Offices across Asia, Africa
and Latin America

www.***MicroSave***.net
info@***MicroSave***.net

Innovations in Financial Services Lessons from Bangladesh for East African MFIs

A Report of the Study Tour
by Leonard K. Mutesasira
MicroSave

March 1999

Introduction

This is a report based on observations made during a study tour to Bangladesh sponsored by the British Council and ***MicroSave*** and co-ordinated by the South Asian Network of Micro Finance Institutions (SANMFI). Below is a list of the participants

Participants included

Mr. Samuel Maeda, Chief Accountant, Kilimanjaro Co-operative Bank, Tanzania
Mr. Godwin Seiya, Senior Economist, Tanzania Postal Bank, Tanzania
Mrs. Nyambura A. Koigi, Assistant General Manager, Marketing and Corporate Planning, Kenya Post Office Savings Bank,
Mr. Augustine Cheruiyot, Manager, Research and Evaluation, K-Rep, Kenya
Mrs Eva N. Mukasa, General Manager, Uganda Women Finance Trust,
Mr. Januario Ntungwa, Supervision Manager, Centenary Rural Development Bank, Uganda
Mr. Paul Musoke, General Manager, PRIDE Africa - Uganda,
Mr. Wozei Muloni, Executive Director, FOCCUS-Uganda,
Mr. Henry Bagazonzya, Technical Advisor, Poverty Alleviation Project, Office of Prime Minister – Uganda
Mr. Godwin Kihuguru, Branch Manager, Faulu – Uganda,
Ms. Mary Margaret Nansubuga, Director of Credit Operations, FINCA.-Uganda
Mr. Leonard K. Mutesasira, Microfinance Officer, DfID/UNDP ***MicroSave*** Initiative

Participant Expectations

- Share experiences with Bangladesh MFIs in the areas of best practices
- Learn about the experience of Bangladesh MFI regarding product innovation and the product development cycle
- Learn about the range of microfinance products on the Bangladesh, there relevance to the “poor” market and the associated cost of delivering them
- Learn about the Bangladesh experience in developing sustainable institutional models
- Learn about the legal frame work for NGOs/MFIs and the process that is driving it in Bangladesh
- Learn about the impact and effectiveness of the different microfinance methodologies
- Learn about issues of governance, ownership, human resource development, and institutional development.

IMPORTANT OBSERVATIONS AND LESSONS

SAVINGS INNOVATIONS

- Bangladesh MFIs have registered phenomenal growth in savings mobilisation partly because they need alternative sources of financing their credit operations to supplement the otherwise dwindling donor funds.
- Open access to savings, according to the experience of MFIs in Bangladesh has led to increased savings once the people have tested the system and have proved that they can withdraw there savings anytime they want. This is relevant to for East African urban and rural areas. It is useful especially in cases of emergencies like sickness. Open access does not necessary result in frequent withdraws and therefore may not result in increased transactions. One NGO MFI in Uganda have already successfully pilot tested open access to savings. Initially the clients withdrew a lot of their money. Later they started savings and saved much more that what they would have under force closed saving. The earlier withdraws indicated that clients were testing the institutions intentions and seriousness and once confidence was built they started depositing more money than they needed to secure a loan. As a principle one can say that open access to savings results in increased demand for savings services.
- The new wave of innovations by progressive MFIs were inspired by an understanding of client needs and not the needs and convenience of the institutions. This highlights the need for market research to aid the design of products to meet the various needs of clients. This addresses the often mentioned "problems" of loan diversion.
- The MFIs in Bangladesh are mobilising savings in a legal vacuum and that the government is practising what some people called "benign neglect". Most of the MFIs visited indicated they intermediated deposit/savings under an ambivalent legal and regulatory environment. They believed this was a very important service for the people.
- Without intermediating the savings it is almost impossible to cover the savings mobilisation expenses. Like Bangladesh, East African regulatory environment cannot let MFI lend out the savings. The difference for Bangladesh is that the Central bank does not enforce the regulation because most of the MFIs are mobilising and intermediating savings. In order to the costs of intermediation East African MFIs may consider levying a fee for savings services. This is a common practice in the informal sector both in India and some parts of Western Africa. A few cases of this have been found in Uganda.[1]
- It was observed that innovative Bangladesh MFIs learn by understanding their social cultural dynamics of their environment. They seek to understand the strengths, weaknesses and opportunities of the informal and formal financial service sector and use that knowledge as a basis of innovation. This is certainly evident with *SafeSave's* roving savings and loan officers. If East African MFIs did the same they would probably get much better results that "imported" systems that are rarely responsive to local

[1] Use and Impact of Savings In Uganda

client needs and preferences. There is therefore an urgent need to re-design models used in East Africa and adjust them to local circumstances. This may result in changes to repayment periods, frequency of meetings, etc. For this matter a critical appreciation of the operations of RoSCAs, ASCAs and Informal Insurance systems could be an excellent beginning point. In this regard some studies conducted by ***MicroSave*** would be invaluable especially The Use and Impact of Savings in East Africa by Stuart Rutherford et al, 1998.

- Insurance products (*Gono Bima* and *Grameen Bima*). This product is offered by a private for profit company called Delta Life Insurance and is posting over $8 million dollars in premium income after 5 years of product existence. A lot of private companies have started replicating this product. Micro-insurance products are worthy of serious market research and pilot testing in East Africa. (For a more detailed discussion of Gino and Grameen Bima – see the Appendix). It was observed that health micro-insurance was still a challenge to innovators in Bangladesh although there is a tremendous amount of enthusiasm in this direction.

Table of Savings Products Offered by Bangladesh MFIs visited

Saving Product	***MFI***
Compulsory Savings	*Grameen, BRAC, ASA*
Open Access to Savings	*BURO Tangail, SafeSave*
Cumulative Contractual Savings	*BURO Tangail, SafeSave*
Fixed Deposit	*ASA, BURO Tangail, ASA, SafeSave*

Loan Products:

Many MFIs have successfully introduced several innovative loan products for micro clients. The process varies and but follows a general pattern which includes market research, concept development, pilot testing at a few branches and then rolling out to other branches after the pilot testing phase. Several Bangladesh MFIs were offering multiple loans to one client simultaneously with success. This is something worthy of piloting in Uganda because most clients in Uganda have multiple loans simultaneously sourced from MFIs, ASCAs, relatives and friends. Caution should be exercised tempered with careful market research regarding multiple loans because they have the potential of over-stretching the household budget.

The Loan Products include

- ***Supplementary Loans*** or sometimes referred to as "top-up" loan. The supplementary loan is an innovation by BURO Tangail. It is an important innovation that recognises that as the client pays off the loan the working capital is depleted and so needs replenishing. This allows the clients to maintain an optimal amount of working capital. The supplementary loan is extended after the client has made 25 instalments on a 50 instalments loan. The borrower can receive 50% of the current loan amount as the supplementary loan. The supplementary loan carries a one year term. This facility is accessed by about 15% of the borrowers.
- ***Seasonal loans*** are a Grameen Bank Innovation that is mainly used for that part of the year when agricultural production requires a lot of input especially during the harvest season. This loan can be extended concurrently with other loans. This product warrants serious consideration in East Africa especially in areas driven by the agricultural seasons
- ***Line of credit*** similar to those offered by commercial banks. This an innovation by BURO Tangail for its successful clients. This is in recognition of the fact that weekly repayments may deplete working capital of the business in consideration the business cycle of the business. A ceiling is established beyond which a borrower cannot go. The borrower can draw down on this facility any time in any instalment size and make repayments anytime based on the capital needs
- ***Medium Size Enterprise Loans*** this is in response to the demand of larger loans by growing micro entrepreneurs who seek to expand or diversify into new areas. Participating in this are BRAC (MELA) and ASA (SEDP
- ***Leasing:*** This is a Grameen innovation in response to the needs of experienced clients. The lease term ranges between 2 (animals) to 3 (equipment) years with a one month grace period. Ownership is transferred to the borrower upon completion of payments.
- ***Housing Loans***: This another of the Grameen Bank Innovations and is designed to address the poor's housing needs. There are various types of loans namely. The pre-basic housing loan (design stage); pre-basic housing loan (design stage II); Basic housing loan and general housing loans. The term ranges between one to ten years at 8% interest.
- ***Education Loans***: These are loans extended by Grameen Bank to clients with children wishing to go to University etc.
- ***Sanitation wells***: These loans are offered by several MFIs including BRAC, BURO Tangail, and ASA. The uses are mainly tube well and latrine purchase and construction. The interest rate ranges between 8% to 40% per annum for a one year term requiring weekly repayments.

WHOLESALE LENDING

- Wholesale institutions like PSFK specifically created to serve MFIs play a significant role in financing MFIs in Bangladesh especially in providing finances to small MFIs. In East Africa such organisations as the Postal Office Savings Banks and NSSF should examine the possibility of wholesaling loans to MFIs. The net effect could be mutually beneficial. The loans could be extended under a guarantee scheme. On the other hand this service, important as it may sound may face some practical difficulties as have already been faced by PSFK[2]. This difficulties tend to result in a declining quality of performance especially among the borrower MFIs. Wholesale lending presupposes a thorough knowledge of Microfinance in order to do risk analysis and the related due diligence that precedes closing. This kind of expertise is lacking in these organisations.

SUSTAINABILITY ISSUES

- One MFIs, like ASA, have reached operational and financial sustainability largely because of cost control and pursuing a minimalist approach. There are significant lessons here for Ugandan MFIs. Cost reduction and containment has been realised the following areas.
    - Transport costs: the staff of ASA do not have any vehicles. They use low cost public transportation known as rickshaw – equivalent to a bicycle boda boda.
    - Training costs: ASA does not conduct training session or have a training institution. Instead its uses an apprenticeship approach which results in considerable lower cost of training new staff. Recruits work along side seasoned staff until they have mastered the skills.
    - Recruiting high school graduates who tend to demand lower salaries and tend to be more stable at the job because they attach a far greater value to it given their lack of many options.
- There are lots of potential opportunities to start innovating for the East African market in the area of leasing, credit cards, payment systems, housing loans, education loans, seasonal loans, emergency loans etc through NGO-MFIs, banks, and user owned and managed associations like FSAs.(Financial Service Associations)
- It was observed that the Bangladesh MFIs did not use the "magic sixteen weeks" loan term which is so typical of the Ugandan MFI. It was observed that the commonest loan term among MFIs is about 50 weeks. This is an issue that needs to be revisited and necessitate a revision of the Memorandum of Understand signed by Uganda MFI that stipulates the 16 week period as the best practice. A suggested approach currently being used by a few of the Ugandan MFIs is to increase the terms as the size of the

[2] **Wright**, Graham A.N., "Microfinance Systems: Designing Quality Financial Services for the Poor", UPL, Dhaka and Zed Books, New York and London (forthcoming)

loan increases. The term could increase from 16 weeks to 52 weeks for example varying with the size of loans. This will have positive impact on repayment rates because of the reduced stress caused by larger weekly repayments.

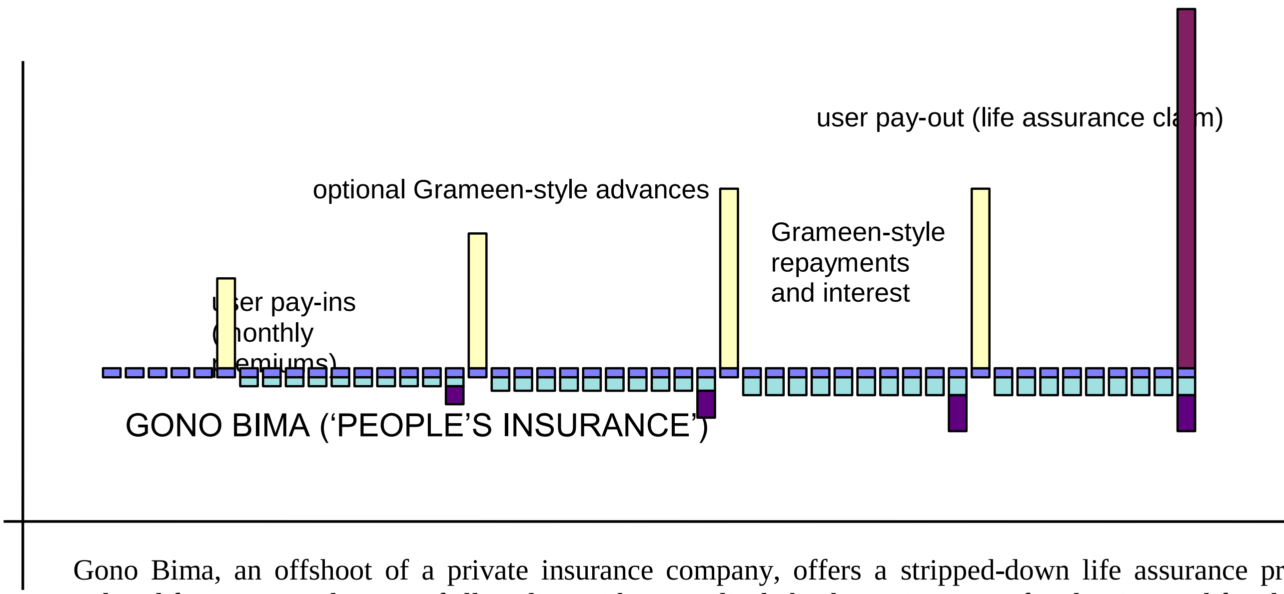
REGULATION AND SUPERVISION

- MFI practitioners etc has been established to draft a regulatory policy Bangladesh was far from establishing regulations and a supervisory framework for MFIs. This is mainly because the bigger MFIs are not interested in being "regulated" by a central banks that is not fully conversant with the issues that define the industries growth and spirit of
- Regulator and policy makers should be careful not to design constraining law and regulations that might drive MFI from poverty alleviation into becoming banks. This may be the beginning of their migration from a focus on poverty reduction to corporate banking leaving the poor once again to there own devices. This seems to be the trend in Bangladesh. Regulators should remember that MFI were created because formal banks were not meeting the needs of the poor. Regulations that force NGOs to become banks would be one way of killing the poor peoples alternative. East Africa should take heed.
- There is a critical need for MFIs to be actively involved in carefully deliberating the regulatory framework with a full view of the impact it can have on the entire financial sector and the overall national effort on poverty reduction. This consultative approach, which is being used in Bangladesh will create a better regulatory framework which will be mutually beneficial for the clients, central banks, and MFIs.

REACHING THE POOREST OF THE POOR

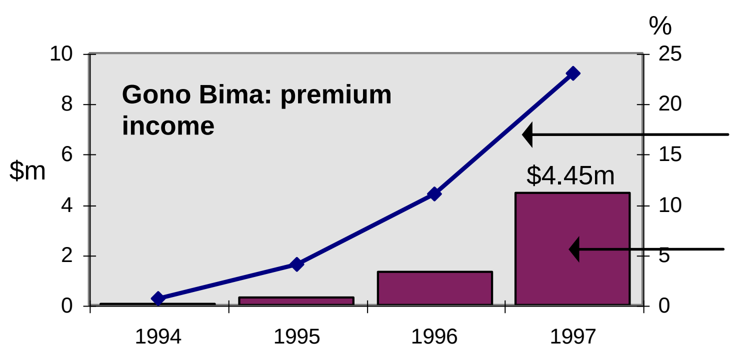
Like Uganda, MFIs in Bangladesh have also failed to reach the bottom 15% of society. Uganda's cases is worse with 30% of the bottom not reached. It is for this reason that MFIs are looking at other ways of reaching the poorest the strongest of which is offering savings services. The poorest segment of society tend to be averse to exposing themselves to the high risk of taking loans because they increase their vulnerability in case of shocks. They prefer savings services until they have crossed a certain threshold of asset ownership. Therefore if MFI are to reach the poorest, saving services need to be incorporated in the menu of products and services.

APPENDIX: *Gino Bima: popular insurance for the poor*



Gono Bima, an offshoot of a private insurance company, offers a stripped-down life assurance product tailored for poor people - a no-frills policy with no medical check requirements, fixed ratios, and fixed equal monthly premium payments. The cash inflow from premiums is recycled in Grameen-style loans.

The product thus combines the annual fixed savings-to-lump-sum swap as practised by Grameen and ASA with long-term savings against one event (death of the insured person). The product is popular and Gono Bima is expanding fast. Growth rates and performance are summarised below**.**



Gono Bima premium income as % of all company premium income (right scale)
Gono Bima premium income, $m, (left scale)
Gono Bima, as at end December 1997: 513,000 policy holders insured for $112m assured sum ($220 each). 11,500 borrowers with loans outstanding of $511,000. Loan value disbursed $782,000 ($67 per borrower). On-time recovery rate of loans, 79% . (chart and table: source, Gono Bima [Delta Insurance Co])

Additional information:

1. According to M.A. Aziz (Division Manager of Delta Life), the number of Gono Bima policyholders has recently reached 1.8 million. (This needs verification)
2. Delta has two variants of the same micro-insurance product - Grameen Bima (for rural households) and Gono Bima (for urban households). They are essentially the same product, except that Gono Bima's premium is paid monthly while Grameen Bima is paid weekly.
3. The face value of policies range between $100 to $1,000 and premiums vary accordingly. Most clients take the lower amount policies. The premiums are small and affordable, and based on statistics below, the product is gaining a great deal of popularity among low-income and poverty groups.
3. If sold in great quantities, the premiums collected can amount to a lot of money. The annual premium income on Gono Bima has been exponentially increasing during the last few years: Gross premium income was $34,000 in 1994, $8.4 million in 1998. Who says poor people have no money to save?
4. There are now at least five private insurance companies which have introduced micro-insurance products copied from Gono Bima. Initial reports from those companies show that indeed there is big demand for such a product. The Delta Life model is replicable by many NGOs and life insurance companies and is worthy of pilot testing in East Africa.
5. One of the "success" secrets of the Company is the big number of Field Organizers (FOs) it recruits and trains. Around 90% of its 16,000 employees are FOs. The FOs are the people which sells the product on a door to door basis. The Company representative goes out to the village and looks for young, aggressive and articulate people and offer them jobs as FOs. Those who sign up are given a basic one week training which includes basic information on the company, the product, identification of potential clients, selling skills, collection procedures, etc. All FOs are drilled on door to door selling. They are paid on commission basis, that is they get $20 Taka for every $110 monthly premium income they collect.
6. Gono Bima is like an endowment plan (you get your money back plus "bonuses" after the policy period.) The "bonus" is currently set at 40% of total premiums paid. Using qualified actuaries, the Company conducts a valuation of risks and reserves every two years and declares the amount of bonus payable on matured policies. So far, the rate of bonus is gradually increasing over the past four years.
7. Gono Bima has a policy loan feature, where the policyholder can apply for a loan with the Company up to a certain maximum amount.
8. The Company is very profitable. It declared a 36% dividend last September 1999 to all shareholders. In spite of short average lifespan of Bangladeshis, claims (due death) to premium income is less than 2 % (maybe 1.7%), meaning Delta is not really losing heavily due to high claims. They say that this claims ratio is compatible with experiences in other countries.