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PoP Briefing Note # 6

Portfolios of Bangladesh's Poor

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The Portfolios of the Poor financial diaries in Bangladesh span 1999-2005. As well as giving a unique insight into the challenges faced by poor households, they show how the households interact with the uniquely saturated and rapidly growing microfinance industry in the country. Unlike many studies of microfinance that feature poor Bangladeshi households, these financial diaries depict the entire financial picture, showing how they use microfinance alongside the many informal financing mechanisms and the few formal services available to the poor.

The Bangladeshi diaries were conducted in two waves. A general study was done in 1999-2001, but in 2003-2005 a second set, involving Grameen Bank and other MFI clients and ex-clients, was carried out in order to track the effects of the new products offered by 'Grameen II', the reformed set of services introduced by the Bank from 2001 (see Grameen II Briefing Note). The sample households for both studies had per capita incomes below or around $2 a day. Results reflect the universal themes found in all three countries studied: active and complex financial lives, large cash flows relative to income, and the use of multiple distinct financial tools. The 1999-2001 sample was composed of participants from three urban slum locations in Dhaka, the country's capital city, as well as three rural villages. The 2003-2005 set featured households in three contrasting rural areas-one near a prosperous market, one deeply rural but well-connected to a highway, and one isolated by poor communications. A major characteristic of these households was a high reliance on "casual" rather than formal employment-that is, employment which is irregular and unpredictable in terms of availability, income generation, and duration.

MAJOR EXPENSES

In contrast to the Indian and South African diarists, many of the Bangladeshi households suffered their severest financial stress as a result of expenditure needed to recover from damage to or loss of property, especially the loss of homes to fires, floods and eviction in Dhaka's illegal slum settlements. As in the Indian sample, Bangladeshis also faced considerable financial strain because of health problems. As in India, weddings were a major social "life cycle" expense which required substantial financing.

MIXED FINANCIAL TOOLKIT

As with the diarists in all three countries, Bangladeshi households had access to several formal and informal financing mechanisms, which they employed regularly, even when given access to microfinance institutions. This continued use of informal financing mechanisms could illustrate an unmet demand for greater product flexibility within the microfinance sector. (See Grameen II Briefing Note for further explanation).

Informal Borrowing

The use of interest free informal loans was particularly high in Bangladesh relative to the other two countries studied. Although every single Bangladeshi household studied was found to be saving in some way, when we compared the sums they formed by taking loans with sums formed through savings, loans outnumbered savings by a ratio of four to one. Strikingly, 88% of all local loans taken in Bangladesh were informal and interest free. However, such loans were found to be limited in their size and maturity, and were highly dependent on the financial health of those in diarists' social networks. The drawback of that situation is that an occurrence of a large-scale shock such as a flood can affect everyone within a household's network and therefore limit the capacity for informal lending.

Informal Savings

All the Bangladeshi households made some kind of saving at home or with neighbors. Informal savings clubs were familiar to the Bangladeshi sample, and used by many of them, though generally not as often nor as successfully as in the South African case. Savings clubs involve members making a small, regular contribution to a communal pot, and eventually receiving a large lump sum. This helps mobilise small, steady flows, transforming them into one usefully large sum. As with informal interest free lending, the size and duration of savings is limited because savings clubs are highly dependent on one's network. Additionally, diarists often reported that accumulating savings in an unstructured manner is difficult and, as a result, it is not used as regularly as borrowing. As already outlined, a major finding of *Portfolios of the Poor* is that microfinance customers often prefer to "borrow to save" (see Briefing Note), because the payment discipline provided by microfinance loans is stronger than among savings clubs.

Private "Pro-Poor" Life Insurance
The financial diaries illustrated a clear contrast between the paths of private life insurance schemes in India and Bangladesh. Pre-dating the successful Indian model, "pro poor" life insurance products in Bangladesh were an attempt by the private sector in the 1990s to target poor populations in a manner very similar to that of the rapidly growing microfinance sector. The high proportion of diarists in the 1999-2001 study enlisted in these schemes reflects their initial popularity. In theory, these schemes were meant to serve both as safety nets in the event of a death of a family member as well as a mechanism for long term savings. However, efforts by companies to design products that could be delivered cheaply to poor populations meant that normal safeguards were overlooked. Information asymmetry problems were not addressed as potential clients received no health or age screening. Additionally, despite being private, formal, and regulated, many of the private life insurance products proved unreliable. Management of these schemes began to unravel, with poor bookkeeping, fraud, nepotism, and agents visiting areas irregularly. This behavior resulted in many of the diarists losing substantial sums of money. The financial diaries chronicle both the initial growth and the dramatic descent of the "pro poor" private sector in Bangladesh[1].

Credit-Life Insurance
Debt forgiveness upon death, or "credit-life" insurance, is offered to most microfinance clients in Bangladesh. The payment for these schemes is often built into the price of the loan. We found it available to nearly half the Bangladeshi sample. Some providers have gone beyond this basic form of insurance and offer payouts on the death of any current client, or of her husband, irrespective of her loan or savings status.

Microfinance
In the first 1999-2001 set of Bangladeshi diaries, microfinance institutions reached 30 of the 42 diary households (21 households held microfinance loans and savings during the research year and another nine held savings only). But despite this widespread use of microfinance, it proved to be a relatively small part of households' overall financial activity. Microfinance products accounted for only 13 percent of all household financial assets, and 21 percent of debt. The later set, in 2003-2005, showed some improvement on this low figure, through the use of credit-life insurance, loan top-up mechanisms, increased savings capacity with a greater variety of both short and long term savings products, as well as the overall increased reliability of products. These are major triumphs of the sector, but microfinance's still relatively small share of the total transactions of poor households indicates the need for further microfinance product innovation.

[1] More recently, the sector has been reviving.