



TO: Catherine Gwin
FROM: Kamal Ahmad *Kamal Ahmad*
DATE: November 1, 1990
SUBJECT: Grameen Trust

CC: Peter Goldmark, Ken Prewitt, Phil LaRocco

1. As requested, I have reviewed the docket item for Grameen Trust and the background materials in your files. This memo is intended to provide you with some additional information that may be helpful in considering the proposal, as well as to offer you with my own assessment of the project idea. Moreover, as my assignment for LaRocco Associates requires, I have also sought to see if there is any "bargain" to be made in this area.

2. As you have noted in the docket item, "The Grameen Bank is a development success story." The Bank has succeeded in elevating the income levels for the 600,000 households which participate in its program. That Grameen Bank has enhanced the income potential of the marginalized population in its target villages has been documented in a study by the Bangladesh Institute of Development Studies (BIDS). (There is no data, however, showing the profitability of Grameen ventures.) Other studies have noted the significant social and cultural transformation that have resulted from Grameen's efforts. Although in certain quarters the management style of Grameen has been described as "quasi-military", the organizational genius of it is clearly demonstrated by the exponential rate at which it has grown while retaining its standard of high repayment. (The Phase II operations of Grameen in 1986-88 increased the number of branches from 152 to 500).

3. At the core of Grameen's success lies a series of tactics that were adopted through trial and error. These are: (i) Peer pressure as a substitute for collateral; (ii) Loans in small sizes; (iii) Weekly repayments; and (iv) The belief of "Borrowers Know Best" as to what to do with their money. The first three of these items are self explanatory. The fourth, however, requires some explanation. The notion of "Borrowers Know Best" has meant that the vast amount of Grameen's funds have gone into supporting a survival economy where no new technologies are introduced and problems of marketing and management are avoided. This is not to say that the Bank's lending has systematically reduced risk. The single most popular item for lending in the Grameen portfolio is the purchase of milk cows -- a fairly risky venture in a setting where animal morbidity and mortality are high. At the economic front, Grameen has allowed the villagers to do more of what they had always done -- activities related to livestock and fisheries (46% of general loans in 1987); milk cows (27% of general loans the same year); and paddy husking (15%).

4. Grameen has been successful in the first tier of microlending. The \$67 loans are invariably paid back. A number of significant social and cultural practices, most notably the status of women, are altered in the process of organizing Grameen groups. (Curiously enough, institutionally Grameen remains heavily male dominated and hierarchical, typical of most institutions in Bangladesh).

5. There are problems with the above approach which can be broadly described as "the problem of two plateaus". First, there are limits to the demand for traditional products and services in a village economy. In other words, only so many people in a village can get into rice husking and raising poultry and milk cows. After a certain point, under the existing system of minimal management and marketing involvement, the demand for such loans are bound to plateau. Already this problem has risen in older Grameen Bank branches. It is in those pioneering branches that Grameen faces its real tests of success.

Second, according to available evidence, 48% of Grameen Bank village members lived in extreme poverty compared to 75% for non-members. While these figures are encouraging in some ways, as a Bangladeshi my own sense is the economic leap made possible through Grameen Bank falls short of what is desperately needed. Unless Grameen can graduate its borrowers to a stream of higher value-added activities, I fear that the initial gains will soon begin to stagnate and the income level of Grameen borrowers will plateau at a level much below an acceptable one from the point of view of poverty alleviation.

6. Experience to date indicates that if Grameen forays into higher levels of management and introduces new technologies, it begins to face considerably higher prospects of failing. Marketing becomes an issue with which borrowers find themselves unable to deal. All this is not surprising given the fact that vast majority of Grameen borrowers are illiterate, with minimal contact with modern technology and the world beyond their individual villages. Moreover, once the Grameen borrowers start getting involved with larger enterprises I would suspect that they would come directly in conflict with the power holders, jeopardizing the tacit understanding with the village elites that the Bank has so far been able to forge.

7. Professor Yunus is clearly aware of this issue. In 1984, Grameen created SIDE (Studies, Innovation, Development & Experimentation). This group was set up (with support from the Ford Foundation) within the Grameen Bank to help introduce new technologies and skills to Grameen borrowers for enterprises that would be collectively owned and managed. However, as the 1988 Donor Consortium's Appraisal Report says "Because of problems in finding borrowers who would adopt any experimental techniques and difficulties encountered with loans for joint activities, SIDE changed its strategy and became an entrepreneur."

Grameen Bank started the unenlightened practice of lending itself monies to launch larger enterprises that its borrowers would not commit themselves to. Moreover, this arm of Grameen started acquiring from the Government of Bangladesh for-profit enterprises such as fish farms often in areas with little Grameen Bank presence. The Donor Consortium reported that "the large enterprises are particularly risky and have yet to establish a record of profitable operation." It noted that "The Loan Approval Committee is engaged both in the running of these enterprises and in providing credit to them" which it went on to say was "in conflict both with the profit center theory and prudent banking practice." It was suggested that if Grameen wanted to continue its practice of using SIDE as its venture fund it ought to separate this function from the Bank by establishing a different entity, preferably a Trust. It was argued that a Trust could shield Grameen from suffering a deteriorating repayment rate resulting from the failure of SIDE ventures as well as eliminate the conflict of interest arising from the Bank lending funds to itself.

8. The Grameen Trust was established to take over the high risk ventures from the portfolio of SIDE projects. In experimenting with these new ventures, it was also expected to address the structural problems associated in graduating microlenders from a survival economy to a more profitable economic domain where the potential for value-added is greater. I recently came to know that the Ford Foundation is in the process of transferring to the Trust over U.S. \$1 million of a PRI originally made to the Grameen Bank to help with the above purpose. The importance of understanding the issue of enterprise transformation cannot be overestimated. It deserves to be clarified before Grameen embarks on a replication project which will have a longer-term program horizon. (It is noteworthy that neither Grameen Trust nor Ford Foundation has given RF any indication of the impending transfer of the Bank's PRI funds to the Trust).

9. In this connection, I would like to note that the Trust's "Statement of Purpose" (copy attached) makes no reference to it undertaking any replication effort in the first ten objectives. It is only in the eleventh objective that the Statement hints at such a possibility: "To offer training and consultancy services to other national and international organizations relating to the objects of the Trust."

10. Given the paucity of development successes worldwide, it is not surprising that there would be a strong interest in replicating a model such as Grameen that appears to be working. There is nothing new or innovative in that practice. In fact, there is a long pedigree in such thinking. The highly successful development models of the West were ill-fatedly adopted for "replication" in the developing world. The microproject successes too received similar attention. Bangladesh -- the setting where the Grameen Bank made its debut -- was in fact the site of a brilliant success story in the 1960s -- the Comilla Experiment

spearheaded by the legendary Akhtar Hameed Khan. The Dairy Development Board in India was another one. The record to date, however, indicates that replication is not easy and rarely achieves the success of the original project. Somehow the strategy that worked so well in Gujarat (a natural milk shed) didn't quite work as well in Punjab (where the people preferred to drink their milk rather than selling it to a Cooperative as the Gujaratis did). This is not to say that replication as an objective is doomed. Certain lessons can obviously be learnt from past experiences. Your docket item clearly takes cognizance of it as it states "If only as many as 25% of the assisted replication project succeed over the next five years in establishing and sustaining Grameen-type institutions, officers will consider that outcome a major success."

11. Grameen's success can be traced, in addition to its operational tactics outlined earlier, to many characteristics peculiar to Bangladesh. The high population density in Bangladesh villages has allowed Grameen Bank's labor-intensive operations to be cost-effective because of the participation of a large number of borrowers per bank worker. The vast pool of unemployed high school and university graduates in Bangladesh has made it possible for Grameen to easily recruit its 10,000 staff of bank workers at a relatively low cost. (The World Bank reported, for example, that in one African country it was estimated that an institution serving a largely noncorporate clientele would require a minimum of 2,500 deposit accounts to cover the cost of a single employee for a year!) Not insignificantly, the long history of usurpation by village money-lenders and the consequent hatred that they have engendered in public minds have helped build Grameen's image as a liberating agent that Grameen look-alikes elsewhere may not have.

The point here is simply that the local conditions in Bangladesh which have paved the way for Grameen's success can be quite different from the conditions in other parts of Asia or Latin America or Africa. There is also little point in trying to replicate Grameen in settings where indigenously bred highly successful microenterprise projects already exist: The BKK in Indonesia could be considered to be just as successful as would be case with ADEMI in the Dominican Republic and several other programs developed by ACCION over the years. Even in Africa the so called ROSCAs (Rotating Savings and Credit Associations) have a good record of success. A sound replication project ought to be able to introduce to possible new entrants in the field a range of successful practices and principles at work instead of selecting those experiences out. Monopoly is bad in capitalism; it is worse in the arena of ideas and experiences.

12. Microenterprises have an important role in alleviating poverty, and it is the creation of microenterprises that is at the heart of Grameen experience. But Grameen and Grameen-like initiatives need a strategy that will encompass a longer time horizon. It strikes me that Grameen needs to figure out this part of

its strategy rather than spend all of its time and energies trying to replicate a model which might very well run out of fuel in a few years. It should be noted again that the very task of client graduation through experimenting with new forms of enterprise and technology stands as a key element of the Trust's mandate as expressed in its original statement of purpose.

13. In order for the Rockefeller Foundation or others to support Grameen type initiatives -- which is simply a tactic to make available a greater level of resources for microenterprises -- at least three issues will have to be dealt with. First, there needs to be a systematic effort to address the question of graduating microborrowers. Second, it would be helpful to start building a network of organizations that would increase the demand for successful microlending across the developing world. The proposed Grameen Trust project could help in that process. However, as it is presently formulated it isolates only one model of microlending for replication worldwide. Other already established successful models such as BKK in Indonesia, ADEMI in the Dominican Republic and a variety of Rotating and Savings & Credit Associations (ROSCAs) are wholly ignored. A less proselytizing approach that would expose would-be microlenders to different successful methods would offer more potential.

Third, microenterprises is an area where many large donors have already committed a significant share of their resources. The U.S. Agency for International Development (USAID) has been Congressionally mandated to provide at least \$75 million dollars a year to such projects; the Inter-American Development Bank intends to provide loans of up to \$100 million dollars in this fiscal year for microenterprises. While the AID funds (which are all grants) can go into supporting NGO projects without routing the money through Government ministries, IDB loans require Government guarantees and normally need to be disbursed through Government ministries. The International Consortium of Donors for Small Enterprise now has a membership of nearly two dozen international agencies with substantial investments. In such a context RF's involvement in this sector is likely to make an impact if it focuses on (i) **overcoming structural problems associated with microenterprise graduation that have not received adequate attention from donors yet; and (ii) leveraging resources for microenterprises at a much higher order of magnitude than is presently available.**

14. The Grameen Trust may very well be an appropriate institution to focus on the graduation issue. In parallel to that there might also be a "bargain" within this concept, one aimed at triggering a flow of resources well beyond the capacity of private foundations. The World Bank and other multilateral finance institutions currently lend money to governments only. In a few cases, as in the Togo Grassroots Development Project, the World Bank has financed NGOs. However, in all cases, the funds have to be channelled through the government because the

state has to act as a guarantor of all these loans. Such procedures rob the independence of NGOs and other autonomous organizations that engage in microlending. As in the Togo case, NGOs become an extension of the Government Ministry supplying them with the funds. As long as the state has to guarantee all such loans, it is unlikely that the multilateral financial institutions, such as the Bank, would be able to provide NGOs with monies for microlending without encumbering them with complex bureaucratic hassles and without hurting their independence. (The Togo Project provides concrete evidence to this effect). Moreover, microlending with a few exceptions has not been a popular agenda in Government circles. Hence, it is unlikely that governments will seek major increases in multilateral funding for such projects. Yet, without a guarantee from a creditworthy institution -- in this case the State itself -- the World Bank and others cannot lend money at their highly favorable rates. **A "bargain" through which foundations and others could combine and substitute for the State in guaranteeing loans from the World Bank for microlending by Grameen and Grameen-like institutions in the South could lead to the establishment of a new window of lending in multilateral financial institutions.** Within the World Bank System, IBRD and IDA lend to the governments, the International Finance Corporation (IFC) lends to private corporations, and this proposed window could lend to the so called "third sector" with guarantees from their well-endowed counterparts in the North. The World Bank currently lends at or around 7% for IBRD countries and at less than 1% for IDA countries -- a margin of subsidy that might allow these loans to be repayable by projects like Grameen. Therefore, it is possible to envision a lending arrangement through which foundations could jointly guarantee up to \$500 million of World Bank/Asian Development Bank/African Development Bank funds for lending to NGO-sponsored microprojects in the developing world. Such a venture would minimize the possibility of government intrusion in Bank-funded NGO projects as is the case now as well as significantly increase the total volume of dollars available for microprojects.

15. The Rockefeller Foundation because of its entrepreneurial image in the outside world is particularly well suited to pursue this idea. As a first step in this direction it could assemble a small group of economists and others who have been studying microenterprises. Several of the most prominent academics who had seriously looked into the economics of microenterprises are RF alumni: Donald Mead of Michigan State University, who did much of the available empirical work demonstrating the viability of microenterprises and currently manages the most extensive data base on microenterprises anywhere, was an RF employee in Uganda; Charles Mann of the Harvard Institute for International Development

(HIID) is another former RF staff. Such a group, in collaboration with Grameen Trust and others, could focus on the graduation aspects of microenterprises and advise the Foundation on possible demand for additional funding for microenterprise projects as well as the potential of creating the "third window" of lending in multilateral finance institutions.

16. In short, the Grameen Trust initiative is a fundamentally sound idea that should be re-formulated to pay more attention (1) to the problem of graduating lenders and lending; (2) to use Grameen Trust as a magnet for disseminating training about more than just the Grameen model; and (3) as a platform for triggering greater donor flows to Grameen-type initiatives and, in turn, to microenterprises.

17. Attached for your information is a recent article from Time magazine on Grameen and the statement of objectives of the Trust. Please let me know if I can provide any further information.