

# Interest rate behavior and lending in microfinance

Finance



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## An Essay on Interest Rate Behavior and Lending in Microfinance Abstract:

This essay analyzes factors which affect interest rate behavior and its subsequent impact on lending in microfinance. Here we have used regression model for our analysis. Furthermore comparison has been drawn among the different sources of loans outside Bangladesh. Here the experience of microfinance outside Bangladesh like India, South and South-East Asia, Latin America has been fully illustrated. This essay conducts analysis on the basis of the existing literatures on Microfinance.

Interest Rate Behavior Determinants of interest rate of lending in Microfinance: \* to expand and improve business operation \* recruiting personnel , \* marketing the services , \* improving financial information system, \* constructing new offices \* Default \* Unwillingness to pay \* Poor Management \* Economic recession \* Inability to pay \* Staff identifying \* Checking creditworthiness \* processing loan applications, \* disbursing loans, monitoring \* collecting repayments, \* costs of the space occupied, \* communications, transport, \* support staff, Grant \* Equity \* Foundation \* Trust \* Saving Account We can observe that in MFI lending there is higher interest rate than the commercial bank's lending rate. The interest rate charged here is higher as cost of funding, processing, cost of risk of loan losses and profit are higher in this case. The graph below shows the different ingredients interest rate. As above-mentioned factors are very much crucial in this sector that is why require extra attention and thereby require the MFI to charge high interest rate. Rosemberg, R. , A. Gonzalez and S.

Narain (2009) and Gonzalez (2010), suggest that though small loan provided by the MFI has low default rate but has higher administrative cost that most

of the cases cannot be offset by economies of scale. These administrative costs are the single largest contributor to interest rates. Finally, they suggest that, a bigger loan size may help them to reduce their lending interest rate. Further, they also emphasize if higher loans were received by more experienced borrowers then credit risk would decline and thereby interest rates. Lending in Micro-finance: Accordingly the loan transaction may be described in the following steps.

First, the financial firm decides how much to charge and what the optimal loan size to offer must be in order to reach its profitability goal. Once known the value of the lending interest rate and the average loan size the financial institution offers, a potential customer decides whether s/he wants to request a loan. Taking into account the credit history of the potential borrower and its income-expenditure stream, the financial institution builds a risk profile of the individual. With this at hand, they decide where to lend or not. The loan transaction process is given below: P. otler of Groningen university with his vast research wanted to show that profitability will increase when lending interest rates and/or productivity and/or the loan size increase or when the funding cost declines . He also showed that The lending interest rate will be negatively correlated with the loan size. So if they wish to achieve a higher profitability it is likely that all else equal they will offer loans of higher size. When microfinance institutions start operations they usually offer loans of small amounts because they do not have much capital or experience and debtors tend to be people without credit history.

We find that the lending interest rate is negatively correlated with the productivity of financial institutions and years of operation and positively

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correlated with the funding costs. What Can Reduce the Interest Rates in Microfinance? P. cotler also shows that probability that financing boosts growth is weakened if interest rates are extremely high. There are two policies to reduce interest rate : \* One is to reducing funding cost and \* Another is increasing productivity. How could productivity be raised? Institutional factors such as technology use and management quality and commitment to efficiency should be variables to consider.

Further, it should depend on with what capacity loan officers to reach their target clients. Such capacity not only depends on the quality of infrastructure but maybe more important on the geographic and demographic characteristics of the country in which microfinance institutions operate. 1 Effects of Competition over Lending Behavior in Microfinance Competition in a good influencing factor for the markets, consumer protections, efficiency of allocation and incentive for the development of new products. MFI's enjoyed a monopolistic market in the early years of its inception.

Monopolistic market power is associated with allocative inefficiency. Allocative inefficiency refers to the welfare losses as a consequence of high prices a monopolist charge. There is even further loss if the monopolist employs inefficient technology (productive inefficiency). Besides, there may not be demands to invest in efficient technology and introduce new products. Therefore, it would be realistic to assume competition can be beneficial in the context of microfinance market as it may result in improved and new financial product designs, better customer services, lower costs and lower interest rates.

The other side of the argument is that microfinance market makes use of soft-information and depends on strong MFI-client relationship. MFIs provide financial services for the poor that are considered not creditworthy by the conventional banks. They are often praised for overcoming the problem of information asymmetry and providing loans without collateral requirements. They do so by establishing strong personal relationship with clients. Another tool is the usage of other forms of collateral such as group lending that generates social collateral.

Competition and the effort to win clients and expand market share, therefore, may lead to low screening and lending standards. There are some indications of loose MFI-clients relationship with intense competition. Increased competition is also associated with an increase in information asymmetry, which makes it difficult for MFIs to know about the general debt level of clients. This in turn may lead to manifold borrowing, serious debt burdens, low repayment rates and poor portfolio quality.

The effect of competition could go both ways and deserves an empirical investigation. However, very few examine the effect of competition among MFIs and the literature on competition in microfinance is limited. Below is an overview of the few available related works. The focus on making MFIs profitable and financially-sustainable started in the 1980s and 1990s. The essential elements of this approach are competition, regulation and profitability. The essay explores the Latin American microfinance market where the commercial approach to microfinance proceeded rapidly.

It describes the market as facing rising competition, which leads to market saturation in some countries. Olivares-Polanco (2005) examines some of the <https://assignbuster.com/interest-rate-behavior-and-lending-in-microfinance/>

subjective and descriptive evidences. He investigates the effect of competition by mainly focusing on outreach (measured by loan size). His findings show that increased competition results in lower outreach. Navajas et al. (2003) studied competition in the Bolivian microfinance market by focusing on two major MFIs (Casa Los Andes and BancoSol), which collectively have around 40 percent market share.

The results suggest that outcome of competition is ambiguous since competition leads to innovation thereby expanding outreach. However, it reduces the ability of lenders to cross-subsidize less profitable smaller loans. In a similar study, Vogelgesang (2003) examines how competition affects loan repayment performance for Caja Los Andes. The analysis indicates competition is related with multiple loan taking and higher levels of borrower indebtedness. The probability of default is also shown to be high with higher levels of indebtedness.

On the other hand, he argues the probability of timely repayment is high in areas where there is high competition and high supply of microfinance services. Thus, the results seem inconclusive. A theoretical model developed by McIntosh and Wydick (2005) characterizes the effects of competition between MFIs where increased competition leads to increased information asymmetry. As a number of competing MFIs amplify in a market, which makes information sharing between them challenging, borrowers may engage in multiple borrowing which increases the debt level of clients and the probability of default.

This in turn can make worse off borrowers with a single lender since this behavior will create an externality by inciting MFIs to respond to multiple

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borrowing by adjusting interest rates upward. In a Ugandan microfinance market, which McIntosh et al. , (2005) studied, there is a rise multiple borrowing and decline in repayment rate as competition intensifies. Other works that do not address the effect of competition among MFIs but present an argument about the possible effects of competition includes Hermes et al. (2009). Their work examines how overall level of financial development in a country affects the efficiency of MFIs.

After presenting a balanced argument that the effect of financial development on efficiency could be both negative and positive, they empirically document a positive effect of financial development of efficiency of MFIs. They suggest competition, among other channels, through which financial development could affect efficiency. On a related work, Cull et al. (2009b) investigates how MFIs perform under the pressure of competition from formal banks. Their results show that in a country where there is larger formal bank presence, MFIs tend to deepen their outreach (i. . , extend their outreach to women and also lend in small amounts). However, the effect on other performance indicators, such as profitability, appears weak. Findings Given significantly large numbers of people in developing countries are financially excluded and the relative success of MFIs in promoting access to finance for the poor, it is not surprising to see MFIs get the attention they are enjoying. With the growth of the microfinance sector and increasingly varied players comes intense competition, which the effects on MFIs outcomes are not clear.

In this essay, we take the first approach in measuring competition in a standard way. Interestingly, the measure shows indeed competition is

growing in the microfinance market. As a next step, a critical question is addressed, namely what is the effect of increased competition. We consider important dimensions of MFIs' performance. These are outreach, loan repayment, efficiency and profitability. The results document strong negative effects of competition on performance of MFIs, after controlling for various macroeconomic and MFI factors.

We show competition is negatively related with outreach while it is associated with rising default rates. Furthermore, declining efficiency and deteriorating financial performance is shown to be associated with intense competition. The results might appear rather depressing for microfinance enthusiast, anyone for that matter, who would like to see the sector grow and bring all the positive benefits along. What could be done? These calls for measures that do not put a halt on the growth of the sector rather ensure the (negative) competitive effects are minimized.

This may include designing ways that makes sure MFIs do not compromise lower lending standards for increased market share. At the same time, designing ways that promote information sharing between MFIs, so that a borrower that default on one MFI loan could not turn to another MFI in the neighborhood and granted a loan, can contribute to lower delinquency as well as better borrowers' welfare. In addition, promoting financial literacy among clients may help them in their borrowing decisions, which in turn may limit multiple loan-taking. Finally, as we show in the results, increased competition is negatively associated with efficiency of MFIs.

Innovative ways among MFIs that could enhance efficient service provision may also help in ensuring benefits from the growth in the microfinance

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market. Incentives and Disincentives that Affect Lending Behavior in Microfinance In late 1980s and early 1990s thousands of non-governmental organizations (NGOs) and specialized finance institutions around the world initiated micro enterprise finance programs. Most of these programs are financially supported by the international donor agencies or governments to improve the lives of the poor.

Therefore, for NGOs micro enterprise finance appears to be socially motivated. Reasons Why Banks Make Micro and Small Enterprise Loans

Frequency of Response*	% of total
a) Profitability of micro and small loans	72 49%
b) Changing market conditions and increasing competition in lending to large/medium enterprises	64 44%
c) Regulations imposed by the government	25 17%
d)Povertyalleviation / social objectives	29 20%

Disincentives for Making Micro and Small Enterprise Loans

Frequency of Response	% of total
a) Higher administrative costs	29 40%
b) Risky borrowers	12 17%
c) Interest rate controls	21 29%
d) Not interested in micro enterprises	5 7%
e) Lack of network and personnel to serve this market	23 32%
f) Other	18 5%

Banks' Lending Behavior and Loan Characteristics

Banks Age and Their Portfolio Share in Micro/Small Business Loans Out of 148 banks, 119 banks answered to the question on loan portfolio analysis. When these banks are classified according to the number of years since they were established, it is found that the newly established banks, on average, have a larger share of loan portfolio delegated to small and micro enterprise loans than the older banks. Loan Terms The findings of this research indicate

that, the loan terms provided by these commercial banks for small and micro enterprises ranges between three months to six years.

On average, the loan term for micro enterprise loans is 2.4 years and for small businesses it is 2.9 years. These loan terms are much longer than the loan terms provided by NGOs, which are generally between one to three months. Average Loan Terms for Micro and Small Enterprise Loans Sample Size Average (years) Median (years) Micro 57 2.4 1.75 Small 46 2.9 3.00

Loan term: In micro and small business finance, the loan term or the loan repayment schedule can affect the ability of the borrower to pay his/her loan back.

The shorter loan terms or frequent payments of installments can make it easier for the borrower to pay his/her loan back, whereas the longer loan terms and infrequent payments of loan installments can make it difficult for micro/small business owners to pay their loan on time. Therefore, the longer the loan term, or the less frequent are the loan installments it is more likely for banks to have higher arrears which indicates a positive relationship between the length of the loan term and the level of arrears for a bank.

Average interest rate on micro/small loans: In the micro finance literature, it has been widely accepted that micro and small enterprises are capable of borrowing at commercial, or market interest rates. Furthermore, it is also argued that, if micro or small enterprise loans are subsidized by governments, loan default or corruption may be encouraged which may result in higher arrears in banks' loan portfolios. These arguments suggest a negative relationship between loan rates and banks' arrears.

On the other hand, the higher nominal interest rate paid on a loan implies a greater cash flow burden on the enterprise hence increasing the likelihood of arrears. Due to data limitations, other financial costs, such as fees and commissions associated with the loan could not be taken into account in this research. Findings: The higher the loan interest rate given everything else is held constant; the higher will be the rate of arrears.

This finding contradicts with the common argument that the micro and small enterprises are capable of borrowing and paying their loan back with a high rate of interest. It is however important to note that micro and small enterprises may show different characteristics in loan repayment with respect to given interest rates. One of the most important findings of this study is that many banks are using inappropriate lending criteria when making loans and managing their portfolio of small business loans.

In the case of small business loans the banks that require collateral have higher than average levels of loan arrears. Hence reliance on collateral tends to cause poor borrower evaluation and inadequate follow up once the loan have been made. It is also found that the level of interest rate charged on the loans is not a factor affecting the rate of arrears for micro enterprise loans but it is a factor affecting the level of arrears for small business loans.

Justification of high interest rate in Micro finance

Small businesses normally struggle to find out the sources of fund due to the small size of business where lenders face difficulties to cover up the loan money. From several evidences it is observed that small businesses are very efficient to utilize the funds and can rapidly realize profits though borrowing at very high interest rate. An author explained this through an <https://assignbuster.com/interest-rate-behavior-and-lending-in-microfinance/>

example of a fruit seller who takes loan in the morning, buys fruit, sells it and pay lender outrageous rates to repay the money by the end of the day.

So, It is very critical that though rates are high that MFIs have, small business can cover the spread. How can interest rate be reduced? Evidences from Bolivia pursue us that interest rate in micro finance sector can be reduced by great regulation and create a competitive environment among the micro finance institutions. If situation looks like that MFIs are managing huge profits in that case government should take some initiatives that will discourage MFIs to make extra ordinary profit.

Government can give licenses to new MFIs to create competition. But it should be remember that regulatory framework is a vital element. So, before giving licenses government should strengthen the monitoring function. Then we can expect that at least some of that profitability will be passed back to the customer either through lower rates, reduced fees or another way. Should Subsidy Be Provided To Reduce Interest Rate? From the very beginning of the history of Micro finance we see that it has been growing at an exponential rate over the years.

Many evidences about the recovery rates convince us that interest rate is almost justified so subsidy may create distortion in this sector. According to Mary Ellen Iskenderian, President and CEO of Women's World Banking, " I don't think a subsidy is the way to go about reducing rates because, in the end, the reason that microfinance has been so successful to-date is that it has always been about sustainability—sustainability of the institutions to recover their costs as well as sustainability of the borrower to make on-time payments. Responsiveness of lending amount to the changes in interest

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rate: Example from Bangladesh Bangladesh is a poverty-stricken country. It is a great pleasure for marginal people to get loans from MFIs because it is almost impossible for them to manage loan from conventional commercial banks. So, poor people are willing to pay even high interest rate to get loans. Now the question is that how are poor people responsive to increase in interest rate charged by MFIs? SafeSave, a credit cooperative in the slums of Dhaka, Bangladesh, operate three branches across the city to provide credit.

Administrative records kept by this MFI asserts that when interest rate increases suddenly, less wealthy borrowers reduce their demand for loan and they are relatively more sensitive than the wealthy borrowers. Another important thing is that the loan portfolio of this organization shifts from less wealthy borrowers from wealthy borrowers with the increase in interest rate. Influential advocates now argue that poorhouseholds are so insensitive to interest rates so interest rate in micro finance sector should be deregulated.

If this is so, microfinance can readily expand to serve the hundreds of millions of currently excluded households, without sacrificing depth of outreach. This claim is far from clear as a general proposition. First, diminishing marginal returns to capital disregards the possibility of unequal access to non-capital inputs like managerial skills and human capital by poor borrowers. Moreover, raising interest rates can in principle exacerbate moral hazard and adverse selection, worsening loan repayment rates and screening out the most reliable borrowers.

And, while microlenders may still find a pool of customers after real interest rates are raised, the customers may not be from the same pool that was reliable, willing and able to pay the lower rates. In addition, Moral perception

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to keep costs as low as possible for the poor, have compelled the larger microlenders in Bangladesh to keep real interest rates below 40 percent per year, even if it means turning to subsidized resources to cover costs (e. g. , Morduch, 1999). The average fees charged by two large lenders in Bangladesh are just under 30 percent.

The Grameen Bank (which is not one of the two) keeps their interest rates and fees close to 20 percent per year (nominal) on their main lending products—and they ignore suggestions to raise rates. Experience inside Bangladesh Credit delivery system by Grameen bank Grameen Bank Credit Delivery means taking credit to the very poor in their villages by means of the essential elements of the Grameen credit delivery system. The credit delivery system of this authentic micro-finance is very much well-functioning. The credit delivery is the most productive weapon of Grameen bank to reach the highest number of its beneficiaries.

Grameen Bank credit delivery system has the following features: 1 There is an exclusive focus on the poorest of the poor. Exclusivity is ensured by: i) establishing clearly the eligibility criteria for selection of targeted clientele and adopting practical measures to screen out those who do not meet them ii) ii) in delivering credit, priority has been increasingly assigned to women iii) iii) the delivery system is geared to meet the diverse socio-economic development needs of the poor 2 Borrowers are organized into small homogeneous groups. Such characteristics facilitate group solidarity as well as participatory interaction.

Organizing the primary groups of five members and federating them into centres has been the foundation of Grameen Bank's system. The emphasis <https://assignbuster.com/interest-rate-behavior-and-lending-in-microfinance/>

from the very outset is to organisationally strengthen the Grameen clientele, so that they can acquire the capacity for planning and implementing micro level development decisions. The Centres are functionally linked to the Grameen Bank, whose field workers have to attend Centre meetings every week. 3 Special loan conditionalities which are particularly suitable for the poor. These include: i) very small loans given without any collateral i) loans repayable in weekly instalments spread over a year iii) Eligibility for a subsequent loan depends upon repayment of first loan iv) Individual, self chosen, quick income generating activities which employ the skills that borrowers already possess v) close supervision of credit by the group as well as the bank staff vi) stress on credit discipline and collective borrower responsibility or peer pressure vii) Special safeguards through compulsory and voluntary savings to minimise the risks that the poor confront viii) Transparency in all bank transactions most of which take place at centre meetings Simultaneous undertaking of a social development agenda addressing basic needs of the clientele. This is reflected in the " sixteen decisions" adopted by Grameen borrowers. This helps to: i) Raise the social and political consciousness of the newly organized groups ii) Focus increasingly on women from the poorest households, whose urge for survival has a far greater bearing on the development of the family iii) Encourage their monitoring of social and physical infrastructure projects - housing, sanitation, drinking water, education, family planning, etc. Design and development of organization and management systems capable of delivering programme resources to targeted clientele. The system has evolved gradually through a structured learning process, that involves trials, errors and continuous adjustments. A major requirement to operationalize the system is the special

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training needed for development of a highly motivated staff, so that the decision making and operational authority is gradually decentralized and administrative functions are delegated at the zonal levels downwards. 6| Expansion of loan portfolio to meet diverse development needs of the poor. | As the general credit programme gathers momentum and the borrowers become familiar with credit discipline, other loan programmes are introduced to meet growing social and economic development needs of the clientele. Besides housing, such programmes include:| | i)| Credit for building sanitary latrines| | ii)| Credit for installation of tube wells that supply drinking water and irrigation for kitchen gardens| | iii)| Credit for seasonal cultivation to buy agricultural inputs| | iv)| Loan for leasing equipment / machinery, ie. cell phones purchased by Grameen Bank members| | v)| Finance projects undertaken by the entire family of a seasoned borrower. Three Cs in Credit delivery: Character: means how a person has handled past debt obligations: From credit history and personal background, honesty and reliability of the borrower to pay credit debts is determined. Capacity: means how much debt a borrower can comfortably handle. Income streams are analyzed and any legal obligations looked into, which could interfere in repayment.

Capital: means current available assets of the borrower, such as real estate , savings or investment that could be used to repay debt if income should be unavailable. | | The loan disbursement has been robust year after year and profit has also been increasing year after year. The loan disbursement schedule and profit are summarized below: year| Loan disbursement (million Tk)| Profit/loss (million Tk)| 2001| 146538. 20| 58. 45| 2002| 162286. 24| 59. 67| 2003| 183575. 33| 357. 52| 2004| 209166. 76| 422. 13 | 2005| 3248163.



17| 1000. 44| 006| 306368. 63 | 1398. 15| 2007| 356798. 22| 106. 91| 2008| 418903. 07| 1305. 00| 2009| 498311. 47| 371. 57| 2010| 594460. 61| 757. 24| Interest rate charged on different loan on different duration are given below: Description of the loan| EAIR(Old Payment Method)| EAIR(New Payment Method)| 10-Year stable Level Loans @ Tk. 2, 000| 350%| 556. 44%| 10-Year Increasing Loans| 18. 48%| 44. 13%| Actual 7-Year Center Loan History| 15. 39%| 35. 57%| The “ Old” Payment System: Under the “ old” system, Grameen borrowers made weekly payments for 50 weeks.

Their principal balance was reduced by the full amount of the payment, and no interest payment is credited. The “ New” Payment System: Under the “ new” system, the entire structure of loan payments was altered. The loan payment period is now defined as 46 weeks in length, but factored into the system is the anticipation of 6 official “ national holidays” when the week’s payment is suspended. ASA Microfinance in Bangladesh: ASA has been working relentlessly to reduce poverty since its inception in 1978.

The formal banking sector in developing countries, like Bangladesh, does not typically provide financial services to the poor. This sector concentrates on large loans to the upper class, thereby completely excluding low income groups. The microfinance movement, however, has shown that there is a thriving market among the poor when financial products cater to their specific needs. The poor are a quite active group in any economy. ASA has shown that their needs can be met while at the same time making the providing institution profitable as well.

Up to October 2011 ASA's cumulative Loan disbursement has been BDT 481, 381 million (US\$ 6, 326 million) while loan outstanding (principal) is BDT 44, <https://assignbuster.com/interest-rate-behavior-and-lending-in-microfinance/>

972 million (US\$ 591 million) among 4. 43 million borrowers. At the end of June 2011 ASA's Operational Self Sufficiency(OSS) was 182. 48%, Financial Self-sufficiency (FSS) 118. 82% and rate of loan recovery 99. 83%. The loan disbursement over the years are given below: Year| Disbursement in million Tk. (during the year)| 2008| 61, 108, 00 | 2009| 61, 495, 00. | 2010| 68, 486, 00| 011| 44, 835, 00| The rate of interest charged by the ASA is given below:

Category	Eligible Criteria	Initial Maximum Loan Size	Interest Rate	Loan term
Primary Loan	Economically active poor to undertake or strengthen income generating activities (IGAs).	BDT 8, 000-20, 000 to maximum BDT 50, 000 at first loan cycle.	Maximum 27% declining	4, 6 or 12 months based on nature of IGAs
Special Loan	Small/micro enterprises or entrepreneurs and traders to promote and scale up production, business activity and employment generation.	BDT 51, 000-500, 000	Maximum 27% declining	12, 18, 24 or 30 months based on nature of enterprises

BRAC, a development organization, was formed in 1972 under the Societies Registration Act 1860. Although it was first set up to resettle refugees in post-war Bangladesh, BRAC later redesigned its strategies in accordance with its philosophy of poverty alleviation and empowerment of the poor. At present, BRAC has a large number of development programs that cover the areas of health, education, credit, employment and training for the poor people of Bangladesh.

BRAC carries out licensed banking activities through the BRAC Bank Ltd. and also earns from various income generating projects such as Aarong Rural Craft Centre, BRAC Printers and Printing Pack, BRAC Dairy and Food project, BRAC Tea Estates, and various programme support enterprises such as

poultry farms, feedmills, seedmills and prawn hatcheries. Microloans: These loans, which range from USD 50 - 700, are given exclusively to individual women who are serviced in a group setting, namely the VO. The VO acts as an informal guarantor by creating peer pressure to ensure timely repayment.

Borrowers repay through weekly or monthly installments and deposit savings during the regular VO meetings. These loans are generally used for small operations in poultry, livestock, fruit and vegetable cultivation, handicrafts or rural trade. Microenterprise loans (Progoti): These loans, which range from USD 700 to 10, 000 are given to both male and female entrepreneurs to support and help expand existing small enterprises which are too small to qualify for credit from mainstream banks. Borrowers generally use these loans to finance shops and small-scale manufacturing activities.

A ladder of opportunity : BRAC have developed a ' ladder' of financial services to target different poverty groups because we understand that the financial needs of the poor are diverse. The most vulnerable are the extreme poor who do not benefit from microfinance - for this group BRAC have developed a grant-based programme that incorporates asset transfers with non-financial support; BRAC's Ultra Poor programme. Similarly, it has launched, with the help of the Government, a specific customised product for marginal farmers, which combines access to finance with technical support.

Another specialised microloan scheme aims to financially empower adolescent girls, helping them continue their education, build savings and receive livelihood training to start smaller home-based enterprises. The rate of interest charged by the BRAC Bank SL no. | Types of loan| Annual interest Rate| 1| General micro credit (Rural and Urban)| 25%-33%| 2| Micro  
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Enterprise loan| 26%-40%| 3| Ultra poor loan| 22%| 4| Agriculture loan| 22%-33%| 5| Seasonal loan| 26%-33%| 6| Disaster management loan| 2. 8%-21%|

Loan Disbursement over the year is given below: Sl no. | year| Loan disbursement(TK)| | 2009| 75680756900| 2| 2010| 38749653600| 3| 2011| 39554248779| 4| 2012| 42235412000| Experience outside Bangladesh There is a vast array of experience outside Bangladesh as microfinance is now a globalphenomenon. The information below is simply intended to give a snapshot of the differentexperiences in a few countries, and to show how the complex issue of interest rates has beenaddressed, either by inaction or explicit action by governments. Figures on interest rates fromvarious countries in different parts of the world are given below, in particular those nearby inAsia.

Countries are also mentioned where the government or parliament (not necessarily thesame) has sought to impose a ceiling on interest rates in the twin belief that poor peoplecannot afford to pay the high interest rates charged by MFIs and that it is indeed immoral thatthose who are poor should pay higher interest rates on loans than those paid by richerindividuals. South and South East Asia The table below (prepared for the Joint Donor Strategy initiative) gives a summary picture ofthe situation in selected countries in the S. nd SE Asia Region, showing data assembled byEDA Rural Systems, with the comparative rates in Bangladesh at the bottom of the table forcomparison: Three important conclusions can be drawn from these figures. 1. First, that the interest rates charged by MFIs are invariably higher than the rates charged by commercial banks, on average approximately 100% higher. 2. Second, that in general the rates charged by informal

moneylenders vary much more widely than either the rates charged by the banks or by MFIs, and almost always are substantially higher than the rates charged by the MFIs. . Third, the interest rate charged by almost all NGO-MFIs in Bangladesh, 30% effective annual rate, is by no means out of line with what is being charged elsewhere in South and South East Asia. If any person wants to borrow from traditional banking system he has to fill out application form. He has to go to the bank for many times for the sanctioning of loan that incurs substantial amount of transportation cost for him. In addition to high transportation cost, there are some processing cost and commissions charged by banks.

Ultimately, Effective interest rate is quite higher in case of borrowing from traditional banking system. On the other hand, traditional banks can't cover up administrative cost by providing small loans. Comparison of Interest Rates of Various Sources of Loans in India Quoted Cost and Cost after Adjustment for Transaction Costs From the table we see that there is no transaction cost in case of borrowing from MFIs loan. From the evidence of India, we have found that MFIs are used to make election engineering.

The main motive of MFIs is to provide credit to women and poor. But, politicians are trying to use it as a political tool. Government provides subsidy which are distributed through MFIs. Large number of impoverished people is a big vote bank for politicians. In this process government influences the decisions of the voters in time of election. In Tamil Nadu we see that government passed ordinance that MFIs could not charge more than 12% interest that may ultimately drive out huge number of lenders from the market.

So, poor people have to rely on nonchalant public sector banks and according to Mahajan and Ramola they will not have no recourse except money lenders for borrowing. Interest rate, Lending ; Microfinance Less Dependence on Money lenders, Mahajon etc More economic activities because of easy funding reduce asymmetry of information, rural development possible. Downward competitive environment in informal market. Rise in income level, Purchasing power, Overall standard of living. Production, consumption level increases. Result

Eliminate the practice of charging usury, greater financial leverage, only does it help to reduce poverty, it Scales down inequality as well. Fig: Effect of Interest rate, Lending ; Microfinance On the Perspective of Latin America In Latin America, the leading MFIs all operate under a formal legal framework, usually as specialized MFI banks, under the supervision of the central bank. Figures for five of the best known institutions are given below, all of which have substantial numbers of clients (by the standards of the region) and are currently operating profitably.

Probably the most interesting (for Bangladesh) is Comparators which has from its inception deliberately targeted poorer clients, as can be seen from the current average size of loans (\$277). Leading Microfinance Institutions Primary Indicators (End Third Quarter 2003) The figures below for the same five MFIs show the average rates of interest which they are receiving on their various loan products. Descriptive Statistics | Mean| Std. Deviation| N| NO. CLIEN No of CLIENTS| 94000. 00| 65490. 457| 5| AVG. LOAN Average Loan| 1002. 0| 501. 657| 5| LOANST Total Loan| 78000000. 00| 42361539. 160| 5| Regression Variables Entered/Removed(b) Model| Variables Entered|

Variables Removed| Method| 1| NO. CLIEN No of cLIENTS(a)| . | Enter| a All requested variables entered. b Dependent Variable: LOANST Total Loan Model Summary Model| R| R Square| Adjusted R Square| Std. Error of the Estimate| Change Statistics| | | | | R Square Change| F Change| df1| df2| Sig. F Change| 1| . 169(a)| . 028| -. 295| 48213878. 375| . 028| . 088| 1| 3| . 786| Predictors: (Constant), NO. CLIEN No of cLIENTS The unstandardized parameters tell you the difference in Y per unit change in X whereas the standardized tells you the difference in Y in standard deviations per standard deviation difference in X. With the exception of BancoSol, these rates are all higher than those charged by the NGO-MFIs in Bangladesh (in the case of Compartamos substantially so), but their operating costs are also higher than the leading NGO-MFIs in Bangladesh due largely to the higher costs of staff.

Nonetheless all five institutions are profitable and the high returns achieved by the three most profitable institutions have enabled them to achieve the most rapid rates of growth in client numbers in the 21 months covered by thee figures; almost triple by Banco Solidario; more than double by Compartamos; and over two thirds by Mibanco. Leading Microfinance Institutions: Costs and Interest Rates (End Third Quarter 2003) As reported by Helms and Reille, when BancoSol in Bolivia began as a bank in 1985, it charged a combination of interest and fees equivalent to 65% effective annual interest rate. Today, BancoSol, operating in a highly ompetitive environment, has brought down its costs and charges interest rates on its products yielding the 24% shown in the table above. According to one of the managers at BancoSol, the banks growth from 4, 500 to 55, 000 clients in

just ten years has been possible by its ability to charge sustainable rates of interest. Further, whilst its return on average assets is a modest 1.6%, its current return on average equity is over 11% (because of the leverage it has been able to exercise on its equity). Conclusion Obtaining financial information from institutions involved in microfinance is no easy task.

In most countries because there is no financial authority that collects it and makes it available to the public. Furthermore, the absence of governmental or organized market supervision means that these entities can freely decide how to measure - if they want to do it- the variables describing their different sources of income and expenditure. Finally, even if there were an informal consensus on how to measure these variables, that would not necessarily ensure that the information is reliable since it is very likely that accounting deficiencies might exist. 1. David L. Wright, Dewan A. H.

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