

# **Access to Finance for Inclusive Businesses and Agriculture in Bangladesh**

Summary of Survey Findings

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# 1. Background

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- The Business Innovation Facility (BIF) Bangladesh is a UKaid-funded project.
- BIF aims to support Inclusive Businesses (IBs).
- IBs have a profitable core business activity that also tangibly expands opportunities for the poor and disadvantaged in developing countries.
- The social benefits of IBs include:
  - increased employment opportunities for marginalised groups,
  - the growth of markets for local smallholders and tradesmen, and
  - potential food security improvements.
- BIF works in 5 countries: Bangladesh, India, Nigeria, Malawi and Zambia: see [www.businessinnovationfacility.org](http://www.businessinnovationfacility.org).
- Challenges Consulting which is part of the Challenges Worldwide group works on behalf of BIF: see [www.challengesworldwide.com](http://www.challengesworldwide.com)

# The Role of SMEs and Agriculture

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- Challenges Consulting were asked to conduct a survey of the financial landscape for access to finance for IBs. IBs can be compared to Small and Medium Enterprises (SMEs).
- In the Poverty Reduction Strategy Paper (PRSP)-II, which is currently in force, the development of SMEs has been identified as a critical element of pro-poor growth.
- In April, Bangladesh Bank (BB) Governor, Dr Rahman, emphasised again the need for investment in agriculture and SMEs, the two largest contributors to employment generation.

# Definition of SME



Client Size	Definition
Small	<u>Manufacturing</u> : Fixed asset value* between Tk5m and Tk100m or 25 to 99 employees
	<u>Service and Trading</u> : Fixed asset value* between Tk0.5m and Tk10m or 10 to 25 employees
Medium	<u>Manufacturing</u> : Fixed asset value* between Tk100m and Tk300m or 100 to 250 employees
	<u>Service and Trading</u> : Fixed asset value* between Tk10m and Tk150m or 25/50 to 100 employees

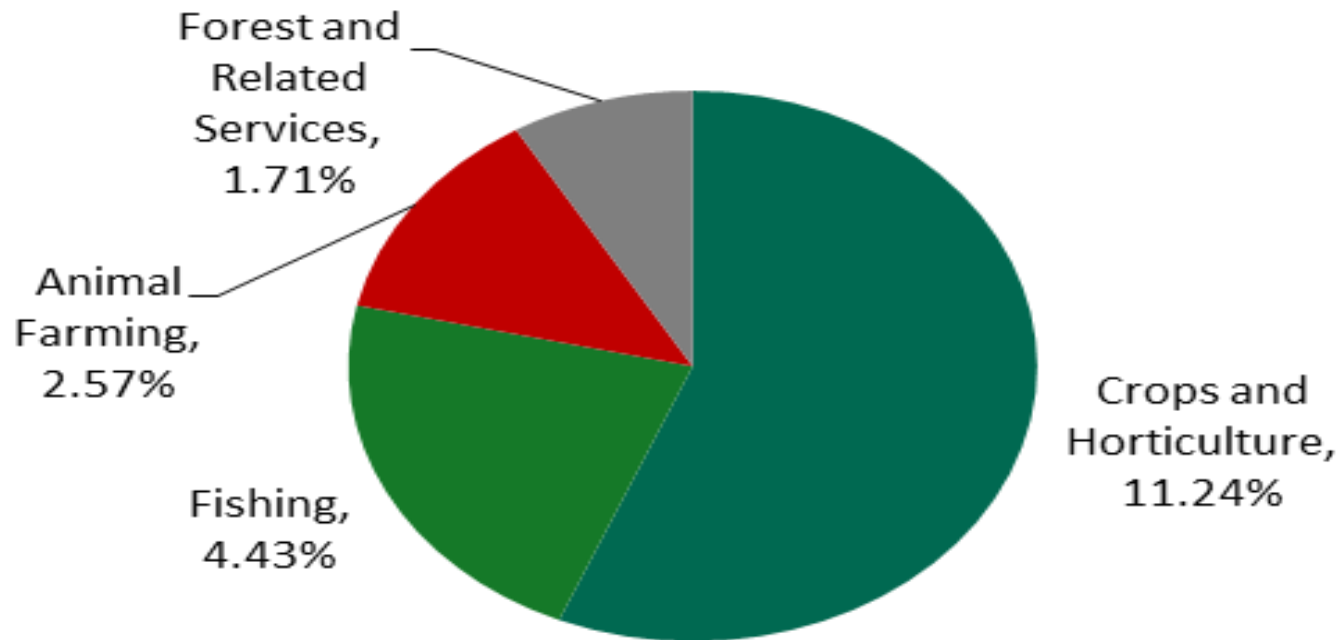
\*excluding the value of land and building

## 2. Contributions to the Economy

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- Agriculture contributes about a fifth of GDP



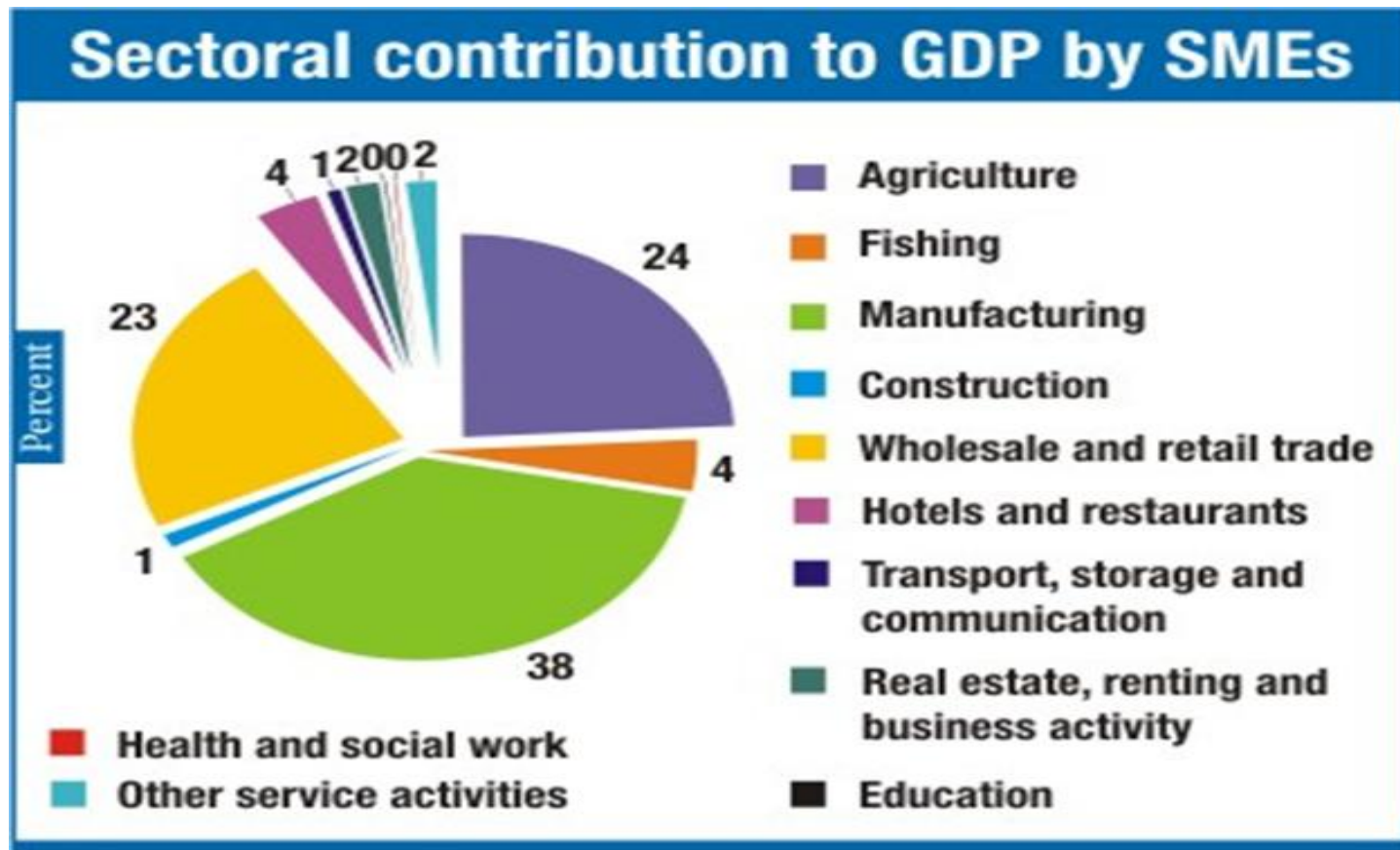
# Contributions to the Economy (cont.)

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- Services contribute half of GDP, whilst industry is about 30%.
- SMEs number between 6m (ADB) and 3.3m (registered) SMEs.
- SMEs make up 25% of the total labour force, 80% of industry employment, and 90% of enterprises.
- SMEs contribute a quarter of Bangladesh GDP, but in some countries it can be as high as 70%.

# Overlap between Agriculture and SMEs

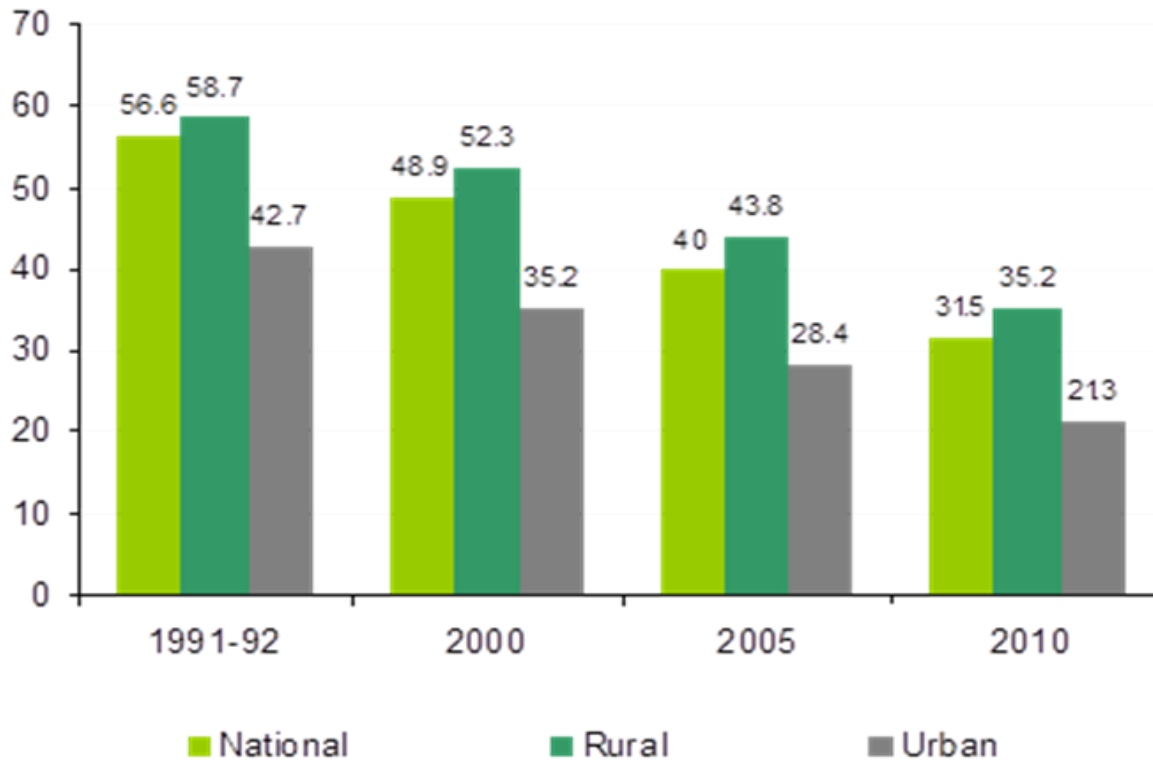


### 3. The Economic Environment



	FY2000	FY2010	FY2011
Nominal GDP (US\$bn)	47.1	100.1	108.4
Per Capita Income (US\$)	377	751	818
FX Reserves (US\$bn)	1.6	10.7	10.9
<b>Private Sector Credit/GDP (%)</b>	<b>21.3</b>	<b>39.1</b>	<b>52.9</b>
External Govt. Debt / CAR (%)	173.9	71.2	66.1
Government Debt / GDP (%)	46.4	37.1	37.1
Budget Deficit excl. grants (%)	-6.1	-4.5	-4.4
Investment / GDP (%)	23.0	24.4	24.7

# Poverty Rates (upper band)



## 4. Why Access to Finance is Important

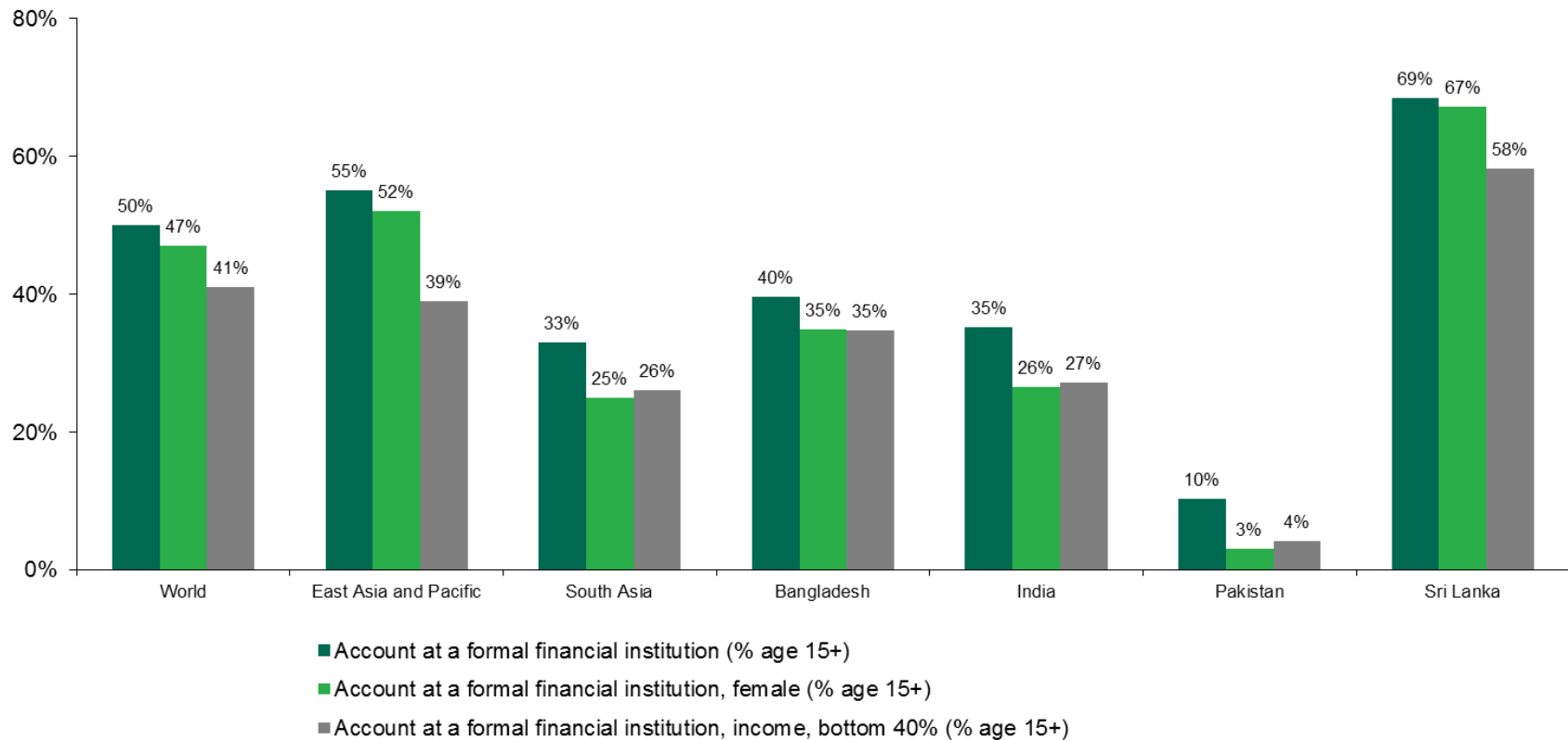
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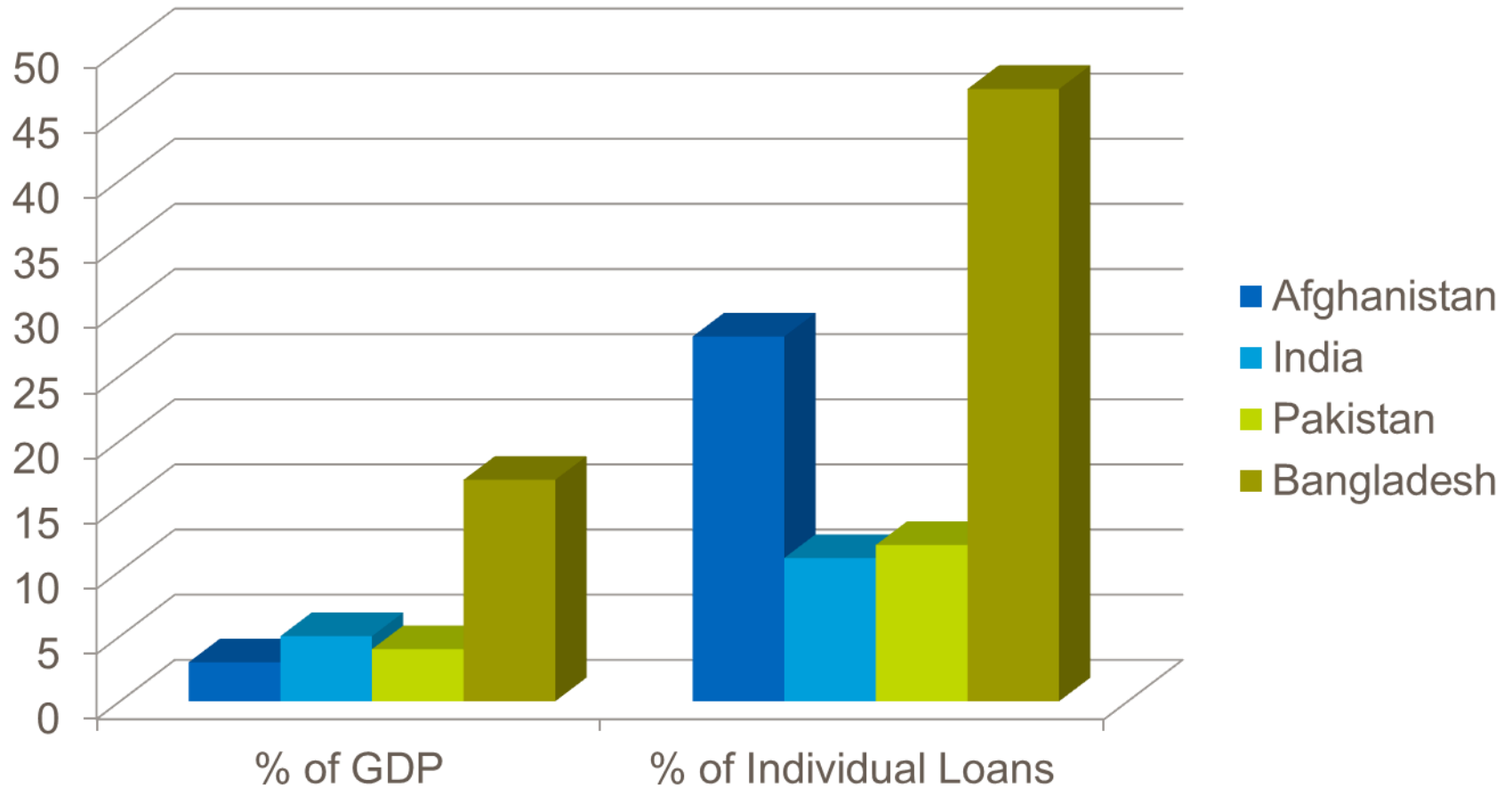
- Access to a well functioning financial system can economically and socially empower people, particularly the poor, to:
  - better integrate into the economy,
  - improve their development, and
  - protect themselves against economic shocks.
- Financial inclusion can be assessed in a number of ways:
  - People with a bank account: 25.5% or 43.8%,
  - Index (banking penetration, availability of services and usage of services): 43/55 countries



## Accounts at a formal financial institution (% age 15+)



# SME Access to Finance



# Role of Government

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- SMEs and Agriculture recognised as crucial.
- BB agrees targets for lending:
  - SMEs (2012): Tk590bn.
  - Agriculture (FY 30 June 2012): Tk138bn.
- Established SME Foundation.
- Runs three funds:
  1. SME Refinancing: Tk23bn by April 2012, 15% to women,
  2. JICA SME Fund: Tk5bn over 5 years, and
  3. ADB Fund: \$95m.All provide subsidised funds to banks.

## 5. Who is Lending to SMEs?

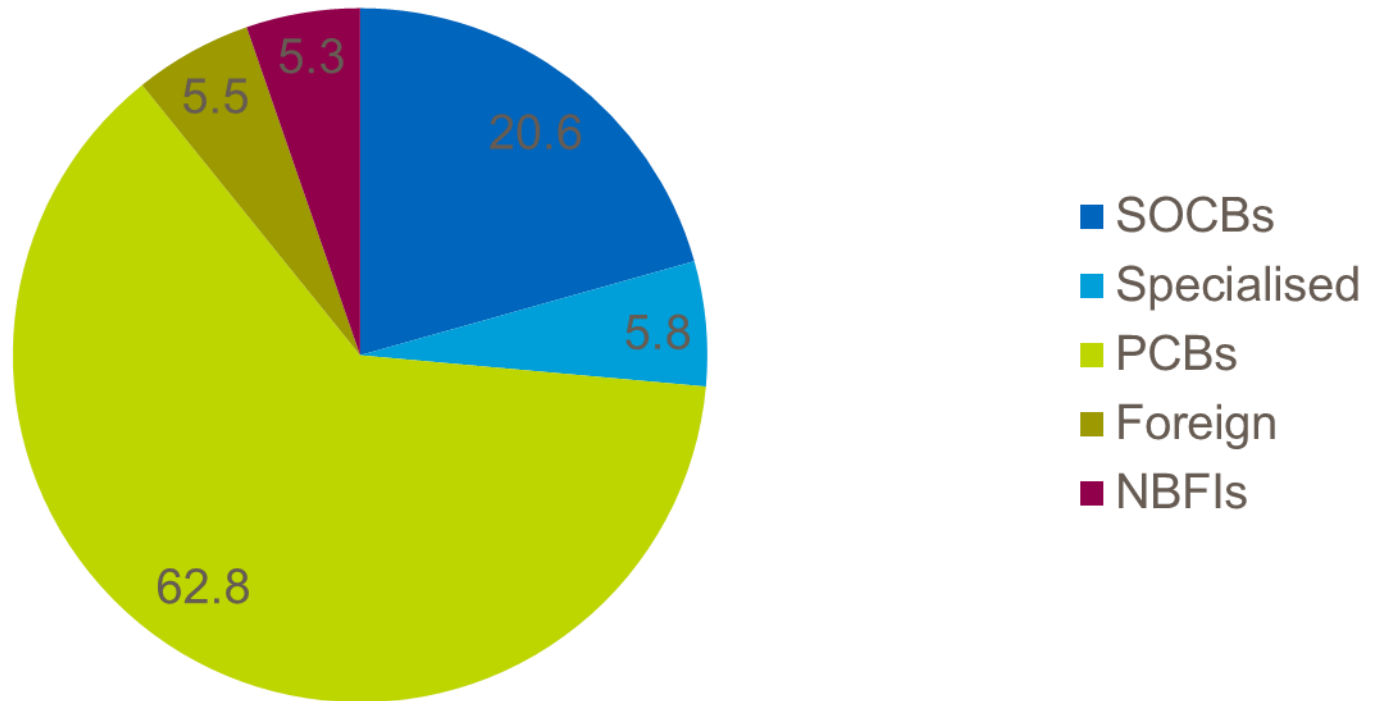


<b>BANKS (31 March 2012)</b>	<b>TkBn</b>
4 State Owned Commercial Banks (SOCBs)	84
4 Specialised Banks (also fully or majority owned by the Government)	24
30 Private Commercial Banks categorized into two groups (23 Conventional PCBs and 7 Islami Shariah based PCBs)	255
9 Foreign Commercial Banks	22
PLUS: 29 Non-Bank Financial Institutions (NBFIs)	22
<b>TOTAL</b>	<b>410</b>

# Banks and NBFIs Lending to SMEs



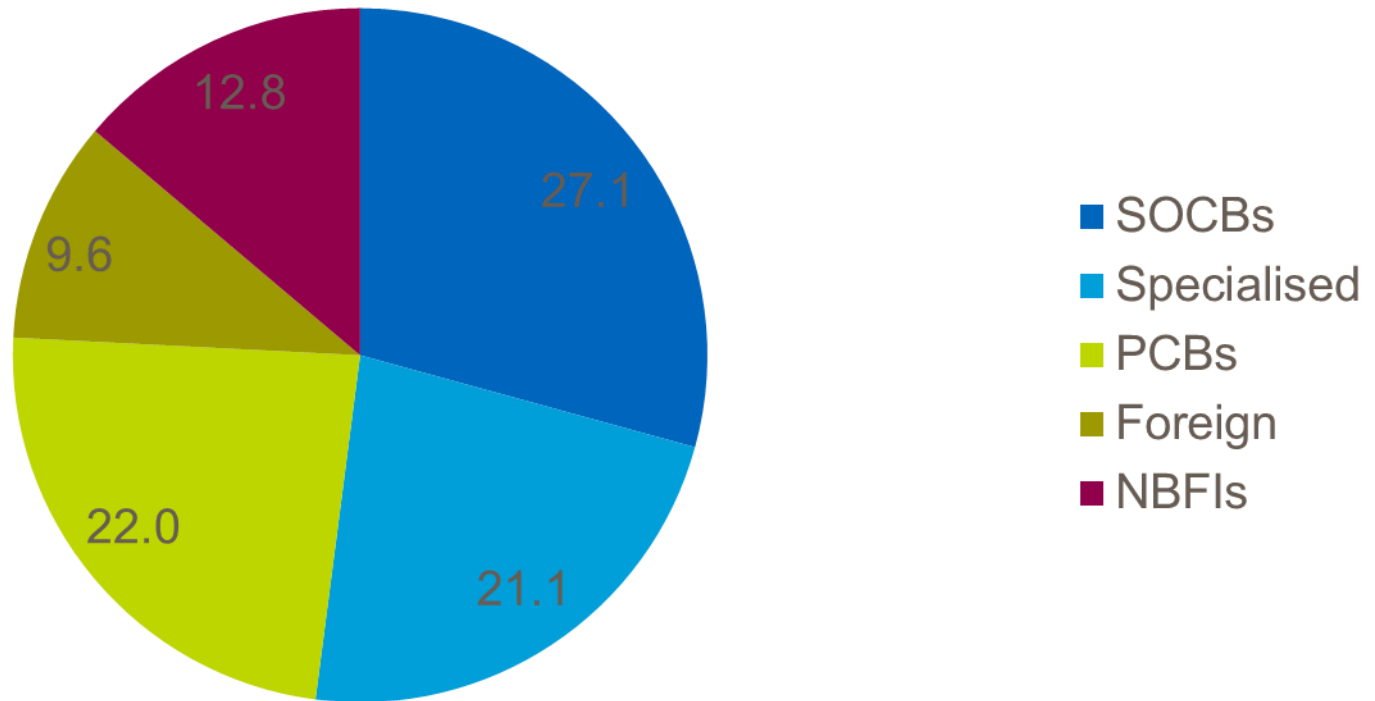
% of SME Lending (31 March 2012)



# Banks and NBFIs Lending to SMEs



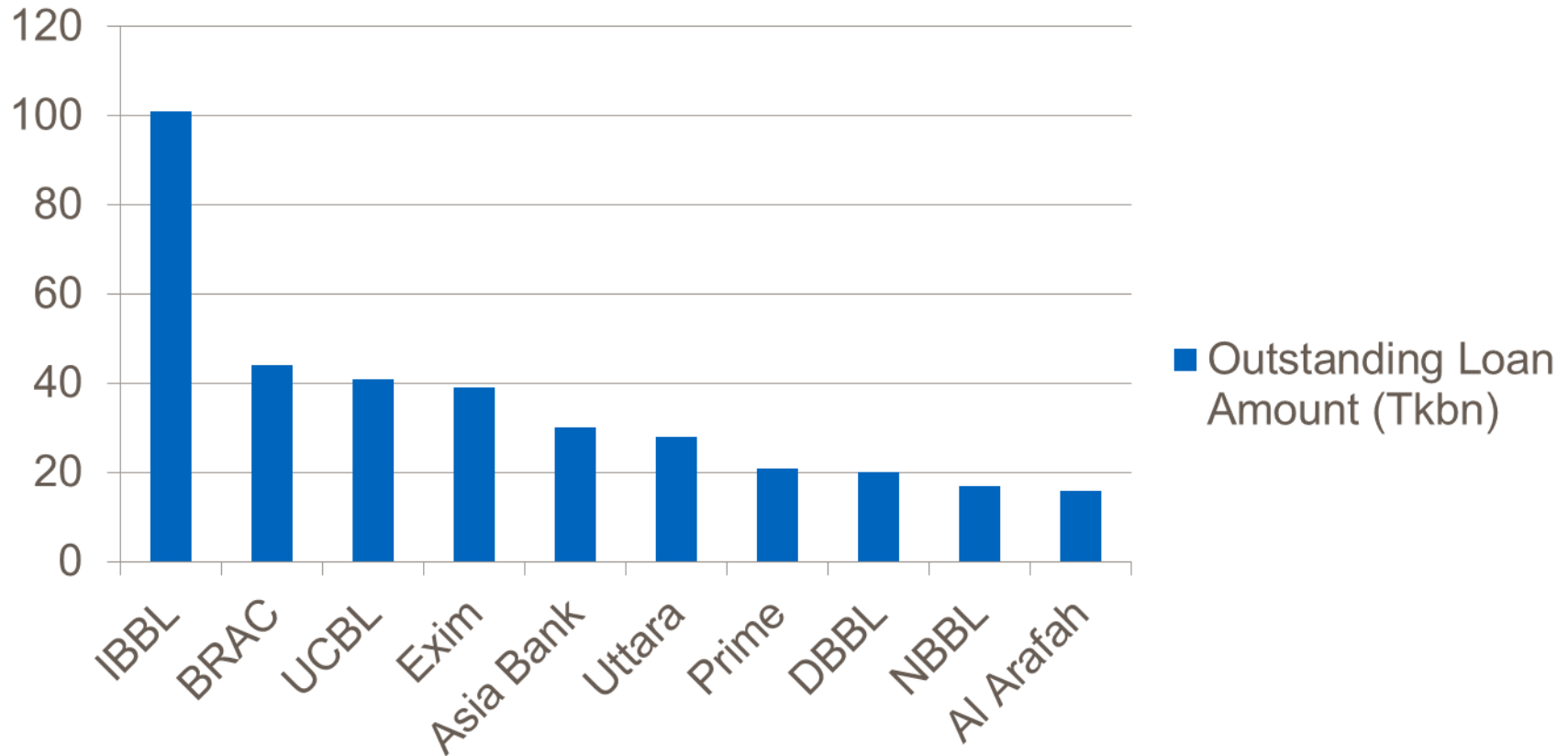
% of Total Lending (31 March 2012)



# Leading Lenders to SMEs (31 Dec 2011)

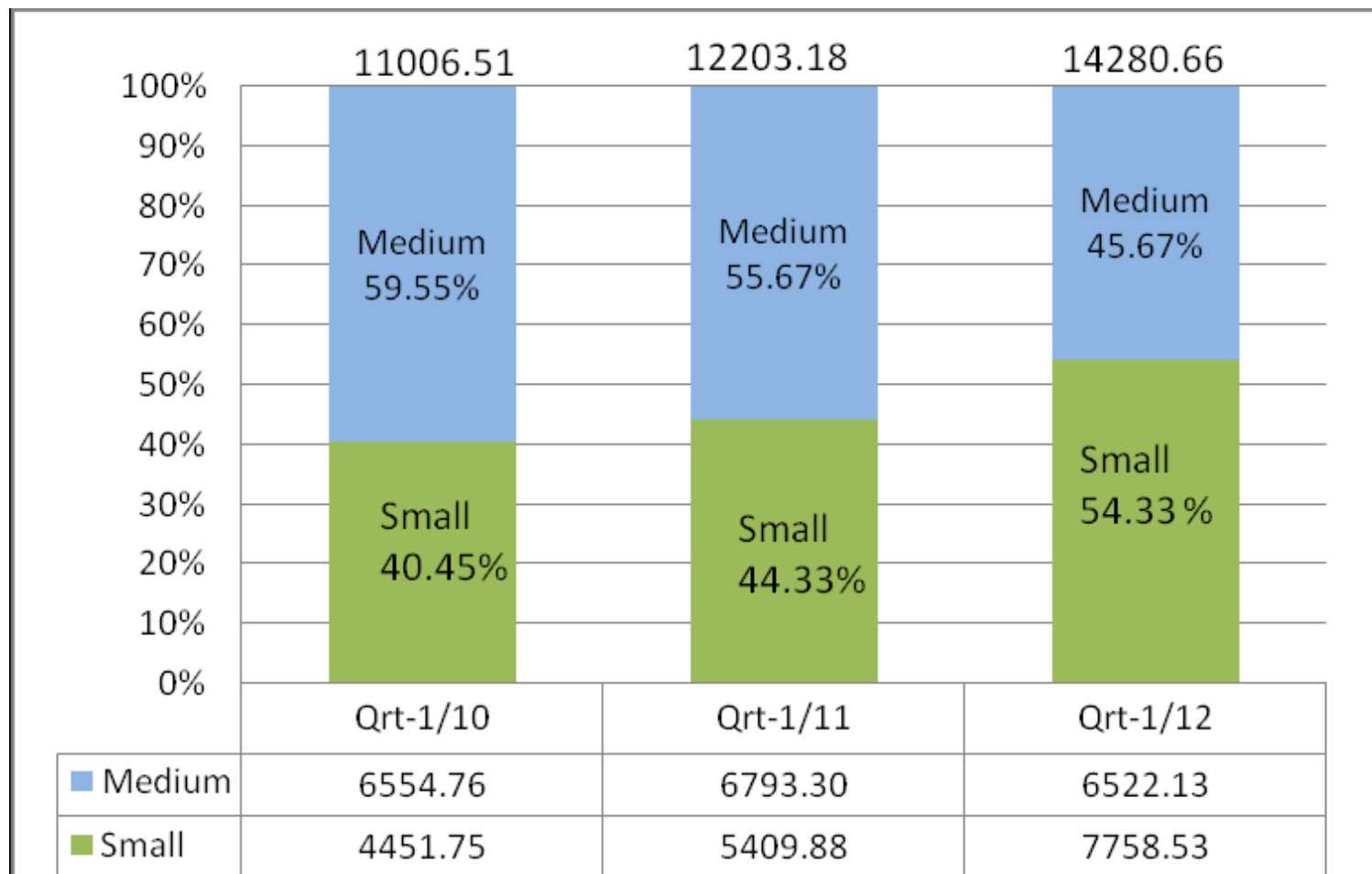


## Outstanding Loan Amount (Tkbn)





# Loans Disbursed to SMEs



## 6. Banks Lending to Agriculture

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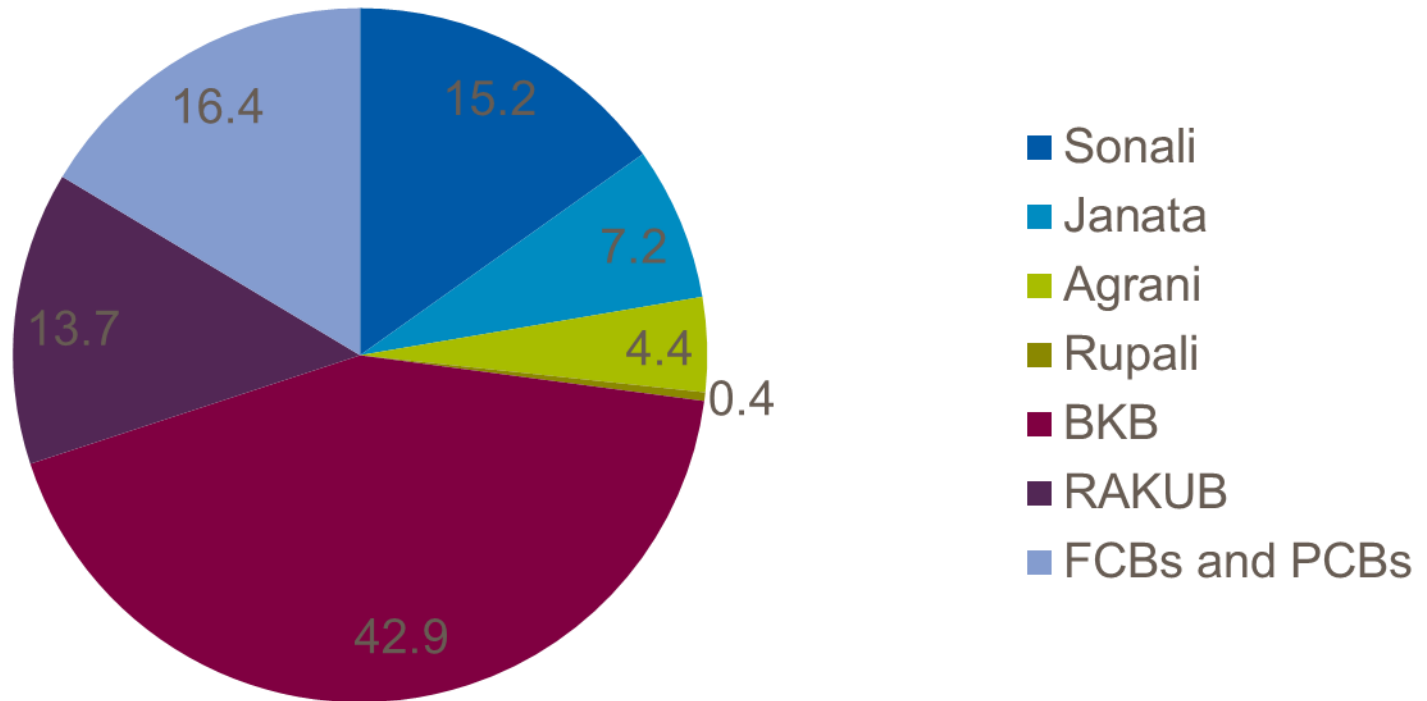


- The total outstanding at 31 May 2102 was Tk247bn.
- The Agriculture Credit comes mainly from the four SOCBs and two Specialised banks: Tk206bn.
- Foreign banks and PCBs also contribute: Tk42bn.
- Finally lending comes from BRAC (Sharecropper scheme through BB) and BRDB (government fund).

# Banks Lending to Agriculture (cont.)



% of Outstanding Loans (31 May 2012)





## 7. Lending by MFIs

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- Bangladesh microfinance sector is mature.
- Assets constitute around 3% of GDP in 2011.
- 599 Microfinance Institutions (as of October 2011) licensed by MRA (Grameen Bank operates under its own Act).
- Total outstanding loans increased by 20% from Tk145bn in June 2010 to Tk174bn in June 2011.
- Savings (from members only) increased by 23% over same period to Tk63.3bn.
- Women comprise 93% of 26m clients.

# MFI Operating Statistics



Particulars (as at June)	2008	2009	2010	2011
No. of Licensed NGO-MFIs	293	419	516	576
No of Branches	15,077	16,851	17,252	18,066
No. of Employees	98,896	107,175	109,597	111,828
No. of Clients (Million)	23.45	24.85	25.28	26.08
Total borrowers (Million)	17.79	18.89	19.21	20.65
Amount of Loan Outstanding (Tk. Million )	134,680.96	143,134.03	145,022.66	173,797.60
Amount of Savings (Tk. Million)	47,386.19	50,610.04	51,362.93	63,304.44



Name	Loan Outstanding (Tk million)	Loan in Agricultural sector		Loan in SME/ME sector			Loan for SME only	
		Amount (Tk mill.)	% of L.O	Amount (Tk mill)	% of L O	Client number	Amount (Tk mill)	% of L.O
<b>BRAC</b>	52635.6	5838.4	11.1	23495.7	44.6	249585	4367.1	8.2
<b>ASA</b>	47383.3	25814.4	54.5	10538.0	22.2	140496	1343.4	2.8
<b>BURO</b>	6381.3	2927.9	45.9	334.6	5.2	4857	147.1	2.3
<b>TMSS</b>	5906.0	2798.7	47.4	2182.5	37.0	8816	1561.4	26.5
<b>Jag Chakra</b>	4470.7	1405.9	31.4	1515.1	33.9	15008	447.1	10.0
<b>Shakti</b>	3009.6	212.4	7.1	218.0	0.7	3885	68.9	2.3
<b>UDDIPAN</b>	2618.2	287.7	11.0	692.4	26.4	7310	29.0	1.1
<b>Palli Mong</b>	1502.6	24.5	1.6	749.5	49.9	---	---	--
<b>CARITAS</b>	1302.7	1302.7	100.0	--	--	---	---	--
<b>Sajida</b>	1528.2	83.4	5.5	519.3	34.0	---	---	---
<b>POPI</b>	1342.9	815.7	60.7	136.3	10.1	---	---	--

# Conclusion regarding Debt

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- Most SMEs are small and, whilst bank lending going to the medium enterprises component is reducing, small enterprise clients may be less than 50,000.
- Most “agriculture” lending is actually “non-farm rural credit”.
- Much of the agriculture lending by banks (to reach the 2.5% minimum) is wholesale to MFIs.
- Most MFI SME clients are long standing clients “graduating” to larger loans.
- Therefore, it may still be right to say: “Notwithstanding all these arrangements for financing of SMEs, the actual delivery of institutional credit to this sector has been grossly inadequate”: Khan (2010).



## 8. Products and Services

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- The Banks provide a range of working capital and term loans, with limited non-financial services.
- Some interest rates are capped, eg woman entrepreneurs (10%) and subsidised agriculture (13%).
- Otherwise, all lending subject to Circular 01/2012: “lower single digit” over cost of funds, except for “high risk loans and SME loans”.
- Despite this, many banks still operate at a 5% margin for SMEs, with interest rates at 18-22%.
- All banks require collateral above small loans (T100,000 to T2.5m) below which personal guarantees needed.
- Other requirements include the need for a business history of at least a year.

# Products and Services: MFIs

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- Six broad groups: i) general microcredit for small-scale self employment based activities, ii) microenterprise loans, iii) loans for ultra poor, iv) agricultural loans, v) seasonal loans, and vi) loans for disaster management.
- Interest rate capped at 27%.
- MFIs are not allowed to take deposits from the public.
- Many MFIs offer other services, such as micro-insurance and remittances.
- With NGO base, many MFIs also provide non-financial assistance, such as training on enterprise creation, business skill development, and financial literacy and financial management training.



## 9. Equity Providers

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- This is not a concept widely accepted in Bangladesh. But there are some avenues, eg:
  - **SEAF** operates three funds: Business Development Ventures, Venture Investment Partners, and (soon) Bangladesh Agriculture Ventures,
  - **Tindercapital**: a small self-funded facility,
  - **Frontier fund**: large ticket venture capital, and
  - **Danida**: operates a B2B facility.
- ADB and KfW are examining possible social entrepreneurship / IB funds.
- Leopard Capital will launch competitor to Frontier this year.



## 10. Other Finance Providers

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- Input suppliers, eg ACI and Syngenta, facilitate short-term credit via retailers
- Leasing companies, but mainly large ticket equipment items in urban areas
- Cooperatives exist but are much smaller than in other countries, and lack capital and credibility
- Rotating savings and credit associations (ROSCAs)
- Money lenders and pawn shops
- Private donors
- International NGOs
- Specific Government Departments.



# 11. What Potential Clients Can Do

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- Seek Most Appropriate Products:
  - Compare interest rates
  - Other terms can be just as crucial
  - Align repayment terms with cash flow
  - Agriculture ventures particularly fraught, eg climate, disaster
- Ability to Qualify:
  - Title to property to allow for collateralisation
  - Inability to meet lenders' minimum client criteria, especially years of business operation
  - Physical access to financial services
  - Poor infrastructure, eg power, roads
- Application and Reporting Processes:
  - Ability to prepare application, given complexity of forms
  - Allow for detailed reporting required.

# What Potential Clients Can Do (cont.)

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- Purpose for Loan:
  - Lack of product range to meet financing needs, eg cash flow based not asset backed
  - Limited loans for agriculture activity
  - Lack of insurance coverage, particularly for agriculture
  - Find the lender most aligned with clients' interests
- Improve Business Attributes:
  - Business skills, eg planning, marketing, product development, quality control, HR, cash/debt management
  - Maintain transparent and proper accounts
  - Seek to comply with difficult business licensing regime
  - Low levels of productivity, lack of skilled technicians and workers, lack of market research and R&D facilities.
- Capacity to grow, eg internal controls, risk management

## 12. Issues for Providers

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- Banks:
  - Government involvement in institutions and markets, eg interest rates
  - SME departments mandated but not all banks fully committed
  - Inability to assess loan applications
  - Ticket size versus cost: need more efficient loan assessment process, eg credit scoring
- Capacity:
  - Limited capital, eg competing demands for banks and inability of MFIs to take savings
  - Difficulties in enforcing collateral
  - Many field staff need training in SME and Agriculture lending
  - Need to decentralise operations to reach clients.

# Issues for Providers (cont.)

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- Lending:
  - Loan monitoring approach needs to change for SMEs and Agriculture credits
  - Portfolio quality and delinquency management
  - Disproportionate exposure to crop failures and other rural disasters
  - New product development and appropriate pricing, based on proper risk assessment
- Not well coordinated with providers of TA and assistance to potential clients.



## 13. Suggestions for Clients

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- Focus on improving their own capacity to be credit ready and comply with loan agreement
- Make use of available assistance by third parties, eg
  - BB website comparing interest rates: [www.bb.org.bd/econdata/index.php](http://www.bb.org.bd/econdata/index.php)
  - SME Foundation
  - Facilities such as BIF
- Consider whether it makes sense to seek loan from an MFI initially: more attuned to IB and agriculture
- Approach banks that are more agriculture and SME friendly
- Consider relaxing ownership constraints to utilise other sources of funds, such as equity.



# 14. Recommendations for Change

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## **MICRO / INSTITUTIONS:**

- Increase efficiency of existing providers:
  - Loan product development , e.g. based on “soft” data
  - Increase savings (for MFIs)
  - Continue expansion of insurance and telephone banking
- Encourage entry of new providers
- Forming better linkages between institutions and TA providers

## **MESO / SUPPORT:**

- Institutional Support:
  - Encourage more financing by guarantees and other instruments
  - Offer grants and TA to build institutional and client capacity
- Expand remit of Credit Information Bureau
- Consider SME Rating Agency, as used in India
- Extend role of the SME Foundation

# Recommendations (cont.)

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## MACRO / REGULATION:

- SMEs and Agriculture have been put at the centre
- Role of Government crucial:
  - Should continue to focus on supporting an appropriate enabling environment
  - Consider the removal of interest rate caps or directives, so that loans can be priced for risk
  - Expand deposit-taking MFI numbers
  - Consider need for SME wide regulation
  - Make fiscal policies less SME unfriendly
- Business training and awareness of financing options
- Continue to improve land titles and court system

# Discussion

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For further information, go to: Practitioner Hub on Inclusive Business: [www.businessinnovationfacility.org](http://www.businessinnovationfacility.org)

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