rest of the group. In this way the program builds a sense of community and self-reliance. It lends loans from as small as US \$ 60 up to \$2500 to support projects like poultry raising or providing community mobile services.

The method of action primarily being to:

- Start with the problem rather than solution
- Adopt a progressive attitude
- Credit system to serve the poor
- Borrowers to be able to repay the loans
- Savings with credit
- Associate close monitoring of borrowers
- Ensure systems financial balance
- Invest in human resources

Strengths

In the past few years, savings-led microfinance has gained recognition as an effective way to bring very poor families low-cost financial services. For example, in India the National Bank for Agriculture and Rural Development (NABARD) finances more than 500 banks that on-lend funds to self-help groups (SHGs). SHGs comprise twenty or fewer members, of whom the majority is women from the poorest castes and tribes. Members save small amounts of money, as little as a few rupees a month in a group fund. Members may borrow from the group fund for a variety of purposes ranging from household emergencies to school fees. As SHGs prove capable of managing their funds well, they may borrow from a local bank to invest in small business or farm activities. Banks typically lend up to four rupees for every rupee in the group fund. Groups pay an annual interest rate of 11% to 12%. Nearly 1.4 million SHGs comprising approximately 20 million women now borrow from banks, which make the Indian SHG-Bank Linkage model the largest microfinance program in the world. Similar programs are evolving in Africa and Southeast Asia with the assistance of organizations like Opportunity International, Catholic Relief Services, CARE, APMAS and Oxfam. Micro financing also helps in the development of an economy by giving everyday people the chance to establish a sustainable means of income. Eventual increases in disposable income will lead to economic development and growth.

Microcredit Practices

Credit Products

Credit is given for both individual and group activities and there is no collateral requirement. The types of loans include general loans, program loans, housing loans, etc. *General Loans* are made for any profitable and socially acceptable income generating activity, such as: rural trading; rural transport; paddy husking; food processing; small shops and restaurants and so on. Loans are usually between \$15 to \$160. However, members may take larger loans after repaying their first loan. Group members can obtain sector *programme loans* in areas such as poultry, livestock, agriculture, sericulture, fisheries and social forestry. In these areas they are also provided with training, technical assistance and inputs. Members can also take one loan to construct or upgrade their homes. Besides, there are various forms of credit such as: flexible credit

services, supplementary credit services, micro enterprise credit services, hand/emergency credit, disaster credit, sanitary latrine credit, tube-well credit etc.

Savings

For almost every MFI, there are now savings opportunities for their borrowers. A large share (30 percent) of the sources of funds for micro-credit now comes from member savings. In BRAC, for instance, a member can save in three ways: own savings, compulsory savings and current account savings. The GB has many savings products that include personal savings, special savings, Grameen Pension Scheme, time deposits, a savings scheme in which the amount deposited doubles in seven years, and fixed deposits with monthly income. The GB's total net savings now constitute 56% of total microfinance NGO net savings deposits (with 23% of GB's net savings coming from nonmembers).

Currently, the savings products available in the microfinance NGO sector (for members only) include mandatory savings, special savings, contractual savings, time deposits, and daily savings. There has been conscious effort by Bangladeshi MFIs to mobilize additional local resources through new savings products. ASA and BURO Tangail, in particular have now moved to a regime of more flexible savings products which enable members to withdraw savings. BB now offers house-building loans to MFIs at the rate of 1 percent per annum to lend to the member of MFIs. The loan size is typically \$310 per member.

Insurance and Social Services

Microfinance NGOs in Bangladesh are gradually becoming interested in offering insurance products, particularly life insurance, to their existing credit and savings clients. Interest has been generated following the successful micro insurance experiences of a private sector provider, Delta Insurance.

There are various kinds of products offered under life insurance and social services programmes by MFIs. They are health insurance, life insurance, credit insurance, property insurance, crop insurance, etc. For instance, all BRAC members are entitled to life insurance facilities that offer \$77 to the family if a member dies. Proshika has Life and Property Risk Coverage Policy (LPRCP) for group members, Economic and Social Security Policy Scheme (ESSPS) which covers housing,

education, health and some other facilities for the group members who are the regular savers and Livestock Compensation Fund (LCF) to pay for the loss caused by the sudden death of farm animals and poultry.

Training/Counseling/ Marketing/ Institution Building:

Some MFIs offer services for business planning & management, entrepreneurship development, basic accounting & cash management, products diversification, innovation, research. Some others offer services in the area of marketing outlay, production center, promotional activities, infrastructure support, while there are some MFIs who work in the areas of group formation, awareness raising, leadership development, linking/networking, information sharing.

Innovations

Even with the huge expansion of micro-redit in Bangladesh the poor households were struggling to benefit from the standard micro credit model despite joining the programs. To cater for the constraints hindering poor households, some programs have introduced innovations. These are:

- a. Introduction of more flexible repayment schedules such as ASA's Flexible Loan Program.
- b. Lowering first loan levels so that amounts as small as \$8 can be borrowed,
- c. A Grameen program that offers zero interest loans to beggars
- d. The Resource Integration Center's program that specializes in offering loans to a specific vulnerable group – elderly poor.
- e. Various programs that combine food aid with micro credit and training e.g.; BRAC's IGVD program, and
- f. Targeting remote areas through for instance ASA's cost-effective mini branch system and integrated development foundations work in the Chittagong Hill Tracts.

Furthermore, there are several other innovated programs such as: flexible savings and credit shift towards 'enterprise loans', micro-insurance, linking MFIs with formal financial markets, private sector involvement in the microfinance distribution, individual financial products.

Over time, the Grameen model has been copied modified and attempts made to improve the approach by the major MFIs. The variations to this model, introduced by latter day entrants, have incorporated the introduction of new savings and loan products. The variations in loan products include

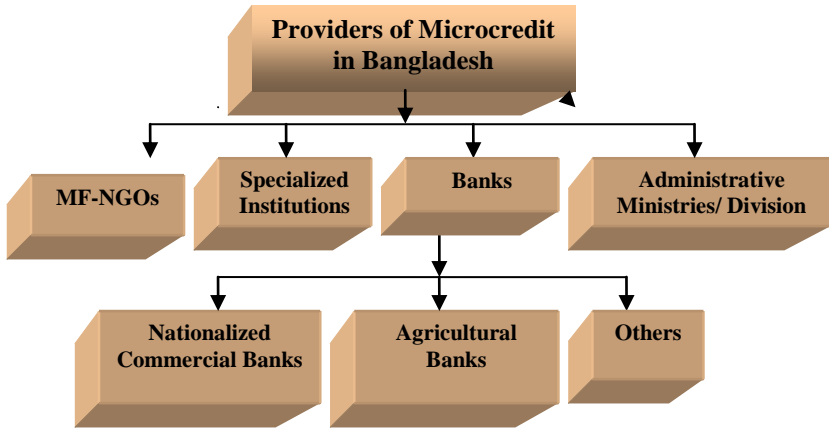
1. Collection by Proshika and Rangpur Dinajpur Rural Service (RDRS) of monthly instead of weekly installments of GB model.
2. Variations in Association for Social Advancement (ASA)'s loan conditions with the number of weekly installments reduced to 45 spread over the year, and abolition of the group guarantee as well as of the requirement to be presented in weekly meetings at the same time;
3. Introduction of seasonal loans of three month's duration by most MFIs, and
4. provisions for larger micro enterprise loans for specific activities by some organizations such as BRAC, ASA, and the urban, Dhaka-based MFI, the Shakti Foundation

Providers of Microcredit in Bangladesh

The World Bank is supporting Bangladesh's micro credit movement through a US\$105 million credit for a Poverty Alleviation Microfinance Project through the Government of Bangladesh. The project channels funds to Palli Karma Sajhayak Foundation (PKSF), a quasi-government agency, which lends to more than 160 promising NGOs of all sizes to expand their micro credit programs, covering about 1.2 million borrowers.

Large NGOs such as BRAC, Proshika and ASA, covering a total about 4.2 million borrowers, are also PKSF borrowers. The project also helps strengthen PKSF and partner organizations and ensure their institutional and financial viability through training, research, impact evaluation, and disseminating best practices for increasing cost effectiveness. Through PKSF, the World Bank is working to help shore up beleaguered micro credit institutions and meet the demand for new loans.

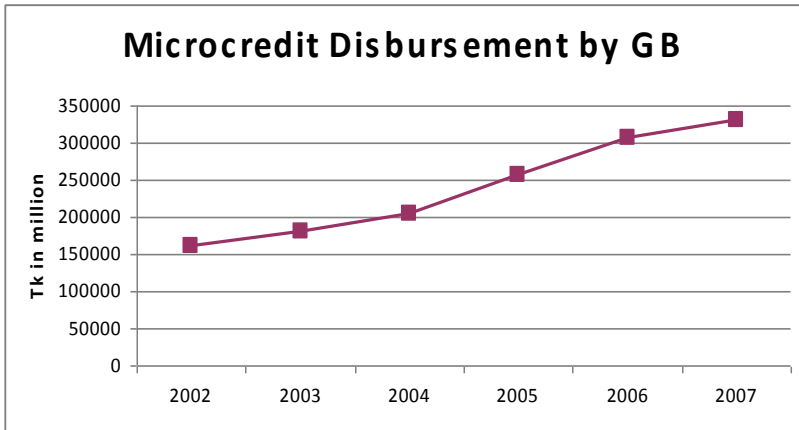
The principal microfinance service providers are usually categorized into four major groups as shown by the chart:

Fig: 5.1 Provider of Microcredit in Bangladesh

Microcredit Programs of Two Specialized Institutions

Grameen Bank (GB)

GB was established in 1983 by an ordinance; however, it started its activities in 1976 as an experimental project. Later it expanded the operation by organizing people without assets and providing them credit support for income generation and capital and asset building. It is a specialized microfinance institution giving micro loans especially to women. At present GB works in 57000 villages with its countrywide 1658 branches and reaching 5.3 million poor, 95 percent of whom are women. Up to June 2007, it expanded its activities to 72.08 lakh members living at 470 upazilas and 64 districts through 2431 branches. An amount of Tk. 33,114.91 crore was disbursed as credit by June 2007 and the amount of recovery was Tk. 29,729.62 crore. Grameen Bank provides collateral and interest-free loan through “struggling members programme” to the poorest segment of the society regarded as beggars.

Fig: 5.2 Microcredit disbursements by Grameen Bank

Palli Karma-Sahayak Foundation (PKSF): Apex Funding Organization

Palli Karma-Sahayak Foundation (PKSF), since its establishment in May 1990 by the Government, has been working as an apex microcredit and capacity building organization for eradicating poverty initially in the rural areas and subsequently in urban areas. The basic operational strategies of PKSF (Rural Employment Support Foundation) are the following:

- It does not directly lend money to the landless and the assetless people rather reaches its target groups through its Partner Organizations (POs);
- It provides greater thrust to institutional development, both its own capacity as an apex organization as well as the capacities of POs;
- It favors no particular model; instead, innovations and different approaches based on experience are encouraged;
- It acts as an advocate for appropriate policies and regulations useful for the microcredit sector.

Some of the best practice lessons evident in the PKSF experience include:

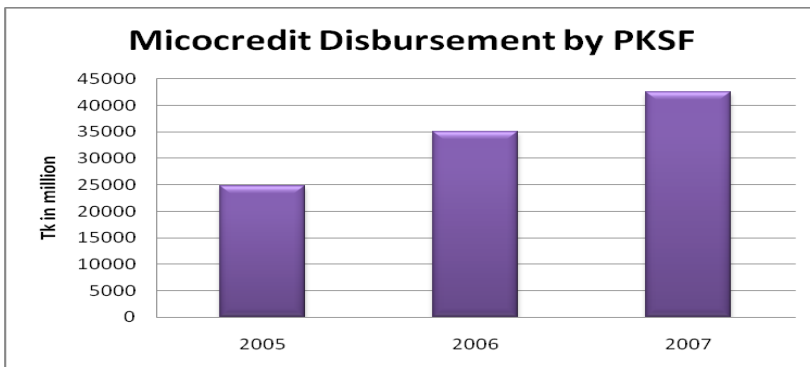
- PKSF has been established and funded by the government, but it has been kept as an independent organization outside government bureaucracy. This has enabled PKSF to form its own policies and develop its own management practices suitable for its activities.

- The outstanding quality of the Governing Body has contributed most in guiding the management and forming and revising policies whenever necessary.
- The policy of recruiting officials of above average quality has contributed greatly to the growth and performance of PKSF.
- PKSF has been successful in utilizing the capacities of local NGOs in quickly reaching the poor and developing the POs to deliver the financial services to the poor. Selection of the right POs was the most crucial factor for PKSF's success.
- PKSF has created a congenial "microcredit culture" in Bangladesh by introducing several standards, norms and guidelines for operation of microcredit programs.
- PKSF's pragmatic policies and practices have made it the world's largest and most successful autonomous apex funding agency (wholesale fund) for microcredit and PKSF model is now being replicated in different countries of the world.

Currently, five categories of micro-credit programmes are being implemented with mainstream Microcredit activities like

- a. rural micro-credit
- b. urban micro-credit
- c. micro-credit for the poorest of the poor
- d. micro-enterprise and
- e. Seasonal credit.

Apart from mainstream programme, PKSF is implementing some other programmes for the poorest of the poor, which are: Financial Services for the Poorest Project, Micro Finance and Technical Support (MFTS) Project, Training, Employment and Income Generating Programme (TEIGP) in Jamuna M ultipurpose Bridge Area” project, South-West Rehabilitation Loan Programme (SRLP), Integrated Food Assisted Development Project (IFADEP), Participatory Livestock Development Project (PLDP 11), Micro-credit project for the poorest, Micro-enterprise Loan project, Micro-finance for Marginal and Small Farmers project, Food security for Vulnerable Group Development and Ultra-Poor beneficiaries (FSVGD & UP) project, Livelihood Restoration Programme (LRP), Rehabilitation of Non-Motorized Transport Pullers and Poor Owners’ (RNPPPOP), Rural Electrification Development Project (REDP) and Promoting Financial Services for Poverty Reduction (PROSPER) project.

Fig: 5.3 Microcredit disbursements by PKSf

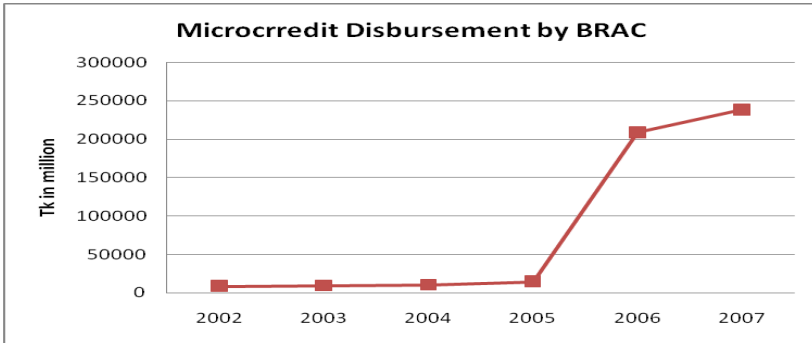
As of June 2007, PKSf disbursed a cumulative amount of loan of Tk. 4,256.84 crore to its 248 partner organizations. Serving this period, the number of borrowers at the field level was 77,23,029 where more than 91 percent were women. PKSf has been able to maintain a loan recovery rate above 98.82 percent.

Microcredit Programs of Three Big and Other NGOs

Bangladesh Rural Advancement Committee (BRAC)

Established mainly for relief and rehabilitation activities in 1972, BRAC is, at present, operating in a range of areas such as credit disbursement, non-formal education for both children and adults, primary health care, legal counseling on women rights and so on. Up to December 2002, a total amount of Tk. 88610.2 million has been disbursed as microcredit to about 3.5 million beneficiaries (female 99 percent) in 460 upazilas of 64 districts, and the recovery rate is 99.27 percent. The amount of savings of the beneficiary groups is Tk. 5294 million up to December 2002. The member savings of BRAC until December 2004 was \$118.9 million. As of December 2004, total borrowers of BRAC were about 4.5 million, which is 22 percent of total microcredit borrowers. BRAC estimates that it contributes more than 1 percent to the GDP of Bangladesh. Up to June 2005, a total amount of \$2.28 billion has been disbursed as a microcredit to its targeted client's beneficiaries (98 percent women) in 64 districts through 1373 branches, and the recovery rate is 99.63 percent. BRAC disbursed a cumulative of Tk. 23,829.92 crore and recovered Tk. 20,643.76 crore up to June 2007 and the total number of beneficiary was 55.70 lakh where female members were 53.60 lakh and male members were 2.11 lakh.

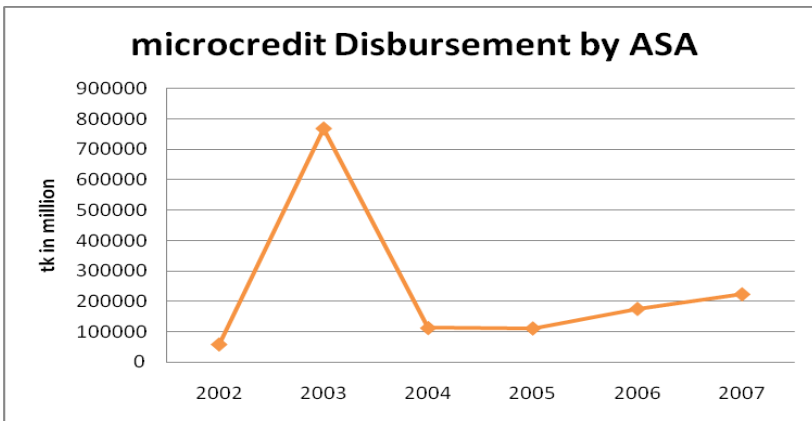
Fig: 5.4 Microcredit disbursements by BRAC



ASA (Association for Social Advancement):

ASA established in 1978, operating microcredit program since 1992. ASA provides two types of loans: small loans and small business loans. Small loans are given to women whose monthly income does not exceed \$31 and who possess less than 50 decimals of cumulative land. The initial loan size is \$62 to \$93 and may increase by \$16 to \$31 per year. Its small business loan is usually given to men but given to women subject to demonstrating competence in business. The cumulative credit disbursement and recovery are Tk. 59361.6 million and Tk. 50109.8 million respectively up to December 2002.

Fig: 5.5 Microcredit disbursements by ASA



The recovery rate is 99.96 percent. The number of beneficiaries is 2.1 million of which 95.71 percent are women. In 2002 the average loan disbursed per member was Tk. 7507.00. At the end of the year 2004, the number of members in ASA stood at nearly 3.0 million. ASA disbursed

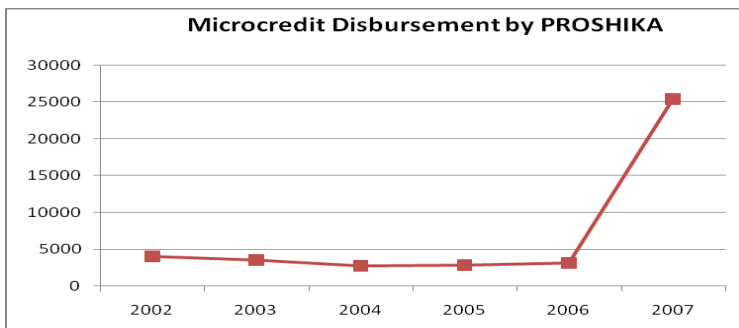
loans of \$1692.05 million by the end of 2004. ASA's own fund comprised about 30 per cent. At the end of June 2007, ASA had 70.94 lakh active members. At the same time, the number of borrowers stood at 54.9 lakh. From July 1992 to June 2007, total savings deposits stood at Tk.3,138 crore and Tk. 2,729 crore was withdrawn and returned by the members. At the end of June 2007, the savings balance was Tk. 410 crore and cumulative total loan disbursed with service charge was Tk. 22,415.7 crore out of which Tk. 17,145.22 crore was realised. The rate of recovery was 86.88 percent.

PROSHIKA

Proshika, established in 1976, matches member savings with credit and provides technical and marketing assistance where needed. Initially it fulfilled its social intermediation objectives through group formation and consciousness raising, rather than service provision, but it has moved into the provision of a wider range of social programmes.

PROSHIKA has so far helped more than 12 lakh 40 thousand poor households to overcome poverty. Currently, it is expanded in 24 thousand 139 villages and 2 thousand 108 slums in 59 districts. Now, it works with more than 28 lakh 02 thousand men and women members drawn from 21 lakh 44 thousand rural and urban poor households, and has organized them into 1 lakh 49 thousand 602 primary groups. It provides them with a broad range of programmes in education and training leading to income and employment generation, health education, building of health infrastructure, and environmental protection and regeneration, etc. So far, Tk. 25383.8 million against the total of 80.97 projects have been disbursed to the groups and created employment/self employment opportunities for more than one crore people.

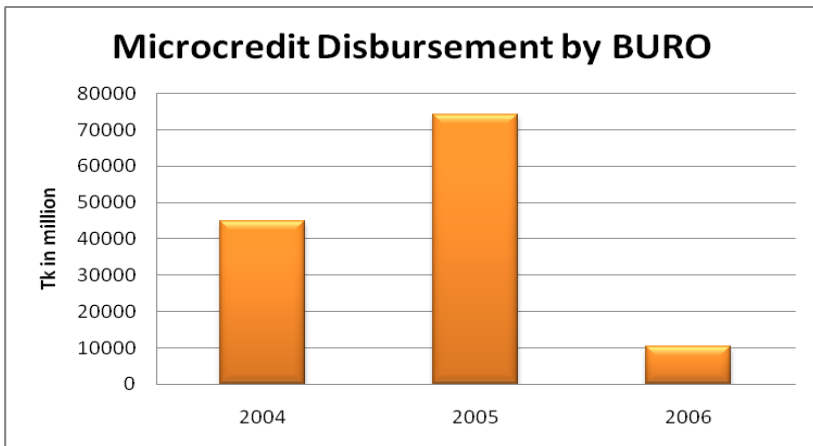
Fig. 5.6 Microcredit disbursements by PROSHIKA



BURO, Tangail

BURO (Bangladesh Unemployment Rehabilitation Organization), Tangail has been involved with innovative microfinance programs since 1991. Today it operates in eight districts in north-central Bangladesh. BURO is renowned for the number of loan products specifically designed to serve its clients. It has various products as: loan and credit products, flexible financial services, flexible savings services, general savings, contractual savings, time deposit savings, flexible credit services, general credit, supplementary credit, line of credit, hand/emergency credit, disaster credit, sanitary latrine credit, tube-well credit etc. As of December 2004, BURO, Tangail have disbursed loans of tk 44,820million to its 155,819 borrowers whereas the active members are 265,572. During the same period, it has \$11.54 million in outstanding loans and \$13.50 million in revolving loans.

Fig: 5.7 Microcredit disbursements by BURO, Tangail



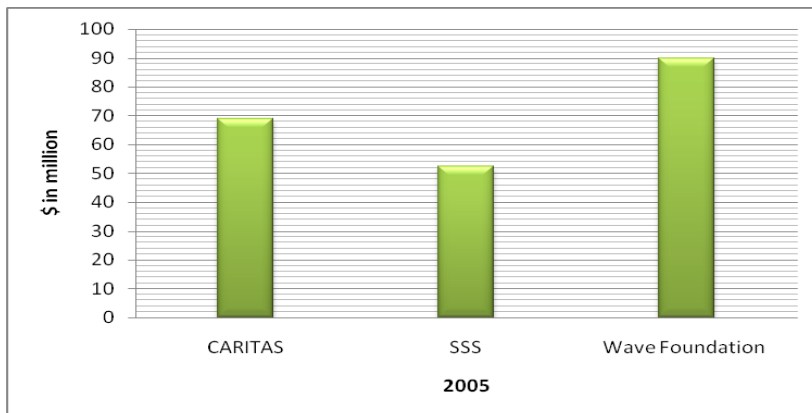
CARITAS – Bangladesh

CARITAS started its operation in Bangladesh in 1976. It now works 72 thana (sub-districts) in Bangladesh. At present, it is the sixth largest MF-NGO in Bangladesh in terms of cumulative disbursement, net savings, outstanding borrowers, active membership and revolving loan fund and seventh in terms of outstanding loan amount. As of December 2004, its cumulative microcredit disbursement, net savings, outstanding loan amount and revolving loan fund are \$68.87 million, 390.14 million, 699.31 million and 919.878 million respectively. Its total outstanding borrowers are 248,947 and active membership is 347,857 during the aforementioned period.

Society for Social Service (SSS)

SSS was established in 1986 and has since been operating for rural microcredit, urban microcredit, credit for rural enterprise development, agriculture, rural house building etc. As of December 2005, SSS is the 10th and 11th, largest MF-NGO in Bangladesh in terms of cumulative disbursement as well as outstanding borrowers, and in terms of outstanding loans as well as active membership respectively. In this period, its cumulative disbursement is \$52.39 million with outstanding borrowers of 106,998 and active memberships of 133,404. Its outstanding loan amounts to \$7.30 million and net savings of \$3.74 million.

Fig: 5.8 Microcredit disbursements by CARITUS, SSS, Wave Foundation



Wave Foundation

Wave foundation is one of the top fifty MF-NGOs in Bangladesh. As of December 2004, its cumulative disbursement is \$15 million with net savings of \$1 million. Its outstanding borrowers are 40,034 and active memberships are 51,761. Its revolving loan fund is \$3.2 million and outstanding loan amount is \$2.6 million.

SafeSave

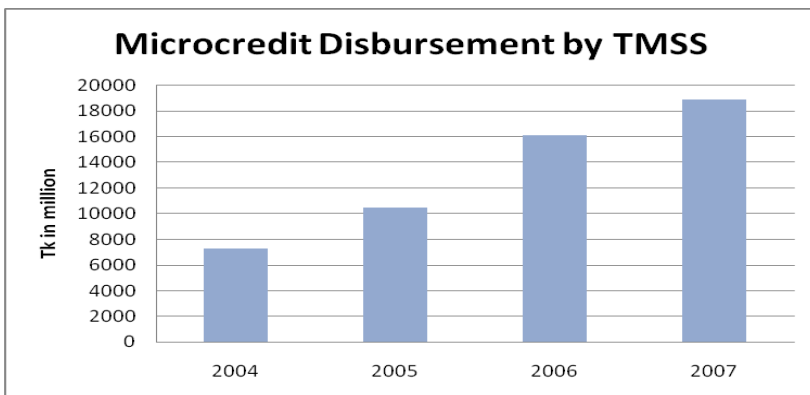
SafeSave was initiated as a research experiment in 1997 to explore sustainable methods for providing individual (i.e. not based on peer groups) financial services to poor and very poor slum dwellers in Dhaka. Female slum-dwellers were employed to make daily doorstep visits to clients. In 2002, SafeSave became a permanent, self-sustaining microfinance institution, and in 2004 reached operational

sustainability. SafeSave remains small – at the end of 2004 it was serving fewer than 10,000 clients, with 76 staff and six branches – and geographically limited to urban Dhaka. In mid-2002 SafeSave established a rural experimental project called *Shohoz Shonchoy* (EasySave) in a remote area northeast of Dhaka. By the end of 2005 Shohoz Shonchoy had over 1,000 clients, and was established as a cooperative from 2006 (SafeSave website).

Thengamara Mohila Sabuj Sangha (TMSS)

TMSS was established in 1980 as an NGO. Its microfinance program includes loans, voluntary savings, training and consulting. It is one of top fifty MF-NGOs in Bangladesh. As of December 2004, its cumulative disbursement was Tk 7301.40 million to 284,986 outstanding borrowers and with 777,412 active memberships. During the same time its outstanding loan amount was \$17.66 million and its revolving loan fund was \$239.58 million.

Fig: 5.9 Microcredit disbursements by TMSS



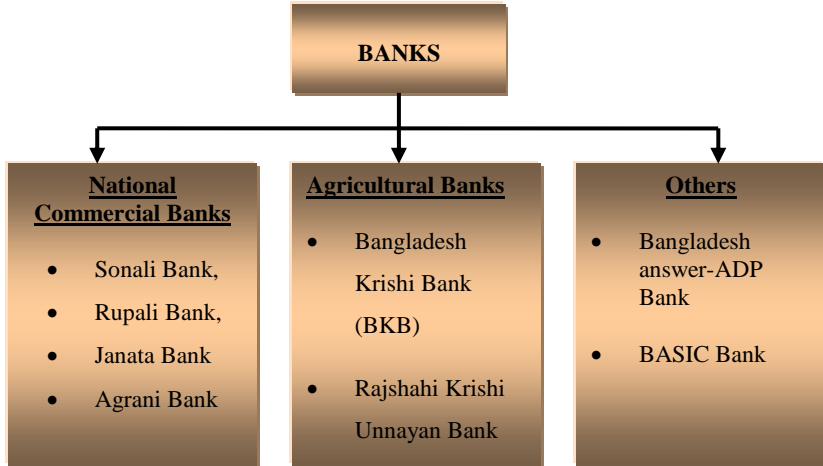
TMSS is a widely acclaimed women development organization. Up to June 2007, the amount of loan disbursed Tk. 1, 8914.3 million, the amount recovered Tk. 1,6197.3 million, 1,891.43 and the number of beneficiaries stood 6,13,201. It was awarded gold medals in 1992 and 1997 for its services to different sectors. (Fig: 4.10).

Banks

Commercial banks and specialized banks are now involved in providing microcredit in a limited scale. Commercial banks have the direct program in addition to the linkage programs with the NGO-MFIs. Under the programs of poverty alleviation, credits are provided mainly to the landless people and marginal farmers.

The banks involve in microcredit delivery in Bangladesh can be divided into three groups such as National Commercial Banks, Agricultural Banks and others which are shown by the charts in Fig: 4.11.

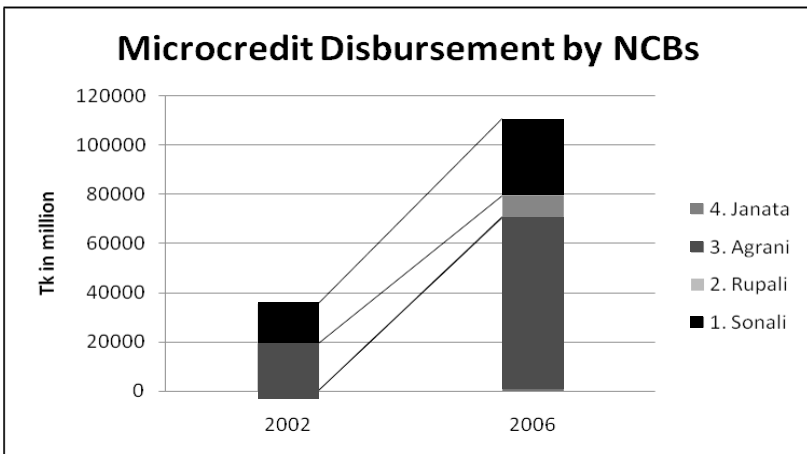
Fig: 5.10 List microcredit disbursements by different banks



Nationalized Commercial Banks:

The status of microcredit of 4 NCBs and up to December 2006, the cumulative credit disbursement Tk.110585.7million and the recovery rate was 83.18 percent.

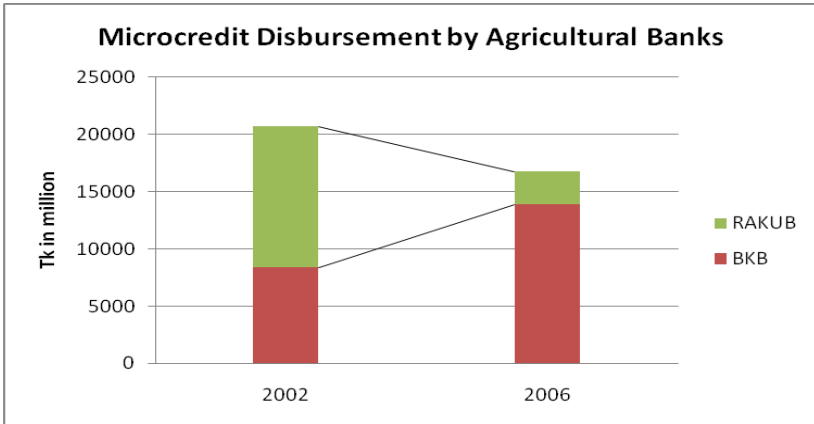
Fig: 5.11 Microcredit disbursements by nationalized banks



Agricultural Banks

The status of microcredit of the two agricultural banks up to December 2006 are the cumulative credit disbursement Tk.16713.14 million and the recovery rate was 90 percent.

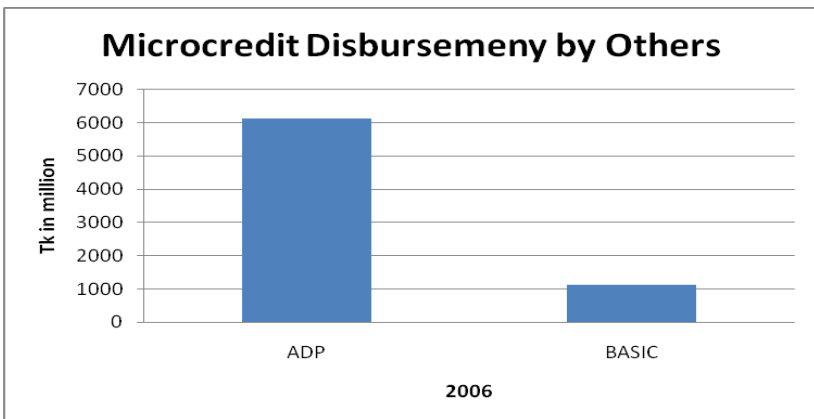
Fig: 5.12 Microcredit disbursements by Agricultural Banks



Others

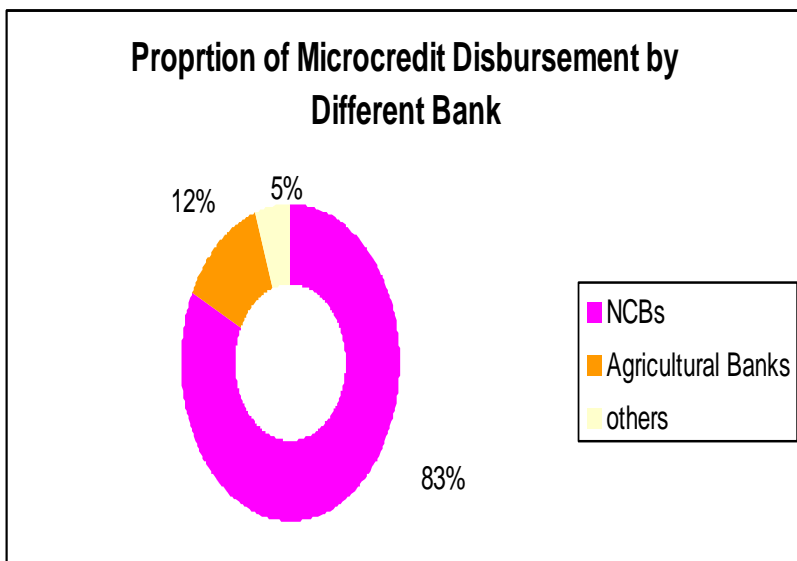
Other banks involve in microcredit delivery are Bangladesh answer-ADP Bank and BASIC Bank. The cumulative credit disbursements of the two banks up to December 2006 were the Tk. 7274.401million and the recovery rate was 33.45 percent.

Fig:5.13 Microcredit Disbursement by Others



As of December 2006, eight banks have provided credit to Tk 144,094.30 million through direct programs. Of the eight, Sonali Bank, Agrani Bank and Bangladesh Krishi (Agriculture) Bank are notable in terms of both number of beneficiaries and disbursement of loan. The cumulative disbursement of all banks is 12.77 percent of the cumulative national Microcredit disbursement by the end of December 2006. The loan recovery rate is about 84 percent.

Fig: 5.14 Proportion of microcredit disbursements by different banks



Administrative Units

At present there are thirteen ministries and fifteen divisions of the government of Bangladesh that have been carrying out microfinance activities. It is estimated that 15 percent of the clients of the microcredit program have benefited through the program of these administrative units of the government. The thirteen ministries providing Microcredit are shown by the charts:

Administrative Ministries

- Ministry of Finance
- Rural Development & Co-operation Division
- Ministry of Women & Children Affairs
- Ministry of Social Welfare
- Ministry of Labor & employment
- Cabinet Division
- ministry of Fisheries & livestock
- Ministry of industries
- Ministry of Agriculture
- Ministry of Land
- LG Division
- Ministry of Youth & Sports
- Ministry of Textile

Rural Development & Co-operation Division:

Bangladesh Rural Development Board (BRDB), the largest microcredit provider of the government, has been working in the field of rural development, especially, towards poverty alleviation through cooperatives and non-formal group network throughout the country with the financial and technical support of the Government of Bangladesh and development partners. The target groups of the program include small farmers (holding up to 0.50 acre of land), and women and men without assets. Family planning, health and education programs are also included in the credit and training activities.

The cumulative microcredit disbursement by Bangladesh Rural Development Board in June 2002 in Tk 3017.47 crore and in December 2006 was Tk 5571.42 crore. The yearly microcredit disbursement by this division from the year 2002 to 2007 is shown by the following figure. 5.15:

Fig: 5.15 Microcredit disbursements by BRDB, RDA, BARD

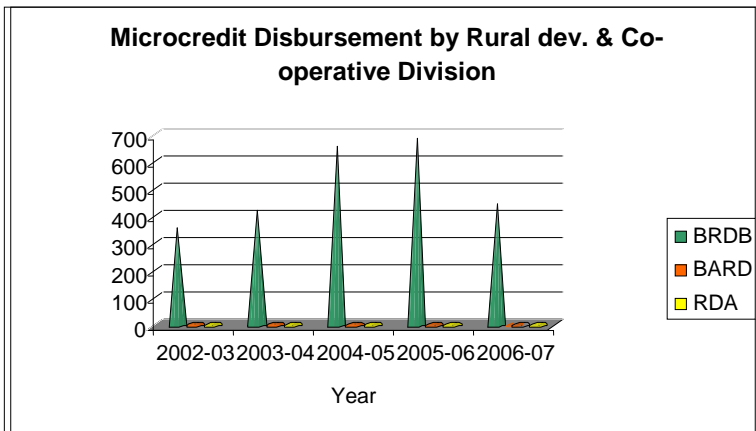
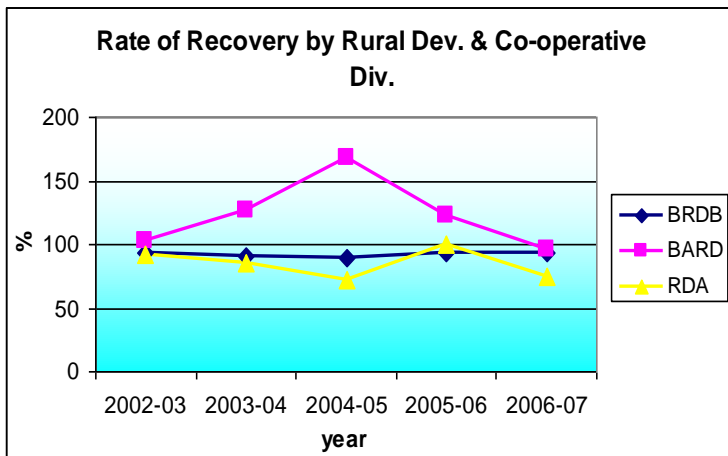


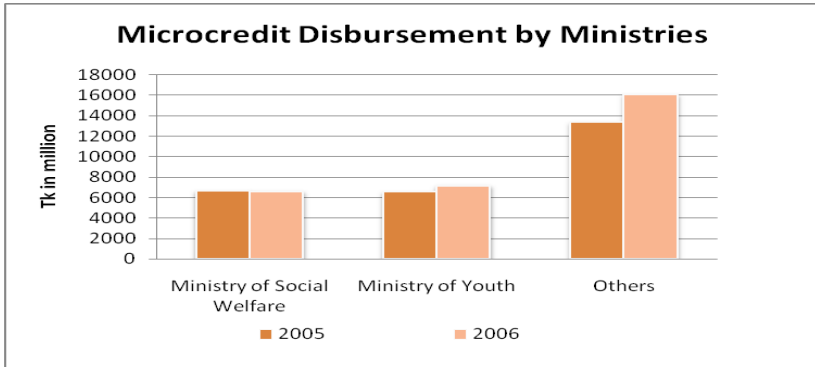
Fig: 5.16 Recovery rates of BRDB, RDA, BARD



The recovery rate of these RDB, BARD and RDA from the year 2002 to 2007 was always satisfactory as shown in the above figure 5.16.

Other Ministries

Beside rural development and cooperative division, other ministries are continuously delivering microcredit to alleviate poverty. The total disbursement of microcredit by Ministry of Social Welfare, Ministry of Youth and other ministry from the year 2005 and 2006 are shown by the following figure 5.17.

Fig: 5.17 Microcredit disbursements by Ministries

The cumulative disbursement of loan by these all ministries was Tk 86,689.90 million by December 2006. The recovery rate is about 84.16 percent. Ministry of Rural Development and Cooperative provide the highest amount of credit- the cumulative disbursement of the ministry was about Tk 56,758.50 million by December 2006.

Source of funds for Microfinance Institutions

The major sources of funds for MFIs in Bangladesh are

- Loans from national agencies(mainly PKSF),
- External Donors grants
- Internal Savings of members
- Sponsors Equity and others (including interest and service charge.)

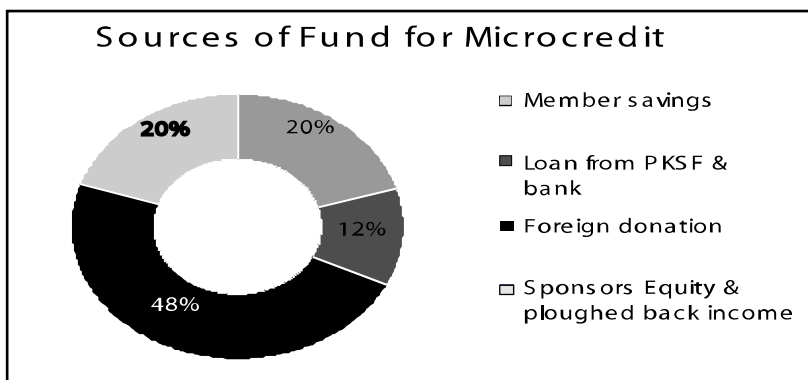
Meanwhile the emergence of the Palli Karma-Sahayak Foundation (PKSF) as second tier institution to provide fund to the NGOs has added a new dimension to the above issue. The objective of the organization is to undertake and promote various activities aimed at poverty alleviation. PKSF has, at present, been working as an apex financing organization for the NGOs (termed - Partner Organizations) running micro-credit programme in rural areas. PKSF has a mandate for undertaking wide ranging activities for poverty alleviation including capacity building of it's Partner Organizations (POs). The performance of PKSF as on 31st March 1998 in respect of NGO enrolment, loan disbursement and recovery is shown in Annex -1. The POs of PKSF serving about one million beneficiaries are classified into two categories based on their area coverage and focus/dimension of activities. The large ones are under BIPOOL (Big Partner Organizations Operating in Large areas) category and the small ones are under OOSA (Organizations Operating

in Small Areas) category. Out of the total 164 POs, 3 are under BIPOOL while the rest 161 are under OOSA. PKSf's programme is spread over about 21000 villages in 1728 Unions under 313 Thanas of 58 districts. The above coverage of PKSf is however, meagre in comparison to the large scale demand of fund for poverty alleviation.

External sources of Revolving Loan Funds (RLF) have reduced by 2.7 percentages in 2005 from 10.7 percent in 2004. This implies that MFIs are now less dependent on donor funds. Of the total RLF, member savings and service charge constitute more than half, while PKSf accounts for about 17 percent. Loans from local banks have increased in recent years from about 8.3 percent in 2004 to about 12.7 percent by the end of 2005. Among several sources of loan, the trend in the external sources of fund for MF-NGOs is declining. The external source contribution decreased from 30.4 percent in 1997 to only 10.7 in 2005.

Due to falling in the external source of fund, MF-NGOs are funding by themselves, as in the before mentioned period, their share of funding and their revolving loan has increased from 35.7 percent to 56.57 percent. They managed their funds from the savings of their members.

Fig: 5.18 Proportion of sources of fund for microcredit disbursements



The NGO activities in this part of the globe mostly started with welfare and relief oriented missionary objectives backed by external donors grant. Part of this grant and/or surplus income has been being used as revolving loan fund for undertaking income generating activities by the grassroots members. This fund still constitutes the major portion of loanable fund of the MFIs. The sponsors' equity and ploughed back earning also form significant part of the loanable fund. A recent

publication of Credit & Development Forum (CDF) a network of MFIs reveals the following status of sources of fund for 351 MFIs as on 31.12.96 (Taka in million).

Criticism

Gina Neff of the Left Business Observer has described the micro credit movement as a privatization of public safety-net programs. Enthusiasm for micro credit among government officials as an anti-poverty program can motivate cuts in public health, welfare, and education spending. Neff maintains that the success of the micro credit model has been judged disproportionately from a lender's perspective (repayment rates, financial viability) and not from that of the borrowers. For example, the Grameen Bank's high repayment rate does not reflect the number of women who are repeat borrowers, and have become dependent on loans for household expenditures rather than capital investments. Studies of micro credit programs have found that women often act merely as collection agents for their husbands and sons, such that the men spend the money themselves while women are saddled with the credit risk. As a result, borrowers are kept out of waged work and pushed into the informal economy.

Many studies in recent years have shown that risks like sickness, natural disaster and over indebtedness are a critical dimension of poverty, and that very poor people rely heavily on informal savings to manage these risks (see for example *The Microfinance Revolution: Sustainable Finance for the Poor* by Marguerite Robinson). It might be expected that microfinance institutions would provide safe, flexible savings services to this population, but- with notable exceptions like Grameen II- they have been very slow to do so. Some experts argue that most micro credit institutions are overly dependent on external capital. A study of micro credit institutions in Bolivia in 2003 for example, found that they were very slow to deliver quality micro savings services because of easy access to cheaper forms of external capital. Global data tables from *The Microbanking Bulletin* show that savings represent a small source of funds for micro credit institutions in most developing nations.

Bangladesh's Finance and Planning Minister M. Saifur Rahman charges that some microfinance institutions use excessive interest rates.

Chapter 6

Impact of Microcredit Disbursement on Poverty

Introduction

Microcredit has become a much favored intervention for poverty alleviation in the developing countries and least development countries. Although Bangladesh has huge potential for development, it is, for various socio-economic reasons, among the poorest countries in the world. The government of Bangladesh faces an enormous challenge in reducing poverty. However, the government can not act alone as it can not command all the resources, personnel, administrative outreach or expertise necessary to maintain progress in poverty alleviation. The MFIs have taken a key role in poverty alleviation efforts and they have been providing credit to these poor people who lack savings and capital but wants jobs in the farm and non-farm sectors.

To analyze the impact of disbursement of microcredit by the different organization on eradication poverty, this chapter is divided into the following three parts:

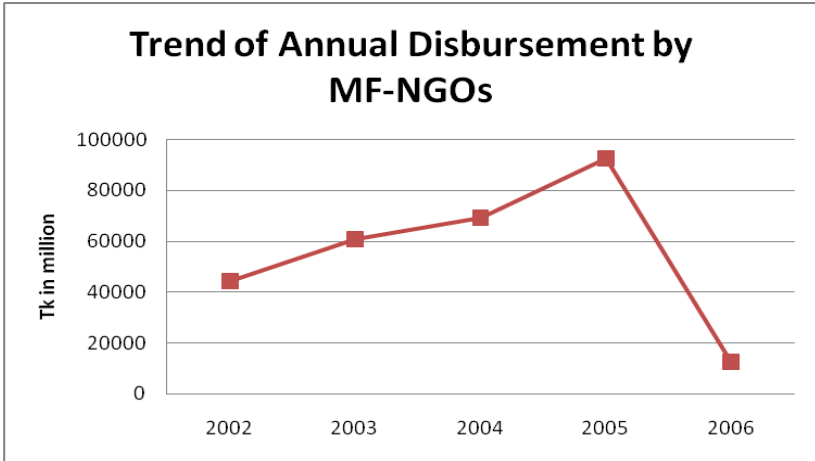
- Trend a of microcredit disbursement by different organization
- Impact of disbursement of microcredit on poverty
- Regression analysis of micro credit disbursement with per capita GDP at current price

Trend Analysis of Microcredit Disbursement

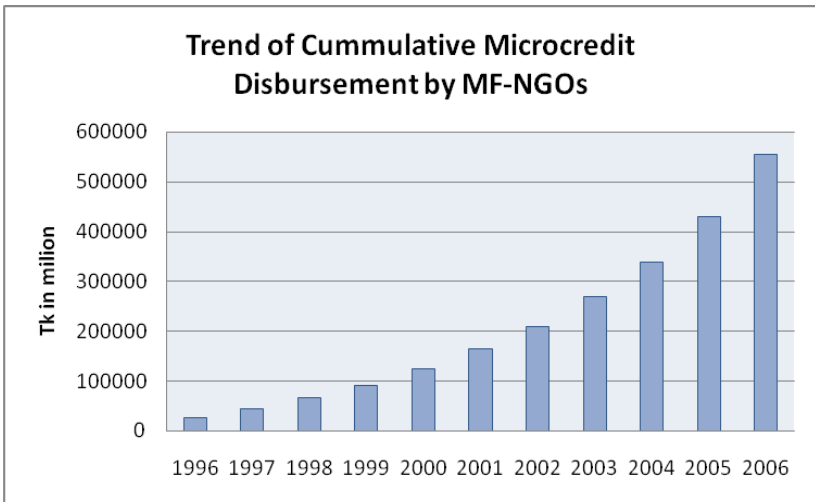
To evaluate the cumulative trend of microcredit disbursement, first of all, the credit disbursement of various organizations like MF-NGOs, specialized institutions, banks and administrative ministries should e analyzed.

MF-NGOs

The annual microcredit disbursement by MF-NGOs from the year 2002 to 2006 shown by the figure 6.1 shows that it was upward growing trend from the year 2002 to 2005. But from the year 2005 it shows a sharp downward trend. It implies that though MF-NGOs are contributing a lot in delivering microcredit in this country, their annual disbursement is not satisfactory.

Fig: 6.1 Annual microcredit disbursement by MF-NGOs

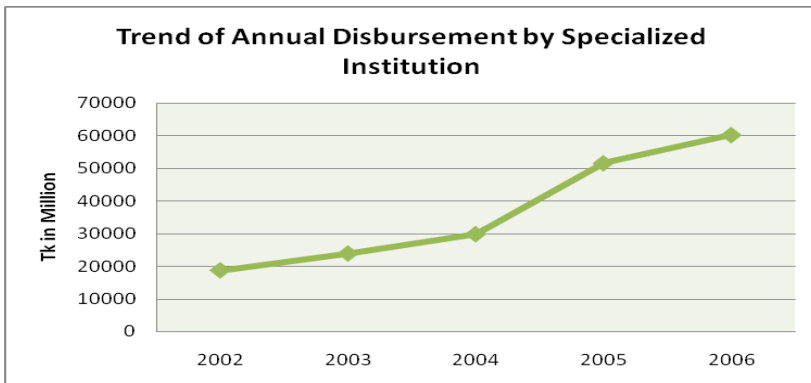
On the other hand, the cumulative microcredit disbursement from the year 1996 to 2006 Had a steady increasing trend as shown in the figure 6.2

Fig: 6.2 Cumulative microcredit disbursements by MF-NGOs

Specialized Institutions

The annual microcredit disbursement by specialized institutions from the year 2002 to 2006 shows in the fig 6.3 that it was upward growing trend and highest growth rate at 2005.

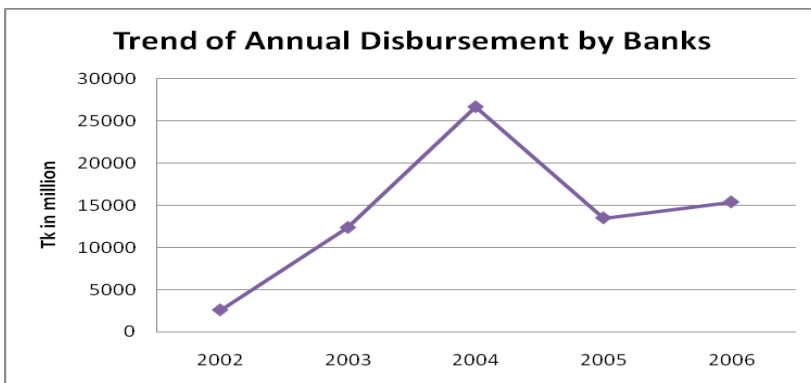
Fig: 6.3 Annual microcredit disbursement by specialized institutions



Banks

The annual microcredit disbursement from the year 2002 to 2006 by banks shown in the figure 6.4 indicates that it was upward growing trend from the year 2002 to 2004. But from the year 2005 it shows a sharp downward trend. It implies that their annual disbursement is not satisfactory by the year 2005, but increased by the year 2006.

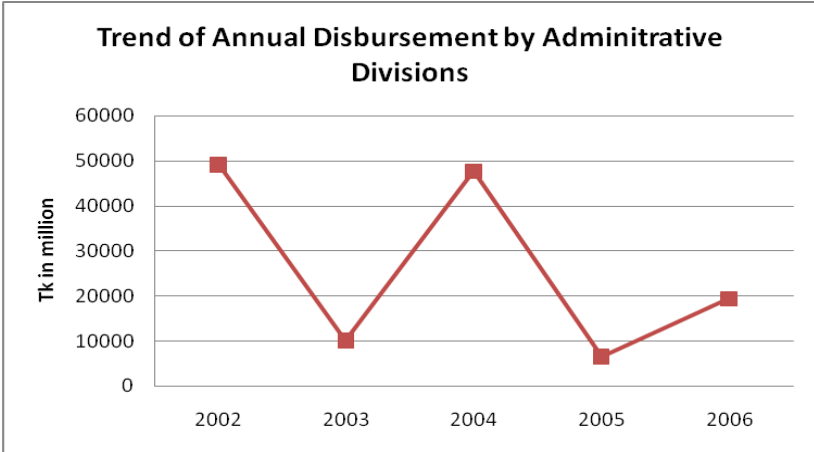
Fig: 6.4 Annual microcredit disbursement by banks



Administrative Ministries

The thirteen administrative ministries and fifteen divisions disbursed microcredit but their delivery was not steady. Its contribution to microcredit disbursement from the year 2002 to 2006 was fluctuated continuously. But from the year 2005 to 2006 it was upward trend as shown by the fig 6.5.

Fig: 6.5 Annual microcredit disbursement by administrative ministries



Finally, all organizations participated in delivering microcredit in the country in 2006 shown by the fig 6.6 indicates that specialized institution were contributed most among others and it delivered almost 56% of total microcredit to eradicate poverty.

Fig: 6.6 Proportion of microcredit disbursement in 2006

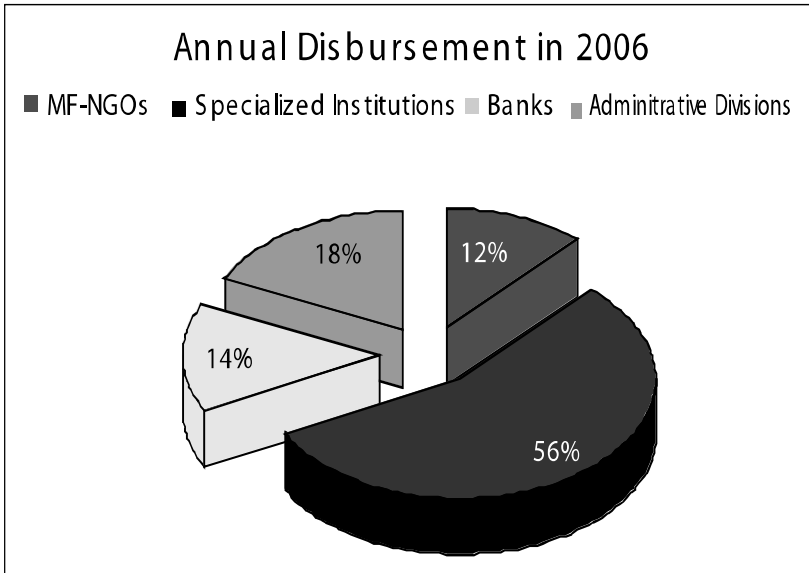
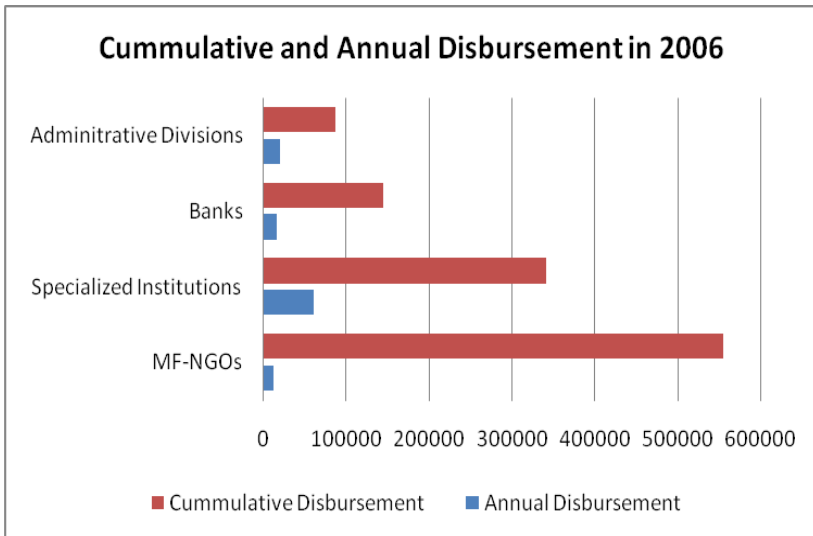


Fig: 6.7 Cummulative & Annual microcredit disbursement in 2006

Though specialized institutions were contributing most by the year 2006, MF-NGOs were disbursing highest amount cumulatively and it was Tk 555676.68 million as shown by the Fig 6.7. As they are contributing more in cumulatively, for comparison and analysis in many cases, this amount is used where exact data could not be found.

Impact of Microcredit Disbursement on Poverty

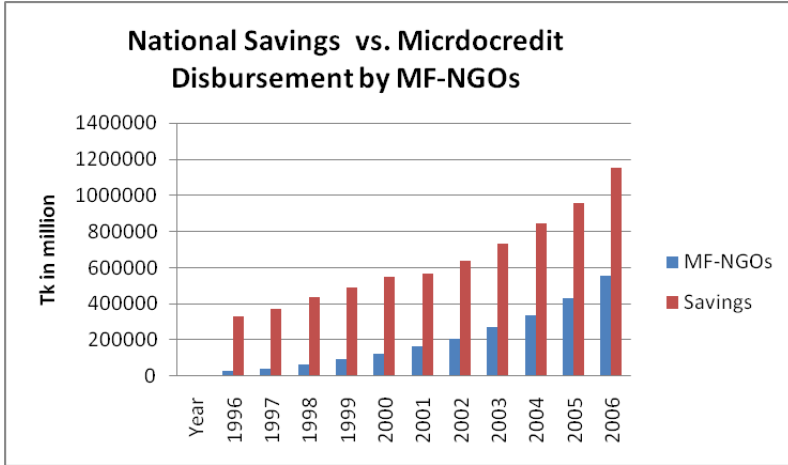
Poverty can be considered to eradicate or alleviate through microcredit disbursement if and only if it can positively impact on some of the activities of the poor people. Here the impact of microcredit disbursement on the following activities would be analyzed:

Savings, Revenue & Expenditure, Food & Non-food CPI, Income, Investment, Land ownership, Employment, Women Empowerment, DCI, CBN, Poverty etc

Savings and Microcredit Disbursement:

In 2006 MF-NGOs had disbursed cumulatively highest amount of credit. So the saving performance of these MF-NGOs compared with the microcredit disbursement shown in the following figure. Here it is found that there exists positive correlation between microcredit disbursement and national savings. (Fig 6.8) So by providing microcredit poverty eradication is possible, if people use these savings for productive purpose or generating revenue.

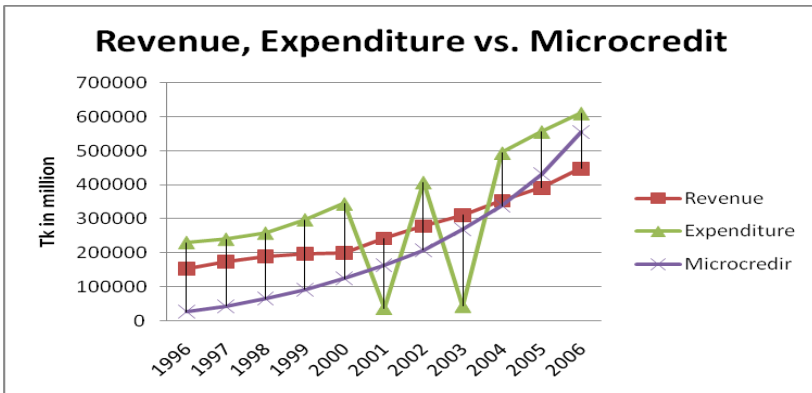
Fig: 6.8 National savings & Cumulative microcredit disbursement by MF-NGOs



Revenue, Expenditure and Microcredit Disbursement

Using the data from 1996 to 2006 it is found that there is a positive relationship between the microcredit delivery by MF-NGOs and revenue, but there is no significant relationship between microcredit disbursement and expenditure as shown by the figure 6.9. It indicates that microcredit disbursement had at least some impact on eradicate poverty by increasing revenue.

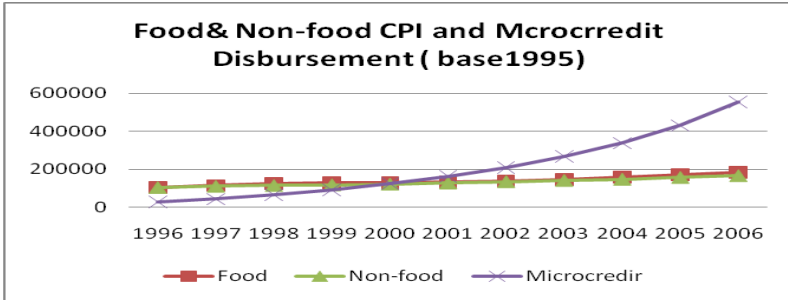
Fig: 6.9 National revenue and expenditure & Cumulative microcredit disbursement by MF-NGOs



Food and Non-food Consumer Price Index

The food and non-food consumer price index increases a little bit year by year from 1996 to 2006 but from the following figure it is found that there is no positive correlation between consumer price index and microcredit delivery by the MF-NGOs. When microcredit delivery was lower by the year 1996 , CPI was not so much varied than the year 2006 when disbursement of microcredit was almost Tk 555676.68 million.(Fig 6.10)

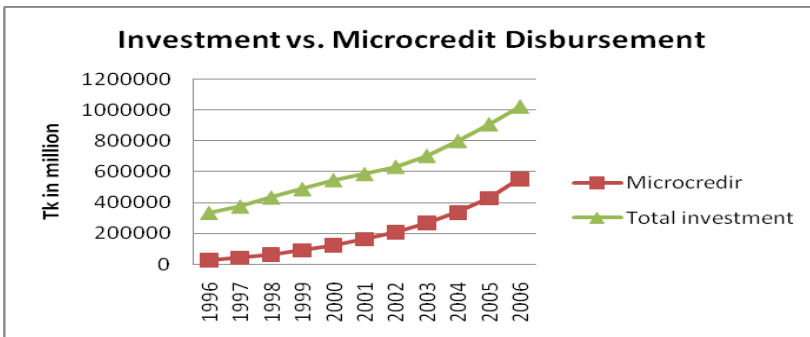
Fig: 6.10 Relation of CPI with microcredit disbursement by MF-NGOs



Investment and Microcredit Disbursement by MF-NGOs

Microcredit disbursement by MF-NGOs and trend of investment from the year 1996 to 2006 shows that there is a strong positive relationship as shown by the following fig 6.11. It indicates that by delivering microcredit effectively, it is possible to increase investment in productive sector, to earn revenue and thus contribute on per capita GDP to eradicate poverty.

6.11 Relation of National Investment with microcredit disbursement by MF-NGOs



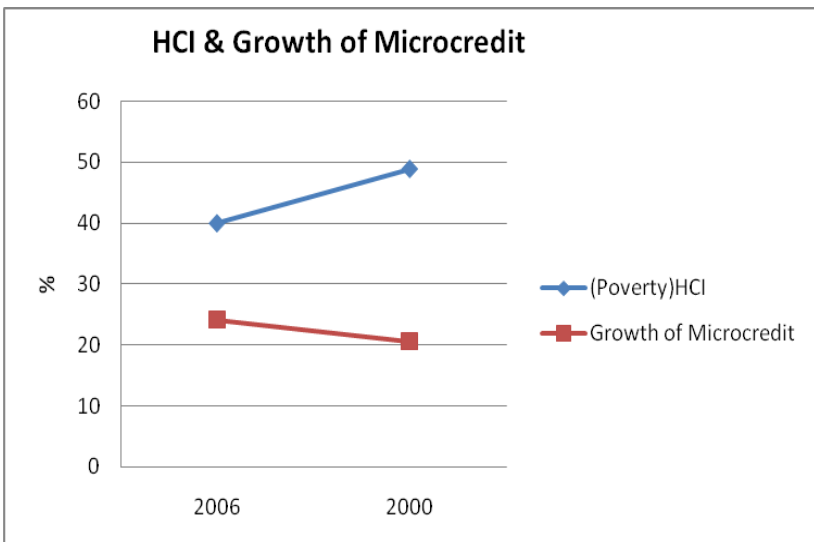
Poverty Picture based on CBN Method:

Cost of Basic Needs (CBN) method for constructing poverty lines uses head count index, size of household (no of person), land ownership etc. As CBN is represented by percent, so growth of disbursement of microcredit is used to compare the performance of the year 2000 with 2006.

Head Count Index (HCI) and Growth of Microcredit Disbursement

National poverty based on HCI had a decreasing trend from the year 2000 to 2006 with the increasing trend of growth of cumulative microcredit disbursement as shown in the Fig 6.12. It indicates that poverty can be minimized by efficient delivery of microcredit to the poor people.

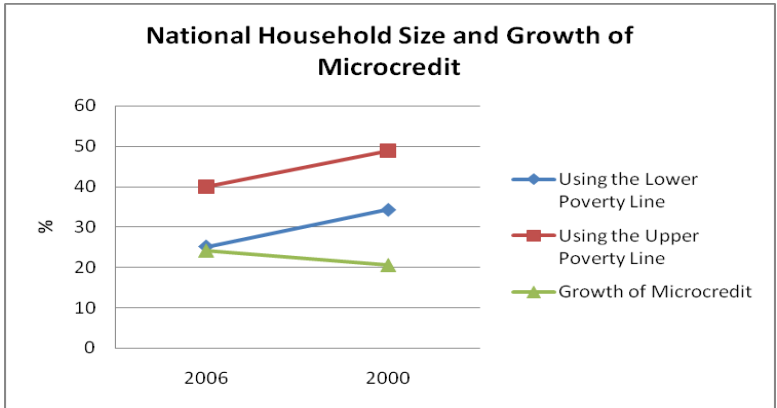
Fig: 6.12 Relation of HCI with growth of microcredit disbursement



Size of Household and Growth of Microcredit Disbursement

National poverty based on household size (no of person) had a decreasing trend from the year 2000 to 2006 in both case of using upper poverty line and lower poverty line. Here cumulative growth of microcredit disbursement was increasing as shown in the Fig 6.13. It indicates that poverty can be minimized by efficient delivery of microcredit to the poor people.

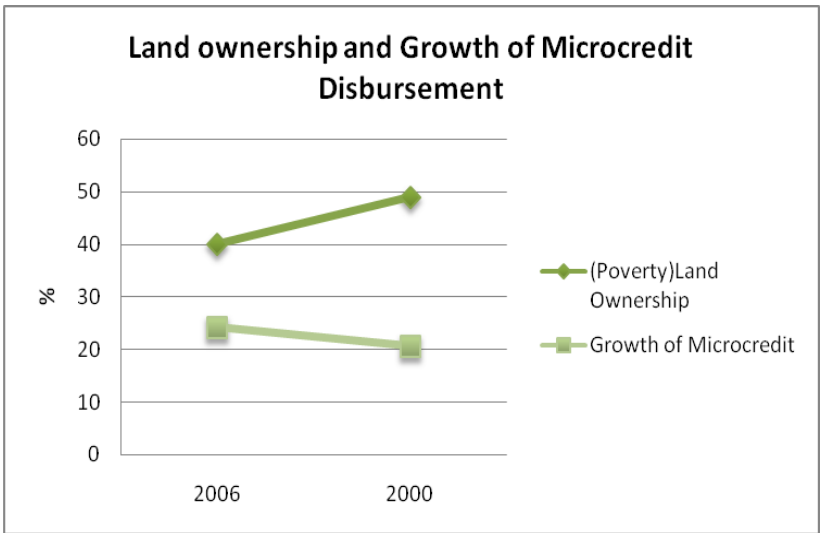
Fig: 6.13 Relation of size of household with growth of microcredit disbursement



Land Ownership and Growth of Microcredit Disbursement

National poverty based on land ownership a decreasing trend from the year 2000 to 2006 and Here cumulative growth of microcredit disbursement was increasing as shown in the Fig 6.14. It indicates that poverty can be minimized by efficient delivery of microcredit to the poor people by ensuring land ownership to increase production.

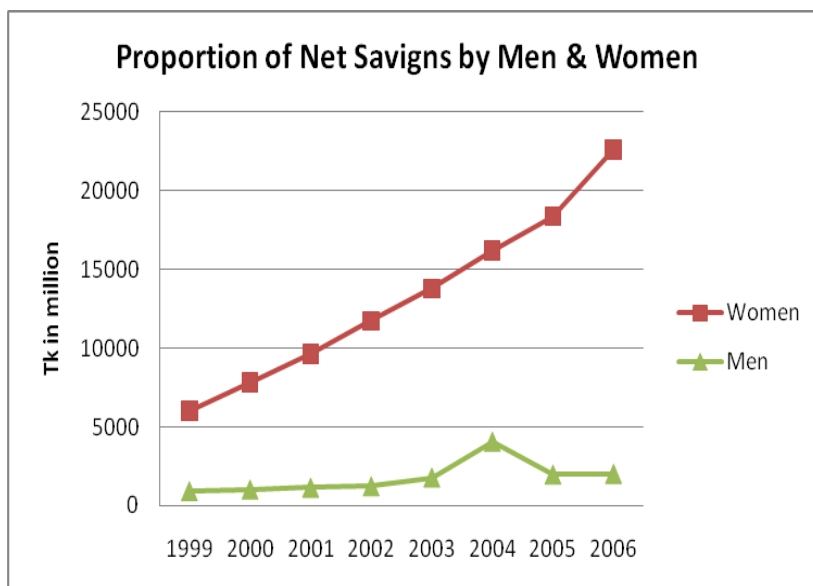
Fig: 6.14 Relation of Land ownership with growth of microcredit disbursement



Women Empowerment

Women empowerment is another indicator that can ensure poverty alleviation. MF-NGOs plays a vital role to empowering women and evidence from the year 1999 to 2006 shows that women were contributing much higher than men in case of generating savings. Fig 6.15 shows that savings of women were increasing year by year where savings of men were fluctuating. It indicates that sufficient disbursement of micro credit can influence women to generate income and thus contribute in per capita GDP.

Fig: 6.15 Prportion of net savigns in MF-NGOs



Employment

Sufficient disbursement of micro credit can influence people to generate income and thus contribute in per capita GDP Fig 6.16 shows that microcredit is mostly delivered to the rural people. On the other hand, fig 6.17 shows that most of the credit is disbursed in the trade and communication sectors. Actually it distributed 42.65 percent to the small businessmen and the 26.28 percent to the agricultural sector. So by providing credit to the rural poor for small business, it increases opportunity of employment and productions, and thus contributes in per capita GDP.

Fig: 6.16 Proportion of microcredit disbursement by MF-NGOs in rural & urban area

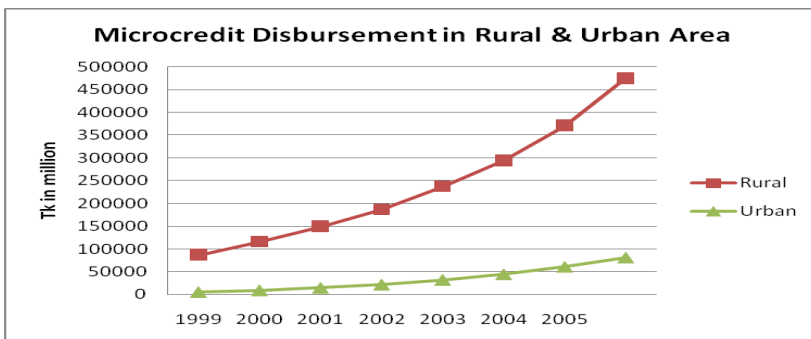
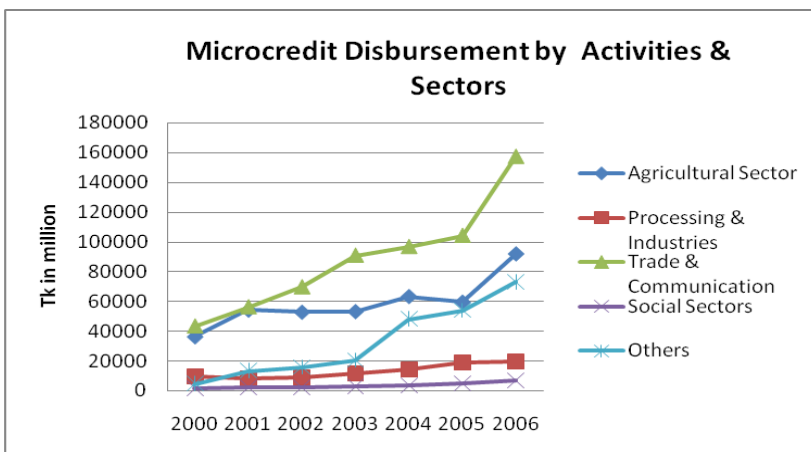


Fig: 6.17 Sectors & activitywise microcredit disbursement by MF-NGOs



From the above analysis of the impact of disbursement of microcredit to eradicate poverty it is found that in case of national savings, investment, revenue generation, women empowerment, rural development, employment etc has apposite relation with microcredit which are indirectly eradicate poverty. In case of poverty based on CBN method Head Count Index, size of household and landownership are positively related with the microcredit delivery. But microcredit delivery doesn't have any impact on expenditure and consumer price index of both food and non-food.

Regression Analysis of micro credit disbursement with per capita GDP at current Price:

Conventionally it may be said that the per capita GDP at current price depends on the efficient disbursement of Microcredit as it increases the saving behavior, productivity, empowerment, income etc. But as opposed to conventional thinking, it can be justified that per capita GDP at current price depends on a number of both internal and external factors.

Multiple regression analysis was done to analyze the relationship between per capita GDP at current price as dependent variable and variable microcredit disbursement by MF-NGOs, banks and specialized institutions and administrative ministries (sismin) as independent variables. In the report, it was assumed that the relationship among the variables was linear as:

$$Y = a + b_1X_1 + b_2X_2 + b_3X_3$$

(The calculation of regression equation is shown by the related tables in appendix)- B

Where,

Y was the value of dependent variable, per capita GDP at current price

a was the value of constant

X_1 was the value of independent variable microcredit disbursement by MF- NGOs

X_2 was the value of independent variable microcredit disbursement by banks

X_3 was the value of independent variable microcredit disbursement by specialized institutions and administrative ministries (sismin).

b_1, b_2, b_3 were the regression coefficients

The estimated regression model for the variables was:

$$Y = 146769.81 + .299X_1 + .5078 X_2 - .203 X_3$$

Linear equation shows:

- $b_1 = .299$ which indicates if per capita GDP at current price increases by BDT 1 million, then microcredit disbursement by MF- NGOs increase for BDT .299 million provided the other independent variables remain unchanged.

- $b_2 = .5078$ which indicates if per capita GDP at current price increases by BDT 1 million, then microcredit disbursement by banks increases for BDT .5078 million provided the other independent variables remain unchanged.
- $b_3 = -.203$ which indicates, per capita GDP at current price increases by BDT 1 million, then microcredit disbursement by Specialized institutions and administrative ministries (sismin) decrease for BDT .203 million provided the other independent variables remain unchanged.
- $R = 1.00$ indicates that there exist a very high degree of positive relationship among variables.
- $R^2 = 1.00$ indicates that 100% of the variations in the per capita GDP can be explained by the combined variations of microcredit disbursement by MF- NGOs, banks, Specialized institutions and administrative ministries (sismin).

From the ANOVA table, it can be concluded that the results were statistically significant at the 5% level, as the significance level indicated in the ANOVA table was 0.002 or 0.2%, which was less than 0.05 or 5% level.

As indicated by the t-statistics (from the Coefficients table) it can be concluded:

- b_1 (microcredit disbursement by MF-NGOs) was statistically not significant because it was significant at 0.065 or 6.5% level which was greater than 0.05 or 5% level.
- b_2 (microcredit disbursement by banks) was not statistically significant because it was significant at 0.053 or 5.3 % level which was greater than 0.05 or 5% level.
- b_3 (microcredit disbursement by specialized institutions and administrative ministries or sismin) was not statistically significant because it was significant at 0.132 or 13.2% level which was greater than 0.05 or 5% level.

T-test shows that total cumulative disbursement from the year 2002 to 2006 was not well enough to alleviate poverty.

The betas of the independent variables represent the degree of the influence of the independent variables on the dependent variables. From the coefficient table, the following facts were pointed out,

β MF-NGOs = 1.125

β banks = .317

β sismins = -.441

As beta for MF-NGOs was highest than the betas of banks, specialized institutions and administrative ministries (sismin) exert more influence on per capita GDP at Current price.

Multicollinearity exists when correlation coefficient between the independent variables may be higher than the coefficient between dependent and any other independent variables or when correlation coefficient between the independent variable is greater than 0.8. According to the Pearson correlation,

r MF-NGOs, banks = 0.991

r banks, sismins = 0.986

r MF-NGOs, sismins = 0.999

Here, it can be firmly concluded that the problem of multicollinearity exists because correlation coefficient between the independent variables are greater than 0.8 or 80% and lower than the coefficient with dependent variable.

Chapter 7

Concluding Remarks

Findings

In recent years, the disbursement of microcredit by different institutions is increasing to meet the development goal of government and thus alleviate poverty. Though of this upward trend, there are some findings about its impact on eradication of poverty:

Though MF-NGOs are contributing a lot in delivering microcredit in this country, their annual disbursement is not satisfactory. The annual microcredit disbursement by MF-NGOs from the year 2005 to 2006 shows a sharp downward trend. MF-NGOs were disbursing highest amount cumulatively and it was Tk 555676.68million. On the other hand, annual microcredit disbursement by specialized institution in 2006 was highest among others and it delivered almost 56% of total microcredit to eradicate poverty. The contribution to microcredit disbursement of Administrative division was lowest from the year 2002 to 2006 and annual disbursement was fluctuated continuously. The cumulative microcredit disbursement by bank hold third position their annual disbursement is not satisfactory by the year 2005, but increased by the year 2006. From the above analysis of the impact of disbursement of microcredit to eradicate poverty it is found that in case of national savings, investment, revenue generation, women empowerment, rural development, employment etc has apposite relation with microcredit which are indirectly eradicate poverty.

In case of poverty based on CBN method Head Count Index, size of household and landownership are positively related with the microcredit delivery. MFIs' preference for larger loan sizes that lead to the exclusion of the poorest which is not desirable. Microcredit delivery doesn't have any impact on expenditure and consumer price index of both food and non-food.

From regression analysis $R = 1.00$ indicates that there exist a very high degree of positive relationship per capita GDP among microcredit disbursement by different organizations. $R^2 = 1.00$ indicates that 100% of the variations in the per capita GDP can be explained by the combined variations of microcredit disbursement by MF-NGOs, banks, Specialized institutions and administrative ministries (sismin).

From the ANOVA table, it can be concluded that the results were statistically significant. T-test shows that total cumulative disbursement from the year 2002 to 2006 was not well enough to alleviate poverty. As beta for MF-NGOs was highest than the betas of banks, specialized institutions and administrative ministries (sismin) exert more influence on per capita GDP at current price. But the problem of multicollinearity exists because correlation coefficient between microcredit disbursements by different organizations is greater than 0.8 or 80% and lower than the coefficient with per capita GDP at current price. And last of all, there are some lacks of rules as well as regulation and their implementation in the Bangladeshi microfinance sector.

Recommendation

There are some recommendations to make effective microcredit disbursement to eradicate poverty. As MF-NGOs are cumulatively contributing more in disbursing microcredit, proper incentive should be provided them to increase annual disbursement also. Moreover, Government should focus on MFI financial accountability and regulatory framework of MF-NGOs. Though specialized institutions have effective infrastructural support, problem of lack of resources should be resolved by government and donors by providing funds. Again administrative ministries and banks had delivered the comparatively lower credit both annually and cumulatively. Infrastructural framework of these organizations should develop to ensure poverty eradication and side by side, regulatory framework of the Bangladeshi Central Bank should be revised.

Moreover, practices in terms of services such as credit, savings, insurance and social services, training, counseling, marketing and institution building would attract more poor people to participate in microcredit program. Again proper regulation about the loan size would help the MF-NGOs to reach the poorest Introduction of flexible repayment schedules; lowering first loan levels; combining food aid with microfinance and training would help the institutions to involve the poor people's participation in microcredit and thus helps to eradicate poverty. Lack of initiative in creating financing institutions and lack of conceptual clarity of the related officers should be eradicated first by logistic training to ensure eradication poverty.

Conclusion

Although the intensity of poverty lessened in Bangladesh due to efforts made over the last three decades, its depth and severity still persists. Addressing this problem is a great challenge mainly due to resource constraint. Bangladesh has so far implemented five Five-Year Plans and one Two-Year Plan and a Three-year PRSP Rolling Plan. The overarching goals of these plans were to accelerate economic growth and poverty reduction. As an outcome of these development activities, Bangladesh has made commendable progress in terms of reduction of income and human poverty. Logically poverty alleviation and creation of rural employment are top priorities in the development agenda of the government of Bangladesh (GOB) which has adopted a broad-based approach to poverty alleviation, emphasizing macroeconomic stability, economic liberalization, and support for a number of government agencies and non-government organizations (NGOs).

MF-NGOs are contributing a lot in cumulative delivery of microcredit in this country, on the other hand, annual microcredit disbursement by specialized institution in 2006 was highest among others and it delivered almost 56% of total microcredit to eradicate poverty. But administrative division and banks hold forth and third position respectively in annual disbursement of microcredit. From the analysis of the impact of disbursement of microcredit to eradicate poverty it is found that in case of national savings, investment, revenue generation, women empowerment, rural development, employment, poverty etc has apposite relation with microcredit which are indirectly eradicate poverty. But microcredit delivery doesn't have any impact on expenditure and consumer price index of both food and non-food.

Again, from regression analysis $R=1.00$ indicates that there exist a very high degree of positive relationship per capita GDP among microcredit disbursement by different organizations and $R^2 =1.00$ indicates that 100% of the variations in the per capita GDP can be explained by the combined variations of microcredit disbursement by MF- NGOs, banks, Specialized institutions and administrative ministries (sismin).

From the ANOVA table, it can be concluded that the results were statistically significant. But T-test shows that total cumulative disbursement from the year 2002 to 2006 was not well enough to alleviate poverty. As beta for MF-NGOs was highest than the betas of banks, specialized institutions and administrative ministries (sismin)

exert more influence on per capita GDP at current price, but the problem of multicollinearity exists.

Moreover, although Bangladesh has huge potential for development, it is, for various socio-economic reasons, among the poorest countries in the world. Effective microcredit disbursement required to eradicate poverty, Government should focus on MFI financial accountability and regulatory framework of MF-NGOs, lack of resources of specialized institutions, infrastructural framework of administrative ministries and regulatory framework of banks. Again practices in terms of services such as credit, savings, insurance and social services, training, counseling, marketing and institution building would attract more poor people to participate in microcredit program. So for eradication of poverty, proper regulation about the loan size of MF-NGOs, introduction of flexible repayment schedules; lowering first loan levels; combining food aid with microfinance and training would help the institutions to involve the poor people's participation in microcredit and thus helps to increase their contribution in per capita GDP. Moreover, government should take proper attempts to provide incentives for financing institution to deliver more microcredit and lack of conceptual clarity of the related officers should be eradicated first by logistic training to ensure eradication of poverty. Thus poverty can be eliminated and eradicated by distributing huge amount of microcredit efficiently and effectively.

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