MicroSave Briefing Notes on Grameen II # 8

Lessons From The Grameen II Revolution

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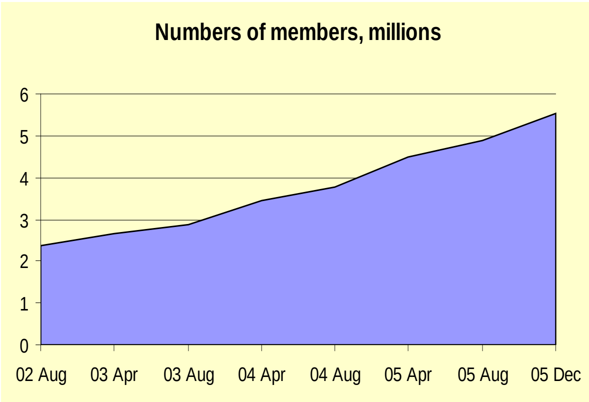
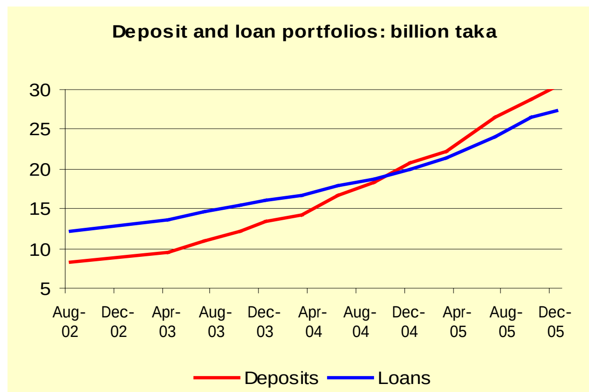


The Grameen II system represents a revolution in the way that Grameen Bank does business. It is the culmination of years of hard work to assess the aspirations and needs of the poor in Bangladesh and re-design the "classical" Grameen system to respond to those needs. The bank's success (and the success of the many Bangladeshi MFIs who copied it) reflects how well the basic working capital loan repayable over one year met one of the core requirements of the poor in Bangladesh. But those requirements have been evolving and there has been a growing recognition that credit alone does not meet the needs of the poor. With its new range of products, the Grameen II system reflects and meets many of the diverse needs of Grameen's target market and has become more clearly "market-led".



The results have been extraordinary. After a difficult period of stagnation and compromised portfolio quality, the bank has grown significantly both in the number of customers served and in profitability. Grameen took 27 years to reach 2.5 million members – and then doubled that in the full establishment of Grameen II. Even in Bangladesh's fiercely competitive environment Grameen continues to grow at a remarkable rate attracting around 140,000 new members each month – a staggering 1.7 million new members every year. In the three years to December 2005, Grameen's deposit base tripled and its loans outstanding doubled. In the same period the bank has introduced a more conservative provisioning policy and built up a formidable loan provision for its troubled housing loan portfolio. At the same time the quality of the loan portfolio has significantly improved. As did profitability: despite much heavier loan loss provisioning, profits soared from around 60 million taka in 2001 to 442 million taka (about $7 million) in 2004. Drop-outs are returning, and even some old defaulters are repaying and re-joining. Market-led Grameen II is yielding very encouraging results.

Rutherford et al.'s work shows that the Grameen customers are using the Grameen II products in a wide variety of ways, to meet the diversity of needs and challenges that face them. The introduction of individual passbook savings accounts and contractual or programmed savings products allows them to save "up" as well as "down"[1], and increases the range of financial instruments and options that they have to manage their complex household budgets. The top-up loans allow members to maintain the capital in their businesses or to manage unforeseen challenges/shortfalls and extend repayment periods in a structured (and carefully tracked) manner where necessary. There is evidence that for some members Grameen is meeting most of their needs, leaving them much less dependent on the informal financial services sector. In short, Grameen II shows that as the breadth of products on offer increases, the utility to the users increases dramatically[2]. It is this increased utility that is encouraging drop-outs to return and defaulters to repay and rejoin Grameen – access to a range of market-responsive products is a valuable asset. It is not unreasonable to surmise that with the increased utility and ability of the poor to manage their meagre financial resources, the developmental impact will be higher too.

In short, the Grameen II's responsiveness *to* the market has created a very positive response *from* it – both the clients and the institution have benefited greatly from the change.

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[1] See **Rutherford** Stuart, *The Poor and Their Money*, Oxford University Press, Delhi, 2000, for an explanation of the terms saving "up" and saving "down".

[2] For many years BURO, Tangail was able to charge a 60% higher interest rate on its loan products <u>because</u> it offered a range of credit and savings products that were greatly valued by its membership.

The challenge for classical "Grameen replicators" across the globe will be to develop the systems, front-line staff and management capability to take the next step … and where they wish to offer the savings services, to obtain the licences from the regulatory authorities. The move from the "plain vanilla", classical Grameen model with its relative simplicity, and associated limited options for clients, to a more market-led approach, is likely to be immensely challenging for most. It will involve new skill sets – not least of all to complete the necessary market research and product development. For those initiating savings services, the change is likely to be profound. In the words of Marguerite Robinson and Graham A.N. Wright, "*mobilising voluntary savings from the public will change the institution dramatically, management, organisation, internal supervision, liquidity management, and financial intermediation are likely to need fundamental restructuring*[3]". And as can be seen from Rutherford's work, the nature of the relationship between the client and the front-line staff, of necessity, changes (this is discussed further below).

Furthermore, international rollout of Grameen II will almost inevitably mean a more diverse implementation of the Grameen "model" as the real needs and demand of the poor in the different countries and regions where the replicators work are reflected in product and delivery system design. Even without adopting many of the more challenging aspects of the Grameen II approach, the news that group guarantee or joint-liability is not to be enforced will challenge the basic operational principles of many replicators, a substantial proportion of whom enforce joint liability with alarming zeal[4]. For many involved in microfinance, it has long since been apparent that after 3-4 loan cycles group guarantee is increasingly ineffective, and that ongoing access to financial services was the key to ensuring repayment. It is logical therefore that the higher the quality of those financial services, and the more responsive they are to clients' needs, the more likely clients are to repay on time. This conclusion is demonstrated in the large number of Grameen drop-out and defaulters who have returned and repaid long over-due loans to get access to Grameen II's new range of market-led products.

Looking forward it is possible to predict interesting times ahead for Grameen Bank. As it continues with its successful range of products it may face some difficult cultural adjustments. At present centre managers, who remain very close to their customers, often determine the products they believe are most suitable for their clients. But the gradual spread of product knowledge among Grameen members is putting much greater control into the hands of customers than has been case in the past. This suggests that the role of the centre manager as "teacher" may evolve to that of an officer who supplies information and financial advice to clients who themselves determine the products and services they require. Grameen Bank could explore the impact of these changes, by providing more detailed marketing information to clients in a pilot test area.

The gradual spread of product knowledge and increased transparency of services, may in turn have consequences for the delivery of products, with customers expecting more consistent levels of service across the institution. Greater consistency need not mean a lack of flexibility, if flexibility is designed into products and services. Indeed, consistency should enable easier identification of problems and consequent improvements in service levels. Moreover, greater consistency in delivery may be a prerequisite if benefits from the use of information technology are to be maximised. As Rutherford posits "*The potential of IT is waiting to be explored".*

Finally, with the rapidly increasing liabilities driven by the programmed savings product, Grameen will face increasing pressure to lend in order to finance the 12% per annum interest rate that these savings attract. Grameen is unlikely to find this level of return on investment in the traditional market place and is therefore likely to have to finance the interest payable through its own lending operations – either to its traditional client base (and those that have graduated out of poverty as they used Grameen Bank's services) or to the other better-off members who have joined the Bank to access the attractive contractual savings product.

We are privileged to have been able to work with Grameen Bank on this study, and are grateful for the support, enthusiasm and openness of the Grameen Bank management and staff. We are particularly delighted that Grameen Bank, as one of the flagship institutions of microfinance, has been shown to have responded so positively to the needs of the market – and emerged all the stronger and larger for having done so.

[3] See **Robinson**, Marguerite and Graham A.N. Wright, "Mobilising Savings", *MicroSave* Briefing Note # 3, Nairobi, Kenya.
[4] At the extreme one African Grameen replicator locks the groups into the meeting hall until they have settled all outstanding loan repayments for that week.