

Grameen Bank Has Hit a Repayment Snag (from the Wall Streetz Journal)

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Grameen Bank, Which Pioneered Loans For the Poor, Has Hit a Repayment Snag

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Microcredit is a great idea with a problem: the bank that made it famous.

Grameen Bank, launched in Bangladesh in 1976 by an economics professor named Muhammad Yunus, popularized the idea of giving poor people tiny loans to launch businesses. The bank has helped inspire an estimated 7,000 so-called microlenders with 25 million poor clients worldwide.

To many, Grameen proves that capitalism can work for the poor as well as the rich. It has become an icon for the drive to give needy entrepreneurs a share in economic development. And that iconic status owes a lot to an almost miraculous loan-repayment rate of 'over 95%,' as the bank's Web site says. (www.grameen.org) But Grameen's performance in recent years hasn't lived up to the bank's own hype. In two northern districts of Bangladesh that have been used to highlight Grameen's success, half the loan portfolio is overdue by at least a year, according to monthly figures supplied by Grameen. For the whole bank, 19% of loans are one year overdue. Grameen itself defines a loan as delinquent if it still isn't paid off two years after its due date. Under those terms, 10% of all the bank's loans are overdue, giving it a delinquency rate more than twice the often-cited level of less than 5%.

Some of Grameen's troubles stem from a 1998 flood, and others from the bank's own success. Imitators have brought more competition, making it harder for Grameen to control its borrowers. The bank's loan portfolio grew rapidly in the early 1990s, but it has now shrunk to 1996 levels, at \$190 million. Profits have declined about 85%, to the equivalent of \$189,950 last year from \$1.3 million in 1999. The bank, with 1,170 branches, all in Bangladesh, has high operating costs. Grameen would be showing steep losses if the bank followed the accounting practices recommended by institutions that help finance microlenders through low-interest loans and private investments. And the situation may be worse than it appears; the bank is converting many overdue loans into new 'flexible' loans that Grameen reports as up-to-date.

Safeguarding an 'Idea'

Microlenders have been reluctant to call attention to Grameen's troubles. 'Grameen's repayment rates have never been as good as they've claimed,' says Jonathan J. Morduch, associate professor of economics and public policy at New York University. 'Because Grameen has been so well-known, nobody has wanted to risk undermining the reputation of the idea.'

Microcredit is getting renewed attention as other poverty-fighting tools come under attack. Left-wing protesters accuse the World Bank of selling out the poor to corporate interests. Right-wing U.S. politicians argue that aid to the Third World has been wasted. U.S. lobbies often try to quash efforts to open American markets to imports from poor countries.

But microcredit is an idea everyone can agree on: It uses private enterprise, can be profitable and gets money straight to the poor. Bridging the gap between rich and poor 'will help eliminate conditions of despair and hopelessness that breed violence and extremism,' declares an e-mail message circulated after Sept. 11 by Bill Clapp, the chairman of Global Partnerships, a microcredit support organization based in Seattle.

Alarmed by Rumors

The microcredit industry knows its reputation rides largely on Grameen's. Damian von Stauffenberg, chairman of a Washington-based microcredit rating agency called Microrate, was alarmed by recent rumors of financial weakness at Grameen, even though the agency doesn't rate the bank. 'If it's true, it would be a blow to the rest of us, because of the symbol Grameen is,' Mr. von Stauffenberg says. He says he repeatedly asked a Grameen affiliate, Grameen Foundation USA, this summer for detailed information on the bank's loan portfolio, but got only a brochure and a 1998 annual report.

'I didn't hear back from him after that, so I assumed he had the information he wanted,' says Alex Counts, president of the foundation, which promotes Grameen in the U.S.

Mr. Yunus, a congenial man of 61, acknowledges that Grameen has had some repayment difficulties in the past five years. He blames political upheavals, the 1998 flood and management errors. Told that the Web site still claimed a 95% recovery rate, Mr. Yunus said it was through 'inefficiency' that Grameen hadn't updated some information. Grameen has added a footnote to the Web site saying the information was true as of 1996. But more recent figures still aren't listed.

The repayment troubles are temporary, according to Mr. Yunus. 'There is no problem,' he said in an August interview in his modest office, which has no air conditioning despite Bangladesh's steamy climate. He says three-fourths of borrowers repay on time every week, and Grameen assumes that the poor will repay even long-delinquent loans. The bank, he says, is stronger than ever.

Mr. Yunus says borrowers have surprised him with their ability to take on new challenges. Borrowers who reach a certain level of savings can buy one share in Grameen, and collectively they own 93%. Mr. Yunus is setting up a mutual fund allowing borrowers to invest in other ventures under the Grameen umbrella: mobile phones, textiles and high-tech office space for rent on the top floors of the Grameen Bank tower.

'We have proved beyond a reasonable doubt that poor people are bankable,' Mr. Yunus says. 'We are not looking for charity.'

Grameen, which means 'village' in Bengali, got started after Mr. Yunus visited a village in southern Bangladesh. He met a woman who wove bamboo stools but had to sell them for meager profits to the man providing the materials. As an experiment, Mr. Yunus lent a total of \$27 to 42 women in the village. All of them repaid.

When Mr. Yunus approached the Bangladesh government for funds in 1979 to expand his experiment, government bankers were skeptical that poor, landless women would repay. So Mr. Yunus conducted an experiment in Tangail, a fertile district north of Dhaka. His staffers showed up unannounced in villages and recruited groups of women to take loans. Again, all of them repaid.

The '16 Decisions'

The new bank was a kind of small-business lender, with some unusual policies. It took no deposits at first. It lent only to poor women who had no collateral. Borrowers formed groups of five, each member getting loans only as long as everybody made payments. Borrowers recited Mr. Yunus's '16 decisions' -- including enforcing loan 'discipline' within the group, keeping families small and not giving a dowry for a daughter's wedding -- a difficult 'decision' to follow in this culture.

Grameen, which has provided millions of poor Bangladeshi women with access to credit, became the industry's symbol mostly through Mr. Yunus's personality and proselytizing. He set up the Grameen Trust, which gives loans and holds workshops for start-up lenders who have adopted the Grameen model from Arkansas to Zimbabwe, with mixed results.

Mr. Yunus is also the guiding force behind the industry's main public-relations vehicle, the Microcredit Summit. At the first summit, in Washington in 1997, Mr. Yunus sat at the head table at a private lunch with Queen Sofia of Spain and World Bank President James D. Wolfensohn, who ended the meal by giving Mr. Yunus a big hug. At a regional summit last month, he gave an opening address beside Mexican President Vicente Fox. Friends tout Mr. Yunus for a Nobel Peace Prize.

Mr. Yunus's 1997 autobiography, 'Banker to the Poor,' gave no hint of doubt in Grameen's future. 'All the strength of Grameen comes from its near-perfect recovery performance,' he wrote. 'It is not merely the money which is reflected through the recovery rate, it is the discipline.'

Even then, however, Grameen's recovery rate was slipping. In 1997, 4.6% of Grameen's loans were more than two years overdue, up from 0.7% a couple of years earlier. And Tangail has now become Grameen's worst region, with 32.1% of loans two-years overdue as of August.

One reason is that microlending has lost its novelty. In Tangail, signboards for rival microlenders dot a landscape of gravel roads, jute fields and ponds with simple fishing nets. Shopkeepers playing cards in the village of Bagil Bazar can cite from memory the terms being offered by seven competing microlenders -- a typical repayment plan for a 1,000-taka (\$17) loan is 25 taka a week for 46 weeks. At an annualized rate, that works out to 30% in interest. Surveys have estimated that 23% to 40% of families borrowing from microlenders in Tangail borrow from more than one.

Rebellious Borrowers

Borrowers have also become more rebellious. 'The experience was good in the beginning,' says Munjurani Sharkan, who became leader of a Grameen group in Tangail's Khatuajugnie village in 1986. To put pressure on 'lazy' group members who were slow making payments, she says she used to start removing the tin roofs of their homes. But one day, the whole group decided to stop making payments.

They were protesting Grameen's handling of a fund it created for each group, using 5% of each loan and additional mandatory deposits. The 'group fund' was meant for emergencies, but many borrowers wanted to withdraw money from the group fund. After a protest movement, complete with placards and amplified speeches, Grameen finally agreed to give borrowers easier access to the fund.

Borrower groups had become lobbying groups, and Mr. Yunus hadn't noticed the change, says Muhammad Yahiyeh, former director of Grameen Trust. 'An entire group would say, 'Unless you pay this person 5,000 taka, we will all stop paying,' ' says Mr. Yahiyeh, who now runs a small microlender. Mr. Yunus says he still thinks groups are good for loan discipline. Grameen just didn't explain the group fund properly, he says, and politicians stirred up the borrowers.

The typical Grameen success story features a woman who turns a small loan into a successful shop or craft business. But Grameen also has customers such as Belatun Begum, a borrower in Khatuajugnie since the late 1980s. She took one loan in three installments, totaling 30,000 taka (about \$525). She says the original loan was to buy a cow, but she actually gave some money to her husband, a well-digger, and used the rest to improve her house. She confesses to borrowing a neighbor's cow to show Grameen at meetings. One recent study found one-fourth of microcredit loan money in Bangladesh is used for household consumption.

Mr. Yunus says that doesn't bother him as long as borrowers repay. Grameen tells women to think of a loan as a mango tree and to eat only the fruits, he says, not the tree itself.

But Grameen introduced so many loan options in the early 1990s -- housing loans, student loans, seasonal loans -- that borrowers were often paying off one with another, says Aminur Rahman, an anthropologist based in Ottawa, Canada, who studied Grameen borrowers in a Tangail village six years ago. Returning earlier this year, he found only six of 120 borrowers were getting income from Grameen-funded investments.

Massive floods in 1998 hit Grameen's borrowers hard. The bank let borrowers skip several payments. Grameen borrowed \$80 million from Bangladesh's government banks, with a sovereign guarantee, and used the money to make new loans to borrowers. Informally, it forgave the old loans.

A 'Flexible Loan'

Grameen also bailed out borrowers whose problems had nothing to do with the flood. Ms. Begum, for instance, stopped paying when she had to provide dowries for two daughters. She skipped group meetings, but Grameen workers came to her door asking for her 200-taka weekly payment, she says. 'Let us make some income and we'll pay you,' she told them.

Earlier this year, Grameen came up with a proposal: pay just 50 taka a week for six months, and then take a new Grameen loan for twice the amount she repaid. Ms. Begum accepted. Grameen calls the program a 'flexible loan,' and treats the old, delinquent loans as back on schedule, as long as some regular payment is being made.

At a Grameen branch near Khatuajugnie, manager Mohammed Imam Modem shows his computer-printed ledger, full of cross marks to indicate missed payments. The rescheduling program and Grameen's personal visits to husbands as well as wives are improving the picture: The branch had 1,510 defaulters before; now it has 846. Attendance at weekly meetings is up to 66%, from 47% before.

'Grameen Bank's philosophy is not to abandon but to rehabilitate,' says Muzzamal Huq, a Grameen general manager.

But Grameen may simply be delaying inevitable defaults and hiding problem loans. One paper produced by the Consultative Group to Assist the Poorest, or CGAP, a donor group that sets industry standards, warns that heavy use of refinancing 'can cloud the ability to judge its loan-loss rate.' CGAP is a collective of 27 public and private donors, including the World Bank, the U.S. Agency for International Development and several U.N. agencies, that account for the vast majority of aid to microcredit institutions around the world.

CGAP says refinanced loans should at least be listed separately. Grameen doesn't do so. It says refinanced loans are one-fifth of its portfolio.

CGAP recommends that microlenders report as at risk the entire remaining balance of any loan with a payment more than 90 days overdue. The Palli Karma-Sahayak Foundation (PKSF), which Mr. Yunus helped set up in 1991 to distribute foreign funds to other Bangladesh microlenders, requires its microlenders to report as overdue any loan that is one week late. The average overdue rate among the foundation's lenders is 2%. It's impossible to know Grameen's overdue rate by that standard, since it reports only loans that are one year and two years overdue.

PKSF also says it requires borrowers to make a 50% provision against potential loan losses for any loan overdue by a year. Grameen made a 15% provision for such loans in 1999, and none last year. Following PKSF guidelines would have produced a loss of more than \$7.5 million for 2000 instead of Grameen's reported profit of less than \$200,000.

In early 1998, Grameen approached the International Finance Corp., the business-finance arm of the World Bank, about turning some of Grameen's portfolio into securities. The IFC declined to proceed, in part because Grameen 'didn't provide all the account information the IFC requested,' an IFC official said. The official requested anonymity because the IFC is reticent about discussing its negotiations with clients.

Mr. Yunus denied the IFC official's claims. He said Grameen is 'generously covered' against loan defaults.

Other microlenders have become much more stringent. Accion International, a U.S.-based network of microfinance institutions, requires its affiliates in Africa and Latin America to list as 'at risk' any loan overdue by 30 days or more. Asked about Grameen's two-years standard, Accion Chief Executive Maria Otero says, 'I don't think any [bank] superintendency in a million years would agree to something like that.'

Grameen Bank isn't under any formal supervision. 'They are regulated, but they are regulated by themselves,' says Akhtaruz Zaman, director of the Financial Institution Department for the Bangladesh Bank, the country's central bank. He means the board of directors, which is led by borrowers. Mr. Zaman says Grameen's deposits are 'well-protected' and the bank is 'doing fine.'

Harder-headed microlenders are stealing the spotlight, though. One rising star is the Association for Social Advancement (ASA), a Bangladesh charity, which boasts 1.5 million borrowers and just 0.7% of loans overdue, even by a week. Dispensing with borrower groups, ASA leans on borrowers' husbands and relatives if payments are missed, says the managing director, Shafiqul Haque Choudhury. To him, Grameen's approach is an ingenious idea that didn't stand the test of time.

'If we manage our operation in the Grameen way,' says Mr. Choudhury, 'we'll never be able to cover our costs.'

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