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What makes microcredit programmes effective? Fashionable fallacies and workable realities

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Summary

There is an influential, orthodox explanation of the success of large scale micro-credit programmes, based particularly on interpretations of the Grameen Bank in Bangladesh. There are three core elements: the alleged importance of strong social bonds among small borrower groups; the notion of substantial borrower participation in management; and the belief in the centrality of charging unsubsidised rates of interest. While it resonates strongly with fashionable development ideologies, this orthodox explanation does not correspond to the facts. The real explanation lies in careful attention to managerial and strategic "fundamentals": keeping transactions costs low; matching loan repayment schedules to borrowers' income and savings potentials; finding ways of obtaining good work performance from large and widely dispersed field staff; addressing basic client needs in an efficient way; and, above all, attacking on many fronts the perennial micro-credit problem of borrower default. Creating and sustaining a strong and distinct organisational culture has been an important means of achieving these goals. The main practical conclusion is that there is more than one route to achieving the core objectives that make micro-credit systems viable. The route to success lies not in replicating a particular organisational and policy blueprint (the "Grameen model"), but in finding organisational forms and policies that will meet these core strategic objectives in particular circumstances. The major micro-credit providers in Bangladesh pursue a diversity of strategies; in an increasingly competitive business, each is creating its own niches in the market. A further lesson is that success generates its own problems. While a static "Grameen model" is being promoted for the rest of the world, it is being adapted continuously in its place of origin.

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1 Introduction

1.1 Context

In 2001, microfinance programmes in developing countries began to lose much of the lustre that had been painstakingly developed around them over previous decades. Two of the star performers ran into serious problems. In La Paz, the lending and repayment programme of the BancoSul became enmeshed in wider problems of political and commercial instability in Bolivia. Borrowers stormed the offices of the Superintendency of Banks demanding debt forgiveness. In November, the *Wall Street Journal* ran a well researched article making public what many insiders had known or suspected for years: Bangladesh's Grameen Bank, *the* global exemplar of micro-lending to the poor, was not achieving the repayment rates it had been claiming. Then, on 23 February 2002, *The Economist* reported serious problems with two South African banks specialising in micro-lending. These events appear to vindicate Graham Wright's warning that:

> the most dangerous form of "replication" is that driven by consultants, leaders or donors recommending systems they only partly understand, in environments which they only partly comprehend. With the success of the Microfinance industry, the growing international reputation of the Grameen Bank, and the drive to reach large numbers of the poor, there are many alarming examples of this happening.
>
> (Wright 2000: 264)

These setbacks may turn out to be salutary checks for the microfinance movement. For the movement has increasingly become burdened with problems of its own making: a sustained public presentation of the reasons for undoubted achievements that is consistently misleading; and a very successful and sustained public relations operation that has tended to sweep problems and weaknesses under the carpet. In reality, microcredit programmes – and here we deal only with organisations that have focused on lending – have been successful in large part because the social entrepreneurs who have created and managed them have developed and refined some hard-nosed commercial, organisational and sociological practices that are well adapted to the circumstances in which they are required to operate. Yet, because they needed the support of development aid, these same entrepreneurs have explained and justified their programmes to appeal to soft hearts, wishful images, and fashionable ideas about the practice of development. They have been largely silent on those elements of their strategies that have contributed most directly to success, and have exaggerated the contribution of practices that are peripheral to organisational performance – but central to a favourable public image and to donor support. The driving role of public relations has made it difficult for managements publicly to admit problems and, more importantly, for outsiders to learn the useful, transferable lessons.[1]

Both the field of microcredit and the literature relating to it are large, fast growing and diverse. We need to state clearly what we are and are not attempting here. There are three star microcredit programmes in the developing world: the mainly-rural Bank Rakyat Indonesia (BRI) programme; urban programmes in Bolivia, where the BancoSul has been the leader; and the Grameen Bank in (rural) Bangladesh. We concentrate here on the Grameen Bank, because this has been the dominant model that others have tried to emulate, especially those aiming to develop credit programmes for the *rural* poor. The "Grameen model" is being actively promoted in the rest of the world, notably by the Consultative Group Against Poverty (CGAP). Major international institutions like the International Fund for Agricultural Development and the Asian Development Bank, as well as many national funding organisations, have been willing to support only those microcredit programmes that are based on the Grameen model. Why is this model so important, and so widely chosen for replication? It is partly a matter of timing: the Grameen Bank's microcredit programme was the first to become large and famous. Second, its leadership has been especially active and effective in publicising the virtues of the Grameen model – and doing so in terms that appeal to the aid donors who have been so important is underwriting microcredit organisations. Third, the other two star performers are, for different reasons, not generally considered so suitable for general replication. The programme of the Bank Rakyat Indonesia (BRI) has some very committed admirers, but there is widespread perception that it works effectively because it is an official programme, organised by the Central Bank of Indonesia, and heavily dependent for its repayment record on the unusual capacity of Indonesian village-level authorities to monitor and influence individual households. The BRI model is unlikely to travel well outside Indonesia. The BancoSul approach is distinctly different, as it is essentially the downward extension of commercial urban banking to poorer clients. To some degree, its fast expansion – and recent check – stem from special features of recent Bolivian history (Mosley 2001). Most of the global expansion in microfinance in the near future may come from this kind of commercially-based programme. But, to date at least, this approach has not seemed to offer a realistic prospect of reaching the *rural* poor, in particular.

Our central concerns are with the scope for extending the Grameen approach. For that reason, we are dealing with *microcredit*, not *microfinance*. Neither the Grameen Bank nor similar organisations have been able to develop a large business in deposit mobilisation. It is at least arguable that they never will, because they have

[1] There is an enormous volume of literature purveying the images of microcredit that we are critiquing. We can only cite a few illustrative publications, chosen largely at random. Mohammed Yunus, founder of the Grameen Bank and doyen of the field, has told his own version of the story many times (e.g. Yunus 1997). For a eulogistic story of the growth of microfinance in Bolivia, by a leader of the ACCION microcredit organisation, see Rhyne (2001). Marguerite Robinson (2001) tells a slightly more sober story of Bank Rakyat Indonesia programme, but fails seriously to address the issues of organisation and management that concern us here.

become locked into a particular strategy – essentially one of dispersing a limited range of loan packages against what some would regard as (limited) forced savings (Section 4).

We are only peripherally concerned with the question that has animated most academic commentators and researchers in this field (e.g. Kabeer 2001): how far does Grameen-type credit get to the really poor and needy? We agree with other commentators that the very character of Grameen-type loan and repayment packages makes them unsuitable for some categories of poor people (Section 3).

This paper is based on extensive fieldwork by Pankaj Jain during November 1999 to April 2000[2] on five microcredit organisations that we classify, for present purposes, as part of the "Grameen family": they are large independent not-for-profit organisations that work principally in rural areas, mainly deal in microcredit rather than in microfinance more generally, and to some degree follow Grameen-type lending practices.[3] Four of these organisations – the Association for Social Advancement (ASA), the Bangladesh Rural Advancement Committee (BRAC), the Grameen Bank itself, and Proshika – are located in Bangladesh. Each has more than one million members. The fifth organisation, CARD (Centre for Agriculture and Rural Development, based in San Pablo City), is the largest, fast growing microcredit programme in the Philippines.

Section 1.2 comprises an introductory thumbnail sketch of each of the five organisations studied. This is followed, in Section 1.3, by a brief summary of the orthodox explanation of the success of the Grameen model. In Section 2, we explain why the orthodox explanation of the success of the Grameen model is misleading or false. Our understanding of the real reasons for success is contained in Section 3. In Sections 2 and 3, we concentrate on what our five case study organisations have in common. In Section 4 we shift to exploring the differences among them, in order to illustrate that microcredit is a dynamic business. There is a continual process of learning within and between the different organisations evolved. In Bangladesh in particular, because the market for rural microcredit is relatively well provided and increasingly competitive, individual providers are each trying to develop their own specialisms and niches. Collectively, their experiences demonstrate that, even within this relatively homogenous group of microcredit providers, there are a variety of ways of doing the job well. The data and financial analysis of microcredit programmes in the Annex supplements this section of the paper in particular. They illustrate that, even within the context of contemporary Bangladesh, managers of large microcredit programmes have a wide range of choices about routes to achieve financial sustainability. In Section 5 we consider in a little more detail the reasons why the social entrepreneurs who have created and managed microcredit have been responsible for, or complicit in,

[2] This follows on from his earlier research on the same subject (Jain 1996).

[3] These generalisations will all be challenged, and need some qualification at the margin. The Grameen Bank got off to a good start because it had the support of the Central Bank of Bangladesh. While this category of organisations are generally characterised as development NGOs, the Grameen Bank has from the beginning been registered as a bank, and has never pretended to be anything else. The other large Bangladeshi microcredit organisations generally do not see themselves as following the Grameen model. As we explain in the text, ASA and BRAC adopt most of the core features of that model. Proshika appears to differ in some fundamental ways, but is converging toward the Grameen approach.

misleading interpretations of how they operate and why they have been successful. The core explanation lies in their need to generate financial and other support from the aid donor community. We stress that our critique is not criticism. The ability to create and sustain supportive organisational myths is often essential to effective leadership. We admire the way it was done in these cases. But we admire much more the organisational design and management skills that have been left in the shade because of the prevalence of myth.

1.2 Cases

The conclusions of this paper are based principally on field research on the following five microcredit programmes (henceforth MCPs):

Grameen Bank

Grameen was initiated in 1977 as a project to try out a new approach to rural credit in Bangladesh. It was initially rooted in the Central Bank of Bangladesh, and later spun off as an independent bank. Grameen gave loans without asking borrowers either to provide collateral or engage in paperwork. It pioneered what has come to be known as group based lending. The borrowers were provided financial services at their doorstep. Contrary to most earlier experiences, Grameen established a system of reliable loan repayment from the borrowers who were below the poverty line. Grameen was serving more than 2.3 million borrower members in Bangladesh in 1999 and replication projects had been started in many countries. A 1993 World Bank study established the significant economic and social development impact of participation in Grameen's microcredit programme (Khandker *et al.* 1995). This helped Grameen become the acknowledged leader of international microcredit movement, which was organised in the Microcredit Summit. Mohammed Yunus, the founder of Grameen, headed the Summit. Grameen has had access to low cost capital; it has generally charged a nominal interest rate of around 16–20 per cent on outstanding loans.

ASA

ASA (the Association of Social Advancement) started in the early 1980s with a relatively radical agenda of social transformation. In 1990–91, its leadership decided to focus on an economic empowerment agenda. They chose microcredit as the core activity, and adopted the Grameen approach. Starting from scratch in the credit field in 1991, ASA ran a programme that grew fast and became one of the largest and best regarded in Bangladesh. Over a six year period, 1992–98, ASA increased its borrower–base ten fold to reach 0.8 million people, and its loan portfolio around twenty times to around 2.2 billion Taka. By the end of 1990s, many specialists believed that ASA had emerged ahead of Grameen as the new leader of microcredit model, even though Grameen was still growing fast and feted worldwide. Two factors were chiefly responsible for this success. First, despite its fast growth, ASA had maintained a high quality loan portfolio, with an on-time repayment rate of close to 99 per cent. In contrast, the Grameen's on-time loan recovery rate had dropped to less than 90 per cent, with many believing it to be as low as around 70 per cent. Second, unlike other microcredit programmes, ASA relied very little on donor funds or low cost finances. Charging a higher interest rate than Grameen, ASA reached financial viability within two years of starting.

BRAC

BRAC (the Bangladesh Rural Advancement Committee) started in 1972 as a relief and rehabilitation programme for Bangladeshi refugees returning home after the liberation of their country from Pakistan military rule. It first shifted from relief to integrated community development, building rural infrastructure and providing services to the rural community at large, and later focussed all its programmes on poor households. In the mid-1980s BRAC initiated a microcredit programme that was similar to Grameen's in most respects, but had an additional component. BRAC staff believed that many poor borrowers would not find it easy to make effective use of credit unless they had access to technical advice and help with obtaining business inputs and marketing. They introduced a sector development component that provided this kind of support and, believing in integrated development, also began education and health programmes. All BRAC activities were founded on intensive initial work in forming and sustaining member groups. Microcredit has been BRAC's largest single programme, reaching more than 2 million households in 1999. BRAC has charged similar interest rates to ASA. A 1994 World Bank study revealed that BRAC borrowers did not obtain higher rates of returns on their investments than members of Grameen or RD-12 (another credit programme), although the latter organisations provided no technical support (Pitt and Khandker 1996). Another study by Montgomery, Bhattacharjee and Hulme (1996) showed that BRAC's borrowers were relatively poor, but they were also less successful in freeing themselves of poverty compared to the borrowers in another government supported MCP. However, we view the BRAC credit programme as successful and competitive. It reached financial sustainability ahead of ASA.[4]

Proshika

Proshika's main original mission was to organise poor people and, through training and conscientisation, assist in building self-sufficient local organisations. Accumulated group savings were used as seed capital for collective economic activities. In the mid 1980s, Proshika started supplementing groups' capital by supplying a revolving fund. Some of that money was on-lent by the group to individual members, but a large proportion was used to support group economic enterprises. Over time, the Proshika credit programme has become more individualised (see below), but continues to have a substantial collective dimension, including group-leadership development, members' training, education and health improvement.

[4] The interest earned from the BRAC lending programme fully covers costs, including the costs of sector development, provision of technical services, formation of borrower groups and supervision visits.

Unlike the Grameen approach that was adopted by BRAC, ASA and a host of other NGO programmes, Proshika does not give out loans directly to members or collect repayments directly from members through its staff. These tasks are left to local group leaders. The primary groups are federated into a hierarchy of local people's organisations, with each level having a carefully demarcated role. The primary groups decide the amount of loan to be given to each member and play an active role in securing revolving loan funds from Proshika and recovering the loan repayment from the members. The higher level federated units focus on the social development and empowerment agendas, with an emphasis on seeking the representation of poor on various local social and political forums. Around one third of Proshika's total membership of around 2 million receive microcredit. Until 1993, Proshika's credit programme was small and ill organised. After 1994, it started catching up with the performance standards prevalent in the microcredit sector, with an on-time loan recovery rate in the range of 90–95 per cent. Proshika's emphasis on local group organisation has the potential to reduce the transaction costs that arise when, as in the other programmes, employed staff members have to interact directly with individual borrowers. However, Proshika still provides relatively small loans, serves only a minority of its members with credit, and has yet to demonstrate that it can run a large microcredit programme with high repayment rates.

CARD Rural Bank

CARD was started in 1986 by a group of development professionals who had been working in various organisations in Philippines. In 1991, CARD launched its microcredit programme modelled on Grameen, with some new features. For example, members had to go through a means test, in which an index of the quality of their housing played a major part. They were then required to take part in a 24 hour Continuous Group Training. The microcredit programme acquired momentum only after 1995, once CARD had lined up capital resources from donor and national agencies. CARD normally charged an interest rate of 20 per cent per year on the face value of loans, amortised over the loan cycle. With various charges, the effective interest rate came to around 50 per cent per year on outstanding loans. CARD management believed that poorer members valued the flexibility of repeated and expanding loan cycles more than the one longer loan cycle typical of the Grameen model, even if the latter has smaller loan instalments. It is willing to provide individual borrowers with multiple loans. In 1998, CARD introduced a voluntary savings scheme, both for members and non-members. It had around 30,000 borrower-members in 1998.

1.3 Issues

Microcredit for the poor has become a major item on development and aid policy agendas. In line with the declarations of the 1995 Microcredit Summit, NGOs, governments and international development agencies are now working to provide microcredit to 100 million poor families worldwide. This is not a passing whim, but a target based on real and impressive experience and achievement. The emergence of sustainable large scale MCPs in very poor countries is arguably one of the more significant forward steps that has been made for decades in finding new means directly to tackle poverty. MCPs are loaning money to large numbers of people and, in a radical break from past experience, (mostly) getting their money back. How have they been successful? The experience of the Grameen Bank has been central to debate on this question. It was the first organisation to operate a very large-scale microcredit programme and demonstrate its success in both outreach to the poor and high loan recovery rate. It is widely believed that the success of microcredit in Bangladesh is due principally to the adoption of the Grameen organisational and policy blueprint and, as explained above, the Grameen model is still the prime candidate for replication.

What does the "Grameen model" comprise? There is no single authoritative interpretation, but a widespread operational consensus, underpinned by publicity material, that it consists of three key elements:

- *Social collateral*: the notion that individual borrowers repay because of strong socially-constructed collective responsibility at the level of the small group, of about five people, to which each borrower-member belongs. The group will (a) only approve of, and take responsibility for, loans to individual members who are likely to repay; and (b) in case of individual default, jointly assume the repayment obligations. The group mechanism is seen as a solution to the problem of high transactions costs, in both identifying reliable borrowers and ensuring repayment, that plague most microcredit programmes (e.g. Stiglitz 1990).
- *Borrower participation*: the idea that there are strong participatory elements to the management of microcredit, through the involvement of borrowers in both operational and policy decisions. For this reason, organisational policies are responsive to borrower needs and circumstances, and borrowers collectively have a strong sense of identification with, and commitment to, the organisation.
- *Absence of subsidy*: the belief that the interest rates paid by borrowers are not subsidised. Charging a relatively high interest rate that covers the full cost of the programme, and which the poor are apparently willing to pay, appears to be a win–win proposition (Morduch 1997). This strategy is consistent with the lessons learnt from the experience of earlier cooperative and other government aided credit programmes for the poor, whose failure has been blamed on the subsidised interest rate policy (Adams *et al.* 1984). The absence of subsidy is expected to (a) provide a discipline that will give borrowers an incentive not to try to grab more credit than they can afford to re-pay; (b) discourage the relatively wealthy from monopolising the service; and (c) discourage management from trying to establish or expand programmes mainly to get access to subsidies and the patronage, rent-seeking or other improper benefits that these might generate (Yaron 1992).

This orthodox understanding of the reasons for the organisational success of microcredit is, in varying degrees, either misleading or wrong. It is wrong to the extent that its core elements either (a) are not found in some successful microcredit programmes or (b) play a much smaller role than is commonly believed. It is misleading to the extent that it diverts attention from the real reasons for success. Successful MCPs are essentially *businesses* that have succeeded by doing two things that successful businesses do. First, they have devised and pursued a business strategy that is appropriate to the particular features of the markets in which they operate and the clients they intend to attract. Second, they have designed organisational structures and procedures that enable them to run very efficient banking operations in difficult circumstances: providing financial services to match client needs; minimising "leakage" of funds through loan default or misappropriation of money by staff; and keeping transaction costs low, mainly by reducing the need for and cost of following up cases of loan defaults. The elements of the successful microcredit model that have received so much public attention often are subsidiary elements to these strategic choices, and sometimes play mainly a public relations function.

2 Orthodoxy and fallacy

In this and the succeeding section, we shall be concerned mainly with the commonalties among these five MCPs. We explore differences in Section 4. In order to talk about their commonalties, albeit in a stylised way, we need to establish a few basic facts and define some terms. Each member (= borrower) of ASA, BRAC, CARD and Grameen is a member of what we will term a *primary group* of about five to six people. These primary groups are in turn federated into *secondary group*s, that, as we shall explain below, were for most purposes the more significant level of member organisation than are primary groups. The terms primary group and secondary group are ours. We use them generically in this paper, and talk of *groups* when referring to both levels. The Grameen Bank calls their secondary groups *centres*, and constitutes them from eight primary groups – no more, and no less. Once eight primary groups exist within a centre, any new group in a locality forms the nucleus of a new centre. The secondary groups in other MCPs had 30–50 members. Proshika is the exception; it had one level of groups, each of 20–30 members.

We have explained above that there are three key elements to the orthodox interpretation of the success of MCPs. We explain below the reality in relation to each, presenting either the typical practice in this group of five organisations or, where that is significantly diverse, the practices of Grameen itself.

2.1 Social collateral

The orthodox story is that primary groups play a major role in the success of MCPs, both by excluding risky borrowers, through refusing to accept them for membership; and by assuming responsibility for the repayment obligations of defaulters. It is true that all MCPs, except Proshika, follow the practice of obtaining from the members of the primary group a formal joint guarantee of repayment of loans allocated to individuals. Proshika is even more group-focused: loans are given to groups (of 20–30 people), who in turn pass the loans on to individual members. While group members formally accept the notion of joint group liability for loan repayment, in practice borrowers are *individually responsible* for repayment in all five programmes, including Proshika. If a member fails to repay her loan, both the programme field staff and group leadership attempt to secure repayment *only* from the individual defaulter. Demands for repayment are not made on other members of the primary group. Other studies – Jain (1996), Matin (1997) and Ito (1999) – confirm that "strong" forms of group liability are not enforced in practice. Even a "weaker" form of joint liability – non-renewal of loans for borrowers in the same primary groups as defaulters – is not routinely enforced. Only in the initial years of the programmes was it common to deny loans to other group members if an individual member defaulted. In all MCPs, the delayed repayments or defaults accumulated as unpaid debts while the cycle of issuing new loans and securing repayment continues uninterrupted for non-defaulters within the primary group. The concept of effective group responsibility for loan repayment is best viewed as one small and largely nominal element within an array of norms and practices designed to give borrowers a sense of affinity with "their" microcredit organisation and to instil within them a culture of financial responsibility and discipline.

2.2 Borrower participation

Do members in some significant way influence the operational routines or policies of MCPs? In all the MCPs we studied, secondary groups meet weekly, or almost weekly. All borrowers are expected to attend, for this is the occasion when they meet with programme field staff to undertake financial transactions, i.e. to submit loan applications and obtain approval, and deposit repayment and saving instalments. To the extent that public group meetings can provide a semblance of participation, these practices could be – and often have been – viewed as participatory. It is probably the frequency of secondary group meetings, allied to myths detailed above about the significance of the primary groups, that underpin the view that borrowers played a significant role in both operational decisions (e.g. determining who got how much credit) and in setting organisational policies. The reality is very different: there is barely any effective participation of members in either operational or policy decisions. The main exception lies in the fact that, within Proshika, groups receive loan money and then allocate that to individual members. However, here as with all the other programmes, Proshika management set the terms and conditions of loans. In all MCPs, primary groups do exercise influence through their power to sanction the recruitment of new members, but even here the programme field staff have veto power. There is otherwise very little participation, in the sense of influence – as opposed to physical attendance at meetings. None of the organisations have a formal mechanism through which borrowers are involved in shaping programme-wide policies. While some members sit on the Grameen Bank's board of directors, the organisation's operational policies are not decided at that level. Further, borrower representation is on the basis of nomination by the programme management. In all five programmes, all decisions relating to individual loans are guided by standard programme norms. These norms, relating to interest rates, repayment patterns, required savings rates etc., are set by central management, with no scope for local adaptation or local participation. Borrowers play no role in sanctioning new loans to fellow members at the local level: these are given as a normal entitlement to each member after they have completed repayments of previous loans. The loan size is shaped by the expressed need of the concerned borrower and is usually subject to an upper limit specified by the programme management. In all five programmes, there is a general trend towards diminishing the latitude of decision making available to groups.

2.3 Absence of subsidy

The failure of government supported credit programmes in developing countries has often long been attributed to their policy of subsidising interest rates (e.g. Adams *et al.* 1984). This, it is argued, (a) undercuts financial sustainability; (b) diverts loans from the poor to powerful groups that wished to benefit from cheap credit; and (c) signals to programme managers that cost recovery and financial discipline were not critical issues. Contemporary microcredit programmes have been lauded for *not* following a regime of low interest rates. Yet all five programmes we studied obtained subsidised funds for initial capitalisation and, in many cases, for meeting part of the operating costs. In other words, they were – and in some cases are – being subsidised. nformed observers of the microcredit sector have asserted that not more than five per cent of microcredit programmes worldwide could become financially viable without subsidy.[5] Although our sample of microcredit programmes would fall within this category of best performers, they all depended on subsidies for a considerable period during their early years. By the late 1990s, only BRAC and ASA appeared to have attained the capacity to meet full operational costs and capital needs without any kind of subsidy.

If microcredit programmes have *not* enforced joint group liability; have *not* involved borrowers in sharing information or making decisions; and have *not* avoided dependence on subsidy, what explains their success in reaching the poor and in maintaining loan recovery rates of 95 per cent and above?

3 Reality: explaining success

Credit is a business in which one party, the lender, provides a set amount of money to another party, the borrower, who promises to repay the original sum with interest within a fixed period of time. Formal sector credit has traditionally been organised around two principles. First, the loan is provided only if the borrower is considered to have adequate future earning possibilities. These are determined through assessments of existing income and expected return on planned investments, on the assumption that borrowers will be able to repay loans and fulfil their contractual obligations only when their existing and new income flows are, given reasonable margins, collectively large enough to cover the repayments. Second, conditional property rights are created on

[5] Morduch (2000) reports a panel discussion at Boulder, Colorado where such views were voiced by the senior and experienced donor and NGO representatives involved with microcredit.

the borrowers' assets in the form of collateral. This is done to ensure the security of the lender by assuring loan recovery if the borrower fails to repay. This commercial bank perspective appears to have shaped the conventional understanding of Grameen-type MCPs. Their success has been attributed to factors that seemingly enable them to fulfil effectively, albeit in unconventional forms, these two functions of loan assessment and assertion of collateral claims. The alleged involvement of (primary) borrower groups in loan assessment decisions has been understood to overcome the problem of information asymmetry, which had limited the capacity of commercial banks to operate at sufficiently low cost in the informal sector. Neighbours, it is believed, know who is creditworthy. And the apparent collective liability of those neighbours (primary groups) for loan repayment has been interpreted as social collateral, a substitute for the asset based collateral that the poor are unable to provide (Stiglitz 1990). This interpretation has been repeated so often that most MCP managers appear to regard these group-based mechanisms as the core reason for their success.

The conventional understanding is misleading. Loan assessments and collateral claims are best viewed as means for facilitating repayment, not ends. The critical challenges facing MCPs are significantly different from those facing conventional banking. They are above all the need to handle, at low cost, a large number of very small cash loans and repayment transactions, each of them providing the potential to generate only a very small interest income. It is this problem of high transactions costs that had hitherto largely prevented formal commercial banking organisations from operating in rural areas of poor countries, leaving the field open for informal "moneylenders" and a few loss-making government programmes. We can better understand the success of the Grameen model by exploring how MCPs simultaneously have managed to meet three objectives: (a) keeping costs low; (b) offering a set of products (loans) that are attractive but matched to the income-savings potential of individual borrowers; and (c) enabling, encouraging and enforcing a high level of loan repayment. The Grameen-type MCPs achieved these goals through experimentation, (increasingly) through competition with one another for members and/or donor support, and through integrating an eclectic set of ideas and practices into relatively coherent wholes – that are nonetheless undergoing continuous evolution. Many of the key ideas and practices are interdependent, in the way they are implemented or in their effects. It follows that one could categorise and present them in many different ways. We have tried to be as concrete as possible in suggesting that there are five broad sets of principles and practices underlying the success we want to explain. They overlap to some degree.

- First, the MCPs have a strong operational focus on providing a narrow and standardised range of services. While this is in some respects problematic for borrowers, it greatly facilitates the task of running an efficient, low cost operation characterised by strongly hierarchical monitoring and management practices.
- Second, the financial product and operational policies are designed to match the existing income and savings potential of borrowers, creating the right basic conditions for high repayment levels.

- Third, the loan product, while not cheap and often inconvenient to borrowers because of inflexible loan and repayment schedules, is attractive to them relative to the available alternatives.
- Fourth, the programme managements have created a social and institutional environment that places strong social and moral pressures on borrowers to follow programme norms, above all to repay loans on schedule.
- Fifth, these organisations have evolved systems of personnel management and motivation that evoke good work performance from field staff operating in difficult environments.

3.1 Operational focus

Our MCPs offer a very focused (i.e. narrow and standardised) range of services. First, they are microcredit, not microfinance, organisations: they deal only in credit – lending and repayment – and do not engage to any significant degree in deposit (savings) mobilisation. The standard requirement that members make compulsory savings to be eligible for loans is not an element in an integrated set of financial services, but a test of commitment and discipline. These compulsory deposits provide a very small proportion of total lending resources. Second, with the exception of Proshika, these MCPs provide only credit, and none of the associated services of loan appraisal or advice that are found in conventional banking. Members make their own decisions about loan use. How then do providers deal with the likelihood that every borrower will require a product – a loan amount and a repayment schedule – that is specific to her circumstances? This would impose high computation and transaction costs on the lender. The MCPs deal with this by offering only a very limited range of loan sizes and no choice about repayment schedules. ASA, for example, issues loans only in units of 1000 Taka. All MCPs have standard operating rules to specify the size of loan that can be granted to a borrower for a particular loan cycle. Loan repayments typically are weekly. The first becomes due the week after the loan is issued. Each repayment is for an equal amount. A typical loan repayment period is 50 weeks. Borrowers are not permitted to take a new loan until the previous one is discharged.

This operational focus (standardisation + narrow range of services) contributes greatly to the efficiency of the whole microcredit operation, through at least five separate but related mechanisms:

- First and perhaps most importantly, focus reduces routine operational costs. The MCP field and supervisory staff can concentrate on two closely related activities: issuing loans, and collecting repayments. Compared to more conventional banking, there are fewer decisions to be made and fewer procedures and routines to be followed. MCP staff are in some important respects very committed, but they do not require the level of training or the range of abilities that are required in more conventional banking. They can be hired more cheaply.
- Because all staff are focused on one closely-integrated set of activities, united by a common metric of money, it is relatively easy to monitor and assess the performance of individuals and small units, and thus to assert managerial control. The central performance questions concern the amounts of loans disbursed, and

repayment rates. The aspect of MCP activities that visitors are taken to see – the regular meetings where borrowers collectively meet field staff and make their financial transactions – are backed by intensive, hierarchical monitoring and supervision of staff performance at all levels in the organisations.

- The clarity of operational goals makes it relatively easy for lower level staff, in particular, to resist pressures to exercise discretion in favour of individual borrowers, or generally to adopt too sympathetic an attitude to problems of default.[6] The field staff of Grameen, BRAC and ASA have a reputation of being tough on defaulters. In isolated cases, Proshika has accepted the help of the police to effect loan recovery.
- As is explained in the next section, an indirect but nevertheless very useful result of the narrowness of the range of loan types and repayment schedules is that one large category of potentially problematic borrowers – those without the capacity to repay loans from pre-existing savings – find it difficult to access loans at all.
- Operations are transparent to members because of the combination of (a) the narrow range of services and (b) the public nature of the regular meetings between borrowers and field staff where loan decisions are announced and repayments actually made.[7] These meetings, that involved secondary groups – and therefore perhaps 30–40 people – are normally held weekly. All transactions are public. Such transparency contributes to programme success in several ways. It increases the trust of members in the integrity of the programme, since all can understand what is going on. It reduces the chances that field staff or more powerful members will abuse their power over ordinary members, who are mostly poor and female.[8] And it provides, as we explore in more detail below, highly visible evidence of the need to adhere to repayment schedules.

3.2 Repayable loans

Providing such a narrow and standardised range of loan services greatly reduces transactions costs. But how do MCPs protect themselves against borrowers taking loans larger than they can repay? In practice, they try to restrict loan amounts to the capacity of borrowers to repay *from their regular savings*, and not, as in conventional banking principles or according to the prevalent image of MCPs as promoters of micro-entrepreneurship, according to the expected income from the investment that the loan is supposed to be financing. This is an important and under-appreciated departure from conventional ideas, and a significant cause of the misunderstanding of the reasons for the achievements of Grameen-type MCPs. It is now widely accepted that

[6] For example, a member of CARD failed to repay a loan instalment in time, and according to programme rules, she was not entitled to a new loan. However, after she explained her situation to the field manager, he was convinced that her failure to adhere to the repayment schedule was unintentional and that she was capable of making effective use of the loan. She requested a new loan and a rescheduled (overlapping) payment cycle for the old loan. After investigating the case, the field manager made the discretionary decision to authorise the special request. This decision had considerable knock-on effects. The repayment performance of other members began to decline and many rescheduling requests were reported. The field manager was thus faced with the difficult and time-consuming task of discriminating between apparently similar requests. CARD subsequently made a policy decision to follow the rules in an inflexible manner.

[7] Loan disbursements are made from office premises, but normally in a transparent manner.

[8] Senior managers were concerned about the potential for such abuse.

even poor rural households save, often through non-banking financial services. A survey of rural informal finance in Bangladesh and India, for example, revealed that the poor make use of a variety of non-formal mechanisms to save small amounts regularly (Rutherford and Arora 1997). Our MCPs kept their loans within the repayment capacity of poor households, from normal savings, through employing two particular techniques, neither of them requiring investigation into the finances of individual borrowers. One was insisting that each member starts small, and demonstrate their capacity to re-pay before moving on to larger loan amounts. For example, an initial loan of around 2,000–2,500 Taka is typical for the Bangladesh programmes.[9] This might increase by, say, 500 Taka in each new yearly loan cycle. The other technique was the universal insistence that repayments were to begin immediately – the week after the loan was disbursed – and were to be made in equal weekly instalments. Borrowers faced a concrete discipline and limited temptation to give repayment anything but high and immediate priority. All our Bangladesh programmes required their starter loans of 2,000–2,500 Taka to be repaid through fifty weekly instalments of around 55 Taka. That amounts to around 12 per cent of the weekly income of a five-person family living on half the poverty line income of US $0.5 per person per day (US$ 1=Taka 50). Even if the new investments financed by the loan failed to generate additional income for the household, many borrower households could still meet the weekly repayments by drawing on their existing savings potential. Those that could not were deterred from taking a loan in the first place by the obligation to begin repayment the next week and the fact that, as we explain below, the mechanisms to enforce repayment were quite compelling.

One implication of this set of practices has been widely noted: Grameen-type MCPs tend to lend mainly to people who have the scope to re-pay from existing savings or income, whether their own or, for example, a reliable relative earning a regular salary. The poorest are by necessity excluded (Ito 1999; Zaman 1999; Wright 2000: 262). The set of loaning practices described above not only keep low the costs of dealing with actual borrowers, but contribute to the same objective by excluding the kinds of borrowers who will generate high costs – not through necessitating a very large number of small financial transactions, but by defaulting and thereby upsetting the smooth running of an organisation whose financial viability depends on its capacity to process an enormous number of transactions in a very standardised fashion, without disturbance.[10]

[9] Note that there were no formulae directly linking the amounts of compulsory savings that borrowers were obliged to deposit with the MCPs to their loan entitlements or repayment obligations.

[10] Prior to 1994, Proshika followed a different procedure to try to protect itself against borrower default. Repayment instalments were scheduled according to the expected income flows from new investments. Even though the loan decisions were taken with active and repeated consultations with local people to check the capacity of the borrower to successfully and profitably invest the loan, the income was often found to be lower than projected, due partly to unforeseen changes in the market or investment failures. Repayments were often delayed. From 1994 onwards, Proshika revised the repayment schedule to incorporate a link with borrowers' regular weekly savings, although it retained a partial linkage to projected additional income flows from the new investments. Loan recovery performance improved significantly. This is additional evidence of how and why the Grameen-type loan package works, at least in the conditions of rural Bangladesh.

3.3 Attractive loans

We have already explained above that the range of borrowing and repayment options available to clients of MCPs is generally very limited, and especially so if one begins with the illusion, much fostered by the proponents of these programmes, that they are intended mainly to support entrepreneurship. Anyone schooled in normal banking would find it hard to reconcile this inflexibility with the conventional image of our MCPs financing millions of small rural businesses. There are clear limits to the attractiveness of MCP loans, notably to (a) people who need regular business financing; (b) people who lack the capacity to meet the tight repayment schedules from their regular savings; and (c) relatively high status families, especially women, who are unwilling to go through a weekly ritual of sitting on the ground in groups at a public meeting, chanting in unison slogans in praise of the credit-provider or of microcredit, and having their financial transactions made common knowledge. MCP loans nevertheless appeal to millions of clients. In what sense? Part of the answer lies in two quite specific attractions.

First, MCP loans are physically and socially accessible to poor people. Even government-supported special banking services for the poor are located in urban centres, and often are not easily accessible. Many poor people, particularly women in Bangladesh, have little experience of life outside their immediate neighbourhoods. They feel vulnerable and uncomfortable with the prospect of travelling to formal offices to undertake financial transactions and participate in decision making. The MCPs were structured to provide financial services to borrowers and conduct all programme transactions in a familiar setting; close to their homes and in the presence of other community members. Recall that rural Bangladesh is very densely populated. Many people can access loans without leaving their immediate home locality. None of the programmes required borrowers to visit programme offices more than once or twice a year; and this visit was mainly to collect loan money about which decisions had already been communicated in a local meeting.[11]

Second, while informal financial markets ("moneylenders") can rival MCPs in providing services on borrowers' doorsteps, they tend to be more expensive. Interest rates on MCP loans, although high, are attractive in comparison with the alternatives. For example, in 1999 CARD charged a nominal interest rate of around 50 per cent on outstanding loans, when inflation was only around 10 per cent. In their early years of operation, ASA and BRAC charged around 36 per cent and 30 per cent, respectively. In 1998 both were charging around 22–25 per cent. These interest charges were in addition to group saving and insurance charges that most programmes instituted as a compulsory part of credit programmes. At this time official agricultural loans from the Government of Bangladesh were available at around 16 per cent. The supply was however restricted. For most people, the alternative was the informal credit market, where interest rates were higher than those asked by MCPs.

[11] CARD is a partial exception. One type of CARD loan, that is issued frequently, requires borrowers to visit the branch office.

There are another set of reasons, much less well documented, why MCP loans remain attractive despite their inflexibility. As far as one can judge (Matin 1997; Ito 1999) many borrowers find ways of offsetting the inflexibility of loans from individual MCPs through using them in conjunction with other, more informal sources of credit: either "moneylenders" or, increasingly in Bangladesh, as market coverage increases and different MCPs operate in the same areas, other MCPs. Some individual borrowers can use individual MCPs more as providers of a component of a financing package than as a total credit service.[12]

3.4 Social and institutional pressure to repay

Much of the success of microcredit programmes lies in ensuring that 95 per cent of borrowers do not delay loan repayments. Organisations that have to put much effort into collecting overdue payments are already in trouble. MCP managements have created a social and institutional environment that places strong social and moral pressures on borrowers to repay loans on schedule.

Contrary to the conventional myth about the central role of "social collateral" embodied in the *primary group* of about 6 members, the socialisation processes that contribute to high repayment occur mainly in the context of meetings of *secondary groups* of 20–50 members. Though the MCPs organise borrowers into primary groups, none of the organisations had any formal mechanism to facilitate, explicitly direct or monitor interactions at that level. Borrowers do not meet or undertake any activity at this group level. Indeed, it was difficult to ascertain whether these groups were more than paper entities, or if social interactions at the primary group level were substantially different than those normally found between neighbours. In each of the MCPs studied, the secondary groups meet weekly, fortnightly or monthly. This is where members request and receive loan authorisations, and make repayments – all in the context of substantial formality and ritual. Although it is likely that there is continuous informal contact between members of these secondary groups, it is only in this kind of meeting that members come to know of the activities of fellow group members in any definitive sense. In all programmes except Proshika, the field staff of the MCP attend and manage the meetings and conduct all financial transactions.

When a borrower fails to repay her loan, field staff exert pressure on the defaulter, both through their own actions and through requests to other members to support them. The field staff do not limit their search for support to the members of primary groups, who formally bear co-responsibility, but mobilise all members of the secondary group present at the meeting, especially influential individuals. Pressure on defaulters to repay appears largely to entail ceaseless follow-up and hectoring to propel the defaulter to find the required money, even if that meant borrowing from another source. One informant suggested that field staff would lash even the grave of a member if she died before repaying her loan. The statement sounded rhetorical. However, Anne Marie Goetz reports seeing a fieldworker urging a group of women to raid the house of a defaulter to seize possessions that could be sold to pay off the loan (personal communication). At a more routine level, field staff told us that

[12] Correspondingly, loans are sometimes used for on-lending to other women, hoarding commodities or dealing in smuggled saris (Goetz 2001: 181).

they do not return to their offices until defaulters have paid. Given their schedule of weekly visits to meetings of secondary groups, this kind of follow-up can be undertaken without adding much to staff time and costs. Note that "traditional moneylenders" follow similar default recovery procedures: ceaseless follow-up and use of influential local people to exert pressure. In both cases, such "harassment" serves both an immediate purpose of trying to get the money back and a more important and broader purpose of signalling publicly that the consequences of becoming a defaulter are very unpleasant. MCPs cannot afford to get into the business of pursuing defaulters in a big way, even if they could find cheap and effective ways of doing it. Their success depends on defaults being rare occurrences.

A comparison of the history of different components of the Proshika loan programme illustrates the power of employed field staff to enforce loan repayment. At one point, Proshika's (single-tier) groups managed both (a) their own saving fund from which they distributed loans entirely at their discretion and on their terms and (b) a revolving loan fund from Proshika, that was lent to members on terms stipulated by Proshika. Even though the Proshika field staff were not directly involved in or responsible for loan recovery from the latter funds, they did in practice engage in monitoring and follow-up efforts. And rates of recovery of loans from Proshika's revolving fund were much higher than those made from the groups' own savings funds. The failure of the group leadership to recover the latter loans depleted many local group funds. Since this, in turn, threatened group survival and Proshika's own funds, the organisation combined the local group savings with its own funds, and used its field staff to monitor repayment.

We emphasise the extent to which good repayment records are the result of social and institutional pressure on defaulters, rather than of the more benign sounding "social collateral" in the orthodox story. This is not to suggest that the group organisation, especially the secondary groups, play no role: the regular meetings of the secondary groups provide the locale and context in which social and organisational pressure can be exerted. Further, secondary groups play a more specific role in facilitating loan repayment in the initial phase of some programmes. When a member can neither meet loan repayment schedules nor source other money for this purpose, field workers encourage her to take a short-term, interest free and typically informal (but publicly known) loan from other member(s) of the secondary group (not especially the primary group) and agree to repay instalments in parallel with the programme loan. This means an immediate obligation to pay double instalments, one instalment for the initial loan and one for the temporary loan. Programme field staff actively participate in and facilitate such informal arrangements to the extent of following up the repayment of the temporary loan as carefully as they monitored repayments of the official scheduled loan. Members sometimes default on these temporary loans, through sheer inability to repay. In the longer established MCPs and secondary groups, willingness to provide such temporary loans has declined over time. In such cases, and especially within the Grameen Bank and BRAC programmes, potential defaulters are expected to find alternate loan sources outside of the secondary group, and prior to the weekly group meeting to avoid disrupting it. Only in the younger programmes, namely, CARD in the Philippines and ASA in Bangladesh, where the groups were three to five years old, did we find instances of informal, short-term loans within the secondary group.

The story is similar with another component of the practices sometimes labelled "social collateral": refusing new loans to all members of a primary group if one or more individuals has defaulted. This group penalty was often enforced in the initial years after programme implementation, for example in CARD. As the groups became mature and members established regular loan repayment records, such group penalties were vehemently opposed by the members who were regular in repayment. Programme managements have found it difficult to enforce these collective penalties. With the exception of CARD, the other, more mature programmes issue loans to individuals largely on the basis of only their personal repayment record.

Many seasoned MCP managers felt that, as long as delays in loan repayments remained limited to 2–3 per cent, most could be dealt with through organising temporary loans from other members (see below). Actual loan recovery, as far as the organisation is concerned, would then approach 100 per cent. Successful MCPs have managed to operate around these levels. If for some reason repayment delays exceed 4–5 per cent, it becomes difficult to contain the slide, as is illustrated by the experience of Grameen Bank over 1997–99. Until 1992–93, Grameen's on-time loan recovery rate had remained at least 95 per cent. During 1993–94, it began a decline which reached 70–75 per cent by the end of 1999. Apparently, tolerance for delayed loan repayments even by a small number of members was a signal to the others that the programme management would tolerate delay.

3.5 Personnel management and motivation

We have argued that a key element in the success of MCPs has been their capacity to keep costs low. This has several components. Two in particular have been discussed above: keeping unit transaction costs low by providing only a narrow range of standardised services; and avoiding as far as possible the direct and indirect costs of significant loan default. Two other aspects of cost containment are the focus of this section: keeping down staff costs; and accounting closely for money. Microcredit programmes are vulnerable on both these counts. Staff remuneration represents their major (non-financial) expenditure. It is important to keep staff costs down. Yet staff are widely scattered in rural areas, and their work performance cannot be directly observed. And they are physically handling large sums of money every day. That money needs to be accounted for – and deposited speedily in banks – to prevent corruption and to allow the organisation to make best use of money markets by putting unused cash on deposit. How do our MCPs achieve these objectives?

Some components of the answer have already been given. In particular, the operational focus on loans rather than savings, and the narrow portfolio of loan types available, contribute greatly to the broader objectives. The tasks of field staff are relatively simple, and require limited training. And both the means and the criteria for monitoring and assessing the performance of each unit in the administrative hierarchy are to a large degree given: quantitative performance in making loans and collecting (and banking) dues. Unlike many organisations, especially organisations involved in rural development activities in poor countries, there is no major divergence, from the organisational perspective, between the quantitative measures available to assess performance and the ultimate objectives of the organisation. By using performance in making loans and collecting repayments as the primary criteria to assess performance (both short and long term), the MCPs face limited risks of stimulating "goal displacement", i.e. encouraging staff to focus on the things that can be measured rather than more important but intangible objectives. To this degree, good organisational performance is latent in the very activities on which the MCPs focus. Latent performance is translated into reality through two main sets of mechanisms. One is the employment by senior management of simple financial performance measures to monitor activity, identify problems, and correct mistakes, on a daily basis. The other set of mechanisms require a little more explanation: managerial practices that encourage good work performance by increasing the extent to which the staff identify with the MCP and its mission. On the staff side as well as on the member side, MCPs are "strong culture" organisations: stakeholders feel and express commitments to the organisation and to their jobs that extend well beyond any immediate instrumental need to fulfil an employment contract, please a particular supervisor, or earn a particular reward (DiIulio 1994; Grindle 1997; Tendler 1997: Chapter 6).

Our MCPs are diverse in their organisational cultures and in the mechanisms employed by managements to create, reproduce or modify these cultures. The following are the most common practices that managements use to create a positive sense of affiliation with the organisation and a commitment to work:

- Considerable efforts are made to disseminate and reinforce messages about the intrinsic importance of microcredit to broader national or humanitarian goals, and to publicise success. Staff tend to feel that their work is "special".[13]
- To compensate for the fact that most work is conducted in what are generally perceived to be unattractive field locations, staff are generally paid salaries similar to those paid by commercial banks, but also have enjoyed substantial promotion opportunities because of the fast expansion of the MCPs and the general practice of promoting from within.
- The social backgrounds and education of most staff to some degree distance them from the villagers among whom they are obliged to live. The MCP managements help ease this tension by encouraging and supporting the sharing of accommodation and living facilities, in villages, by small groups of staff members ("campus style living").
- Campus style living is one dimension of a broader effort partially to insulate employees from social pressures that might adversely affect their job performance. They should have some autonomy from the villagers among whom they live and from their own family obligations. With the exception of Proshika, all of the MCPs had relatively small field staff teams, of 10–12 members or less. This facilitated close contact

[13] For example, Goetz (2001: 207) talks of the 'preoccupation with performance at BRAC', the high general work commitment, and positive public image of the organisation and its staff.

among the staff and the development of peer groups. Teams were relatively un-hierarchical, and led by a "team in-charge", who was trained to work as team leader. S/he was expected to support individual team members and help to solve problems that a field worker could not tackle alone.[14] Organisational norms, such as adherence to time discipline or acceptance of organisational decision making structures, whether hierarchical or participatory, were strictly enforced for all staff members. In all of the programmes, the management actively encouraged staff to avoid social obligations, such as taking a long leave when a family member was ill, if their work would suffer as a result. Creating team norms that were distinctly different from prevalent social norms strengthened peer group coherence and the power of peer reference examples.

- All the programmes placed major emphasis on the field visits of senior officers and on ensuring that they shared the burdens of field work and "campus" life experiences with the field staff. In ASA and Proshika, the area officers were not given any office of their own; they spent all their time visiting the different field offices under their charge. In all the programmes, the regional officer spent as many as 15 days per month in the field. This helped the senior staff members to stand as referent examples of appropriate work culture. In all of the programmes, legends had been created out of the field experiences of senior managers. This heightened team spirit and set the pace for new staff to follow.
- While decision making was centralised, it was mandatory for senior decision makers to hold extensive consultations with the field staff and borrowers to ensure that decisions remained sensitive to grassroots realities. This, along with the extensive field exposure of senior staff, helped ensure that major decisions reflected field level lessons and realities and were sensitive to the viewpoints of those responsible for implementation.

4 Diversity and dynamics

The understanding of the functioning of MCPs in the previous section is a composite. We have focused on what they have in common, rather than how they differ. But there are substantial differences. For example, unlike other MCPs that insisted that loans be repaid in equal weekly instalments, Proshika to some degree synchronised loan repayment schedules to the expected cash flow from investments financed by the loan. Each programme asserts pressure on loan defaulters to different degrees. Each adopts different mechanisms to increase borrowers' incentives to use the services offered, improve access to the programme, increase the credibility and transparency of transactions, strengthen peer group examples, and institutionalise supervision and error correction. Similar diversity could be seen in their policies to enhance staff performance. Some appreciation of these differences is important to the central argument of this paper: that there is no unique model of a

[14] In a typical BRAC office, the total staff exceeded the optimum range of 10–12, but the number of staff involved in microcredit operations remained in this range. Proshika had a much larger field team located at one office, but it had instituted special mechanisms to generate joint team responsibility among field staff. For example, all field level decisions were taken in the fortnightly meetings in which all staff members took part.

Table 4.1 Main organisational and management features of the five case study microcredit programmes

	Grameen	BRAC	Proshika	ASA	CARD
General organisational characteristics					
Inception of the organisation	1977–8	1971	1982	1982	1986
Inception of the microcredit programme	1977–8	1987–8	1994	1991	1991
Number of borrowers (1998)	2.7 million	2.2 million	2.7 million	1 million	21,000
Rate of on-time loan recovery	98% until 1992–3; currently <90%	97–98%	90–94%	99%	98–99%
Borrowers per field staff	350–400	400–450	700–800	250	150–200
Outstanding loans at end of 1998	23000 million Taka	8099 million Taka		4176 million Taka	83 million Pesos
Product characteristics					
Special product or service features	Multiple and large size loans	Single loan with technical assistance	Technical assistance and social action	Fast service and many types of savings	Consumption credit and savings products
Interest rate, 1998	20 %	30%	18%	25%	50%
Savings type	Compulsory	Compulsory	Compulsory	Compulsory and voluntary	Compulsory and voluntary
Business strategy					
Size of secondary group	40	50	15–25	25–30	25–30
Weekly loan repayment	Yes	Yes	In part*	Yes	Yes
Basis of decision on amount of loan	Rules	Rules	Group review	Rules	Rules and review
Organisational control over the mode of loan use?	None	None	Group scrutiny	None	Group review
Management of borrowers					
Physical collection of savings or loan repayments by employed staff?	Yes	Yes	No, by the group	Yes	Yes
Enforcement of loan repayment by the staff?	Yes	Yes	Partly, also by the group	Yes	Yes
Emphasis on group development	Moderate	Moderate to High	Very High	Low	Moderate to High
Staff management					
Campus living for field staff	Yes	Yes	Partly, but strong on group culture	Yes	Yes
Emphasis on reduction in task-strain	Moderate	Moderate	Low	Very high	Moderate
Staff training effort	Moderate	Moderate	High	Low	Moderate
Supervision hierarchy	3 tiers	2 tiers	3 tiers	3 tiers	2 tiers

Notes: * Repayment schedules for Proshika loans have two components: a fixed weekly repayment obligation related to loan size; and a variable obligation related to the expected cash flow from the investment.

successful MCP, and that organisations and programmes need to be adapted carefully to environments. The pioneer Bangladesh MCPs have followed this principle. Their operating environments have changed over time, in large part because so many MCPs have become operational and effective. They have been able to learn from each other, and from perceptions of experiences overseas. To some degree they compete for the same clients. And to some degree they develop specialised niches. We summarise some of these dynamics in this section. Table 4.1 contains a snapshot summary of some of the key differences in organisation and practice between our five case study organisations. The bulk of this section is devoted to a brief summary of how the organisation and practices of the four Bangladesh MCPs have evolved over time.

4.1 Grameen

The Grameen Bank pioneered the new approach to rural credit with some distinctive design features: exclusive focus on the poor; enrolment of women as household representatives for loan transactions; the formation of local borrowers' groups; and the promotion of compulsory weekly savings that are linked with loan repayments. Throughout its existence, Grameen has had access to low cost capital from donors. This has enabled it to both charge low rates of interest and cover some of its operating costs through investing a part of this low cost capital in interest-bearing securities. In the early stages of operation, Grameen focused on providing small loans and establishing a reliable record of timely loan repayments. Once the loan cycle was established, the organisation concentrated on expanding the borrower base while maintaining a low average loan size and a high loan recovery rate. From 1978 to 1992, the design parameters remained essentially unchanged, and the average loan size per borrower did not increase beyond 2,500 Taka even though its borrower base had grown to around one million households.

Towards the mid-1990s, however, three factors led to a shift in policies. First, Grameen felt compelled to respond to the criticism that it was overly dependent on subsidised capital. It took action to raise the average loan size so that interest earnings would better cover operational costs. Second, recognising the varying credit needs of different borrowers, Grameen began to offer a diversity of loan packages. It also began to permit some borrowers to take two or three loans simultaneously. Third, it made attempts to reduce its ratio of staff to borrowers to contain operating costs. This was done mainly through increasing from six to eight the number of (five-member) primary groups in a "centre" (i.e. secondary group). This enabled one staff member to serve a larger number of borrowers in one meeting.

Each of these policy shifts impacted on other aspects of the Grameen programme, resulting in a new programme design. For example, the reduction in the ratio of staff to borrowers reduced the intensity of field supervision and left the lending programme more vulnerable to errors and problems. With the pressure to contain staff cost, the possibilities of continuous career advancement for staff also declined. The organisation and its staff were also ageing: "campus style living" became increasingly unattractive to the increasing number of long-term and older staff. These factors affected staff incentives and motivation, and possibly contributed to a decline in staff performance and to the declining rate of loan recovery that Grameen has experienced since the mid-1990s. While on the surface many design features of the Grameen programme appear unchanged – such as formation of borrower groups and weekly savings and loan transactions – a closer analysis reveals some significant transformations.

4.2 ASA

ASA's microcredit programme started only in the early 1990s. Timing is important: ASA could learn from the experiences of existing programmes. At that time, aid donors were already heavily committed to these existing credit programmes. There was also a growing opinion that "minimalist" microcredit, without much external support, was financially viable. ASA therefore tried to evolve an approach with minimal donor dependence. While following the overall Grameen policy template, it aimed to obtain higher interest earnings per borrower, and hence greater profitability, through increasing the average loan size per borrower. ASA managers assessed other programmes, saw that expenditures in member training and group development had little impact on timely loan repayments, and therefore decided to invest little in them. Correspondingly, ASA placed more emphasis on supervision and control to obtain compliance to repayment norms. The ratio of supervisory to field staff was higher than that of Grameen and BRAC. This led ASA to pay comparatively lower salaries than the other two organisations. ASA benefited from the investments made by Grameen in establishing a tradition and culture of timely loan repayment in Bangladesh. At the same time, it institutionalised stronger mechanisms to enforce repayments, such as taking a "sit-in" approach to loan recovery: field staff staunchly remained in the village or house of a borrower until loan instalments were made. To ensure that the field staff would have time to put this repayment enforcement mechanism into practice, ASA actively sought to simplify accounting and record keeping systems and to minimise the time required for administrative procedures. The policy climate of the early 1990s was shaped by perceptions that ACCION (Americans for Community Cooperation in Other Nations) was a very successful microcredit provider in Latin America despite (or because of) high interest rates. This made it more acceptable for ASA to charge a high interest rate. Charging higher interest rates than Grameen, the established leader in the sector in Bangladesh, ASA had to find other ways to attract borrowers. It thus developed a set of attractive product packages, including faster loan release, flexible savings programmes in which savings could be withdrawn at will, and fewer demands on borrowers in terms of member training.

While no detailed, large-scale study has been undertaken to compare the borrower profiles of different microcredit programmes in Bangladesh, our field research suggests that ASA, compared to other programmes, targeted fewer of the extremely poor and had the largest share of small traders/businessmen among its borrowers. This is compatible with ASA's programme design features that attract borrowers who, for example, value the fast release of loans over relatively higher interest charges. ASA's capacity to respond quickly to loan requests is also linked to its policy of mobilising capital through tapping existing financial institutions (both commercial banks and government sources), rather than relying on donors whose decision making processes are inherently slow and inflexible.

4.3 BRAC

BRAC, an NGO, is older than the Grameen Bank. However, providing credit to the communities in which it worked did not rank high in its priorities until the late 1980s. BRAC introduced a credit programme because of demand from its clientele that was stimulated by awareness of the activities of Grameen Bank. BRAC initially approached credit provision through encouraging community groups themselves to raise money through savings. It soon became clear that demand for credit far exceeded the groups' savings capacities. BRAC thus shifted to external credit provision, following the general approach of Grameen, with some significant policy adaptations. While in other organisations, including Grameen and ASA, microcredit programmes were handled at field level by a cadre of officer-level functionaries, BRAC's established strength in training grassroots workers enabled it to obtain a competitive level of performance from local recruits who could be paid lower salaries. BRAC, however, supplemented this field-level cadre with the support of high calibre and well paid officer-level staff and computerised accounting systems. The financial savings from the use of low cost field staff enabled BRAC to pay officer level staff higher wages, thus attracting highly qualified, talented people. It also made possible the provision of higher quality office infrastructure and support services, which in itself also attracted highly qualified staff. These factors together enabled BRAC to maintain the overall transaction costs per borrower at a competitively low level. BRAC management told us that this combination of local and highly educated staff, together with a relatively generous infrastructure system, both provides effective staff motivation and, to an extent, reduces the problem of an ageing staff experienced by other organisations. Towards the end of the 1990s, BRAC introduced a fortnightly instead of a weekly savings and loan collection schedule to contain operating costs.

BRAC's history as an NGO with a broader set of development programmes has helped generate an approach different to that of Grameen and ASA. BRAC integrated provision of microcredit with its broader local development goals, such as health, education, social awareness (emphasising social mobilisation and self-help) and local economic growth, seeking mutual reinforcement. For example, whenever members (largely women) took out a new loan, a health check-up was also undertaken. This increased health service coverage and helped to establish regular health monitoring and treatment for individuals. BRAC also incorporated credit provision with technical advice and an input supply service across a variety of economic sectors, although it should be noted that the costs of these services were met externally, and not by the microcredit programme itself.

4.4 Proshika

Like BRAC, Proshika entered the microcredit sector with an established approach to development encompassing community based, integrated development and empowerment, and introduced the credit programme in response to members' demands. Further, Proshika also linked the provision of credit with programmes of basic health, training and technical support, which were financed through donor grants. Unlike Grameen, BRAC, ASA and many other microcredit programmes, however, Proshika did not adopt a programme model in which staff play the central role in loan decisions and recovery. Rather, Proshika invested in training and developing group leadership so that borrower groups could take loan decisions and assume responsibility for loan recovery from members. Further, Proshika did not link loan repayment schedules to only weekly savings potentials but rather aligned loan repayments with expected cash inflows from loan investments.

Proshika established a carefully crafted hierarchical structure of borrowers' organisations that enabled staff to focus on both economic and socio-political empowerment. This approach has required heavy investment in developing the capacity of member groups. That in turn explains the relatively slow growth of its credit programme. Proshika is still in learning mode, working to discover design parameters that would enable it to achieve a loan recovery performance in line with that of ASA or BRAC. Proshika aims to set up a borrower-managed credit programme and to maintain low transaction costs through a low staff to borrower ratio, thus maintaining lower interest charges than other programmes. Although projections of loan and cost recovery performances appear to be encouraging, Proshika has not yet achieved a high, sustainable performance record.

While its initial entrance to the microcredit sector was significantly different than the other programmes, especially from Grameen, Proshika now appears to be moving towards the Grameen model summarised in Section 3. In 1994, the organisation began to link a significant part of loan repayments with weekly savings, while only a part of the loan repayment remained tied to expected new income streams. Further, like the other programmes, Proshika discovered that local groups were able to better organise loan recovery if the money originated from Proshika rather than from pooled group savings. This relates to the important role that Proshika staff play in following up on loan recovery even when it is remains the formal responsibility of local group leaders. Over the years, Proshika slowly increased the intensity of staff supervision, becoming more like the other MCPs.

4.5 The broad picture

The emergence of four national scale microcredit programmes and many other smaller programmes in Bangladesh has engendered a dynamic in the microcredit sector that has not yet been explored in literature. All four programmes now offer a wide range of services and packages to borrowers. ASA, BRAC and Proshika represent tree potentially effective alternatives to the Grameen model. Their service packages continue to evolve, and those changes then impact on operational costs and the wider manageability of the programmes. It is not yet clear which, if any, of the current service packages of the big four MCPs will prove stable. ASA appears close to offering a full range of savings and credit services to the poor in a financially viable manner. However, it has yet to fully account for the cost of providing savings services, which currently are subsidised by its credit programme. With an improvement in its management capacity, Proshika could stabilise its loan recovery rate to a level comparable to BRAC and ASA. This would ensure a viable microcredit programme, managed to a large degree by self-help groups, which could compete with ASA even in terms of operational costs and margins. Proshika also appears close to establishing an effective way to link local microcredit groups to broader social development programmes. BRAC has a mature microcredit programme that is effectively linked to sectoral development interventions. It has made some important basic reforms, such as developing a management structure in which each programme is handled by an independent division. However, questions remain about the cost effectiveness of this arrangement.

To date, the Bangladeshi MCPs – and others worldwide – have been competing strongly with one another, albeit in a muted fashion, for donor funds. We demonstrate in the next section that this kind of competition has major implications for how MCPs are understood. Another kind of competition – competition for clients – is beginning to emerge in Bangladesh. This is relatively recent. ASA and Proshika became major credit providers only after the mid-1990s, while Grameen and BRAC have grown rapidly over the 1990s. Prior to this period, there was little geographical overlap in the coverage of the different programmes and hence limited competition for clients at the grassroots level. The wider implications of this emergent competition are yet to unfold, although some early trends can be discerned. They appear to be positive. For example, ASA and BRAC have been influenced by the lower interest rates charged by Grameen and Proshika. ASA's relatively lower operational costs and high loan recovery rates are also gradually becoming the benchmark by which the performance of other programmes will be judged by donors and other stakeholders, including the MCPs themselves.

Let us note finally one significant limit to the potential diversity in the types of services offered by the big four Bangladeshi MCPs: it will be difficult for any of them to move in a major way into the business of deposit mobilisation. For their success in credit provision depends in large part on their achievements in refining organisational structures and practices dedicated to disbursing and recovering large numbers of small loans at low unit cost. Central to those achievements are the standardisation of practices, the simplification and routinisation of control procedures, and the manipulation of the attitudes and behaviour of both members and employees to fit programme needs. Deposit mobilisation is intrinsically far less responsive to such standardisation and manipulation of attitudes and behaviour. Savers cannot be obliged or coerced to meet standard, routine targets, and staff cannot so easily be judged on their ability continually to meet targets for deposit mobilisation. It is difficult for organisations that are specialised in one type of activity to take on board a different type of activity with equal effectiveness. Further, if much of households' savings potential is devoted to servicing loan repayments, the potential for the MCP to mobilise savings is necessarily reduced.

5 Advertising, image and institutional creativity

We have argued that the organisation, practices and success of the big microcredit programmes can to a large degree be understood from the perspective of business strategy. Let us pursue this a little further. Successful enterprises tend to (a) define their business or product in a way that is consistent with the techno-economic features of consumers/target groups; (b) match the product price to the capacity of consumers to repay; (c) establish retail points convenient to the consumer; (d) design a marketing package to elicit a desirable pattern of consumer behaviour; and (e) keep the cost of running the business lower than potential revenue. One could re-tell much of the story we set out above in similar terms. In particular, MCPs have (a) made their services attractive to borrowers/users; (b) ensured a match between the product price (i.e., loan repayment instalments) and the borrowers' paying capacity; and (c) set up local groups as both the convenient retailing outlet where the service is bought and as a major forum where its advantages are promoted.

We argue this analogy with business strategy because it is much more helpful for practical purposes than is any variant of the orthodox myth about MCPs. It provides a useful way of understanding the reasons for success and failure, and highlights the need to adapt organisations and practices to local and changing circumstances. We can however exploit the business analogy a little further. Specifically comparing the strategies of MCPs in poor countries with those of producers and retailers of high value consumer goods in rich countries, we can better understand why certain myths about the "Grameen model" have been actively promoted.

Businesses trying to promote high value consumer goods in high-income markets do not compete with one another, or market their products, principally in terms of their utility or value for money. "Image" is often more important: the creation of an association between the product and a desirable lifestyle or personality. The most important "market" in which MCPs have been competing to date – the "market" for donor funds – has similar characteristics. The customers – the donor agencies – are rarely in a position to optimise the use of their funds according to conventional cost-benefit criteria. Nor is that always a dominant objective. It is often more important for them to support activities which are both seen to be successful and which appeal to several of the various constituencies in donor countries who provide political support for aid budgets. Microfinance in general has had a strong political appeal in donor countries over the last two decades. The notion that microfinance programmes are primarily engaged in the promotion of small-scale enterprise has an obvious appeal in an era characterised by the strength of neo-liberal ideas about the benefits of the market and private enterprise. Concerns about gender equity also rose significantly up many policy agendas in the same period. It remains a matter of disagreement about how far the big MCPs were focused on women because they were simply better and more worthy borrowers, or because they were found to be more pliable members of organisations that demanded a great deal in term of attendance at meetings, engagement in ritual, and tolerance of strong and public moral pressure on loan defaulters. In any event, the positive gender bias of microcredit played very well with aid donors.

The coalition of ideas and interests that would support aid donors in subsidising microcredit was made wider through the specific interpretation of the success of these programmes that we have labelled the "fashionable fallacy". That fallacy has served to bring on board two groups that are of considerable importance in shaping international development policy agendas and ideologies. The first group are the NGOs and (transnational) social movements that recently have become more active and influential in development policy debates. Specialised in acting as the voices of "civil society" or the unorganised poor, they instinctively favour small-scale local citizen organisation and notions of "participation" (Fuglesang and Chandler 1988; Rhyne and Otero 1992; Houtzager 2003 forthcoming). Interpretations of MCPs that give a central role to the solidarity of small face-to-face groups of poor women are tailor-made for this constituency. The second group are "revisionist" economists sceptical of the benefits of unrestricted markets and state-minimalist policies. Virtually all such economists who have sought or achieved policy influence have nailed their intellectual colours to the mast of new institutional economics. This has permitted them to critique orthodoxy from intellectual territory that appears sound, and visibly remains "economics", rather than something more challenging. The implications for economic behaviour of uncertainty and limited information have been central to the intellectual agenda of the new institutional economics. Early intimations of the success of new MCPs in Bangladesh, especially Grameen, were grist to their mill. The notion that members of primary groups guaranteed each others' reliability and loans, although weakly based in fact, was seized on as a practical example of the capacity of the new institutional economics approach to explain the world. It was arguably the best known, and certainly one of the most distinguished, of the new institutional economists, Joseph Stiglitz, who is most often quoted in this respect (Stiglitz, 1990). MCPs were simply substituting neighbours' knowledge of one another ("social collateral") for the information about creditworthiness and the formal collateral required in conventional lending programmes. There was some basis in fact for this interpretation. But it is significantly wrong in several senses. Factually, it gets wrong many issues about MCP lending and repayment practices and misses the greater significance of the larger secondary groupings of borrowers compared to the small primary group. Conceptually, it places too much emphasis on formal organisational structure in shaping borrower behaviour and not enough on social norms and actual behaviour. And practically it ignores the extent to which those social norms underpinning the success of MCPs were continually and consciously reproduced through routinised procedure, ritual, and, on occasion, the public humiliation of deviants.

We are not suggesting here that the leaders of the big MCPs have perpetrated some kind of fraud on the aid and development community, presenting a misleading image of their programmes to justify continuing aid funding. The picture is far more complex than that, and notions of blame or of individual responsibility are irrelevant to our objective of obtaining practical understanding of why and how MCPs have been so successful. Our limited evidence suggests that the orthodox fallacy blossomed and spread in large part because that is what people in aid agencies wanted to hear, thought they had heard, or asked MCP leaders to talk about and publicise. To the extent that MCP leaders did foster a particular image, this could be seen simply as targeted product promotion in a "market" of aid abundance.

We end with a compliment and a paradox. The compliment is that we are deeply impressed by the organisational entrepreneurship of the people who established, managed and adapted the big MCPs. Their achievements are enormous. Unlike most heralded grassroots development programmes, these are virtually entirely homegrown. No expatriate advisers appear in leading roles; aid donors gave money and little else. But, to justify the continuing flow of that money to their own particular organisations and to the microfinance sector as a whole, MCP leaders and spokespersons have gradually found themselves, through a combination of circumstances and pressures, purveying a misleading interpretation of the reasons for their success. They emphasise a few elements in a complex organisational system, and are silent on many key components. That is the paradox. To properly appreciate the great achievements of the microcredit movement, one has to be more sceptical of its self-image than is normally considered polite or respectful.

Annex: operating costs and financial sustainability

Operational costs can be measured in a variety of ways, but we found that, given similarities in core service packages offered to the borrowers, the annual cost of providing the service to one borrower was a good comparative and analytical yardstick. The annual operational cost for providing credit-cum-savings services to one borrower in 1998 was 266 Taka for ASA, 307 Taka for BRAC and 561 Taka for Grameen. The figures on total operational costs include staff salaries and expenditure on other facilities including transport, infrastructural support and office expenses. In terms of the salary cost per borrower, BRAC performed best at 207 Taka, while ASA was on 217 Taka and Grameen on 465 Taka. The major cost difference between ASA and BRAC lies in non-salary expenses, which were around 100 Taka per borrower for BRAC but only 55 Taka for ASA. For Grameen, the figure was around 95 Taka.

Table A1 Comparative performance of three microcredit programmes

Taka (Tk): Bangladesh Currency (1US$= 50 Tk.); All monetary amounts in million Taka (MT) unless otherwise specified

	Parameter	ASA		BRAC		Grameen	
		1992	1998	1992	1998	1992	1998
1	Membership (000)*	144	1440	778	2735	1424	2300
2	Borrower members (000)**	90	800	400	2100	1424	2300
3	Number of loans issued(000)	88	864	358	2003	2016	5504
4	Total loan amount	170	4176	800	8099	5524	23000
5	Members' savings	29	1081	207	1495	2176	5404
6	Outstanding loans at year end	114	2211	774	5193	4424	14202
7	Average amount of loans outstanding during the year	67	1939	707	4539	3488	13396
8	No. of staff working on credit	911	2739	1820	4451	NA	10300
9	Total number of staff	1239	4656	2311	6190	13000	12499
	Income						
10	Interest on loans	11	470	139	1244	522	2660
11	Bank interest	6	16	37	45	178	280
12	Other income	1	18	0	15	72	82
13	Total income (10+11+12)	18	504	176	1304	772	2274
	Less						
14	Loan loss provision	0	43	15	255	56	747
15	Cost of capital ***	4	116	42	272	209	804
16	Total operational income (13+14+15)	14	345	119	777	507	723

	Operational costs						
17	Salaries and benefit	22	174	92	436	389	1072
18	Utilities and stationery		24	8	50	18	43
19	Rent & depreciation			7	30	29	53
20	Other expenses		15	31	129	95	122
21	Total operational cost	28	213	138	645	531	1290
22	Net profit (16–21)	-14	132	-19	132	-24	-567
23	Net profit less other income	-15	114	-19	117	-96	-649
	Performance parameters						
24	Total staff per thousand borrowers	14	6	6	3	9	5
25	Average staff salary cost ('000Tk.)	18	37	40	70	30	86
26	Non-salary cost per staff member (000Tk.)	5	8	20	34	11	17
27	Operational cost per borrower (21/2)	311	266	345	307	373	561
28	Staff cost per borrower (Tk.)	244	217	230	207	273	466
29	Other costs per borrower (Tk.)	67	49	115	100	100	95
30	Interest as % of average outstanding loans	16%	24%	20%	27%	15%	20%
31	Average size of loan per borrower (Tk.)	1889	5220	2000	3857	3879	10000
32	Outstanding loan per borrower (Tk.)	744	2424	1767	2161	2449	5824
33	Interest earnings per borrower (Tk.)	122	588	348	592	366	1157
34	Staff costs as % of operational costs	78%	82%	67%	68%	73%	83%

Notes:
* These figures have been inferred from programme records; ** This item includes members who only save but do not take credit; *** The cost of capital varies from programme to programme but for present purposes, it has been assumed to be 6% per year.

Salary payments accounted for the bulk of operating costs – 60–80 per cent. The non-salary component was also closely linked to the total number of employees. The programmes had many tiers and types of staff, but these were closely related to the total number of field staff employed. Putting aside the cost of capital, the total cost of MCPs was largely proportional to the number of field staff employed. All the programmes aimed to keep the ratio of field staff to borrowers at a chosen level. To the extent that the number of field staff was almost directly proportional to the number of borrowers served under each programme, there were few economies of scale to be reaped by expanding to cover a larger number of borrowers. Many financial analyses of microcredit programmes have been based on the assumption of existence of such economies of scale in such programmes

(Hossain 1988), but our data are cautionary. While the increase in the number of borrowers per staff member over 1992–98 in all the three programmes suggests economies of scale, more detailed scrutiny revealed that a larger number of staff were employed in the earlier years to prepare for planned programme expansion. Further, the programmes needed to pay higher average salaries once they grew large and acquired a public profile. Thus they effectively experienced a certain diseconomy of scale.

The operational cost per borrower had three major policy determinants: (a) number of field staff per thousand borrowers, (b) average staff salary, and (c) other expenses per staff member. Each of these parameters varied greatly between BRAC, ASA and Grameen. BRAC employed the least number of staff per thousand borrowers, but its non-salary expenditure per staff was the highest. This is explained through the superior housing, office, infrastructure and support facilities that BRAC provided. ASA had the highest ratio of staff per thousand borrowers, but its staff salary levels and the cost of other facilities provided to them were significantly lower compared to the other two programmes. Grameen's salary per staff was the highest, and the cost of other facilities per staff stood between the other two programmes.

ASA's success, in terms of lower staff and related costs, is partly related to the relative youth of the programme. It is thus likely that, over time, ASA's salary costs per borrower will rise due to secular growth in salary levels. However, it should be noted that ASA did practise a demonstrably lower cost culture than the other programmes under examination. For example, ASA's office infrastructure and overheads were clearly lower. BRAC, in contrast, appeared almost opulent – and was the most efficient in obtaining a high level of performance per staff member. Grameen's high staff-salaries raise an important policy issue. Grameen took a policy decision to link staff salaries with equivalent salaries in public sector banks. Since the latter salaries have risen steadily, Grameen's total operational costs have mushroomed, even though, in comparison to BRAC, Grameen has institutionalised a relatively low cost culture. Grameen's recent problems of poor loan recovery stemmed from policy decisions taken by the management in an attempt to contain staff costs. It can be argued that a significant reason for the decline of Grameen's performance in the second half of the 1990s is to its legacy of linkage with public sector salary norms.

The costs of capital are also important. Each MCP employed different strategies for mobilising capital. BRAC obtained capital at the lowest cost, followed by Grameen and then ASA. BRAC initially mobilised a grant capital fund far larger than that provided to ASA and later also built up its capital base through accumulated interest earnings on both this capital and programme profits. Grameen mostly has received low cost funds from various institutions, carrying an interest rate of 2–3 per cent. These constituted its loan capital base. But it has relatively little accumulated profits or interest earnings. ASA did not have comparable amount of grants or low cost funds, but since its stock of accumulated profits was rising rapidly, its effective capital costs could eventually decline to a level lower than that of the other two programmes. In terms of capital base, both BRAC and ASA were comfortably placed and in a position to support continued expansion of business operations. In contrast, Grameen required fresh injections of low cost capital to support even its secular growth trend.

Cost recovery from borrowers depended essentially on (a) the average loan per borrower, and (b) the rate of interest on the loan. On both these counts, ASA's record was most aggressive. ASA managed to increase the average loan per borrower at a rate much faster than the other programmes. ASA also charged comparatively higher rates of interest, except for a two-year period during which its rate was slightly lower than that of BRAC. One senior manager of Grameen opined that as the leader in the sector, Grameen was under great pressure to not charge high interest rates to the poor. It is open to speculation whether the lower interest rate policy of Grameen owes its origin to its historical link to public sector banks or to its professed concern that the poor should not be charged a higher rate of interest due to the deleterious knock-on welfare impacts. Grameen was, however, ahead of all the other programmes in sustaining a higher level of loan per borrower and thus in a position to fully recover its relatively higher transaction costs even with its lower interest charges.

This analysis suggests a policy for attaining financial viability that differs from what is asserted in existing literature, such as mechanisms for increasing the rate of interest (Yaron 1992) or economies of scale (Hossain 1988). The programmes under examination relied on other measures, including increasing the loan size per borrower and reducing transaction costs and/or the earnings on the low cost capital fund. BRAC and ASA relied on a combination of the first two, while Grameen relied on the last mechanism, which enabled it to exhibit a profit despite the fact that it incurred losses on microcredit operations. In order to reduce transaction costs, BRAC utilised its management skills to obtain the desired levels of performance, even with a lower number of staff per thousand borrowers, while ASA relied on maintaining low average staff salaries and minimising the costs of other facilities provided to them. The general conclusion is that, even with the context of contemporary Bangladesh, managers of large MCPs have a wide range of choices about routes to achieve financial sustainability.

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