

Grameen Bank's Micro-Credit Model: A Comparative Study With Bangladeshi Commercial Banks' Micro-Credit Performance

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Abstract

Micro-credit has been found the most important tool for fighting with poverty through development of income generating activities among the poor, who do not qualify for bank loans under the traditional banking system. In 1983, Grameen Bank in Bangladesh revolutionized a new banking concept on the fact that credit is a basic human right; poor people must qualify for credits despite their financial and social status. At present, Grameen Bank, which mainly targets the rural women, is the most successful micro-credit institution in the world. Commercial banks in Bangladesh have also been engaged in micro-credit programs aimed at poverty alleviation. However, their success rates in these programs seem unsatisfactory. The study is intended to identify success factors of Grameen Bank, and assess the micro-credit programs of Bangladeshi commercial banks.

1. INTRODUCTION

Micro-credit allows the poor to have access to lending institutions to borrow at bank rates, and start their own small business. In 1976, Muhammad Yunus, a Bangladeshi economics professor first tried the targeted credit programs through an experimental project to test the credit worthiness of the poor without any physical collateral. He became successful in developing a micro-credit model in which group collateral substituted physical collateral. Finally, Grameen Bank was founded as a specialized bank in 1983. Currently, Grameen Bank is the largest rural finance institution in Bangladesh. It has more than 2.3 million borrowers.

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94 percent of whom are women. In 1996, Grameen Bank's contribution alone to GDP was 1.10% (Grameen Bank 1999).

Since 1960s, Bangladeshi commercial banks have been engaged in micro-credit programs targeted for the rural poor, mainly women. Although their micro-credit programs are performing better than their large-scale projects, micro-credit programs seem unsuccessful as in the case of Grameen Bank.

The study is intended to understand the concept of micro-credit model of Grameen Bank, evaluate micro-credit programs of some selected Bangladeshi commercial banks, identify the success factors of Grameen Bank, and explore the possibilities of replication of Grameen Bank's micro-credit model in the commercial banks.

2. RESEARCH METHODOLOGY

Data collection

At present, 35 banks are operating in Bangladesh. These may be categorized into 4 types (numbers are given in parentheses): nationalized commercial banks (2), private commercial banks (19), foreign banks (10), and specialized banks (4). As foreign banks and private banks are out of the scope of the study, they have been excluded from the sample. From among the nationalized commercial banks, Janata Bank has been excluded from consideration, as its micro-credit programs are similar to that of Sonali Bank. In the category of specialized banks, RAKUB has been excluded from the sample as it focuses on a specific region (Rajshahi) of the country. In fine, Sonali Bank (as nationalized commercial bank) and BASIC and BKB (as specialized bank) have been chosen as sample units for the study. The study draws most of its data from secondary sources. Data was collected in between December 1999 and January 2000.

Analysis

Both quantitative and qualitative analyses were done on the findings. The quantitative analysis included deposit mobilization (loan disbursement), coverage, recovery rate, profitability, and share in micro-credit programs. Qualitative analysis, on the other hand, was based on dependence on

NGOs/international donor agencies, the loan decision process, and involvement in social development programs. For each of the above criteria, banks have been ranked on a 1 to 4 scale. The qualitative ranking was based on personal judgment. Finally, an overall finding has been drawn combining the positions of each bank based on both the quantitative and qualitative criteria.

Previous Research and the Study

Several studies have been conducted to compare Grameen Bank, NGOs and micro-finance institutions' (MFIs) micro-credit activities in developing countries. One of the key success factors of NGOs and other MFIs appears to be the introduction of a social mechanism that lowers transaction costs (Yaron 1994; Stiglitz 1990). Its absence calls for the formal sector firms to adopt the same in their lending strategy, instead of being intervened by the government in the form of providing cheap and politicized credit to rural customers (World Bank 1994).

Commercialization of Grameen Bank's micro-credit model may minimize the social cost for the poor by way of overcoming the problem of market imperfection. The previous studies, however, ignored focusing on the possibilities of introducing Grameen Bank-type micro-credit model (collateral-free) in Bangladeshi (or similar) commercial banks. The current study provides an opportunity to compare Grameen Bank's micro-credit activities to that of commercial banks in Bangladesh, and provide recommendations for improving their positions based on the lessons learnt from Grameen Bank operations.

3. GRAMEEN BANK

Founded in 1983, Grameen Bank currently operates in 39,346 villages through its 1,140 branches in Bangladesh. 75% ownership in the bank is held by the poor while the rest remains with the Bangladesh government. The bank has a total of 12,850 employees (as of 1998). As of December 1999, Grameen Bank serves 2,352,867 people in Bangladesh. The bank charges 20% rate of interest per annum. In the year of 1998, the bank earned a net profit (before tax) of Tk. 62.60 million¹. As of December

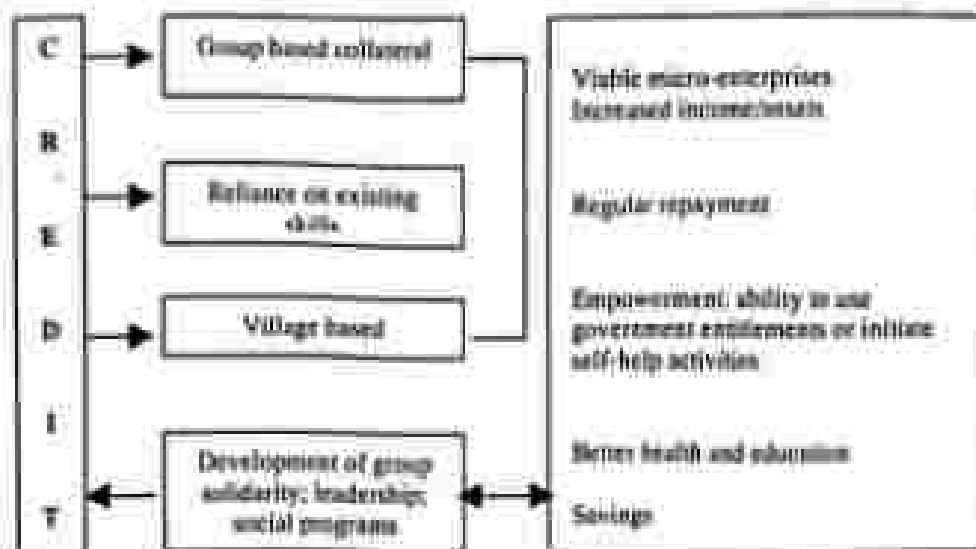
¹ Tk. refers to the Bangladeshi currency Taka. As of 1998, 1 US\$ = Tk. 46.50

1999, its recovery rate stands at 91.06% (Appendix 3). Grameen Bank's collateral-free micro-credit has been replicated in many countries in the world.

The Grameen Bank Micro-Credit Model

The Grameen Bank micro-credit model has been shown in Figure 1.

Figure 1: Grameen Bank's Micro-Credit Model



Source: Helcombe, Susan; *Managing to Empower*; University Press Limited, Dhaka 1995, page-39.

Grameen Bank's flexible organizational structure allows the borrowers (identified as bank members) participate in the loan decision process. Its group approach of 5 like-minded members (and the "center" concept where weekly meetings are held, and all transactions take place) to targeted credit along with strict monitoring and supervision of projects makes the micro-credit programs a success. The bank has a well-trained and dedicated work force; they are given enough authority to fix terms and conditions of loan agreements in field operations. They are highly motivated in serving the rural poor.

Grameen Bank programs are of two types: economic development programs and social development programs. The economic development programs are meant to provide financial security to the poor in case of unprecedented events. These include group fund, emergency fund, special savings fund, and children's welfare fund. The social

development programs include workshop, center school program, and supplies and skill training.

4.0 Micro-Credit Programs - Bangladeshi Commercial Banks' Experience

4.1 Sonali Bank

Sonali Bank, the largest state-owned commercial bank in Bangladesh, was established in 1972. As of March 1999, the bank has 1,311 branches (427 in urban areas, 884 in rural areas) in the country, while 7 branches are functioning outside Bangladesh (6 in UK, 1 in India). As of December 1998, the bank has a paid-up capital of Tk. 3,272 million. Sonali Bank had a total of 26,125 (officer: 11,629, staff: 14,496) manpower by the end of 1998.

Sonali Bank's activities include deposit mobilization and funding productive and priority sectors- crop and agro-based sub-sectors. For its micro-credit programs, the bank follows the group approach, which stands as a guarantee for the collateral-free credit. Compare to other banks, groups formed in Sonali Bank's micro-credit programs are of larger size (5-20 members). The bank charges 10%-12% interest rates with a loan ceiling between Tk. 10,000 and Tk. 15,000. Borrowers repay the loans through installments within 1 year (sometimes, 2 years). Beneficiaries' suggestions are not valued in the loan decision process. The bank is dependent on Partner Organizations (NGOs and international donor agencies), for funding and providing technical assistance to run its 14 on-going micro-credit programs in the country. It earned a profit (before tax) of Tk. 105,358 million in the year of 1998. The bank's recovery rate in micro-credit programs stands at 88.94% (as of June 1998). However, Sonali Bank's micro-credit programs are not well organized. Lack of proper training along with lengthy process of loan decisions and inadequate supervision prevents the bank utilize its funds more efficiently.

4.2 Bangladesh Krishi Bank (BKB)

Established in 1973, BKB is a 100% government owned specialized bank engaged in agriculture financing. As of March 1999, the bank had a

paid up capital of Tk. 1,000 million. As of December 1998, the bank has 836 branches and 11,472 employees.

BKB's activities include deposit mobilization and funding productive and priority sectors- crop and agro-based sub-sectors, such as crop, livestock, poultry farm, fishery, and tea loan. Like other banks, BKB also follows the group approach of micro-credit programs, which stands as a guarantee for the collateral-free credit. The bank targets the land-less and marginal rural farmers. It charges 10%-12% interest rates (flat) or 10%-16% reducing balance interest for its micro-credits, the maximum loan size being Tk. 10,000 per person. Loans are repayable at 50 equal weekly installments. The bank's micro-credit programs do not allow participation by the borrowers in the loan decision process, and are highly dependent on Partner Organizations. Out of total 17 micro-credit programs, only 4 are conducted by the bank itself. Rest of the programs is collaborative with NGOs and international donor agencies, which provide fund and technical assistance to the bank. BKB incurred a net loss of Tk. 2,062 million in the year of 1998. The bank's recovery rate in micro-credit programs stands at 71.58% (as of June 1998), which is not satisfactory. Lengthy loan decision process and inadequate supervision result in such low performance in the micro-credit programs.

4.3 Bank of Small Industries and Commerce Bangladesh Limited (BASIC)

Established in 1988, BASIC is a 100% government owned scheduled bank. At the end of 1998, the bank had a paid up capital of Tk. 160 million. At present, it has 22 branches and 368 employees. The bank has a policy of providing 50% of its fund to small scale and cottage industries.

Like other banks, BASIC's activities include deposit mobilization and funding the priority sector- small and cottage industry. The bank targets the urban poor who earn less than Tk. 5,000 per month for its 4 on-going micro-credit programs. The programs are conducted through 3 modes: BASIC-NGO-beneficiary, BASIC-beneficiary with NGO supervision, and BASIC-beneficiary without NGO supervision. BASIC's loan size varies from Tk. 2,000 to Tk. 15,000 per person. It charges the market rate of interest for its credits. Loans are repayable in equal installments within 2 years. For monitoring and supervising projects, the bank is dependent

on NGOs to some extent. BASIC earned a profit (before tax) of Tk. 227 million in the year of 1998. As of June 1999, the average recovery rate in micro-credit programs was 97%, the highest being 100%, and the lowest 77%. However, lack of staff training in serving the rural poor and absence of rural branches prevent the bank undertake a number of projects under its micro-credit schemes.

5.0 THE FINDINGS

- 1) BASIC has been found the most profitable (in terms of return on total assets) among the 4 selected banks; while BKB was found incurring substantial losses (Table 1).

Name of the Bank	Average profit (loss) 1997-98	Average total assets 1997-98	Return on total assets (%)	Rank
Grameen Bank	59	19,435	0.3036	2
Sonali Bank	56,745	189,966	0.2987	3
BKB	(1,820)	49,557	—	4
BASIC	199	4,986	5.99	1

Source: *Activities of Banks and Financial Institutions 1998-99*, Ministry of Finance, Bangladesh

- 2) Grameen Bank provides nearly half (47.39%) of the entire micro-credit loans to the poor in Bangladesh. NGOs play more important role (25.89%) than commercial banks in micro-credit activities (Table 2).

	Disbursement (cumulative) in Tk. million	Percentage
Government Organizations	16,063.40	7.75
NGOs	53,644.00	25.89
Banks	39,289.80	18.97
Grameen Bank	98,171.10	47.39
Total	207,168.30	100.00

Source: *CDF Statistics 1998*, Grameen Bank, and Ministry of Finance, Bangladesh

- 3) Grameen Bank is the most efficient in deposit mobilization (3,160%). Among the three selected commercial banks, BKB mobilizes its deposit in the most efficient way (20.57%). BASIC's deposit mobilization rate is very low (Table 3).

Name of the Bank	Deposit	Disbursement	Deposit mobilization (%)	Rank
Sonali Bank	152,795	28,197.80	18.45	3
BKB	20,380	4,193.30	20.57	2
BASIC	4,509	100.21	2.22	4
Total	177,684	32,491.31	--	--
Grameen Bank	5,897	186,365.39	3,160	1

Source: *Activities of Banks and Financial Institutions 1998-99*, Ministry of Finance, Bangladesh; and Annual Reports (1997-98 & 1998-99) of the concerned banks

- 4) As of June 1998, BASIC's recovery rate has been found the most satisfactory (98%) in micro-credit programs, followed by Grameen Bank (94%) and Sonali Bank (88.94%). BKB's recovery rate has been found unsatisfactory (71.58%) (Appendices 3 and 4).
- 5) Among the 4 selected banks, Sonali Bank serves the highest beneficiaries (220 per employee) through its micro-credit programs. BKB, on the other hand, serves the least beneficiaries (Table 4).

Name of the Bank	No. of Employees	No. of beneficiaries	No. of beneficiaries per employee	Rank
Grameen Bank	12,890	2,368,347	184	2
Sonali Bank	26,125	5,745,011	220	1
BKB	11,472	718,280	62	4
BASIC	368	30,230	82	3
Total	50,815	8,851,768	174 (average)	--

Source: *Activities of Banks and Financial Institutions 1998-99*, Ministry of Finance, Bangladesh; and Micro-credit Handouts of the concerned banks

- 6) Grameen Bank depends on international donor agencies for sources of funds only. BKB is highly dependent on both NGOs and donor agencies for both sources of fund and supervising micro-credit

activities. BASIC, however, depends on NGOs for supervisory assistance only (Table 5).

Table 5
Dependence on Donor Agencies/NGOs

Name of the bank	State of dependence	Remarks	Rank
Grameen Bank	Low dependence	Depends for fund only	1
Sonali Bank	Moderate dependence	Some % of the projects are NGO/donor-assisted (for both fund and supervision)	3
BKB	High dependence	Most of the projects are NGO/donor-assisted (for both fund and supervision)	4
BASIC	Low dependence	Depends on NGOs for supervision mainly	2

7) Grameen Bank highly delegates authority to its field staff to fix terms and conditions of the loan agreement. As a result, the bank can approve the loan within a very short time (2-4 weeks). Sonali Bank and BKB do not allow their field officials to have significant authority over loan decisions. Besides, Grameen Bank welcomes suggestions from its members (borrowers) so as to improve the viability of any projects. These features are absent in Sonali Bank, BKB and BASIC's loan decision process (Table 6).

Table 6
Loan Decision Process of the banks

Name of the Bank	Approval & disbursement period	Participation by borrowers	Staff authority	Supervision	Rank
Grameen Bank	2-4 weeks	Active	High	Tight	1
Sonali bank	2-6 months	passive	Moderate	flexible	3
BKB	3 months	passive	Low	flexible	4
BASIC	1 month	passive	Moderate	tight	2

8) Grameen Bank is highly involved in social development programs. These include formal education and training, group fund scheme, and emergency fund scheme. BASIC, on the other hand, has the least involvement in social development programs. Both Sonali Bank and BASIC are involved in such activities to some extent (Table 7).

Table 7

Involvement in Social Development Program	Rank
Grameen Bank	1
Sonali Bank	3
BKB	2
BASIC	4

9) Sonali Bank and BKB perform well (recovery rate above 90% and 100%, respectively) in those donor-assisted projects, which are supervised by BRDB² or other similar agencies. On the other hand, recovery rate of those donor-assisted/NGO-supported projects, which are supervised by the banks' officials only, are quite unsatisfactory (recovery rate less than 60% and 70%, respectively) (Appendices 5 and 6).

10) BASIC performs very well (recovery rate 100%) when the loan is disbursed to NGOs, which again lend the amount to the beneficiaries. On the other hand, performance is not satisfactory enough (recovery rate 77%) when BASIC disburses loans to the beneficiaries first, and then NGOs supervise the project implementation phase (Table 8).

Table 8
 BASIC's Micro-Credit Performance (as of June 1999)
 (in Tk. million)

Mode of disbursement	No. of beneficiary	Amount disbursed	Amount outstanding	Recovery rate (%)
BASIC-NGO-beneficiary	28,662	86.84	79.61	100
BASIC-beneficiary with NGO supervision	8	0.32	0.24	77
BASIC-beneficiary	1,560	13.05	6.43	97
Total	30,230	100.21	86.28	97*

Source: Bank of Social Industries and Commerce Bangladesh Limited (BASIC)

5.1 Overall finding

Grameen Bank has been the most successful in micro-credit programs among the selected banks (Table 9), followed by Sonali Bank and

²BRDB: Bangladesh Rural Development Board

BASIC, respectively. However, BASIC serves the poor on a limited scale. Among the 4 selected banks, BKB has been the least successful in micro-credit programs.

Table 9
Overall Position in Micro-Credit Programs
(1 to 4 scale; 1=best position, 4= worst position)

Criteria	Grameen Bank	Sonali Bank	BKB	BASIC
1. Deposit mobilization	1	3	2	4
2. Recovery rate	2	3	4	1
3. Coverage (beneficiaries/employee)	2	1	4	3
4. Independence of donors/NGOs	1	3	4	2
5. Loan decision process	1	3	4	2
6. Social development program	1	3	2	4

Reference: Findings 2, 4, 5, 6, 7 & 8

5.2 Discussion on findings

BASIC, by targeting the urban poor to a limited scale, enjoys the advantage of low credit delivery costs, which in turn, results in higher profit. Grameen Bank has been making less profit (in terms of total assets) than BASIC. This may be caused by higher credit delivery costs in the rural areas. Close monitoring and supervision require substantial investment in human resources and logistics support. However, BASIC's overwhelming success in micro-credit programs does not necessarily mean that urban areas provide more opportunities than that of rural areas. Rather, the bank's close monitoring and supervision of the projects, which are operated in a very limited scale, contribute to such excellent performance.

Sonali Bank's profitability is not satisfactory, which might be the result of high fixed cost of labor (as of December 1998, total employee was 26,125, twice as much as other banks). BKB most probably has been suffering from the low recovery rate on loans granted and high fixed costs such as over-manning. Strong trade union and bureaucracy along with de-motivated work force prevent the bank to re-orient its activities to promising ventures.

Commercial banks and NGOs have different mission. NGOs aim at helping the poor so as to facilitate improving their economic and social

conditions. Grameen Bank also has similar objectives. Commercial banks, on the other hand, aim at increasing their profitability. For them, involvement in poverty alleviating activities is not the prime concern. Moreover, it is convenient for commercial banks to engage themselves in large-scale projects, which are easier to monitor and supervise with their existing resources.

Highest deposit mobilization rates of Grameen Bank show that for granting loans to the members, it highly depends on foreign banks and international donor agencies at competitive interest rates. It indicates the bank's viability as a borrower.

BKB's share in micro-credit programs has been found high because of its specific focus area- the agricultural sector. BASIC, being a new-player in micro-credit programs is still focusing on the urban poor with limited resources. This might be caused by "cautious attitude" of the bank, which seeks to avoid losses from the very beginning.

Of the 4 selected banks, only Grameen Bank has the trained work force and logistic supports enabling it to monitor and supervise micro-credit projects very closely. However, due to lack of adequate sources of fund, the bank has to rely on foreign loans on competitive basis. Grameen Bank used to get grants from international donor agencies until last 2 years. Now, the bank has become self-sufficient in the context that it can borrow at competitive rates from those agencies, rather than accepting grants. However, the bank still receives economic subsidy from the Bangladesh government. The other 3 banks (Sonali Bank, BKB and BASIC) are dependent on NGOs/donor agencies for supervising their micro-credit programs to a great extent. Lack of adequate trained work force and logistics support result in high dependence on NGOs and donor agencies. However, of the 3 banks, BASIC's micro-credit programs are funded by itself. This might be possible as the bank serves only a very small portion of the urban poor.

The findings show Sonali Bank and BKB's inadequacy in monitoring and supervising micro-credit projects. One of the reasons may be the lack of technical know-how of micro-projects by the bank staff. International donor agencies and BRDB have the expertise in delivering credit to the rural poor. They are also able to provide technical know-how for the

projects. Therefore, joint projects with them make Sonali Bank and BKB successful.

In the case of BASIC, it has been found that NGOs monitor and supervise closely when they are directly participating in the loan decision process. It implies that their monitoring and supervising activities of BASIC's projects are directly related to financial matters (lending to the poor and earn profit by themselves). Another reason may be that NGOs prefer direct involvement in the entire projects to merely performing the role of supervisor, which could enhance their acceptability as micro financial institutions.

5.3 Factors contributing to the success of Grameen Bank's micro-credit programs

Factors that contribute to Grameen Bank's success include close relationship between the bank and the borrowers; understanding among the borrowers themselves; peer pressure (in case of loan default) and support (in case of difficulties); targeting the rural women, who are more practical than men; reaching the poorest of the poor; motivated work force with adequate authority; transparency; ownership mode; and visionary leadership by Prof. Muhammad Yunus.

Grameen Bank, however, is not free from criticism. The bank operates in a limited area; its personalized approach is viewed expensive and risky. It expanded too fast to conform quality in all branches; the bank has very limited formal checkpoints too. Grameen Bank has not been successful in including everyone, who falls within the target population, in its groups. It is often argued that the bank does not attempt to make the poor people rich, but simply less poor. However, the bank has succeeded in its ultimate goal- reaching the poor at the bottom and serving them efficiently.

5.4 Factors contributing to the failure of commercial banks micro-credit programs

Factors that contribute to commercial banks' failure include unfriendly legal environment (especially the Banking Companies Act, 1991) that prohibits loan sanction without physical collateral; lack of top management vision; bureaucracy; inadequate employee training and

motivation; lack of customer focus; lack of logistics support, especially information technology; and weak monitoring and supervision of the projects.

5.5 Limitations of the study

The study suffered from the lack of common comparison base among the selected banks. To overcome this problem, data for a very short period (1 or 2 years in some cases) were used. Findings were analyzed both quantitatively and qualitatively. Qualitative analysis was based on personal judgment. No published relative weight of the criteria was available for this purpose. Thus, findings may not necessarily represent the real situation. However, the overall finding was based on equal weight for all the factors (deposit mobilization, recovery rate, coverage, donor dependence, loan decision process and social development programs), which signal the status of micro-credit programs of the banks. This offsets any shortcomings, which could be generated from the use of qualitative factors on the basis of personal judgment.

5.6 Lessons learnt

Lessons learnt from the success stories of Grameen Bank are:

- i) physical collateral cannot be a prime requisite for getting loans from banks
- ii) mutual trust and respect between the banks and the borrowers are essential
- iii) access to credit should be provided in conjunction with other social development services
- iv) the poor do not default to loans willfully; women are the better entrepreneurs.
- v) a well-trained and dedicated field staff can make genuine efforts a success, and
- vi) top management vision and support are necessary for successful undertaking of micro-credit projects

5.7 Recommendations

Grameen Bank has been successful in pursuing its main objective; serving the poor with competitive price. The bank should maintain status

quo at least for some years (e.g. 5 years). This will enable the existing resources to mobilize among the various units within the bank and develop formal checkpoints for ensuring accountability in each activity. Bangladeshi commercial banks, on the other hand, need to re-orient their activities to micro-credit programs. Due to different settings, the banks should not replicate the Grameen Bank's micro-credit model as it is. The banks should establish "special micro-credit units", recruit young professionals with outstanding background, and authorize them to react in the real operating environment, i.e. dealing with the rural poor. For motivation purpose, rewards must be linked to performance. As commercial banks do not have enough logistics support for credit delivery to the rural poor, it is suggested that the banks and NGOs set up a "common cell" to learn each other's experience in working with the rural society. Finally, the Bangladesh Government should modify the Banking Companies Act 1991, and provide all-out supports (by not intervening banks' activities) to the commercial banks in undertaking micro-credit programs aimed at poverty alleviation.

6.0 CONCLUSION

Grameen Bank's micro-credit model has established one of the basic human rights: access to credit. The overwhelming success of the bank suggests that Bangladeshi commercial banks (or similar) should undertake such micro-credit programs, after some modifications. This hopefully will result in better recovery performances, and higher profitability at the end. Thus, through enhancing the scope for increased income-generating activities among the poor, commercial banks would be able to play due role in poverty alleviation.

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