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AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D. C. 20523

PROJECT PAPER

BANGLADESH - RURAL FINANCE PROJECT 48

388-0037

MAY 1983

UNCLASSIFIED

PROJECT AUTHORIZATION

BANGLADESH

Rural Finance Project
Project No. 388-0037

1. Pursuant to Section 103 of the Foreign Assistance Act of 1961, as amended, I hereby authorize the Rural Finance Project for Bangladesh involving planned obligations of not to exceed Seventy-Five Million United States Dollars (\$75,000,000) in grant funds over a three-year period from date of authorization subject to the availability of funds in accordance with the A.I.D. OYB/allotment process, to help in supporting Bangladesh Government policy reform and in financing foreign exchange and local currency costs for the project. The planned life of the project is approximately five years from the date of initial obligation.

2. The project purpose is to create an economically viable nation-wide rural finance system which mobilizes savings and provides credit facilities to a broader segment of private farmers and entrepreneurs. Under the project, assistance in support of rural credit advanced by the system will be provided to the Government of Bangladesh under agreed changes in the system necessary to assure self-sustaining growth. Specific changes will include: (a) the revision of lending and refinance rates to reduce or eliminate subsidies on rural loans; and (b) the introduction of incentives and procedures to mobilize additional savings deposits and assure prompt repayment of loans. Disbursement of the A.I.D. contribution, which is intended in the first quarter of the project to meet the program's credit or refinancing requirements for that quarter, will support the agreed-upon policy reform measures. Technical assistance will also be provided for necessary institutional changes.

3. The Project Agreement which may be negotiated and executed by the officers to whom such authority is delegated in accordance with A.I.D. regulations and Delegations of Authority shall be subject to the following essential terms and covenants and major conditions, together with such other terms and conditions as A.I.D. may deem appropriate:

a. Source and Origin of Commodities, Nationality of Services

Commodities financed by A.I.D. shall have their source and origin in Bangladesh or countries included in A.I.D. Geographic Code 941, except as A.I.D. may otherwise agree in

writing. Except for ocean shipping, the suppliers of commodities or services shall have Bangladesh or countries included in A.I.D. Geographic Code 941 as their place of nationality, except as A.I.D. may otherwise agree in writing. Ocean shipping financed under the project shall, except as A.I.D. may otherwise agree in writing, be financed only on flag vessels of the United States or Bangladesh.

b. Condition Precedent to First Disbursement

Prior to the first disbursement, the Grantee will provide a plan acceptable to A.I.D. for the implementation of initial policy changes.

c. Additional Disbursement

Prior to additional disbursement for technical assistance or to issuance by A.I.D. of documentation pursuant to which such disbursement will be made, the Grantee will, except as the Parties may otherwise agree in writing, furnish to A.I.D., in form and substance satisfactory to A.I.D., acceptable contracts for services and equipment.

d. Special Covenant

The Grantee shall covenant to undertake a series of discussions with A.I.D. on means to improve the economic viability of its rural finance system.

Signature


N. Peter McPherson
Administrator

5/27/83
Date

Clearances:	Date	Initial
Charles W. Greenleaf, AA/ASIA	<u>5/27</u>	<u>[Initials]</u>
Richard A. Derham, GC	<u>5/2</u>	<u>[Initials]</u>
John R. Bolton, AA/PPC	<u>5/27/83</u>	<u>[Initials]</u>

GC/Asia:SAllen:hp:5/24/83:X28092

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AGENCY FOR INTERNATIONAL DEVELOPMENT PROJECT DATA SHEET		1. TRANSACTION CODE <input checked="" type="checkbox"/> A = Add <input type="checkbox"/> C = Change <input type="checkbox"/> D = Delete	Amendment Number _____	DOCUMENT CODE 3
2. COUNTRY/ENTITY BANGLADESH		3. PROJECT NUMBER <input type="checkbox"/> 388-0037 <input type="checkbox"/>		
4. BUREAU/OFFICE ASIA <input type="checkbox"/> 04 <input type="checkbox"/>		5. PROJECT TITLE (maximum 40 characters) <input type="checkbox"/> Rural Finance Project <input type="checkbox"/>		
6. PROJECT ASSISTANCE COMPLETION DATE (PACD) MM DD YY <input type="text" value="0"/> <input type="text" value="6"/> <input type="text" value="3"/> <input type="text" value="0"/> <input type="text" value="8"/> <input type="text" value="8"/>		7. ESTIMATED DATE OF OBLIGATION (Under 'B.' below, enter 1, 2, 3, or 4) A. Initial FY <input type="text" value="8"/> <input type="text" value="3"/> B. Quarter <input type="text" value="3"/> C. Final FY <input type="text" value="8"/> <input type="text" value="5"/>		

8. COSTS (\$000 OR EQUIVALENT \$1 =)						
A. FUNDING SOURCE	FIRST FY 83			LIFE OF PROJECT		
	B. FX	C. L/C	D. Total	E. FX	F. L/C	G. Total
AID Appropriated Total	1,000	24,000	25,000	2,544	72,456	75,000
(Grant)	(1,000)	(24,000)	(25,000)	(2,544)	(72,456)	(75,000)
(Loan)	(-)	(-)	(-)	(-)	(-)	(-)
Other U.S.						
1.						
2.						
Host Country		140,000	140,000		420,000	420,000
Other Donor(s)						
TOTALS	1,000	164,000	165,000	2,544	492,456	495,000

9. SCHEDULE OF AID FUNDING (\$000)									
A. APPROPRIATION	B. PRIMARY PURPOSE CODE	C. PRIMARY TECH. CODE		D. OBLIGATIONS TO DATE		E. AMOUNT APPROVED THIS ACTION		F. LIFE OF PROJECT	
		1. Grant	2. Loan	1. Grant	2. Loan	1. Grant	2. Loan	1. Grant	2. Loan
(1) FN	200	040	-	-	-	25,000	-	75,000	-
(2)									
(3)									
(4)									
TOTALS						25,000		75,000	

10. SECONDARY TECHNICAL CODES (maximum 6 codes of 3 positions each)						11. SECONDARY PURPOSE CODE			
246	253	041	042	043					
12. SPECIAL CONCERNS CODES (maximum 7 codes of 4 positions each)									
A. Code	BR	BS	EQTY	PART	TNG				
B. Amount									

13. PROJECT PURPOSE (maximum 480 characters).

To create an economically viable rural financial system which mobilizes savings and provides credit facilities to private farmers and entrepreneurs.

14. SCHEDULED EVALUATIONS				15. SOURCE/ORIGIN OF GOODS AND SERVICES			
Interim	MM YY	MM YY	Final	MM YY			
	0 3 8 4	0 3 8 5		0 3 8 6	<input type="checkbox"/> 000	<input type="checkbox"/> 941	<input type="checkbox"/> Local <input type="checkbox"/> Other (Specify) _____

16. AMENDMENTS/NATURE OF CHANGE PROPOSED (This is page 1 of a _____ page PP Amendment.)

17. APPROVED BY	Signature	18. DATE DOCUMENT RECEIVED IN AID/W, OR FOR AID/W DOCUMENTS, DATE OF DISTRIBUTION	
	Title	Date Signed	MM DD YY
	Director USAID/Bangladesh	09/29/83	05/02/83

BANGLADESH: RURAL FINANCE PROJECT
(No. 388-0037)

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BANKING GLOSSARY FOR BANGLADESH

Agriculture Loan - Loan intended for on-farm activities, such as: crop raising, cattle rearing, poultry, hunting, forestry, fishing, and sericulture. For example: an agricultural loan covers growing, but not commercial processing, of rice.

Classification - Categorization of loans into risk categories. In Bangladesh, there are four classes: overdue, substandard, doubtful, and loss (i.e., "loss" is the worst case).

Cost of Funds - Costs incurred by a bank for funds, computed as weighted average cost of funds which includes costs of demand deposits, time deposits, refinance facilities, and equity. In developed markets, often computed as marginal cost of funds.

Crora - 10,000,000, usually written 1,00,00,000.

Effective Rate - Nominal interest rate plus service fees, charges, and required balances.

Inspection - Examination of a bank to determine the quality of its assets and compliance with central bank regulations. In U.S. terminology: "examination."

Lakh - 100,000; usually written 1,00,000.

Nationalized Commercial Banks - Six commercial banks which were nationalized in 1972. They are: Sonali Bank, Janata Bank, Agrani Bank, Uttara Bank, Rupali Bank and Pubali Bank.

Nominal Rate - Interest rate as stated and without adjustment.

Normal Program - Normal Program is the regular agricultural lending program of BKD and NCB backed by land mortgage as security and careful selection of borrowers.

Overdue - Loan which remains unpaid after its maturity date.

Real Rate - Nominal interest rate deflated by inflation factor.

Refinance - Borrowing of funds from the central bank by individual banks. In U.S. terminology: "discount" or "rediscount."

Rural - Statistical term for geographic areas which lie outside of the 75 designated municipalities.

Sanction - To approve. For instance: loan sanctioning authority is loan approval authority.

Special Agricultural Credit Program - The Special Agricultural Credit Program (Taka 10) Crere Program) was started in 1977 to substitute for the Normal Program. Its original objective was to provide credit to small farmers or tenants unable to meet bank security criteria. Loans were based on hypothecation of crops and borrower selection was made partly on political lines. The SACP is now being phased out.

Security Balance - Deposit placed with bank which reduces risk and increases effective cost of borrowing. In U.S. terminology: "compensating balance."

Spread - Difference between two interest rates. For instance: spread over cost of funds means the difference between the lending rate and cost of funds.

Stuck-up - Same as "overdue."

Transfer Rate - Interest rate charged to bank branches by headquarters. In U.S. terminology: "inter-branch" rate.

Urban - Statistical term for geographic areas which lie inside of the 75 designated municipalities.

VII

ABBREVIATIONS

- ACD - Agricultural Credit Department (Bangladesh Bank). This is the Department of the Central Bank responsible for all agricultural and rural credit policy and operations.
- ADP - Annual Development Plan
- BB - Bangladesh Bank (the central bank)
- BDC - Bangladesh Government
- BKB - Bangladesh Krishi Bank (the Agricultural Development Bank)
- BRDB - Bangladesh Rural Development Board
- BSBL - Bangladesh Samabaya Bank Limited
- MTFPP - Medium Term Food Production Plan
- NCB - Nationalized Commercial Banks
- NP - Normal Program for Agricultural Lending (see Banking Glossary)
- NRC - National Review Committee for Agricultural Credit
- RFEP - Rural Finance Experimental Project
- SACP - Special Agricultural Credit Program (see Banking Glossary)
- SFYP - Second Five Year Plan

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I. PROJECT RATIONALE AND DESCRIPTION

A. Project Rationale

1. Rural Finance: The Problem

1.01 Bangladesh's rural financial system, as presently structured, cannot support the substantially higher levels of agricultural and rural production and employment generation activities required for economic development. Interrelated problems must be addressed: interest rate rationalization, savings mobilization, lending policies and practices, and institutional performance. Reforms are required that will lead to a self-sustaining system of rural finance which provides timely and efficient deposit, savings and loan services to rural areas. A necessary first step is implementation of a system for establishing deposit, lending and refinance interest rates that provide incentives to savers and lenders and that creates the basic conditions for achieving institutional viability. This step is not sufficient, however, for developing a self-sustaining system. Institutional reforms must be introduced that will streamline and improve operational efficiency, remove some of the current distortions, and overcome some of the serious problems in the areas of employee training and incentives.

a. Interest Rate Structure

1.02 The current interest rate structure requires immediate adjustment. The maximum lending rates of 12 percent for regular agricultural loans and 13 percent for rural industrial loans are preventing the development of a growing, self-sustaining financial system. They discourage efforts to mobilize savings because the rates that must be paid on time deposits are higher than the allowed rates on loans. There is not enough margin between the lenders' average cost of funds and lending rates to cover administrative costs, bad debts and profits. Lenders are forced to depend on a continuous flow of subsidized funds from the government to meet credit demands. Since the implicit subsidy is large, the government cannot afford to provide enough funds for the rural credit program to serve the large number of farmers and small entrepreneurs.

1.03 The established refinance rate of 6 percent charged by the central bank for rural (including agricultural) loans also requires adjustment. The availability of this low cost rediscount facility serves as a constraint on savings mobilization. The banks depend on subsidized refinance facilities to make subsidized loans; and the government budget is indirectly financing rural credit needs at an unknown but high cost. If the present linkages between lending rates, refinance rate, and savings rates are allowed to continue the rural financial system will become increasingly expensive for the government and is unlikely to develop to the extent necessary to serve the rural economy.

1.04 There is no regular system for periodic review and adjustment of interest rates for lending, refinance and savings. A procedure is needed for specifying relationships among the three sets of rates and adjusting them upwards and downwards depending on trends in inflation, administrative costs and loan recovery. Lending rates have been adjusted only twice since 1971 and savings rates, four times. Annual inflation rates have varied from 7 percent to minus 24 percent. A table showing the historical structure of interest rates is attached as Annex E.

b. Rural Savings Mobilization

1.05 Increased efforts are required to mobilize rural savings and provide savers with a safe and convenient way to hold their funds. Deposits and savings must replace refinance facilities as bankers' primary source of funds for credit if the rural financial system is to become self-sustaining. At present, there are a number of constraints on rural savings mobilization, in addition to the low rates allowed on loans and the availability of an underpriced refinance facility mentioned above. They include: lack of incentives for bankers, insufficient number of rural branches, and inadequate rural savings mobilization programs.

c. Rural Lending Procedures

1.06 A number of improvements have been made in recent years in rural lending policies and procedures. Much remains to be done, however, to develop a streamlined and efficient system. Three changes in particular are required. The first involves loan applications. A standardized system of loan application procedures must be implemented for all types of rural credit. Second, restrictions on lending for rural non-farm purposes should be relaxed so loans for all types of purposes are available in rural areas. High demand exists for loans for a wide variety of productive non-farm activities. Finally, loan sanctioning procedures need to be reviewed with the objective of providing greater authority to bank branch managers. For small farmers to have access to institutional credit, it is essential that loans are timely and available when desired. The current system is time-consuming and provides little flexibility for managers to respond to local needs.

d. Management Improvements

1.07 Bank accounting practices vary from existing rules and hide losses, and low rates of loan recovery cause irreparable damage to the banking system. Although there are no authoritative figures, one recent estimate showed that overdues represented 37% of agricultural loans, were valued at Tk. 3 billion (equivalent to \$125 million) and were caused by 53% of borrowers, or nearly 400,000 persons. The rural finance system cannot survive by itself at such rates, and the government must indirectly subsidize it. Two key issues must be tackled

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immediately. The first concerns basic accounting changes for overdues and the second concerns loan recovery. The accounting system lacks a standardized system for defining, classifying and reporting past due loans; banks loosely follow procedures for setting up bad debt reserves and writing off bad debts; and banks properly accrue interest on loans but fail to disclose amounts of overdue interest. Central bank inspection departments need to be strengthened to monitor bank compliance with good accounting standards. Bank financial statements do not reflect real profit and loss. Bankers, however, are reluctant to change present practices because year-end profit bonuses to employees are linked to reported profits. An improved accounting system is necessary for a concerted effort on loan recovery. Poor loan recovery is attributable to a wide variety of factors: a tradition of "taccavi"* loans, bankers' lack of incentives for recovery, politically motivated credit decisions, fraud, and often valid reasons such as death or crop failure. The loan recovery problem is a complex mixture of social, political, legal, and banking issues.

e. Research and Evaluation

1.08 Extensive research is required to identify additional reforms that may be beneficial as well as to monitor the impact of reforms undertaken. Bangladesh lacks an institution to conduct research on practical banking issues; academics seem uninterested and experienced bankers cannot be spared from management tasks.

1.09 The BDG is aware of these problems and has become increasingly concerned with improving the structure of the banking system so that it will contribute to economic development particularly in rural areas. The Government has already taken several important steps. It has conducted a major and unusually forthright review of its agricultural credit system in a forum open to especially interested outsiders. This report is in final stages of preparation. In a second area, the Government has approved establishment of new private banks, some of which opened their doors for business in Spring 1983, and is expected soon to disinvest two of the six nationalized commercial banks. In a third area, the central bank has taken several important steps to improve the effectiveness and rationality of banking services: The Special Agricultural Credit Program** is being phased out; some loan

* Taccavi loans were extended by the Government in times of drought and were often forgiven for political reasons.

** The Special Agricultural Credit Program, started in FY 77 to finance agricultural inputs, has high overdues and was used mainly by new-target group borrowers.

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procedures are being reviewed to reduce paperwork; and a savings account can now be opened with Taka 5 to encourage savings mobilization. In addition to these changes, the Government recognizes and is facing some of the most difficult policy decisions regarding the financial sector: the need to increase lending rates, mobilize additional savings, and improve loan recovery. This project will support the Government's efforts in these and other related areas.

2. Objectives: Relation to CDSS

1.10 One of the BEG's primary production goals, and a key element of Mission strategy, is the attainment of foodgrain self-sufficiency. The BEG Second Five Year Plan (SFYP) and the companion Medium Term Food Production Plan (MTFPP) called for achievement of the self-sufficiency goal in FY 85, with a foodgrain production level in that year of 20 million tons. A succession of disappointing harvests, owing mainly to drought, has left that target far out of reach. Production in FY 83 will exceed 15 million tons and, as stated in the Mission's FY 85 CDSS, would have to increase at an annual rate of 4.7 percent to attain a more limited self-sufficiency goal of 18.7 million tons in FY 1988.*

1.11 A growth rate of this magnitude would be a considerable achievement, but is well within the realm of possibility given favorable weather conditions. However, even assuming such a growth rate in foodgrain output, the agriculture sector alone will fall far short of providing employment for the new entrants to the rural labor force during this period. Creation of off-farm employment opportunities through rural industries development is therefore vital and constitutes an important related aspect of Mission strategy. In short, the need is for accelerated development of the entire rural economy. There are ample indications that inadequate availability of institutional credit has been a key constraint to past rural development efforts.

3. The Need For Increased Agricultural Credit

a. Agricultural vs. Rural Credit

1.12 The available data do not permit an analysis of past trends in rural credit as such. Nor, given the absence of information on rural off-farm activity, is it possible to project in any meaningful way future needs for rural credit. The available data and production goals

* Based on an assumed population growth rate of 2.23 percent p.a. the BEG target would have provided an average per capita consumption level of 17.2 ounces per day. The USAID calculation assumes the presently estimated population growth rate of 2.5 percent and per capita consumption at the present (approximate) level of 15.5 ounces per day.

are far better defined (though still woefully lacking in some respects) with respect to the agricultural sector, which accounts for about 70 percent of all rural economic activity. For these reasons, this portion of the analysis will focus on past and projected trends in the areas of agriculture and agricultural credit.

b. Farm Level Considerations

1.13 The production gains called for in the Medium Term Food Production Plan assume an expansion in the share of total acreage planted to high yielding variety (HYV) rice and wheat strains from 5.95 million acres, or 22.7 percent of all federrain acreage, in FY 80, to 12.15 million acres in FY 85. Interpolating from the MTFPP projections, even the "limited" 71.88 output target of 10.7 million tons hypothesized in Section 2 would imply about 11.3 million acres under HYV cultivation by that year. This expansion can come about only if farmers are able to afford the increased outlays for improved seeds, pesticides, fertilizer, additional labor and irrigation equipment involved in switching from traditional to HYV production.

1.14 Annex F-1 considers the case of a typical small farmer of T. aman rice contemplating an investment in HYV technology. Since he does not have the cash resources to cover the additional costs involved, he must have recourse to financing. The financing alternatives assumed for this purpose are: 12 percent, the present institutional rate; 24 percent, a rate close to full cost recovery; and 100 percent, representing probably the lowest rate that he could hope to obtain on the informal moneylender market (in fact, rates as high as 10 percent a month, equivalent to 214 percent per annum, are not uncommon). Farmers' circumstances vary greatly according to crop, location, market prices, etc., so this example should be taken as illustrative. Nevertheless, the basic points made here are generally valid. They are that, in terms of overall costs to the farmer: (1) the difference between 12 and 24 percent is not of great significance; (2) the difference between 24 and 100 percent may well be prohibitive. For the farmer, the availability of institutional credit may well be the deciding factor in whether he switches to HYV production. The price of that credit, whether 12 percent, 24 percent, or somewhere in between, is relatively unimportant.

c. Trends and Projected Requirements

1.15 As of June 30, 1981, total institutional credit outstanding to the agriculture sector amounted to Taka 6, 129 million. Agriculture, which then accounted for 34 percent of GDP, claimed 16.6 percent of all bank credit. The agriculture and livestock subsector of the overall agriculture sector (which includes hunting, forestry and fishing)

accounted for 42 percent of GDP but only 14.3 percent of all credit outstanding.* Agricultural credit has nevertheless expanded quite rapidly since FY 1976. Table 1-1 depicts the expansion of agricultural credit in terms of annual disbursements through FY 82.

1.16 Annual disbursements increased at a compound rate of 44 percent between FY 76 and FY 82. Measured in real terms, after allowance for price inflation, the rate of increase during the six year period was 29 percent. However, of the real increase during 1976-82, fully 63 percent occurred during 1976-78 alone. Put another way, real agricultural credit expanded at a rate of 70 percent during 1976-78, but only 12 percent during 1978-82.

1.17 The especially rapid rate of growth in agricultural credit during 1976-78 can be explained partly as a "catch-up" effect, reflecting BDG concentration on the area following years of relative neglect. In particular, this period saw the launching in FY 1977 of the "Hundred crore" program, which involved the planned disbursement on a crash basis of Taka one billion to low income farmers (with relatively little regard for repayment capability). The 1978-82 period may be taken as more "normal," even though (or because) it included two years, 1980-82, of generally restrictive credit policies associated with the balance of payments crisis of that period.

1.18 Whatever the past rate of expansion, the availability of agricultural credit is still far from adequate relative to the need. As shown in Table 1-1, agricultural credit disbursements in FY 1982 were only 4.4 percent of the value of agricultural production. Inter-country comparison generally use either of two bases: new agricultural loans/agricultural production or agricultural loans outstanding/agricultural production. Examples indicate substantially larger ratios than for Bangladesh. For instance, the Philippines (outstanding loans basis) is currently 20 percent and ranged from 6 percent to 27 percent during 1951-79. Honduras (new loans basis) ranged from 20 percent to 43 percent during 1970-80. A study of 18 countries in Latin America for the period 1960-68 reveals that in 1960 the average (outstanding basis) was 23 percent and by 1968 the figure had risen to 36 percent.

* Bangladesh Bank Bulletin, May 1982

TABLE 1-1
New Disbursement of Agricultural Loans by Various Agencies
in Bangladesh 1964-65 to 1981-82

Fiscal Year Ending June 30	Agencies				Commercial Banks	Total in Current Taka	Total in 1964-65 Prices ⁽¹⁾	Value Added Ag. Prod.	Percent Ag. Credit to Ag. Production
	Agric. Dept. Taccavi	BKB	BSBL and Cooperatives	IRDP					
	In Current Million Taka								
1964-65	30.2	36.5	25.6			92.3	92.3		
1965-66	17.8	41.6	9.4			68.8	65.7		
1966-67	19.0	47.1	23.2			89.3	77.1		
1967-68	15.3	55.0	70.1			150.4	130.5		
1968-69	25.4	75.3	79.1			180.3	147.8		
1969-70	30.0	130.7	173.3			304.0	241.6		
1970-71	n.a.	69.7	33.5			153.2	115.8		
1971-72	n.a.	96.4	96.4	15.3		208.6	137.8		
1972-73	n.a.	179.0	142.5	29.0		350.5	156.6	26,100	1.3
1973-74	14.6	135.7	77.4	24.6	54.9	307.2	99.7	41,501	0.7
1974-75	10.0	176.3	94.1	39.3	75.7	396.4	77.0	73,523	0.5
1975-76	0.5	135.1	106.2	45.0	169.6	506.4	107.3	57,330	0.9
1976-77	0.4	383.4	113.3	66.3	362.2	930.6	132.6	53,671	1.7
1977-78	0	553.0	153.2	109.0	358.1	1,678.3	308.4	72,243	2.3
1978-79	0	746.6	201.1	124.5	684.0	1,756.2	298.2	78,745	2.2
1979-80	0	1,415.0	270.4	204.5	1,135.5	3,025.4	433.6	93,299	3.2
1980-81	0	2,097.4	276.4	255.0	1,360.4	3,989.2	508.0	95,434	3.8
1981-82	0	2,710.4	335.5	258.4	1,291.9	4,446.5	435.9	101,690	4.4

(i) Loans in current Taka deflated by consumer price index for middle income families in Dhaka, 1973-74 = 100

Sources: Credit: 1965-75 Adams and Nelson
1976-82 Bangladesh Bank Agricultural Credit Dept.

Value Added Ag. Prod: Bangladesh Bureau of Statistics.

Consumer Price Index: Bangladesh Bureau of Statistics.

1.19 Further, survey data as well as field observations provide ample indications of inadequate institutional credit in Bangladesh. The USAID-funded Land Occupancy Survey* showed that in late 1978 only 15.4 percent of farmers used any kind of credit. Of these, only 6.0 percent had access to institutional credit. The remainder was borrowed from friends and relatives or from money-lenders at rates of 100 percent and up.

1.20 The BDG has not attempted a precise projection of agricultural credit needs in Bangladesh. While acknowledging the need for a considerable expansion, the Second Five Year Plan (SFYP) for FY 1980-85 stated only that agricultural credit would have to increase by 20-25 percent per annum (presumably in real terms). This would seem to be on the low side of the real need. If the credit requirement of the HYV cultivator shown in Annex F-1 can be taken as representative, this would imply a need for nearly Taka 10 billion** (in FY 1983 prices) in FY 1988 for HYV foodgrain cultivation alone. Thus, new disbursements of institutional credit would have to expand by 14 percent p.a. in real terms during FY 1982-83 to meet the needs of HYV foodgrain cultivation alone. To be sure, not all HYV farmers will require credit, but other farm and off-farm requirements would surely bring the needed expansion to at least the 20-25 percent rate of growth called for in the SFYP. Finally, even if a 25 percent rate of growth were to obtain, the ratio of new agricultural loans to agricultural value added would reach only 13-14 percent by FY 1988,*** still well below the comparable ratios obtaining in other LDC's.

1.21 In short, the potential demand for agricultural credit, let alone overall rural credit, appears to be substantially beyond the capacity of the present system. The problem arises from the incapacity of the system to expand on a sound basis. The latter point needs to be stressed. Agricultural credit has been expanding quite rapidly due to donor and government funding. What is needed is not only an increase in the rate of expansion, but an expansion based on rural resource mobilization rather than large-scale subsidization. The BDG, for instance, was funding 60 percent of rural credit with refinance facilities as of June 30, 1981, and an estimated further share of 10 percent was financed from foreign donor sources. Further increases in Bangladesh will have to come primarily from expanded domestic savings mobilization. Additional implications of the present subsidization are examined in Section V (Economic Analysis).

* Land Occupancy Survey, Januzzi and Peach, December 1978. The ratios shown here were derived from the data in Tables E-V and E-XI.

** 11.3 million x Tk. 865 = Tk. 9.8 billion.

*** Calculation assumes growth rates in agricultural value added of 3.5 and 4.5 percent, respectively.

B. Rural Finance Experimental Project

1.22 The AID Rural Finance Experimental Project (388-0025) demonstrated that a viable rural financial system is achievable in Bangladesh. The RFEP provided \$7.0 million to finance technical assistance and partial reimbursement of a credit program. The project purpose was to identify and test one or more replicable rural financial systems. The project resulted in 81,595 loans (43,113 separate borrowers) valued at Taka 134 million and savings of Taka 10 million at 98 bank branches. A summary is given below and a more detailed description is given in Annex H.

a. Interest Rate Structure

1.23 Lending rates of 12%, 18%, 24%, 30%, and 36% were tested when the established rates were 11% and later, 12%. Results indicated that rates up to 30% were acceptable to borrowers; however, some resistance appeared at 36%. In the sociological survey, 42% of a sample of borrowers responded that "low interest rates" was an important element of the project.

1.24 Saving rates were tested at 11%, 12%, 13%, 14%, and 15%. It should be noted that the established rate for savings accounts was increased to 10% from 7.75% as the RFEP was starting but project rates were not increased. Consequently, the effect of higher RFEP rates was somewhat diluted. In addition, even RFEP savings rates were slightly below inflation rates during this period. Nevertheless, results indicated that non-target group savers were sensitive to higher interest rates of 14% and 15%.

1.25 Refinance rates were not adjusted. However, the 10% to 13% bank transfer rates (i.e., the rates on funds charged to branches by headquarters) had the same impact on bank branches, which funded most of their loans from headquarters.

b. Rural Savings Mobilization

1.26 Banks mobilized savings equal to only 16% of loans outstanding, which is not sufficient for a self-financing system. There are two probable reasons. First, promotional and other techniques were not used to complement the higher project savings rates. Second, bankers allocated most of their time to lending because the incentive structure under the RFEP provided banks one-third for loan disbursement and one-third for recovery. The RFEP emphasized lending more than savings, as seen in retrospect.

c. Rural Lending

1.27 Lending procedures were simplified and restrictions were relaxed. Some changes were: development of a standard loan application form, delegation of sanctioning authority up to Tk. 5,000 to branch managers, removal of some collateral requirements, and simplification of bank reporting requirements. As a result of these and other changes, 45% of borrowers obtained loans in 14 days or less and 61% of borrowers obtained funds after two visits to the bank. There is no comparable study of borrowers' waiting time on a national basis; however, informed opinion indicates that this performance is better than average.

d. Management Improvements

1.28 Branch profitability was measured by standardized accounting procedures based on actual interest earned, real administrative costs, real cost of funds, and a strict provision for loan loss reserves. Four out of nine banks were able to operate profitably and accounted for 69% of lending.

1.29 Loan recoveries were higher than national averages because of increased supervision and incentives to banks (i.e., one-third for disbursement and one-third for repayment). At the end of the project overdues were 19% and ranged from 5% to 51%. If the worst performing bank is eliminated, recalculated overdues would have been 16% and would have ranged from 5% to 24%.

C. Project Objective

1. Goal and Purpose

1.30 The project goal, drawn from the BDG's Second Five Year Plan, is to accelerate food production and expand opportunities for employment in rural areas. The project purpose is to create an economically viable rural financial system which mobilizes savings and provides credit facilities to private farmers and entrepreneurs. Principal outputs include: a rationalized interest rate system, improved savings mobilization techniques, more efficient lending procedures, improved management systems, and practical banking research. GOB inputs are needed policy changes and assignment of an adequate number of experienced officers and staff, of both the Central Bank and financial institutions, who are dedicated to the success of these policies. AID will provide local currency contributions to support the rural credit system, and technical assistance including foreign and domestic advisors, training programs and equipment to support implementation of policy changes. A log frame matrix is attached as Annex B.

2. AID Policy

1.31 This project conforms to the AID Policy Paper "Pricing, Subsidies, and Related Policies in Food and Agriculture" and State 252939 dated September 9, 1982, which outlined key points of the forthcoming AID Policy Paper "Financial and Capital Market Development." The Policy Paper on Pricing states that "A.I.D.'s primary purpose... (is) to support a system of financial institutions that effectively mobilizes and allocates private indigenous financial resources" (page 10). This project supports interest rate rationalization, savings mobilization and loan recovery. The Policy Paper establishes as a target decontrol of interest rates and "where it is not possible to persuade a government to eliminate interest rate controls," then "significant measures to reduce controls where they adversely affect the mobilization or allocation of credit" (page 11). The BDG is considering major increases in interest rates for rural lending and refinance to achieve economic viability and also establishment of an Advisory Committee on Interest Rates to review and recommend changes periodically. These changes will provide flexibility of the interest rate structure for savings, refinance, and lending rates. Further, this project follows principles of the AID Spring Review of Small Farmer Credit and subsequent work at Ohio State University and elsewhere. The Mission has relied on findings of the RFEP and also of the AID-BANCOOP Project in Peru, which emphasized the importance of savings mobilization through competitive interest rates, promotion campaigns, and incentives to bankers.

1.32 This project covers AID's four key precepts: policy dialogue, institution building, technology transfer and private sector support. Policy issues are the heart of this project. The BDG is prepared to undertake policy changes to create an economically viable rural financial system including fuller cost recovery on lending operations, increased savings mobilization, and improved loan recovery. Institution building is also an important component at different levels. As a consequence of policy changes regarding accounting and incentives, banks will become more performance oriented. Procedural changes in savings and lending practices will increase efficiency of rural financial institutions. Certain elements of central bank operations will also become more efficient as a result of Federal Reserve assistance furnished under this project. The project will also finance technology transfer from the Federal Reserve System and from experts in such technical fields as interest rate methodology and bank branch rationalization. In regard to supporting the private sector, the project will have two major impacts. First, it will expand availability of credit facilities to private farmers and rural entrepreneurs, thereby facilitating private sector trade and investment. Second, it will substantially improve the climate and profitability of the rural banking system and make it a potentially attractive area for private institutional investors. A few private banks already operate in Bangladesh, however, they seek only

profitable business accounts in commercial centers and are uninterested in rural financial markets. The creation of a favorable banking climate and an economically viable rural financial system will support the BDG efforts to disinvest itself of a segment of government owned banks.

3. Project Design

1.33 The project design has drawn heavily on results of the RFEP and working papers of the National Review Committee on Agricultural Credit, sponsored jointly by the Government of Bangladesh and IDA. This Committee prepared five working papers and held meetings to discuss important issues in a broader forum. USAID accepted an invitation to attend these meetings and contributed to the identification of policy proposals which would lead to an economically viable rural financial system. Other reviews are underway (including the World Bank Survey of the Financial Sector and other donor project appraisals). Their preliminary results have contributed to project design.

1.34 USAID and the Bangladesh Bank designed this project. In addition, outside consultants provided substantial assistance. Dr. Richard L. Meyer, Professor of Agricultural Economics, Ohio State University, reviewed the initial project design during February 1983 and offered many constructive suggestions which have been incorporated into the final design. Dr. Charles Lucas, Assistant Vice President, Federal Reserve Bank of New York, recommended assistance for Bangladesh Bank operations in a report dated November 24, 1982, some of which have been incorporated in the final design. The project is responsive to suggestions in the PID approval cable summarized in Annex A.

D. Project Elements

1.35 This project will support BDG policy changes necessary to create an economically viable rural financial system. The \$75 million will be obligated in three tranches during FY 83, FY 84, and FY 85. The first year obligation of \$25 million will support the BDG's planned initial policy changes. Obligations during the second and third years will follow review of performance and implementation of changes to achieve the project purpose. The project has two principal elements: local currency support for use in the rural credit system to support policy changes and technical assistance to help implement policy changes.

1. Local Currency Support for Rural Finance System

Each year, a disbursement will be made for purchase of local currency to be used for the rural credit program. The first year, this disbursement is expected to be \$24 million. This is particularly suitable because of Bangladesh's need for quick disbursing aid and local cost financing.

2. Technical Assistance Element

1.37 Technical assistance will be provided to the Bangladesh Bank to help implement policy changes and related procedural changes. Certain portions of the plan will require short-term advisory services, training, an incentive fund, and equipment, to be financed by the project. The plan is described below. Costs of technical assistance are estimated at \$3.3 million, of which \$1.0 million will be allocated from the first year obligation. Allocations in subsequent years may be increased or decreased depending upon reviews.

E. Rural Financial Reform Plan

1.38 The rural financial reform plan covers two types of activities: those which directly support policy changes and those which support procedural changes. In regard to policy changes, the EDG will concentrate its efforts in three important areas: interest rate rationalization, rural savings mobilization, and loan recovery improvement. In regard to procedural changes, the EDG will concentrate on various means to improve efficiency of rural financial institutions and the central bank.

1.39 This plan, in its entirety, may appear complex for two reasons. First, a relatively large number of seemingly discrete activities will be undertaken. In financial markets, however, seemingly different activities actually reinforce or complement each other. For example, interest rate rationalization (a policy change) may seem unrelated to lending efficiency (a procedural change); however, these two activities actually reinforce each other because as lending procedures become more efficient, costs of administration are reduced which, in turn, permit a reduction in interest rates to borrowers. In this project, almost every activity is related directly or indirectly to one or more policy changes. The second reason why this plan may appear complex is the timing of activities. Timing of activities, however, results from trade-offs among relative importance, need for outside experts, and estimated implementation times. The most apparently complex example is activities to support improved loan recovery (a policy change). In this important area, some activities do not require outside advisors, and changes will be made early. Other changes require

advisors and are scheduled after advisors arrive and have become familiar with rural financial markets in Bangladesh. Another aspect of timing is the need to concentrate rather than diffuse efforts of bankers and advisors, especially when dealing with the three policy areas. Therefore, activities relating to policy changes are scheduled to take place sequentially. A summary follows covering: policy change activities, procedural change activities, and reviews and evaluations.

1. Policy Change Activities

a. Interest Rate Rationalization

1.40 The initial policy change involves rationalization of the structure of interest rates. This policy change will require two activities: an increase in interest rates and establishment of an Advisory Committee on Interest Rates.

(1) Interest Rates

1.41 The BDG is considering increasing both the lending rate to cover fully the costs of funds and operations and the refinance rate for all rural loans to a level that will encourage savings mobilization. The BDG is considering alternative means of increasing costs of borrowing, including: an increase in interest rate, service charges, supplementary interest, and mandatory savings deposits. The National Review Committee on Agricultural Credit, the Rural Finance Project, and additional calculations developed with project design consultant Meyer indicate that achievement of a 24 percent rate will be adequate to cover lending costs and provide a small profit. This rate includes a 14 percent allowance for costs of administration, incentives and bad debts and 10 percent to cover costs of funds and profits. The 14 percent allowance assumes substantial progress in reducing the current high rate of overdue loans. Steady movement toward a rate restructuring along these lines would greatly reduce the linked subsidy on refinance rates for rural loans and would encourage banks to mobilize funds for lending. The rationale for this rate is described in Annex F-2.

(2) Advisory Committee on Interest Rates

1.42 The second part of the interest rate rationalization process involves the establishment of an Advisory Committee on Interest Rates. This Committee will advise the Governor of the Bangladesh Bank on establishing rates for savings, lending and refinance. The Committee will meet at least semi-annually, and more frequently when needed, to review the entire rate structure. A procedure will be developed for specifying relationships among the three sets of rates. Rates need to be adjusted upwards and downwards depending on trends in inflation, administrative costs and loan recovery. A technical unit will prepare the studies and recommendations required by the Committee. Short-term expert services and training for the technical unit will be project financed.

b. Rural Savings Mobilization

1.43 The second major policy change involves rural savings mobilization. Increased efforts are required to mobilize rural savings and provide savers with a safe and convenient way to hold funds. Several changes are required to complement the interest rate restructuring in order to increase incentives for savings mobilization, including improved promotion strategies, review of savings restrictions, innovative savings campaigns, and additional Bangladesh Bank institutional advertising.

1.44 To carry out this change the Bangladesh Bank will develop a Preliminary Savings Mobilization Plan before advisory services are available. This plan will be reviewed by experts after contract negotiations are completed. The Bangladesh Bank and advisors will then develop and implement a Savings Mobilization Action Plan. Some of the tasks to be included are:

(1) Market Research

1.45 Market research of savers' attitudes has not been previously undertaken and will contribute to developing strategies for savings mobilization. This study will assess depositors' and savers' wants, needs, and attitudes towards savings services and recommend improved strategies for promotional campaigns, packaging and delivery of savings services, and types of services offered.

(2) Review of Savings Restrictions

1.46 Deposit account regulations and procedures will be reviewed to make sure that they encourage mobilization of rural savings. The savings account minimum size of Tk. 5 is commendable; however, this review will examine all classes of accounts for reasonable relaxation of additional restrictions.

(3) Innovative Savings Campaign Fund

1.47 Bangladesh Bank may establish a new fund to partially reimburse rural financial institutions for costs of experimental savings promotion campaigns, to be project funded. Individual banks will submit proposals for Bangladesh Bank review and approval.

(4) Bangladesh Bank Savings Promotion

1.48 Bangladesh Bank plans to expand its present institutional promotional efforts through radio, TV, newspapers, brochures, etc. Also, as a result of the marketing study, it may redesign savings services and procedures to elicit increased deposits.

c. Loan Recovery Improvement

1.49 Loan recovery is the third major ^{area of} policy change. Poor loan recovery is a complex problem which will require careful analysis and development of a comprehensive strategy for improvement. Many factors contribute to poor loan recovery and must be improved or effects mitigated, including: accounting procedures, lending practices, branch staffing, attitudes towards forgiveness, legal procedures, attitudes towards collateral, and quality of bank inspection. Some changes, however, do not require outside experts and will be initiated during the first year of the project. After technical services become available, additional activities will be undertaken.

(1) Initial Activities

(a) Accounting Changes

1.50 Bank accounting systems need to be changed to give a true picture of financial condition. The following changes will be made:

- Development of a standard system for defining, classifying, and reporting of overdue loans;
- Requiring financial statements to footnote interest accrued on overdue loans and amounts of overdues by age;
- Development of a standard system for establishing reserves for classified loans and for writing off bad debts.

(b) Revised Penalty Interest

1.51 The present penalty interest on overdues of 3% for agricultural loans will be increased and will be applied to all rural loans to encourage prompt repayment.

(c) New Incentive System

1.52 After accounting changes are in place, a new bankers' incentive system of cash or non-cash awards will be developed based chiefly upon true profits, savings mobilization, loan recovery, and efficient administration.

(2) Later Activities(a) Strengthening Bank Inspection

1.53 The Bangladesh Bank's Inspection Departments which examine rural branches will be strengthened to monitor new standards of accounting for interest earnings, loan classification, overdue debt reserves, and writing off bad debts. Steps include hiring additional staff and obtaining advisory assistance from the Federal Reserve System to recommend improvements in the inspection systems, provide training, and revise the inspection manual.

(b) Loan Recovery Review

1.54 A comprehensive review will be performed of reasons for poor loan recovery. As mentioned above, poor loan recovery arises from a complex mix of banking, legal, political, and sociological issues. This study will require close cooperation with the Bangladesh Bank to develop a program for improvements. Because of relationships among loan recovery and branch location, training, and lending practices, this review will be undertaken after these studies are available, as described below. After the comprehensive review is completed, recommended changes will be implemented.

2. Procedural Change Activities

1.55 In addition to activities associated with the three major policy changes (interest rate rationalization, savings mobilization, and improved loan recovery), the Bangladesh Bank will undertake other activities to strengthen the rural financial system. These activities do not require major policy changes and generally reinforce or complement policy changes. They will be performed throughout the project.

a. Financial Institution Performance Activities(1) Rural Branch Training

1.56 The Bangladesh Bank will develop three standardized "core" courses for banks to use in training programs for officers and managers. At present, each financial institution develops and conducts its own training programs, with variations in quality and expense. An initial supply of manuals and local costs of experimental teaching will be project financed.

(2) Branch Rationalization Plan

1.57 The Bangladesh Bank wants to continue expanding the availability of institutional banking services to the rural population. The strategy of linking urban to rural branch licensing approvals has been successful but was modified in 1991 because of concern about

overbanking in urban areas. The Bank will examine alternative plans to expand rural branch banking and will develop a branch rationalization plan, including training and staffing requirements, with expert assistance.

(3) Lending Efficiency Review

1.58 The Bank has made a number of improvements in rural lending practices in recent years. The Bank will undertake, with advisory assistance, a review of three related areas of lending procedures: lending restrictions, loan application systems and loan sanctioning (i.e., approval) procedures. This review will include recommendations to reduce costs to borrowers and lenders without jeopardizing bank integrity.

b. Implementation Agency Strengthening Activities

1.59 In addition to technical assistance activities related to rural financial institutions, other activities will strengthen the implementation agency, the Bangladesh Bank. The Bank's Agricultural Credit Department (ACD) will need increased staff, training and equipment. Other departments will be provided a limited amount of technology transfer by the Federal Reserve System.

(1) Agricultural Credit Department

1.60 The Agricultural Credit Department, which will manage this project, is competent but needs equipment and observational training. Project success will depend upon the continued search for innovative approaches to resolving issues being addressed with policy changes. Therefore, it is important that senior officers responsible for effecting policy changes be exposed to a broad range of rural financial problems through observational training and short-term training courses in the U.S. and third countries. Also, ACD needs additional equipment and supplies to carry out its duties effectively and efficiently; an indicative list is attached as Annex L-5.

(2) Bangladesh Bank

1.61 Although this project is destined chiefly to support policy changes in rural financial markets, it is important for the Bangladesh Bank to improve other functional areas and improve its relationships with major central banks. It already enjoys a good relationship with the Bank of England. Undertaking of this project together with the recent pegging of the Taka to the U.S. Dollar indicate the desirability of expanding the Bangladesh Bank's relationship with the Federal Reserve System. Consequently, this project will initiate a modest amount of technology transfer to strengthen selected

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functional areas of the Bangladesh Bank. The activities to be undertaken are listed below and details are provided in Annex L-2.

- (a) Review of Accounting and Related Systems
- (b) Project Development Training
- (c) Foreign Exchange Training
- (d) Note Issue Advisory Services.

3. Reviews and Evaluations

a. Policy Change Impact Monitoring

1.62 A system will be developed for frequent monitoring of the impacts of the three policy changes. This system will include both statistical information (e.g., increases in number of accounts) and sociological studies of rural attitudes towards policy changes.

b. Financial Sector Review

1.63 A financial sector review will evaluate the impact of major policy changes and project activities; it will also assess the desirability of additional efforts. This review will be scheduled after major policy changes have been made and most technical assistance activities have been completed. To assist in this review, a data base will be planned and established approximately two years beforehand. Additional information is provided in Section VII - Evaluation.

II. COST ESTIMATE AND FINANCIAL PLAN

A. Cost Estimate

2.01 Estimated project costs of \$75.0 million are to be financed from the AID grant. Of total costs, \$71.7 million is to be disbursed as local currency to support the rural credit program and \$3.3 million will finance foreign exchange and local currency costs of technical assistance. A summary cost estimate and financial plan is given in Table 2-1.

Table 2-1: Summary Cost Estimate and Financial Plan
(US\$ 000)

<u>Use</u>	<u>BDG</u>		<u>AID</u>		<u>Total</u>
	<u>LC</u>	<u>FX</u>	<u>LC</u>		
Refinance Facility	\$420,000				\$420,000
Local Currency Contr.			\$71,700		71,700
Advisory Services		1,512	\$ 424		1,936
Training		563	50		613
Equipment		40	95		125
Local Fund		-	50		50
Sub-Total	\$420,000	\$ 2,115	\$72,319		\$494,434
Inflation factor		116	44		160
Contingency		313	93		406
Total	\$420,000	\$ 2,544	\$72,456		\$495,000

2.02 USAID prepared cost estimates of the technical assistance element. Estimated costs of advisory services and training are based upon previous USAID experience. Costs of advisory services have been appropriately estimated to obtain the very highly qualified experts required for most tasks; in addition, adequate transportation and per diem expenses are included for short-term experts. Estimates of equipment costs are based upon quotations obtained from local dealers in February 1983. Inflation factors are: 6% p.a. for foreign exchange costs and 12% p.a. for local currency costs. The contingency of 15% will permit flexibility in responding to presently unanticipated needs throughout the project life.

B. Financial Plan

2.03 The financial plan shows AID and BDG funding of activities associated with the project. The BDG contribution of \$420 million over three years, or approximately \$140 million per year, is based upon recent amounts of funds used to refinance rural credit by the Bangladesh Bank. In addition, the BDG will contribute substantial staff time of senior government officials and officers of the central bank and financial institutions. These latter costs cannot be practically quantified, and their contribution to total project costs will be relatively small in financial terms. The BDG contribution substantially exceeds the required 25% contribution to project costs.

2.04 Projected disbursement of funds shown in Table 2-2.

Table 2-2
Projection of Expenditures By Fiscal Year
(US\$ 000)

<u>US Fiscal Year</u>	<u>AID</u>		<u>BDG</u>	<u>Total</u>
	<u>Local Currency</u>	<u>Technical Assistance</u>	<u>Refinance Facility</u>	
FY 1983	\$ 24,000	-	\$140,000	\$ 164,000
FY 1984	23,700	\$ 1,104	140,000	164,804
FY 1985	24,000	996	140,000	164,996
FY 1986	-	634		634
Sub-Total:	71,700	2,734	420,000	494,434
Inflation factor	-	160	—	160
Contingency	-	406	—	406
Total:	\$ 71,700	\$ 3,300	\$420,000	\$ 495,000

III. IMPLEMENTATION PLAN

A. Implementation Agency

1. Agricultural Credit Department

3.01 The implementation agency will be the Bangladesh Bank, which is the central bank of Bangladesh. The Bank's Agricultural Credit Department (ACD) will manage this project. The ACD, pursuant to the Bank's charter, studies all questions and coordinates all operations related to agricultural credit. This department is supervised by a Chief Officer who normally reports directly to the Bank's Governor through an Executive Director or a Deputy Governor. The department has an approved strength of 161 employees including 98 officers and 63 staff, of which 124 employees are on board including 91 officers and 33 staff. ACD is organized into two divisions: the credit division and the inspection division. This project will be managed within the credit division. Organizational charts and an ACD functional statement are included in Annex I.

3.02 ACD will establish a new unit to manage this project and the unit will be expanded if needed. ACD has previous experience in managing foreign donor projects (including RFEP, IFAD Small Farmers Credit Scheme, and a Swiss project on post-harvest technology) and many domestic activities. The Department's level of competence is high but it is not fully staffed and could use additional equipment. Unlike the previous RFEP project, where a large consulting team performed most of the implementation tasks, the ACD will implement this project with a relatively small amount of short-term, specialized advisory assistance. Consequently, the ACD must be strengthened. The Bangladesh Bank will review staff needs, develop a revised staffing pattern, and hire qualified persons.

2. Bangladesh Bank

3.3 The Bangladesh Bank was established as a Government agency on October 31, 1972, by President's Order No. 127 to succeed the State Bank of Pakistan. It is financially independent of the Government budget, although its own budget is reviewed along with other semi-autonomous agencies by the Government. The Bank's Board of Directors includes the Governor, Deputy Governor(s), four members nominated by the Government, and one Government official. Bank headquarters is in Dhaka and five regional offices are located in Chittagong, Khulna, Bogra, Rajshahi and Sylhet. The total number of Bank employees was approximately 5,500 as of June 30, 1982, comprised of 2,000 officers and 3,500 staff. The Bangladesh Bank exercises those functions and responsibilities customary for central banks, including: management of the monetary and credit system, issuance and regulation of currency, regulation of banking institutions, management of foreign reserves, maintenance of government accounts, and acting as the bankers' bank. The Bank manages

the monetary system through a series of controls including bank reserve requirements, credit ceilings, and refinance facilities. In practice, bank reserve requirements (which are 25% of deposits) have not been used to regulate money supply, and the Bank has relied chiefly on credit ceilings plus refinance facilities.

3. Rural Financial Institutions

3.04 Bangladesh has an established structure of rural financial institutions which pre-date Independence in 1971. The chief participants are: Bangladesh Krishi Bank (an agricultural development bank); Bangladesh Rural Development Board and Bangladesh Samabaya Bank Ltd. (two cooperative systems); and the six nationalized commercial banks. In addition, moneylenders play an important role. A summary description of institutions is contained in Annex J.

3.05 Rural branch expansion has been a high priority since Independence, and the number of rural branches doubled between 1977 and 1981, as shown in Table 3-1. At present, however, the Bank is concerned with possible over-banking in urban areas and potentially wasted resources, particularly experienced officers.

Table 3-1: Rural Branches

	<u>6/30/77</u>	<u>6/30/79</u>	<u>6/30/81</u>
Rural Branches	1,470	2,242	2,841
Urban Branches	1,063	1,320	1,518
Ratio: Rural/Urban Branches	1.4:1	1.7:1	1.9:1
Ratio: New Rural/New Urban Branches	5.6:1	4.0:1	6.5:1

Source: Based on Bangladesh Bank Bulletin.

3.06 The large rural branch expansion was not matched by equivalent growth in the number of trained and experienced officers. The hiring freeze was lifted in January 1983 and banks are now free to recruit new staff. Higher borrowing rates will support adequate funding for administrative costs. One indicator of overburdened loan officers is account load. Officers presently handle 800-1,000 accounts, which is too many for proper loan supervision and recovery; a reasonable number might be 250-300 accounts. However, the inferred tripling of account officers is not realizable in a short time. This project will finance advisory services for development of "core" training curricula, a branch rationalization plan including staffing and a review of lending procedures.

B. Implementation Schedule and Responsibilities

1. Schedule

3.07 This project contains a large number of discrete but related activities. The most important activities support key policy changes and will be undertaken in three phases; other tasks will be undertaken throughout the project life. An implementation schedule is included in Annex K and estimated dates for key events follow:

<u>Event</u>	<u>Date</u>	<u>Responsibility</u>
Authorization of Project	May 1983	AID
Advance Procurement actions	May 1983	AID
Signing of Project Agreement	June 1983	AID & BDG
Satisfaction of Initial CP's	June 1983	BDG
First Disbursement	June 1983	AID
PSC Signed	Sept. 1983	BDG
PASA Signed	Jan. 1984	AID/BDG
Prime Contract Signed	Mar. 1984	BDG
First Review	Mar. 1984	AID/BDG
Second Obligation	Apr. 1984	AID
Second Review	Mar. 1985	AID/BDG
Third Obligation	Apr. 1985	AID
Financial Sector Review	Dec. 1985	BDG/Contractor
PACD	June 1988	AID/BDG

2. Terminal Dates

3.08 The terminal date for satisfaction of conditions precedent to initial disbursement will be one month after the date of signing of the project agreement.

3.09 The Project Assistance Completion Date is June 30, 1988, which provides a five year life of project. Obligations will be made over three fiscal years and the project schedule shows that most project activities will be completed within four years. However, this project is in its initial phase and both the nature and length of services to support policy changes is not fully known. Therefore, we have added additional time to permit project close-out in an orderly fashion.

C. Procurement

1. Local Currency Procurement

3.10 Disbursements of local currency will be made by U.S. Treasury check.

2. Technical Assistance Element

3.11 Procurement procedures for the technical assistance element will follow AID Handbook 11 (Country Contracting) procedures except for technical services of the Federal Reserve System which will be procured under a PASA with AID. Customary disbursement procedures will be used. Source and origin will be AID Geographic Code 941 and Bangladesh.

a. Interest Rate Advisory Services

3.12 Advisory services will be procured under a Host Country contract with an individual expert. This task will be initiated soon after project effectiveness. Draft Terms of Reference are attached as Annex L-1.

b. Services of Federal Reserve System

3.13 Advisory services will be procured under a PASA with AID. A draft PIO/T is attached as Annex L-2.

c. Prime Contractor for Other Services

3.14 The Bangladesh Bank will contract with a management consulting firm which will function as a "prime contractor" in obtaining and administering the wide variety of short-term services required for the project. The Bank will prequalify firms before requesting proposals. Nationality of eligible firms will be U.S. and the firm may subcontract with firms and/or individuals from countries included in Code 941 and Bangladesh. A draft RFTP is attached as Annex L-3.

d. Project Review Advisor

3.15 Services of a project review advisor will be obtained under a Direct Contract to assist USAID and Bangladesh Bank in conducting reviews of the project during implementation. Draft Terms of Reference are attached as Annex L-4.

e. Equipment

3.16 The Bangladesh Bank will procure a small amount of transportation and office equipment. An indicative list is attached as Annex L-5.

IV. MONITORING PLAN

4.01 Monitoring will be performed by USAID staff which will be in frequent but not daily contact with the Bangladesh Bank, short-term advisors and rural financial institutions. The USAID project manager will spend nearly full time on this project and will require 25% to 40% of the time of an FSN project assistant. The project manager will draw upon assistance from other members of the project committee as needed, including an economist, legal counsel, and controller. Regular reviews of progress will be conducted by Mission top management every other month. Such reviews, when required, will be followed by substantive meetings on project problems with Bangladesh Bank top management officers.

4.02 Reports will be required from Bangladesh Bank on a quarterly basis and formats will be described in a Project Implementation Letter to be issued shortly after signing of the grant agreement. The Bank's Agricultural Credit Department will prepare these reports which will include progress, financial, and shipping information as pertinent.

4.03 Reports will be required of advisors on a monthly basis. These reports will be short because of job specificity and short duration.

V. SUMMARIES OF ANALYSES

5.01 Several analyses have been performed during project preparation. This section provides analyses which are not presented elsewhere in this paper and gives locations of other analyses.

A. Financial Analysis

5.02 A farm level budget analysis was summarized in Section I (Project Rational.) and is attached as Annex F-1.

5.03 A rationale for lending rate structure was summarized in Section I (Project Rationale) and is attached as Annex F-1.

Domestic Resource Mobilization and Private Sector Development

5.04 Reference was made in Section B.2 to the BDG's recent measures to increase domestic resource mobilization. The principal measures taken in FY 83 consisted of increases in administered prices to reduce foodgrain and fertilizer subsidies, and to reduce or eliminate the deficits of public sector corporations. By creating the basis for a viable banking system, this project would directly further that process. Further, through its emphasis on savings generation, it represents the first significant effort to increase private as opposed to public sector resource mobilization.

a. Relation to Public Sector Deficit/Subsidies

5.05 The performance of the public sector corporations worsened steadily in recent years. In FY 82, all public corporations combined recorded a pre-tax loss of Taka 1.2 billion.* The results were in fact worse because corporations concealed losses through incorrect accounting practices with respect to loan obligations and depreciation. Furthermore, the results for all public corporations included a profit for banking and financial institutions of Taka 2.0 billion.

5.06 Bank profits are illusory. It is normal banking practice in Bangladesh to report lending results on an accrual basis, without regard to overdue loans. The national banks have established low and inadequate bad debt reserves. As noted elsewhere in this paper, a high proportion of loans are in fact overdue. In an analysis of the six nationalized commercial banks, Boyd Wennergren has estimated that establishment of a 5 percent reserve for bad debts would have meant a combined FY 82 expense of Taka 961 million which would have reduced reported pre-tax profits of Taka 485 million to a pre-tax loss of Taka 476 million. Extension of this principle to the entire system would reveal a substantial loss rather than a profit and would show a very significant subsidy burden to the BDG.**

* Ministry of Finance and Planning, Budget Estimates For Autonomous Bodies, 1982-83

** Boyd Wennergren, Bangladesh Agriculture Sector Review (unfinished as of this writing), Chapter 5.

5.07 The banks' poor loan recovery rates are partly attributable to the prevailing low lending rates. As a result of these rates, borrowers are not motivated to repay loans since their carrying costs are below the prevailing rate of inflation and banks do not have adequate income to manage their lending activities. The present schedule of lending rates generally does not provide a margin over cost of funds sufficient to cover administrative costs and a profit margin. The project, through its provisions for a rational interest rate structure, and further provisions to improve accounting practices and loan management, will help to put the banking system on a viable basis thereby eliminating a major, if unrecorded, source of public sector subsidies.

b. Private Sector Resource Mobilization

5.08 As a trade-off as they were, the measures taken at the outset of FY 83 dealt entirely with mobilization of public sector resources. Further, the initially adverse impact of the measures fall almost entirely on the private sector.* The provision of real savings rates, along with the other measures to promote savings called for in the project, represents the first significant effort to increase private domestic resource mobilization. This will provide a badly needed push to the inadequate level of private savings, estimated at only 5.9 percent of GDP in FY 81.** Further, the existence of a viable banking system based primarily on savings creation will allow a greatly expanded volume of credit for financing of private sector activities.

* Initially, the private sector bore the brunt of the tax and price increases. However, the private sector is benefitting from the resulting reduction in inflation and greater availability of credit.

** Bangladesh: Recent Economic Developments and Selected Development Issues, IBRD, March 3, 1982, p. 100.

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C. Social Analysis

5.09 The Rural Finance Project seeks to effect broad changes in banking policy, and transformations in bank administrative procedures, through cooperation with the BDG and the Bangladesh Bank. Through these policy changes, banking institutions will be enabled to become more efficient, more effective, and more responsive to a wider range of clients in rural areas. Beneficiary impact, though nationwide in scale, is expected to be diffused as a consequence of the policy-oriented form of the project. Ordinary criteria for social soundness assessment are poorly suited to the task of analysing an essentially innovative and unconventional approach to development intervention.

5.10 Positive beneficiary impact will in the first instance result from increased bank credit on attractive terms, made available to a broader rural clientele. Secondly, increased villager participation in the institutional banking system will mobilize savings, extending the role of this institution in rural development at the expense of traditional non-institutionalized, often usurious, credit. Spread effects resulting from this process should be noticeable in changing agricultural productivity, agriculture-related industries, and marketing in rural areas.

5.11 Equity is an inherently important aspect of the Rural Finance Project. The predecessor Rural Finance Experimental Project documented the limited access to institutional credit in rural areas, and the acceptability of interest rates sufficient to cover banking costs. The choice was between continuing a limited, subsidized, and inefficient rural banking system largely serving the elite, or to expand access to credit for the majority of rural villagers. The Rural Finance Project represents the BDG's and USAID's effort to develop an effective and responsive banking system. The task is complex, and results are, at this stage, not precisely predictable. Over the life of the project, social and economic monitoring will assess change and guide implementation. It is expected that wider rural participation in a national system of credit and savings, managed by a more responsive set of banking institutions, will have profound implications for economic and social change. Additional information on social analysis is given in Annex G.

D. Administrative Analysis

5.12 The Implementation Agency is described in Section III (Implementation Agency) and additional details are included in Annex I.

5.13 Rural financial institutions are summarized in Section III (Implementation Agency) with additional details in Annex J.

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E. Environmental Analysis

3.14 This project qualifies for a Categorical Exclusion under environmental procedures described in 22 CFR 216 dated October 9, 1980. That regulation provides exclusion for "education, technical assistance, or training programs except to the extent they include activities directly affecting the environment (such as construction of facilities, etc.)". This project is comprised of technical assistance and training except for a relatively small amount of office equipment, and it will not have an effect on the natural or physical environment. In regard to the cash transfer, no specific categorical exclusion is listed. However, it appears to be excluded because AID does not have knowledge of or control over the specific uses of such funds.

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VI. CONDITIONS AND COVENANTS

A. Conditions Precedent to Disbursement

6.01 Prior to the first disbursement or the issuance of the documentation pursuant to which the first disbursement will be made under this grant, the BDG shall furnish to A.I.D. in form and substance satisfactory to A.I.D.

1. Opinion of legal counsel acceptable to A.I.D. that the Agreement has been duly authorized and/or ratified by, and executed on behalf of the Grantee, and that it constitutes a valid and legally binding obligation of the Grantee in accordance with all of its terms.

2. A statement of the names of the persons authorized to represent the Grantee as specified in Section 8.3 and additional representatives together with a specimen signature of each person.

6.02 Prior to the first local currency disbursement, the cooperating country shall provide A.I.D. with a plan for initial policy changes designed to improve the economic viability of the rural credit system.

6.03 Prior to the disbursement of any other funds or the issuance of documentation pursuant to which disbursement will be made for services and equipment, the Bangladesh Bank shall furnish in form and substance satisfactory to A.I.D. acceptable contracts for services and equipment.

B. Covenants

6.04 In addition to the Grant Covenants of Annex 2 of the Project Grant Standard Provisions Annex, all of the Standard Covenants prescribed by AID Handbook 3 shall be included in the Grant Agreement. In addition, the following special covenant shall be included:

The Grantee shall continue to undertake a series of discussions with A.I.D. on means to improve the economic viability of rural savings and lending facilities and services to the private sector.

6.05 USAID plans to include an additional covenant to require within six months a revised staffing pattern for the Agricultural Credit Department, showing positions for an adequate number of professional staff. This covenant, however, is not included in the authorization to provide USAID with flexibility in negotiation.

VII. EVALUATION ARRANGEMENTS

7.01 Evaluation activities will concentrate in three areas. First, advisors who perform work associated with policy changes will develop criteria and data systems so that the Bangladesh Bank can monitor impacts and adjust subsequent policy changes appropriately. Second, USAID and BDG will review performance in carrying out the project before disbursement of the second and third tranches. Third, the Bangladesh Bank and Prime Contractor will conduct a Financial Sector Review after most project activities have been completed.

A. Policy Change Impact Monitoring

7.02 Advisors whose work supports policy changes (interest rate rationalization, savings mobilization, and loan recovery) will develop methodologies so that the Bangladesh Bank can measure impacts of policy changes. This system will include both quantitative and qualitative reports. Quantitative reports will be based upon statistics showing increases or decreases in volume, number, and value of new loans, savings, and loan recovery. Also, qualitative reports will assess opinions towards policy changes among both bank customers and non-customers. These reports will be available on a frequent basis to senior officers of Bangladesh Bank.

B. Performance Reviews

7.03 USAID and BDG will conduct performance reviews before disbursement of the second and third tranches. The two distinct components of this project: (a) BDG action in enacting and implementing necessary policy changes affecting interest rates, savings mobilization, loan recovery, and (b) the various activities to improve the functioning and efficiency of the banking system, will be addressed both separately and jointly during these reviews. In regard to enactment and implementation of policy changes, simple determinations will be made as to whether the BDG has undertaken needed policy changes. Review of activities aimed at improving efficiency of the banking system will gauge the project's performance against output targets specified in this project paper and otherwise measure progress toward attainment of the project purpose. Project input schedules and output targets will be revised along with the technical assistance budgets, based upon the outcome of these reviews. A project review advisor, such as Dr. Richard Meyer, of Ohio State University, will assist in performing these reviews.

C. Financial Sector Review

7.04 The Prime Contractor will perform a Financial Sector Review after major policy changes have been made and most technical assistance activities have been completed. This Review will evaluate whether the project has accomplished its purpose, including the success of policy changes and technical assistance activities. It will also assess whether additional policy changes and supporting activities are desirable and, if so, will identify specific areas and tasks. The prime contractor will perform this review in close cooperation with the Bangladesh Bank and financial

institutions. This Review is scheduled to begin in September 1985 and take three months. At, or near the completion of this study, USAID will obtain services of a project review advisor, such as Dr. Richard Meyer, of Ohio State University, to assist in USAID review of the report.

BANGLADESH: RURAL FINANCE PROJECT

PID Approval Table - Excerpts

We propose a three year \$75 million Rural Finance Project aimed at a significant reform of the Bangladesh banking system. The expanded RFP would embody the PRG (i.e., Program Reform Grant) rationale for quick releasing commodity/cash aid in return for essential policy reform, but there would be no discrete PRG as such.

FY 83 funding for the RFP will be up to \$25 million ... to include realistic (i.e., in excess of the perceived rate of inflation) lending and savings rates. Subsequent fund releases would be dependent on BDG progress toward reform of the rural banking structure, pursuant to joint annual reviews. AID/W concurrence may be required for these annual reviews, depending upon the extent to which each year's policy goals have been defined in the project paper. We would prefer not to attempt a definition of "further progress" at this time, but it would have to involve extension of the basic RFP concepts beyond the limits of our own program.

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BANGLADESH: RURAL FINANCE PROJECT
LOG FRAME MATRIX

ANNEX B

<u>GOAL</u>	<u>INDICATORS</u>	<u>MEANS OF VERIFICATION</u>	<u>ASSUMPTIONS</u>
<p>Accelerate food production and expand employment in rural areas.</p>	<p>Production increases are greater in areas where farmers have access to banks & credit than in areas where they have no ready access.</p>	<p>Special Study</p>	<p>A. Normal Weather patterns. B. No major political upheaval. C. Inputs (e.g., fertilizer, HYV's, pumps) available.</p>
<p><u>PURPOSE</u></p> <p>Create an economically viable rural financial system which mobilizes savings and provides credit facilities to private farmers and entrepreneurs.</p>	<p><u>GOALS</u></p> <p>1. All rural banks are charging interest on loans at levels sufficient to cover their cost of funds, administrative costs, bad debt reserves, and reasonable profit. (CY 1983 estimate is that a 24% rate will be required).</p> <p>2. Savings, lending, & refinancing rates will be periodically reviewed (at least twice annually) by the "Bangladesh Bank Advisory Committee on Interest Rates" and rates will be adjusted appropriately, based upon the Committee's recommendations, to take into account trends in inflation, bank administration costs, & loan recovery rates.</p>	<p><u>MEANS OF VERIFICATION</u></p> <p>1. Final Evaluation Study. 2. Final Evaluation Study.</p>	<p><u>ASSUMPTIONS</u></p> <p>A. No dramatic downturn in economy. B. Rate, intensity, and impact of natural disasters (floods, droughts, etc) and political unrest not greater than normal. C. Prices for agricultural inputs and outputs remain at close to same relative ratios as in 1982/83</p>

<u>POPS</u>	<u>MEANS OF VERIFICATION</u>	<u>ASSUMPTIONS</u>
<p>3. Discount rates paid by rural branches (i.e. rates charged by the central bank for funds loaned to commercial banks) are equal to or slightly higher than interest rates paid to their depositors.</p> <p>4. Uniform accounting practices and methods of classifying overdrafts are in use by all banks in the country.</p>	<p>3. Final Evaluation Study.</p> <p>4. Final Evaluation Study.</p>	<p>D. Continued commitment of BDC to moving toward "full-cost" credit. (Committee is established, BDC access recommendations, etc.)</p> <p>E. Banks operating in rural sector implement changes on schedule.</p> <p>F. Need for increased rural credit is sustained throughout period.</p> <p>G. Rural people are increasingly attracted to financial services instruments in response to BDC interest rate policies.</p>

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OUTPUTS	INDICATORS	MEANS OF VERIFICATION	ASSUMPTIONS
A. <u>Studies conducted & recommendations filed regarding:</u>			
1. Structure of Interest Rates	A. 1. Recommendation by end of year 1	A. 1. Existence of report	A. Sufficient AID and EDG financial inputs provided in a timely manner.
2. BB Accounting and Related Systems	2. Recommendations by end of year 1	2. Existence of report	
3. BB Inspection System	3. Recommendations by end of year 1	3. Existence of report	
4. Mobilization of Savings	4. Plan by end of year 2	4. Existence of report	B. No major turnover of staff in the Credit Dept. of Bangladesh Bank.
5. Loan Recovery	5. Plan by end of year 3	5. Existence of report	
6. Establishment of Bank Branches	6. Plan by end of year 2	6. Existence of report	
7. Lending Policies & Procedures	7. Plan by end of year 3	7. Existence of report	
B. <u>Policy changes announced & implemented by the EDG regarding:</u>			
1. Interest rates			
a) Establishment of I.R. Advisory Committee	B.1.a. Completed by end of year 1	B.1.a. Existence and Functioning Formally Established Committee	
b) Establishment of lending rate which significantly reduces existing subsidy.	b. Statement of EDG plan for initial changes	1.b. BB Documents	

<u>OUTPUTS</u>	<u>INDICATORS</u>	<u>MEANS OF VERIFICATION</u>	<u>ASSUMPTIONS</u>
c) Establishment of lending rate which virtually eliminates subsidy.	1.c. By end of year 3	1.c. B3 Documents	
d) Establishment of re-finance rate for rural loans equal to or higher than banks weighted average cost of funds.	1.d. Plan of initial changes submitted prior to 1st Disbursement	1.d. B3 Documents	
e) Maintenance of savings rates at levels sufficiently high to provide real return to savers.	1.e. Quarterly	1.e. B3 Documents	
2. Loan recovery			
a) Accounting and classification system changes making it easier to identify problem loans instituted.	2.a. Done by end of year 1	2.a. B3 Documents	
b) Revision of penalties for non-repayment of loans.	2.b. Done by end of year 1	2.b. B3 Documents	
c) Establishment of incentive system motivating bankers to make vigorous collection efforts.	2.c. Done by end of years 2	2.c. B3 Documents	

<u>OUTPUTS</u>	<u>INDICATORS</u>	<u>MEANS OF VERIFICATION</u>	<u>ASSUMPTIONS</u>
3. Savings Mobilization			
a) Establishment of an incentive system which motivates bankers to aggressively pursue savings deposits.	3.a. Done by end of year 2	3.a. 38 Documents	
b) Establishment of a system within the bank which allows constant monitoring of savings levels.	3.b. Done by end of year 2	3.b. 21 Documents	
C. <u>Manuals Produced</u>			
1. Methodology for Determining Appropriate Interest Rates.	1.1. Completed by end of year 1	C.1. Existence of Manual	
2. Revised Banking Inspection Procedures	2. Completed by end of year 2	2. Existence of Manual	
D. <u>Training Courses Developed</u>			
1. Modern Rural Bank Branch Operations (two weeks)	D.1. Completed by end of year 3	D.1. Existence of Written Course Outline	
2. Rural Bank Branch Management & Supervision (two weeks)	2. Completed by end of year 2	"	
3. Rural Credit (one week)	3. Completed by end of year 3	"	

OUTPUTS

INDICATORS

MEANS OF VERIFICATION

ASSUMPTIONS

1. Individuals Trained

1. Staff members of the Technical Unit Supporting the U.S. Advisory Committee trained in methodology for determining appropriate interest rates.

E.1. 3 by year 1,
6 by year 3

E.1. Interview with
Each Trained

2. Staff members of the Bank Inspection Unit trained in more effective inspection techniques (S-T Training).

E.2. Year 3

E.2. Interview with
Each Trained

3. Approximately 15 senior officers of U.S. and commercial banks trained in savings mobilization, loan administration and collection procedures as practiced in other relevant countries.

E.3. 5 per year

E.3. Interview with
Each Trained

4. Approximately 2,000 rural bank branch managers and assistant managers trained in course material listed under "B" above.

E.4. Approx 700
per year

E.4. BLM and financial
institutions' records

<u>INPUTS</u>	<u>INDICATORS</u>	<u>MEANS OF VERIFICATION</u>	<u>ASSUMPTIONS</u>
I. USAID			
1. Technical Assistance			
a) Interest Rate Advisor	1. a) 6 PM	USAID Records	
b) Federal Reserve System (Bank examination, accounting, foreign exchange, note issue)	b) 24 PM	"	
c) Prime Contractor (Savings mobilization, loan recovery, training curriculum, branch rationalization, lending efficiency, financial sector review)	c) 58 PM-Expatriate 79 PM-Local	"	
d) Project Review Advisor	d) 6 PM		
2. Training	2. 84 PM	Bangladesh Bank Records	
3. Commodities	3. \$ 135,000	"	
4. Cash Transport	4. Yr. 1 \$24,000,000* Yr. 2 \$23,700,000 Yr. 3 \$24,000,000	USAID Record	
II. BXC			
- Staff Members as Required from Agricultural Credit Dept. of BB.		Bangladesh Bank Records	
- Refinance Facility	\$140,000,000 annually	"	
- Facilities on the BIRM		"	

* In each case cash transfer disbursement will be reduced by the amount estimated to be required to finance TA, Training, and Commodities to be obligated that year.

5C(1) - COUNTRY CHECKLIST

Listed below are statutory criteria applicable generally to FAA Funds, and criteria applicable to individual fund sources: Development Assistance and Economic Support Fund.

A. GENERAL CRITERIA FOR COUNTRY ELIGIBILITY

1. FAA Sec. 481. Has it been determined that the government of the recipient country has failed to take adequate steps to prevent narcotic drugs and other controlled substances (as defined by the Comprehensive Drug Abuse Prevention and Control Act of 1970) produced or processed, in whole or in part, in such country, or transported through such country, from being sold illegally within the jurisdiction of such country to U.S. Government personnel or their dependents, or from entering the U.S. unlawfully?

No

2. FAA Sec. 620(c). If assistance is to a government, is the government liable as debtor or unconditional guarantor or any debt to a U.S. citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) the debt is not denied or contested by such government?

No

3. FAA Sec. 620(a)(1). If assistance is to a government, has it (including government agencies or subdivisions) taken any action which has the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property of U.S. citizens or entities beneficially owned by them without taking steps to discharge its obligations toward such citizens or entities? No
4. FAA Sec. 532(c), 620(a), 620(f), 620D; FY 1982 Appropriation Act Secs. 512 and 513. Is recipient country a Communist country? Will assistance be provided to Angola, Cambodia, Cuba, Laos, Vietnam, Syria, Libya, Iraq, or South Yemen? Will assistance be provided to Afghanistan or Mozambique without a waiver? No
5. ISDCA of 1981 Secs. 724, 727 and 730. For specific restrictions on assistance to Nicaragua, see Sec. 724 of the ISDCA of 1981. For specific restrictions on assistance to El Salvador, see Secs. 727 and 730 of the ISDCA of 1981. N/A
6. FAA Sec. 620(j). Has the country permitted, or failed to take adequate measures to prevent, the damage or destruction by mob action of U.S. property? No

7. FAA Sec. 620(l). Has the country failed to enter into an agreement with OPIC? No, agreement signed Jan. 1975
8. FAA Sec. 620(o); Fishermen's Protective Act of 1967, as amended, Sec. 5. (a) Has the country seized, or imposed any penalty or sanction against, any U.S. fishing activities in international waters? No
- (b) If so, has any deduction required by the Fishermen's Protective Act been made? N/A
9. FAA Sec. 620(g); FY 1982 Appropriation Act Sec. 517. (a) Has the government of the recipient country been in default for more than six months on interest or principal of any AID loan to the country? a) No
- (b) Has the country been in default for more than one year on interest or principal on any U.S. loan under a program for which the appropriation bill appropriates funds? b) No
10. FAA Sec. 620(s). If contemplated assistance is development loan or from Economic Support Fund, has the Administrator taken into account the amount of foreign exchange or other resources which the country has spent on military equipment? N/A
- (Reference may be made to the annual "Taking into

Consideration" memo:
"Yes, taken into account
by the Administrator at
time of approval of
Agency OYB." This
approval by the
Administrator of the
Operational Year Budget
can be the basis for an
affirmative answer during
the fiscal year unless
significant changes in
circumstances occur.)

11. FAA Sec. 620(t). Has the
country severed
diplomatic relations with
the United States? If
so, have they been
resumed and have new
bilateral assistance
agreements been
negotiated and entered
into since such
resumption? No

12. FAA Sec. 620(u). What is
the payment status of the
country's U.N.
obligations? If the
country is in arrears,
were such arrearages
taken into account by the
AID Administrator in
determining the current
AID Operational Year
Budget? (Reference may
be made to the Taking
into Consideration memo.) Not in arrears

13. FAA Sec. 620A; FY 1982
Appropriation Act Sec.
520. Has the country
aided or abetted, by
granting sanctuary from
prosecution to, any
individual or group which
has committed an act of
international terrorism?
Has the country aided or No

abetted, by granting sanctuary from prosecution to, any individual or group which has committed a war crime?

14. FAA Sec. 666. Does the country object, on the basis of race, religion, national origin or sex, to the presence of any officer or employee of the U.S. who is present in such country to carry out economic development programs under the FAA? No
15. FAA Sec. 669, 670. Has the country, after August 3, 1977, delivered or received nuclear enrichment or reprocessing equipment, materials, or technology, without specified arrangements or safeguards? Has it transferred a nuclear explosive device to a non-nuclear weapon state, or if such a state, either received or detonated a nuclear explosive device, after August 3, 1977? (FAA Sec. 620E permits a special waiver of Sec. 669 for Pakistan.) No
16. ISDCA of 1981 Sec. 720. Was the country represented at the Meeting of Ministers of Foreign Affairs and Heads of Delegations of the Non-Aligned Countries to the 36th General Session of the General Assembly of the U.N. of Sept. 25 and 28, 1981, and failed No

to disassociate itself from the communique issued? If so, has the President taken it into account? (Reference may be made to the Taking into Consideration memo.)

17. ISDCA of 1981 Sec. 721.
See special requirements for assistance to Haiti.

N/A

B. FUNDING SOURCE CRITERIA FOR COUNTRY ELIGIBILITY

1. Development Assistance Country Criteria.

a. FAA Sec. 116. Has the Department of State determined that this government has engaged in a consistent pattern of gross violations of internationally recognized human rights? If so, can it be demonstrated that contemplated assistance will directly benefit the needy?

No

2. Economic Support Fund Country Criteria

a. FAA Sec. 502B. Has it been determined that the country has engaged in a consistent pattern of gross violations of internationally recognized human rights? If so, has the country made such significant improvements in its human rights record that furnishing such assistance is in the national interest?

N/A

b. ISDCA of 1981, Sec. 725(b). If ESF is to be furnished to Argentina, has the President certified that (1) the Govt. of Argentina has made significant progress in human rights; and (2) that the provision of such assistance is in the national interests of the U.S.?

N/A

c. ISDCA of 1981, Sec. 726(b). If ESF assistance is to be furnished to Chile, has the President certified that (1) the Govt. of Chile has made significant progress in human rights; (2) it is in the national interest of the U.S.; and (3) the Govt. of Chile is not aiding international terrorism and has taken steps to bring to justice those indicated in connection with the murder of Orlando Letelier?

N/A

5C(2) PROJECT CHECKLIST

Listed below are statutory criteria applicable to projects. This section is divided into two parts. Part A. includes criteria applicable to all projects. Part B. applies to projects funded from specific sources only: B.1. applies to all projects funded with Development Assistance Funds, B.2. applies to projects funded with Development Assistance loans, and B.3. applies to projects funded from ESF.

CROSS REFERENCES: IS COUNTRY CHECKLIST UP TO DATE? HAS STANDARD ITEM CHECKLIST BEEN REVIEWED FOR THIS PROJECT? Yes

A. GENERAL CRITERIA FOR PROJECT

1. FY 1982 Appropriation Act Sec. 523, FAA Sec. 634A; Sec. 653(b).

(a) Describe how authorizing and appropriations committees of Senate and House have been or will be notified concerning the project;

(b) is assistance within (Operational Year Budget) country or international organization allocation reported to Congress (or not more than \$1 million over that amount)?

(a) This project was mentioned on pages 24, 25 and 27 of Annex II of the FY 83 CP and on pages 24 and 27 of Annex II of the FY 84 CP. A Congressional Notification will be transmitted before obligation.

(b) Yes

2. FAA Sec. 611(a)(1). Prior to obligation in excess of \$100,000, will there be Yes

- (a) engineering, financial or other plans necessary to carry out the assistance and (b) a reasonably firm estimate of the cost to the U.S. of the assistance?
- (a) Yes
- (b) Yes
3. FAA Sec. 611(a)(2). If further legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of purpose of the assistance?
- Legislative action is not necessary to the project. Policy reforms will be implemented by administrative circulars of the Bangladesh Bank.
4. FAA Sec. 611(b); FY 1982 Appropriation Act Sec. 501. If for water or water-related land resource construction, has project met the standards and criteria as set forth in the Principles and Standards for Planning Water and Related Land Resources, dated October 25, 1973? (See AID Handbook 3 for new guidelines.)
- N/A
5. FAA Sec. 611(e). If project is capital assistance (e.g., construction), and all U.S. assistance for it will exceed \$1 million, has Mission Director certified and Regional Assistant Administrator taken into consideration the country's capability effectively to maintain and utilize the project?
- N/A

6. FAA Sec. 209. Is project susceptible to execution as part of regional or multilateral project? If so, why is project not so executed? Information and conclusion whether assistance will encourage regional development programs.

No

7. FAA Sec. 601(a). Information and conclusions whether project will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; and (c) encourage development and use of cooperatives, and credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture and commerce; and (f) strengthen free labor unions.

- a) Yes, absence of sound banking system is hindering development of trade. Ameliorating this problem should help increase trade.
- b) Yes
- c) yes
- d) yes
- e) Yes
- f) N/A

8. FAA Sec. 601(b). Information and conclusions on how project will encourage U.S. private trade and investment abroad and ~~investment abroad and~~ encourage private U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise).

See 7a, above

9. FAA Sec. 612(b), 636(h);
FY 1982 Appropriation
Act Sec. 507. Describe
steps taken to assure
that, to the maximum
extent possible, the
country is contributing
local currencies to meet
the cost of contractual
and other services, and
foreign currencies owned
by the U.S. are utilized
in lieu of dollars.
- N/A, as American or other expatriate
technical assistance contractors re-
quire payment in dollars
10. FAA Sec. 612(d). Does
the U.S. own excess
foreign currency of the
country and, if so, what
arrangements have been
made for its release?
- No
11. FAA Sec. 601(e). Will
the project utilize
competitive selection
procedures for the
awarding of contracts,
except where applicable
procurement rules allow
otherwise?
- Yes
12. FY 1982 Appropriation Act
Sec. 521. If assistance
is for the production of
any commodity for export,
is the commodity likely
to be in surplus on world
markets at the time the
resulting productive
capacity becomes
operative, and is such
assistance likely to
cause substantial injury
to U.S. producers of the
same, similar or
competing commodity?
- N/A
13. FAA 118(c) and (d).
Does the project comply
with the environmental
procedures set forth in
AID Regulation 16? Does
- Yes

the project or program take into consideration the problem of the destruction of tropical forests?

N/A

14. FAA 121(d). If a Sahel project, has a determination been made that the host government has an adequate system for accounting for and controlling receipt and expenditure of project funds (dollars or local currency generated therefrom)?

N/A

B. FUNDING CRITERIA FOR PROJECT

1. Development Assistance Project Criteria

a. FAA Sec. 102(b), 111, 113, 281(a). Extent to which activity will (a) effectively involve the poor in development, by extending access to economy at local level, increasing labor-intensive production and the use of appropriate technology, spreading investment out from cities to small towns and rural areas, and insuring wide participation of the poor in the benefits of development on a sustained basis, using the appropriate U.S. institutions; (b) help develop cooperatives, especially by technical assistance, to assist rural and urban poor to help themselves toward better life, and otherwise

a) Project is aimed at making savings and credit facilities more available to rural poor.

b) The two cooperative banks in Bangladesh will participate in the project.

encourage democratic private and local governmental institutions; (c) support the self-help efforts of developing countries; (d) promote the participation of women in the national economies of developing countries and the improvement of women's status; and (e) utilize and encourage regional cooperation by developing countries?

c) Yes

d) Yes

e) Yes

b. FAA Sec. 103, 103A, 104, 105, 106. Does the project fit the criteria for the type of funds (functional account) being used?

Yes (Sec. 103)

c. FAA Sec. 107. Is emphasis on use of appropriate technology (relatively smaller, cost-saving, labor-using technologies that are generally most appropriate for the small farms, small businesses, and small incomes of the poor)?

Yes

d. FAA Sec. 110(a). Will the recipient country provide at least 25% of the costs of the program, project, or activity with respect to which the assistance is to be furnished (or is the latter cost-sharing requirement being waived for a "relatively least developed" country)?

Yes

e. FAA Sec. 110(b).

Will grant capital assistance be disbursed for project over more than 3 years? If so, has justification satisfactory to Congress been made, and efforts for other financing, or is the recipient country "relatively least developed"? (M.O. 1232.1 defined a capital project as "the construction, expansion, equipping or alteration of a physical facility or facilities financed by AID dollar assistance of not less than \$100,000, including related advisory, managerial and training services, and not undertaken as part of a project of a predominantly technical assistance character."

N/A

f. FAA Sec. 122(c). Does the activity give reasonable promise of contributing to the development of economic resources, or to the increase of productive capacities and self-sustaining economic growth?

Yes

g. FAA Sec. 281(b). Describe extent to which program recognizes the particular needs, desires, and capacities of the people of the country; utilizes the country's intellectual resources to encourage

See Section I and V.C of the Project Paper.

institutional development;
and supports civil
education and training in
skills required for
effective participation in
governmental processes
essential to self-government.

2. Development Assistance Project
Criteria (Loans Only)

N/A

- a. FAA Sec. 122(b).
Information and conclusion
on capacity of the country
to repay the loan, at a
reasonable rate of interest.
- b. FAA Sec. 620(d). If
assistance is for any
productive enterprise which
will compete with U.S.
enterprises, is there an
agreement by the recipient
country to prevent export
to the U.S. of more than
20% of the enterprise's
annual production during
the life of the loan?
- c. ISDCA of 1981, Sec. 724
(c) and (d). If for
Nicaragua, does the loan
agreement require that the
funds be used to the
maximum extent possible for
the private sector? Does
the project provide for
monitoring under FAA Sec.
624(g)?

3. Economic Support Fund
Project Criteria

N/A

- a. FAA Sec. 531(a). Will
this assistance promote
economic or political

stability? To the extent possible, does it reflect the policy directions of FAA Section 102?

- b. FAA Sec. 531(c). Will assistance under this chapter be used for military, or paramilitary activities?
- c. FAA Sec. 534. Will ESF funds be used to finance the construction of the operation or maintenance of, or the supplying of fuel for, a nuclear facility? If so, has the President certified that such use of funds is indispensable to nonproliferation objectives?
- d. FAA Sec. 609. If commodities are to be granted so that sale proceeds will accrue to the recipient country, have Special Account (counterpart) arrangements been made?

5C(3) - STANDARD ITEM CHECKLIST

Listed below are the statutory items which normally will be covered routinely in those provisions of an assistance agreement dealing with its implementation, or covered in the agreement by imposing limits on certain uses of funds.

These items are arranged under the general headings of (A) procurement, (B) Construction, and (C) Other Restrictions.

A. Procurement

1. FAA Sec. 602. Are there arrangements to permit U.S. small business to participate equitably in the furnishing of commodities and services financed? Yes

2. FAA Sec. 604(a). Will all procurement be from the U.S. except as otherwise determined by the President or under delegation from him? Yes

3. FAA Sec. 604(d). If the cooperating country discriminates against marine insurance companies authorized to do business in the U.S., will commodities be insured in the United States against marine risk with such a company? Yes.

4. FAA Sec. 604(e); ISDCA of 1980 Sec. 705(1). If offshore procurement of agricultural commodity or product is to be N/A

financed, is there provision against such procurement when the domestic price of such commodity is less than parity? (Exception where commodity financed could not reasonably be procured in U.S.)

5. FAA Sec. 604(q). Will construction or engineering services be procured from firms of countries otherwise eligible under Code 941, but which have attained a competitive capability in international markets in one or these areas? N/A

6. FAA Sec. 603. Is the shipping excluded from compliance with requirement in section 901(b) of the Merchant Marine Act of 1936, as amended, that at least 50 per centum of the gross tonnage of commodities (computed separately for dry bulk carriers, dry cargo liners, and tankers) financed shall be transported on privately owned U.S. flag commercial vessels to the extent that such vessels are available at fair and reasonable rates? No

7. FAA Sec. 621. If technical assistance is financed, will such assistance be furnished by private enterprise on a contract basis to the fullest extent practicable? If the facilities of other Yes

Federal agencies will be utilized, are they particularly suitable, not competitive with private enterprise, and made available without undue interference with domestic programs?

Yes. (PASA with Federal Reserve System.)

8. International Air Transport. Fair Competitive Practices Act, 1974. If air transportation of persons or property is financed on grant basis, will U.S. carriers be used to the extent such service is available?

Yes

9. FY 1982 Appropriation Act Sec. 504. If the U.S. Government is a party to a contract for procurement, does the contract contain a provision authorizing termination of such contract for the convenience of the United States?

Yes, such clauses will be inserted in A.I.D.-direct contracts.

B. Construction

1. FAA Sec. 601(d). If capital (e.g., construction) project, will U.S. engineering and professional services to be used?

N/A

2. FAA Sec. 611(c). If contracts for construction are to be financed, will they be let on a competitive basis to maximum extent practicable?

N/A

3. FAA Sec. 620(k). If for construction of productive enterprise, will aggregate value of assistance to be furnished by the U.S. not exceed \$100 million (except for productive enterprises in Egypt that were described in the CP)? N/A

C. Other Restrictions

1. FAA Sec. 122(b). If development loan, is interest rate at least 2% per annum during grace period and at least 3% per annum thereafter? N/A
2. FAA Sec. 301(d). If fund is established solely by U.S. contributions and administered by an international organization, does Comptroller General have audit rights? N/A
3. FAA Sec. 620(h). Do arrangements exist to insure that United States foreign aid is not used in a manner which, contrary to the best interests of the United States, promotes or assists the foreign aid projects or activities of the Communist-Bloc countries? Yes
4. Will arrangements preclude use of financing.
- a. FAA Sec. 104(f); FY 1982 Appropriation Act Sec. 525: (1) To pay for performance of abortions as a method of family 1) Yes

- planning or to motivate or coerce persons to practice abortions; (2) to pay for performance of involuntary sterilization as method of family planning, or to coerce or provide financial incentive to any person to undergo sterilization; (3) to pay for any biomedical research which relates, in whole or part, to methods or the performance of abortions or involuntary sterilizations as a means of family planning; (4) to lobby for abortion? 2) Yes
- b. FAA Sec. 620(g). To compensate owners for expropriated nationalized property? 3) Yes
- c. FAA Sec. 610. To provide training or advice or provide any financial support for police, prisons, or other law enforcement forces, except for narcotics programs? 4) Yes
- d. FAA Sec. 602. For CIA activities? Yes
- e. FAA Sec. 636(i). For purchase, sale, long-term lease, exchange or guaranty of the sale of motor vehicles manufactured outside U.S., unless a waiver is obtained? Yes
- f. FY 1982 Appropriation Act, Sec. 503. To pay pensions, annuities, retirement pay, or Yes

adjusted service
compensation for military
personnel?

g. FY 1982 Appropriation
Act, Sec. 505. To pay
U.N. assessments,
arrearages or dues? **Yes**

h. FY 1982 Appropriation
Act, Sec. 506. To carry
out provisions of FAA
section 209(d) (Transfer
of FAA funds to
multilateral
organizations for
lending)? **Yes**

i. FY 1982 Appropriation
Act, Sec. 510. To
Finance the export of
nuclear equipment, fuel,
or technology or to train
foreign national in
nuclear fields? **Yes**

j. FY 1982 Appropriation
Act, Sec. 511. Will
assistance be provided
for the purpose of aiding
the efforts of the
government of such
country to repress the
legitimate rights of the
population of such
country contrary to the
Universal Declaration of
Human Rights? **No**

k. FY 1982 Appropriation
Act, Sec. 515. To be
used for publicity or
propaganda purposes
within U.S. not
authorized by Congress? **No**

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Department of State

INCOMING
TELEGRAM

ACTION: 710 00

ACTION OFFICE ASPD-03
INFO ASDP-02 PRCE-01 PPPB-02 GC-01 GCAS-01 GCFL-01 PPDC-01
ASTR-01 RELO-01 MAST-01 7501-02 017 46 116

INFO OCT-00 INR-10 LB-08 NEA-07 L-03 023 W
-----152365 0508362 36

R 041045Z MAY 83
FM AMEMBASSY DHAKA
TO SECSTATE WASHDC 1601

ANNEX D

UNCLAS DHAKA 3453

AIDAC

FOR/ ASIA/PD

E.O. 12356 N/A
SUBJECT RURAL FINANCE PROJECT (388-0037)

THE FOLLOWING IS THE TEXT OF LETTER RECEIVED FROM THE BANGLADESH GOVERNMENT REQUESTING ASSISTANCE IN SUPPORT OF THE RURAL FINANCE PROJECT:

QUOTE DEAR MR. NORRIS:

1. THE GOVERNMENT OF THE PEOPLE'S REPUBLIC OF BANGLADESH HAS UNDER ITS ACTIVE CONSIDERATION A PROGRAMME TO FURTHER EXPAND ITS RURAL CREDIT OPERATION. THE GOVERNMENT PLANS TO INTRODUCE SEVERAL CHANGES IN RURAL CREDIT PROGRAMME INCLUDING THOSE AIMED AT RATIONALIZING THE STRUCTURE OF INTEREST RATES, MOBILIZATION OF SAVINGS, AND IMPROVING LOAN RECOVERY
2. WE WOULD LIKE TO REQUEST THE USAID TO PROVIDE SUPPORT TO THIS EFFORT OF THE GOVERNMENT THROUGH A GRANT AMOUNTING TO DOL 75 MILLION. IT IS SUGGESTED THAT THIS GRANT BE DISBURSED IN THREE INSTALMENTS, WITH AN INITIAL TRANCHE OF DOL 25 0 MILLION DISBURSED BY JUNE 1983. THE DISBURSEMENT OF THE LAST INSTALMENT SHOULD TAKE PLACE NOT LATER THAN 18 MONTHS FROM THE DATE OF THE AGREEMENT
3. WE HOPE THE US GOVERNMENT WOULD BE ABLE TO AUTHORIZE THE PROJECT AT AN EARLY DATE SO THAT PROCESSING OF THE DRAFT PROJECT AGREEMENT CAN COMMENCE BY THE END OF MAY, 1983. WE LOOK FORWARD TO THE CONTINUED SUPPORT OF THE UNITED STATES GOVERNMENT IN THE ECONOMIC DEVELOPMENT OF BANGLADESH. WITH REGARDS, SINCERELY,
M. A. MATIN LASKER, DEPUTY SECRETARY, ERD, MINISTRY OF FINANCE. UNQUOTE.
COON

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BANGLADESH RURAL FINANCE PROJECT
Historical Interest Rate Structure

ANNEX E

	Dec. 71 to Jun. 74	July 74 to Mar. 76	Apr. 76 to Apr. 77	May 77 to Oct. 80	Since Oct. 16, 1980
A. Refinance Rates					
1. Bank Rate	5 %	8 %	Same	Same	10.5 %
2. For Bangladesh Krishi Bank & Bangladesh Sama- baya Bank.	3 %	6 %	Same	Same	Same
3. Rural Loans	N/A	N/A	8 %	6 %	Same
B. Loans (a)					
1. Agriculture	7-8%	11-11.5%	Same	Same	12 %
2. Exports	-	10.5%	Same	Same	12 % (b)
3. Socio-economic Projects *	7 %	11 %	Same	Same	13 %
4. Manufacturing & Transport	7-8 %	12-13%	Same	11.5-13%	14.5% (c)
5. Other loans	9-10%	12-13%	Same	11-12%	16% (d)
C. Deposits					
1. Demand Deposits	-	-	-	-	-
2. Special Notice Deposits:					
a. On 7-29 days	3 %	4 %	5 %	4 %	4.5 %
b. On 30 or more days.	3.25%	4.25%	5.25%	4.25%	4.5 %
3. Savings Accounts					
a. With checking	4 %	5 %	6 %	7 %	8.5 %
b. Without checking	4.5%	6 %	7 %	7.75%	10 %
4. Time Deposits					
a. 3-6 months	4.5%	6 %	7 %	7-8.5% (e)	12 %
b. 6-12 months	4.75%	6.5%	7.5%	7.5-9% (e)	13 %
c. 1-2 years	5 %	7.25%	8.25%	8.25-9.25% (e)	14 %
d. 2-3 years	5.5 %	8.25%	9.25%	9.25 %	14.5%
e. 3 or more years	6 %	9.25%	10.25%	10.25%	15 %

Footnotes

- (a) Where a range is given (e.g., 11-11.5%), bankers were free to exercise discretion.
- (b) Reduced to 11.5% for non-traditional exports (i.e., except jute, jute products, and tea) on June 5, 1982.
- (c) Increased from 14% on August 1, 1981.
- (d) Increased from 15.5% on December 5, 1981.
- (e) Lower rates were paid for urban deposits and higher rates, for rural deposits.

* Includes rural entrepreneurs

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Farm Level Budget Analysis

The Table shows, in column 1, the farm budget of a typical one hectare (2.5 acres) farmer of traditional variety transplanted aman rice.* His gross profit, not including cost of land or imputed cost of family labor, is 2,700 Taka per acre (about \$111). To switch to high yielding variety (HYV) production will greatly increase his yields and gross revenues, but will involve substantially higher investments in seeds, fertilizer, pesticides, labor and - in this, as in most cases - irrigation equipment. It is assumed that until now he has not required financing, but that to switch to HYV production he will have to borrow to finance his investment (i.e., those additional costs of traditional variety production). Three alternative finance costs are assumed: 12 percent (the present regular institutional rate), 24 percent (approximating the cost for the project rate), and 100 percent (the minimum rate for those forced to use the informal money-lender market). All loans are assumed to have a one-year term, except for the institutional loans to finance the handpump where a 5-year term loan is assumed (medium term credit is believed to be generally unavailable from informal lenders).

As shown in the Table, the additional investment results in gross profit increases of 980 and 790 Taka (or 36 and 29 percent) under the 12 and 24 percent interest rate scenarios, respectively. At the 100 percent rate, he would suffer a profit decline of over 50 percent.

Given the ever-present risk of crop loss due to the vagaries of weather in Bangladesh, it should not be concluded too readily that the farmer will therefore opt for the HYV investment at the 12 and 24 percent rates. He knows his costs are going up by 800 to 1,000 Taka an acre; he can't be certain of the higher return. A customary way of looking at the matter, designed to take greater account of the crop risks involved, is to consider prospective benefit: cost (B/C) ratios, meaning simply prospective revenues to total costs. Most observers feel that a farmer must be able to foresee at least a 2:1 B/C ratio before investing in HYV technology. In this example, the prospective B/C ratios are a comfortable 4.3 and 3.6 under the institutional borrowing scenarios. In these cases, then, he would very likely undertake the investment. Under the 100 percent scenario he could foresee a B/C ratio of only 1.4. Even a partial crop failure would wipe out his prospective profits, which in any case would be lower in the first year than he had been achieving under traditional

* T. Aman rice accounts for about 46 percent of annual rice production. Approximately 16 percent of T. Aman output is accounted for by HYV varieties.

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Cost and Returns of T. Aman Paddy
(1982-83 season)

Crop yields: Traditional variety: 22 pounds per acre

HYV Variety: 37 pounds per acre

Farmgate price: Taka 138 per pound

	Traditional Variety	HYV Production-Hypothetical Finance Costs	
		12%	100%
1. Gross revenues	3,035	4,830	4,830
2. Costs of production:			
a. Regular Cash Costs ^{a/}	335	720	720
b. Handpump ^{b/}	-	384	2,400
c. Subtotal	335	1,104	3,120
3. Interest Costs ^{c/}	-	46	385
4. Total Costs	335	1,150	3,505
5. Gross Profit (1-4)	2,700	3,680	1,325
6. Benefit: Cost Ratio (1 ÷ 4)	9.1:1	4.2:1	1.4:1

Footnotes: (a) Fertilizer, seeds, pesticides and hired labor
Not including imputed cost of family labor.

(b) Basic handpump cost is 1,200 Taka. Assume 5-year
term financing under the 12 and 24 percent interest
rate scenarios, with equal annual repayments of principal
and with interest payments on the outstanding balances.
This example shows the amount paid in the first year.
A 1-year loan is assumed under the 100 percent scenario.

(c) Applied to all regular cash cost items.

Source: Transplanted Aman Paddy Cultivation Practices Costs and Returns
in Thakurgaon Tubewell Project Area, 1980-81, Bangladesh Rice
Research Institute. Adjusted to reflect 1982-83 farmgate paddy
prices and costs of production, and to reflect handpump rather
than tubewell irrigation.

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variety production. In all probability he would not undertake the investment.

The significant points to note are:

(1) The relatively minor difference between borrowing at 12 or 24 percent. The difference in gross profit margins and B/C ratios is relatively insignificant.

(2) The prohibitive addition to costs reflected in the 100 percent rate. It may be objected that the case against the 100 percent rate has been "loaded" by insisting on repayment in one year, unlike the case with the institutional case where 5-year terms are granted. It might be argued, further, that after the first year, the borrower, on the informal market is clear of charges on his pump, and could look for better returns thereafter. However, the inability to obtain 5-year terms outside of the banking system simply reflects market realities. The first year profit outlook and risk being what they are, the investment will in all probability not be undertaken and there will be no second year.

Many farmers have been able to undertake HYV investments without recourse to credit, institutional or otherwise; others require less credit than the amounts postulated here. There is no question, however, that a great many must have financing to undertake investments of the magnitude exemplified by this model. The model should be considered as illustrative, but is sufficiently representative of the general reality to demonstrate the importance of institutional credit in the farmer's decision-making process.

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ESTIMATE FOR LBN INTEREST

USAID estimates that a rural lending rate of 24% should be a sufficient minimum rate to cover costs of lending and be acceptable to borrowers. Our estimate of an appropriate rate was based principally upon the most relevant findings of reports submitted to the National Review Committee on Agricultural Credit and from the AIC Rural Finance Experimental Project. This estimate was prepared with the assistance of Dr. Richard Meyer, Ohio State University.

The proposed rate was derived from estimates of the principal costs components: actual cost of funds, cost of administration, reserves for bad debts, and profits. These components are addressed in both the National Review Committee (NRC) working papers and Rural Financial Experimental Project (RFEP) evaluations. The NRC working papers cover all relevant banks and include data from accounting systems as presently kept. Difficulties in interpreting these data arise from inconsistency of definitions and data bases among different types of lending institutions and lack of availability of certain information. The RFEP data was carefully obtained, and chief limitations are small size of sample and selective nature of borrowers. The principal information sources are: for NRC, Working Paper No. 3 (Cost of Credit) and for RFEP, Institutional Survey September 1961 to March 1962.

A. Summary of Calculations

1. Cost of Funds

Cost of funds is the bank's cost of obtaining funds for lending. Cost of funds is calculated as a weighted average cost to the bank of its entire capital structure including deposits, refinances, borrowings, and equity. Cost of funds varies among different institutions because of their different abilities to mobilize deposits (ranging from free demand accounts to time deposits at 15%), use of refinance facilities and amount of equity.

NRC working papers estimate weighted average cost of funds for NCB's, BKB, "SEL" and "SRD" to range from 5.7% to 7.7% based on present deposit and refinance terms. This paper also calculates weighted cost of funds on an adjusted basis (cost of refinance facilities at 1.5% instead of 7%) and found a range of 3.0% to 10.5%. (See Working Paper, Supplementary Table)

RFEP cost of credit data is not comparable to NRC's. RFEP loans were sourced partly by banks' head offices (average 74%) and partly by savings (1%). Cost of funds ranged from 6.3% to 17.4%. (See Institutional Survey, Chapter V).

Our calculation for cost of funds was 7.9%, which was rounded to 8.0%. This calculation assumed that banks would mobilize 75% of funds from savings at an interest rate of 7% and obtain 25% of funds from the refinance facility at 10.5%. We expect the average savings rate to increase as banks attract more relatively longer term savings.

2. Cost of Administration

Cost of administration includes operating and management costs. Cost data vary among different banks. Also, agricultural loans generally are more expensive to administer because they are smaller and require more supervision than, for instance, large industrial loans.

NRC estimated administrative costs of agricultural loans at 6.5% to 7.3%, excluding BRDB's cost of 12.5% (see Working Paper, Part II, page 2). On a system-wide basis, which includes highly profitable items such as letters of credit, administrative costs are estimated at 4% to 5%, if the extreme high (12.5%) and extreme low (1%) are eliminated (see Working Paper, page 11).

RFEP estimates included branch salaries and allowances, travel and other operating expenses; they excluded overhead and other costs of head office operations. These figures ranged from 3.6% to 10.7%.

Our estimate is 8.0%, which appears to be adequate for most but not all institutions. It is close to the NRC average for agricultural lending if 1% is added for headquarters overhead. This rate is consistent with other countries' costs of agricultural credit, which range from 7% to 10%.

3. Reserve For Bad Debts

Reserve for bad debts is difficult to estimate because of current banking practices for handling of overdues and allowances for bad debts. Statistics vary in methodology and application, and standard accounting practices are not followed on a consistent basis. The NRC working papers indicate, for instance, that 37% of agricultural credit was overdue on June 30, 1982, and that after five years, recovery of short-term agricultural loans was 88% under SACP and 91% under NP.

NRC estimated an appropriate reserves for bad debts at 2% to 6%. (See Working Paper, Supplementary Table.) Another calculation estimated appropriate bad debt reserves at 2.4% to 10.8%, on the assumption that bad debt reserves were equivalent to short-term crop loans outstanding after five years.

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RFEF established reserves for bad debts progressively, 25% after 3 months; 50% after 6 months; and 100% after 12 months. On this basis, the range of reserves for bad debts was 2.33% to 12.33%. Project consultants recommended a reserve of 2.47% but did not explain the basis for this recommendation.

Our calculations followed a different approach. We estimated that at least 5% of portfolio will require charge off, if banks will take strong steps to improve loan recovery. On this basis, a bad debt reserve of 6.17% was calculated as adequate to compensate banks for losses of 5% in cost of funds and 1.17% for other expenses. This figure was rounded to 6.0%.

4. Profits

Profit is the fourth principal cost component. Profit provides a return on invested capital and establishes a basis for future growth. Profit data for rural lending is not available. Also, available data on bank profits is misleading because of present accounting practices.

NRC estimated that losses on agricultural loans range from 4.97% to 20.8% at present lending rates. (See Working Paper, Part II, page 2). In another section, the same paper provided a profit margin of 4.0% in one estimate of full cost rural lending. (See Working Paper, Part I, page 19).

RFEF data shows profit resulting from a wide range of rural lending rates. The experiment was not intended to estimate a reasonable rate of profit. Net income on loans ranged from a profit of 8.27% to a loss of 13.7% but these figures are not useful guides to establishing a reasonable rate of profit.

Our estimate of profit on rural lending is 2%. It is less than indicated in the NRC papers. This rate is lower than other, more profitable bank services such as letters of credit, etc. Therefore, it is expected to be less than banks' overall profit/total revenue figures, which are 2.57% to 7.57% for NCB's and ONS.

B. Future Adjustments

It is important that lending rates be reviewed and adjusted in the future. Reviews should be conducted at a minimum of six month intervals, with upward or downward adjustments as warranted. Each cost component should be examined separately before revising lending rates. Some items for consideration in these reviews are:

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1. Cost of Funds

Bank savings funds should be expanded so that they provide an adequate return to savers on a real basis, after adjustment for anticipated effects of inflation. Then, adjustment is made in expected weighted average cost of funds. As bankers mobilize additional savings and rely less on refinancing facilities, then their cost of funds can be expected to decrease.

2. Cost of Administration

With increased efficiency, bank operating costs will decrease. However, in the medium term as more bankers are hired, operating costs may increase.

3. Reserve For Bad Debts

Several points are important in regard to reserves for bad debts. First, it is a reserve, which is an allocation, not an actual charge off. Charge-off of individual loans requires case-by-case evaluation of collectibility. Second, full or partial charge-off of individual loans does not require abatement of efforts to collect such loans. Such efforts may well be intensified at this point depending upon individual circumstances.

4. As the banking system strengthens and more staff is hired, loan recovery will improve. As loan recovery improves, then the reserve for bad debts should be decreased.

4. Profits

Banks should earn profits on a reasonable basis. However, while cost of funds, cost of administration and reserve for bad debts decrease, the rate of profit may stay the same. As a result, lending rates would decrease and the banking system would remain economically viable.

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SIMILARITY OF COMPARATIVE COSTS OF LENDING

	NRC Working Papers ^(a)		NFER ^(b)		Proposed Estimate
	Low	High	Low	High	
Cost of Funds	9.5%	10.5%	6.3%	17.4%	3.0%
Cost of Administration	6.0	8.9	5.1	3.6	3.0
Reserve for Late Dates	2.0	4.0	2.3	12.3	6.0
Profits	4.0	4.0	2.0	2.0	2.0
Total:	<u>21.5%</u>	<u>27.4%</u>	<u>15.7%</u>	<u>35.3%</u>	<u>24.0%</u>

(a) NRC Working Paper No. 3, Supplementary Table II. The original table excludes profits which have been added at 4.0% as estimated in the paper.

(b) NRC Working Paper No. 3, Supplementary Table III-C which is based on NRC Institutional Survey. The original table excludes profits which have been added at 2.0%.

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SOCIAL SOUNDNESS ASSESSMENT

1. Introduction

The Rural Finance Project does not lend itself well to conventional social assessment approaches, because of its explicit orientation toward a major restructuring of a complex set of national financial institutions. Examination of beneficiary impact spread effects, and equity relies upon the findings of studies undertaken as part of the Rural Finance Experimental Project, and on other analyses of rural credit in South Asia (see references). The Rural Finance Project is designed to make maximum use of the findings of the RFEF, including those relating to positive beneficiary impact upon low-income rural people.

About 86 percent of the 90 million people of Bangladesh live in rural areas in the most densely settled rural country in the world. Population density is 1,712 per square mile in an area of 55,598 square miles, of which 3,200 square miles are occupied by major rivers and estuaries. Nearly half the population is under 15; estimated per capita income is \$130 per year. Only about one person in five can read his native language. The population of the country is growing at 2.5% a year, and (at present rates) will double within 28 years.

Most rural Bangladeshis depend on agriculture and agro-related industries for their livelihood. In addition, many upper and middle class urban dwellers retain title to agricultural land and receive income from agricultural production. Although agriculture accounts for 58 percent of Bangladesh's gross domestic product, yields per acre and per capita food production are among the lowest in Asia. Nearly two-thirds of all land is under cultivation. Rice constitutes 93% of foodgrain production. The major export cash crop is jute - amounting to almost half the world's supply.

Bangladesh is linguistically and ethnically homogeneous. Nearly all its population speaks Bangla as a mother tongue. English is used widely among the ruling and economic elites. Bangladesh is the second-largest Muslim country in the world, after Indonesia; eighty-five percent of its population is Muslim, with Hindus making up a majority of the remainder.

2. Social Organization

The family household and the homestead, consisting of a cluster of such households, form the basic units of rural life. The homestead (bari) composed of households centered on a group of men related through patrilineal ties, provides a symbolic as well as an economic foundation for an individual's existence. Homesteads, in turn, are linked into para (hamlets), usually based on a core of kindred and associated with

a defined area. Para are the settings for most of the important activities of village life. They are centers for economic exchange, political competition, socialization of children, and ritual interaction. Beyond its constituent para, the village tends to be functionally amorphous with little community-level cohesion.

Rural areas, though isolated in many ways, are linked horizontally to other similar communities through economic and kinship ties and vertically to administrative units such as the thana, district, and nation. Most vertical ties, however, are poorly defined and are mediated by local elites. The Land Occupancy Surveys (LOS) sponsored by AIB in 1977 and 1978 pointed out serious inequalities in land control and access to productive resources in rural Bangladesh. A number of other studies have noted that population pressure, land scarcity, social and economic inequality, and ineffective administration appear to be accelerating relative disparities of income and social class. (Januzzi and Peach 1977; BAED 1978; Thorp 1978). The EDG is now attempting to address the problems of equity in the rural sector through implementation of programs such as the Rural Finance Project, which seeks to increase access to credit. Greater availability of credit is expected to lead to increased productivity and employment opportunities in rural areas.

3. The Pattern of Credit and Debt

According to the RFEF Sociological Report (1982), the picture of rural indebtedness in Bangladesh is less gloomy than previously supposed. Half to three-quarters of all rural households have debts. Debt is related to the developmental cycles of both the family and the farm enterprise. With increasing pressure on the land, increasing costs of food and other items, and increasing expectations for consumption of valued goods, the need for credit is becoming stronger in rural areas.

The Sociological Report and other reports indicate also that there are some signs that institutional credit is assuming a larger role, replacing, to some extent, the traditional sources of credit. Credit is used increasingly for productive purposes. However, most borrowers in the RFEF areas felt that, aside from the RFFV, there was no accessible source of institutional credit for their needs. The Rural Finance Project will expand access to credit, using the experience of the RFEF for guidance.

The borrower-lender relationships found in the Bangladesh studies is similar to that described in Donald (1967: 61-62). The bank official is an educated "expert"; farmers are in a dependent, client position. The banker is unlikely to know much about the farmer's needs from a practical standpoint. The cultural gap between bureaucrat and villager is further widened by the culture of an official, inappropriate regulations governing loan procedures.

4. Beneficiary Impact

The RF Project working through the rural banking system, is aimed at transforming the structure of rural finance. The great majority of Bangladesh's population has little access to institutional credit. Those few who use banks are disproportionately in the upper income elite. The RF Project will attempt to increase the effective access of all income groups to institutional credit, while at the same time putting the banking system on a sound administrative and financial footing. The potential benefits of this process seem self-evident.

First, participation in modernizing agriculture requires funding for purchase of new seeds, fertilizer, pesticides, water, agricultural equipment, and, often, additional labor. As discussed in Section I (Project Rationale), farmers knowledgeable about the new technology and its benefits may be constrained by the lack of timely credit. Non-institutional lenders, who form the back-bone of the current de facto dominant system of rural credit, are poorly prepared to service the demands for financing related to development-related technology. The amounts typically lent by rural money lenders are small. They prefer making a larger number of small loans to many borrowers, rather than investing their resources in only a few persons. For the borrower, the terms of non-institutional loans are often exorbitant, and ill-suited for profit-oriented investment. Therefore, to the extent that the RF Project can enable banks to reach out effectively to rural areas, a vital source of alternative credit will be made available for farmers.

Second, a major constraint to villagers' use of institutional credit facilities has been the gap between the social spheres of the village and the government bureaucracy. This gap, common to all peasant societies (Welf 1966) results from the peasant's reluctance to involve himself in unfamiliar procedures which may adversely affect his financial and social status, and from the well-known attempts by poorly supervised, poorly paid rural officials to augment their income by brokering such procedures for a fee. It is unlikely that the RF Project will be able to work a miraculous transformation in the social relations between farmer and bank officer; nor will the traditional middleman's role disappear soon. However, the structural changes in the rural banking system will, over time, reduce dependence on non-institutional loan sources by providing a viable, accessible alternative. Loan procedures to make them more understandable to the ordinary borrower.

Beneficiaries from the RF Project will be drawn from a broad range of rural people, including not only small and middle-level farmers, but also rural laborers. The RF Project will also

Difficult to specify the exact uses to which loans were to be put. But it did find that most loans were used for productive purposes. It also showed that restricting loans to "target groups" proved difficult, but that the potential clientele for such loans was, in fact, drawn from non-elite groups.

Some "incentive" impacts from the RF Project may also be inferred from the discussion above. For example, the availability of institutional credit in a given area may undermine the role of local money-lenders or, more specifically, may affect the personalized patron-client relations of which money lending constitutes a significant aspect. Little is known in detail of such relationships, but they relate to rural power constellations. (BAPD 1972). Institutional credit, and increased capital directly available to villagers, will accelerate their involvement in the wider rural economy (Majid 1971) in ways requiring skills they may not adequately possess.

It is conceivable that in the short run increased access to capital may intensify the pressures on the market for land - although by a much broader spectrum of rural society. While the sums intended to be lent are too small to be used directly for land purchase, there is some likelihood that, lacking other outlets for investment, farmers participating in the benefits derived from TVV technology fueled with project loan capital will buy or force out their less successful neighbors, adding to the problem of increasing landlessness. Alternatively, bankers, spurred by new incentive systems built into this project, will encourage investment in savings accounts which are virtually riskless and pay real rates of return. Also the movement of interest rates to full economic levels will tend to shift land use away from land purchase.

Finally, the benefits from the RF Project to participating bank staff at all levels, and especially in rural areas, should not be overlooked. Training, incentives, and perhaps above all a better regulated and more explicitly development-related banking system should enhance bank employee morale significantly.

5. Spread Effects

In addition to those institutions which are intended to benefit directly from the rural finance project, many others may be affected indirectly. Due to the explicit concern of the RF Project with national-level policy changes in the banking system, the magnitude of the "spread effects" for this project is difficult even to assess, let alone quantify. The technical assistance, training materials, and transfer of managerial technology to the Bangladesh Bank and other

nationalized banks indicate changes not only in working procedures, but also in the norms and values associated with the sub-culture of banking. Bank employees will be trained to deal with potential borrowers on a new basis; the training should explicitly address social and cultural barriers which have in the past prevented or inhibited the less wealthy or less sophisticated from applying for, or receiving loans. Incentive plans will make loans to a wider range of borrowers more attractive to bank officers. Development of regulations and incentives relating to loan repayment may shift attention of loan activities from personalized to impersonal, yet accessible, and instead of seeing loans as actually a form of "discipline" exacted from the rich" to seeing them as a means to the value of the good credit rating earned by prompt loan repayment.

The goal of the RF Project is increased agricultural and industrial production in rural areas. This goal will be achieved indirectly, as adequate financial services in rural areas become established and as the infusion of capital enables individual farmers and entrepreneurs to develop profitable and self-sustaining enterprises. Spread effects, thus, are planned into the project. Although difficult to identify precisely at the outset, these effects should become viable in bank service areas within the time period of the project, and they should form an important focus for project impact evaluation.

6. Equity Aspects

The Rural Finance Project builds on the experience gained in its predecessor, the Rural Finance Experimental Project, to extend project benefits to those groups best prepared to take advantage of these benefits. Rather than specifying loan types or target groups, the Rural Finance Project is directed at reforming fundamental procedures for extending credit, mobilizing savings, and training bank staff. The intent is to effect fundamental banking reform, which will result in higher rates of loan extension and loan repayment. In order to achieve these goals, the banking system will have to broaden its involvement with individuals and groups which were formerly without access to institutional credit, including lower-income villagers and women.

The Rural Finance Project will result in major transformations of the rural banking system. However, changing banking procedures alone cannot be expected to produce social change (REF 1981). Additional skills such as the ability to maintain accounts, plan finances, and plan future activities are not usually possessed by low-income, landless people. Limited "event horizons" as well as suspicion of banks can work against participation of the relatively poorer farmer in the RF Project.

Participation in plans or scheduling of repayment, rather than simply acquiring the schedules drawn up by officials is essential for development-oriented involvement by low-income people in credit schemes. Unless these schedules can reflect realistic cash flow assessments, the likelihood of loss of funds, default, or the awkward choice between loan repayment at the expense of the enterprise's development vs. default, is increased.

Economic independence, and a wider range of economic alternatives/opportunities, lessen social dependence on local patrons. The Rural Finance Project will provide such opportunities to rural villagers. The findings of the RFA indicate that many are ready and eager to take advantage of such opportunities.

Women were incorporated into the RFEF as local participants and local beneficiaries. The banks participating in the Rural Finance Project may further develop these aspects of the predecessor project. Banks may post women loan officers to rural bank branches to solicit and approve loans to women. The financial sector is one where women may perform professionally. With the progress anticipated from the Rural Finance Project, it is likely that the scope for satisfying - and lucrative - professional careers for women in banking will expand.

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ANNEX H RURAL FINANCE PROJECT
Rural Finance Experimental Project

In 1977 AID financed a \$7 to 11.5 Rural Finance Experimental Project to carry out an experimental credit and savings program. The project goal was the contribution to establishment of an effective nationwide institutional credit system which would provide credit and savings facilities to small farmers and rural producers. The project purpose was to identify one or more replicable rural financial systems to meet financial needs of the productive and potentially productive rural poor.

Five indicators were selected to verify achievement of the project objectives:

- (1) Credit reached a substantial portion of the target group and was not diverted to larger rural producers.
- (2) Target group productivity and incomes were increased.
- (3) Loans have been substantially repaid with interest.
- (4) Lending institutions cover their operational costs through interest and finance charges.
- (5) Rural savings were mobilized.

The key project design elements were:

(1) Target group was limited to those with income of Tk. 5,000 or less and with land of 2.0 acres or less including the landless, thereby making institutional credit available to those who customarily rely on money-lenders charging rates of 100% or more.

(2) Interest rates on loans were set at 12%, 14%, 16%, 18% and 36% (when the Central Bank established rate was 11%).

(3) Interest rates on savings were set at 11%, 12%, 13%, 14% and 15% and were set above the increased bank rates (when the Central Bank rate was 7.75%).

(4) Eight lending models were tested to examine effectiveness of each. These models included variables such as group vs individual lending; village agent; small farmer services center; area development lending approach and banker as ombudsman.

(5) Loan approval procedures were simplified to induce applications from borrowers.

(6) Nine financial institutions participated including the six nationalized commercial banks, the agricultural development bank, and two cooperative associations.

(7) Incentives were provided to banks of one-third of loan amounts upon disbursement and one-third upon repayment, to induce banks to participate.

(8) Bank branch profitability records were initiated to determine profitability at different interest rates.

The project produced 81,595 loans (43,113 separate borrowers) valued at Taka 134 million and savings of Taka 10 million at 98 branches, as of the PACD on August 31, 1982.

Lending Results

The project for the most part achieved its purposes which are highlighted as follows:

- (1) Target Group - 90% of loans reached the target group.
- (2) Interest Rates - Rates of 12% to 30% appeared acceptable to borrowers, however, some resistance appeared at 36%. Within the 12% - 30% range, the increasing cost of credit had relatively little effect on incidence of borrowing. Further, nearly 50% of eligible borrowers took loans and the highest percentage (76%) took them in the 24% interest rate category. Also, more than one-third of borrowers took more than one loan. The sociological survey showed that 42% of all borrowers considered low interest rates the main advantage of the program.
- (3) Loan Purpose - Loans were expected to be predominantly for agricultural inputs, but borrowers used funds nearly equally for crops (24.5%), other agricultural purposes such as purchased cattle (39.2%), and non-agricultural purposes (36.3%).
- (4) Loan Overdue - Average was 19% and range was 5%-51% substantially less than indicated national averages.

Savings

Savings mobilization: at the PACD, total savings were equal to 16% of the loans outstanding which was insufficient for a self-financing system. Only 24% of the participating institutions financed as much as a quarter of their loans with locally mobilized funds.

Bankers appeared sensitive to the cost of funds and preferred to borrow funds from head-offices generally at rates of 10-13% rather than pay higher interest on local savings.

The Bangladesh Rural Bank (BRB) experiment was conducted on a pilot scale with an experimental area of 1000 square miles. It was a limited trial with a potential to be expanded to 10000 square miles. The percentage of loans outstanding increased from 13.1% at the first quarter of 1981 to 37.8% at the end of the fourth quarter of 1981.

Repayment Results

The single most important element of a rural credit project is to lend and recover funds on time. On a national scale, the amount of overdues is not known but is estimated at 30-40 percent. However, the overall performance under RFEF for all participating institutions averaged 19%.

Institutional Viability

Key factors affecting viability were loan volume adequacy and spread over cost of funds, administrative costs and bad debt reserves. Under RFEF a bad debt reserve was calculated based upon 25% for 3 months overdues, 50% for 6 months and 100% for 12 months. Four out of nine banks operated profitably and accounted for 66% of lending.

The evaluation characterized models in three categories: individual, group and cooperative. The individual lending model was rated best for the following reasons: four out of five banks using this model were profitable, loan volume and customer base tended to be highest and overdues tended to be low. The group lending model was rated lowest because of low branch profitability, low loan volume, a high rate of overdues and high borrower transaction costs. The cooperative lending model should have a low cost structure (partly from subsidized administrative costs) and uneven performance among branches.

Incentives

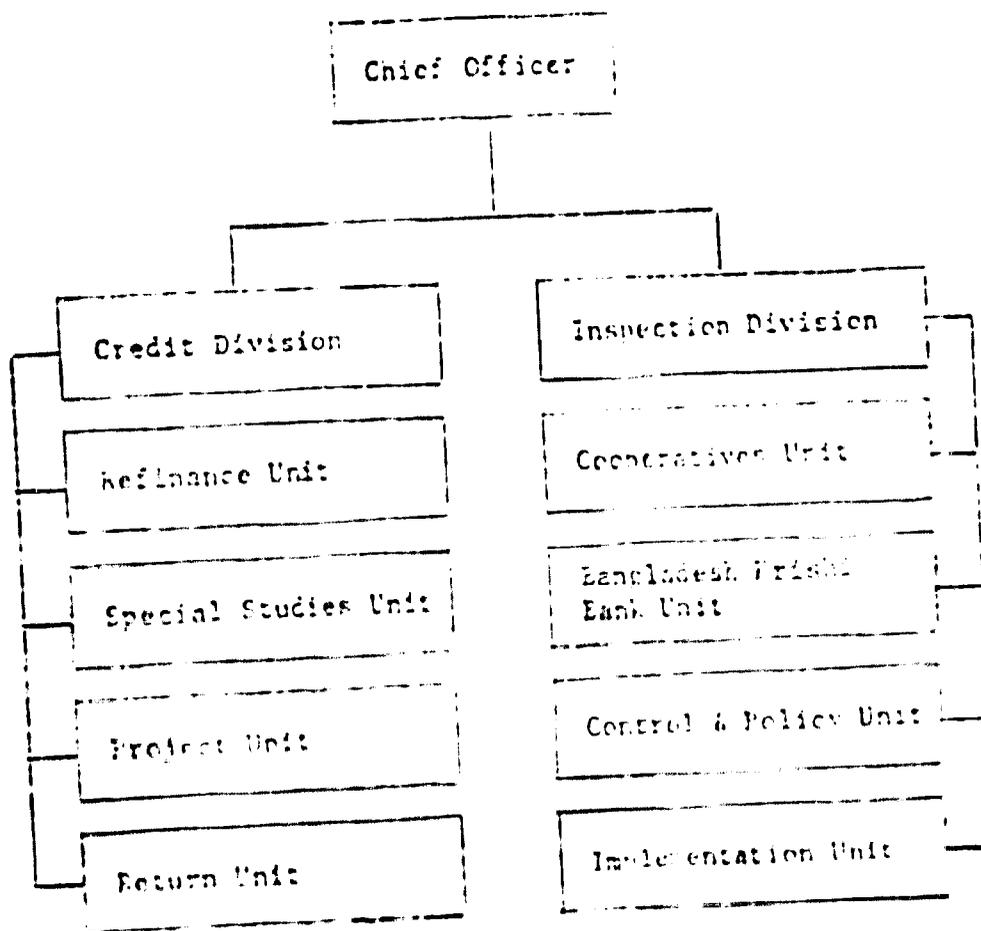
Incentives were limited chiefly to the participating institutions which were compensated on the basis of one-third payment for loans disturbed and one-third payment for prompt recovery. Four of the participating institutions introduced performance incentives: commissions to branch staff and relatives of interest to borrowers for timely repayment of loans. Attempts were made to introduce a system of incentives to bankers, however, the parties were unable to reach a consensus on a payment formula and the matter was abandoned.

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BANGLADESH: RURAL FINANCE PROJECT

ANNEX 1

Agricultural Credit Department - Organizational Chart



Agricultural Credit Department - Bangladesh

Chief Officer: Supervises Department; reports to the Governor

A. Credit Division

1. Refinance Unit

- o Prepares recommendations on refinance policy.
- o Fixes refinance limits for financial institutions.
- o Establishes limits for Special Agricultural Credit Program.
- o Approves refinance loans to financial institutions.

2. Special Studies Unit

- o Secretariat to Standing Rural Credit Advisory Committee.
- o Studies special rural credit project.

3. Project Unit

- o Manages selected credit projects.
- o Prepares new credit project.

4. Returns Unit

- o Reviews financial institutions' returns.

B. Inspection Division

1. Cooperatives Unit

- o Inspects Bangladesh Samabaya Bank Ltd. and Bangladesh Rural Development Bank.

2. Bangladesh Krishi Bank Unit

- o Inspects Bangladesh Krishi Bank.

3. Control & Policy Unit

- o Resolves inspection policy issues.
- o Coordinates inspection teams.

4. Implementation Unit

- o Summarizes inspection reports for senior bank management.
- o Checks compliance with inspection report recommendations.

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Rural Financial Institutions

The principal rural financial institutions are: an agricultural development bank (Bangladesh Krishi Bank), the two cooperative systems (Bangladesh Rural Development Board and Bangladesh Samabaya Bank Ltd.), the six nationalized commercial banks, and moneylenders. The relative importance of institutions in rural markets is indicated by the figures for disbursements for agricultural loans, as shown below.

Disbursements of Agricultural Loans
(Tk. 000,000)

<u>Institutions</u>	<u>5/30/77</u>		<u>6/30/81</u>	
	<u>Amount</u>	<u>Percentage</u>	<u>Amount</u>	<u>Percentage</u>
B. Krishi Bank	700	42*	2,007	53%
B. Samabaya Bank Ltd.	114	12%	276	7%
B. Rural Development Board	66	7%	255	6%
Nat. Commercialized Banks	362	39%	1,361	34%
Total:	931	100%	3,907	100%

Source: Bangladesh Bank

1. Bangladesh Krishi Bank

Bangladesh Krishi Bank, established in 1973 as the successor to the Agricultural Development Bank of Pakistan, is the nation's largest agricultural lender. It extends short, medium, and long-term credit to farmers, agribusiness, and cottage industries. Equity of Tk. 250 million is owned by the Government which nominates the seven-person Board of Directors, including two non-government members. Bank branches have been substantially expanded, particularly in rural areas, from 127 (64% of total branches) in 1978 to 470 (65% of total branches) in 1981. BKB's portfolio in 1981 comprised: short-term agricultural loans, 24%; medium and long-term loans (e.g., irrigation, livestock), 31%; tea gardens, 22%, and agribusiness, 23%. The present portfolio has shifted from heavy reliance on tea gardens and livestock (respectively, 51% and 35% of portfolio in 1978) to more agribusiness.

2. Bangladesh Rural Development Board

Bangladesh Rural Development Board, established in December 1982, is the successor to the Integrated Rural Development Program, which originated with the Comilla Experiment in 1977. BRDB operates the "two-tier" cooperative system which provides credit, agricultural inputs and education in use of inputs to cooperative farmers. The BRDB

is a government agency whose Board includes a minimum of 22 members from government agencies and member organizations. Membership in BRDB sponsored cooperatives has grown impressively: from 244,000 in 1973 to 1,513,000 in 1982. Similarly, the number of KSS (village primary society) has grown from 27,000 to 45,000 and the number of TCCA (Thana Central Cooperative Association) has expanded from 250 to 295 in the same period. (A KSS is the primary, local cooperative society and a TCCA is a thana level federation of KSS's.) The BRDB system required members to purchase shareholdings and to deposit savings to qualify for loans. BRDB supervises credit more carefully than other national financial institutions.

3. Bangladesh Samabaya Bank Ltd.

Bangladesh Samabaya Bank Ltd., established in 1972 and renamed in 1977, is the successor to the apex cooperative bank originally established in 1943 for the "three-tier" cooperative system. It extends loans to its shareholder cooperative organizations, which in turn lend to members. Loans are extended for a variety of short or long-term purposes ranging from agricultural inputs to land purchase, depending upon the purpose of the cooperative bank or society. Of the total equity of Tk. 23 million, 80% is owned by 331 cooperative banks and societies and 20% by the government. The 13-member Board is elected by shareholders. This apex bank operates through shareholder banks or societies; headquarters employees averaged approximately 115 from 1978 to 1981. The EDG has been considering for sometime reorganization of BSBL or merging it into BRDB but has not done so. BSBL's portfolio contained the highest percentage of overdues under RREP: 51%, while other institutions ranged from 5% to 24%.

4. Nationalized Commercial Banks

Nationalized commercial banks (NCB) were formed in 1972 after Liberation from the then-existing private commercial banks. Six banks were established: Sonali, Janata, Agrani, Pubali, Rupali and Uttara. These banks engaged in limited rural activities until 1976. Therefore, they became more active for two reasons. First, the Bangladesh Bank limited licensing of new rural branches to new urban branches in a ratio of 2:1 or more. Actual linkages ranged from 2.4:1 to 6.5:1 in 1977-1981. Second, the government required NCB's to participate in the Special Agricultural Credit Program, which was initiated in 1977 to finance short-term loans for agricultural inputs without collateral. This program is used for about 50% of total rural loans. In contrast to other institutions operating in rural financial markets, the NCB's have made some effort to mobilize deposits, relied less on refinance, and have maintained better recovery rates. The following table shows that Sonali has taken the strongest lead in providing agricultural credit followed by Janata. Other banks appear less interested.

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Disbursements of Agricultural Loans
(Tk. 000,000)

<u>Institutions</u>	<u>6/30/77</u>		<u>6/30/81</u>	
	<u>Amount</u>	<u>Percentage</u>	<u>Amount</u>	<u>Percentage</u>
Sonali Bank	154	43%	280	65%
Janata Bank	70	19%	128	17%
Agrani Bank	52	14%	91	6%
Pubali Bank	36	11%	60	6%
Rupali Bank	41	11%	64	4%
Uttara Bank	7	2%	27	2%
Total	362	100%	1,360	100%

Source: Bangladesh Bank

5. Informal Credit Sources

The informal market includes moneylenders, friends, relatives, and self-financing, which is estimated to account for the major portion of rural credit. However, little quantitative information exists on these operations. Lending is often a mixture of economic and social relationships: patron-client, landlord-tenant, wholesaler-retailer, etc. Social as much as economic benefits and costs are part of the relationship. Negotiations are personal and quick; amounts lent are typically small and interest rates are high. Lending and repayment may be in cash, kind or a mixture. Many informal loans finance consumption or alleviate temporary distress such as: rebuilding destroyed houses, replacing dead bullock, etc. Interest rates, when charged, are reportedly 10% per month or more.

BANGLADESH: RURAL FINANCE PROJECT

IMPLEMENTATION SCHEDULE

Respon- sible	Finan- ced By	Mod.	July 83- June 84		July 84- June 85		July 85 June 86		July 86- June 87	
			XXXXXX	XXXXXX	XXXXXX	XXXXXX	XXXXXX	XXXXXX		
I. <u>CASA TRANSFER</u>										
a. Review of Performance	AID	AID	-	X		X				
b. Disbursement	AID	AID	-	X	X		X			
II. <u>TECHNICAL ASSISTANCE</u>										
1. <u>Rural Financial Markets</u>										
1. <u>Interest Rationalization</u>										
a. Review/Change Rates	BF	BF	-	X	X	X	X	X	X	X
b. Advisory Committee	BF	BF	-	X						
c. Develop Methodology	Adv.	AID	PSC	XX	X	X	X	Y		
2. <u>Savings Mobilization</u>										
a. Preliminary Plan	BF	BB	-	XX						
b. Action Plan	Adv.	AID	Prime		X	XXX				
c. Implement Changes	BF					XXXXY				
3. <u>Loan Recovery</u>										
a. Accounting Changes	BF	BF	-	XXXX						
b. Revise Penalty Interest	BF	BF	-	XXXX						
c. New Incentive System	B	BF	-		XXXXX	X				
d. Strengthen Inspection	Adv.	AID	PASA		XX	X	XXX	XXX		XXX
e. Plan for Review	Adv.	AID	Prime				XXX			
f. Review & Action Plan	Adv.	AID	Prime				XXX	XXX		
g. Implement Changes	BF/Adv.	BF/AID	-					XXXXXXXX	XXXX	

ANNEX 2

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	Respon- sible	Finan- ces: BY	Mode	July 33- June 34	July 34- June 35	July 35- June 36	July 36- June 37
				XXXXXXXXXXXX	XXXXXXXXXXXX	XXXXXXXXXXXX	XXXXXXXXXXXX
A. System Strengthening							
1. Rural Branch Training	iv.	AID	Prime		XXX XX	XXX	
2. Branch Rationalization	iv.	AID	Prime		XXXXXX		
3. Lending Efficiency	iv.	AID	Prime			XXX X	
B. Implementation Agency							
1. Agricultural Credit Dept.							
1. Procure Equipment	iv.	AID	IFB	XXX			
2. Training	iv.	AID	Prime		XXX	XXX	XXX
2. Bangladesh Bank							
1. Accounting Advisor	iv.	AID	PASA	XXX	XXX	XXX	XXX
2. Project Training	iv.	AID	PASA		XXX	XXX	XXX
3. Foreign Exchange	iv.	AID	PASA		XXX	XXX	XXX
4. Note Issue Advisor	iv.	AID	PASA		XX		
C. Reviews & Evaluation							
1. Policy Change Monitor.	iv.	AID	Prime	XX	X X X	X X X X	X
2. Financial Sector Review	iv.	AID	Prime	XX		XXX	

ANNEX K-2

X = the month in each year

POST COUNTRY CONTACT - INTEREST RATE ADVISORDRAFT TERMS OF REFERENCEI. OBJECTIVE

The purpose of these services is to assist the Bangladesh Bank (Bank) in establishing a methodology to rationalize the structure of interest rates.

II. BACKGROUND

The Bank is considering several policy changes to create an economically viable rural financial system. One of the most important changes is an increase in lending and refinance rates for rural loans. After these rates undergo an initial change, the Bank will establish an Advisory Committee on Interest Rates to advise the Governor on setting rates for savings, lending, and refinance. The Committee will meet at least semi-annually, and more frequently when needed, to review the entire interest rate structure. Rates need to be adjusted upwards and downwards depending on trends in inflation, administrative costs and loan recovery. A technical unit will be created within the Bangladesh Bank to prepare the studies and recommendations required by the Committee.

III. SCOPE OF WORK

The Contractor will assist the technical unit of the Bank's Advisory Committee on Interest Rates in undertaking all steps necessary to establish a rationalized interest rate structure including but not limited to the following tasks.

A. Review of Data Base

The Contractor will review and assess the adequacy of the Bank's available statistical information for defining and developing a rationalized interest rate structure. The Contractor will recommend modifications as required.

B. Development of Methodology

The Contractor will develop a methodology to rationalize interest rate structure and to establish relationships among deposit, lending and refinance rates. This methodology will provide for upwards and downwards adjustments depending upon changes in inflation rates, costs of administration, and costs of bad debts.

C. Maintaining in Application of Methodology

The Contractor will train staff of the technical unit in application of the methodology. The training will include case studies and exercises where staff apply the methodology under a wide variety of simulated situations.

D. Methodology Manual

The Contractor will prepare a manual describing the methodology, data bases, and methods of calculation. The manual will be designed so that it can be revised from time to time to allow for improvements in methodology, data bases, and methods of calculation.

E. Impact Reporting System

The Contractor will develop a reporting system to measure the impact of changes in interest rates. This system will be capable of reporting on a continual or frequent basis. The Contractor will design the system including report format and data bases and will train technical staff to prepare reports.

F. Workshops

The Contractor, with staff of the Bank, will conduct workshops to explain to Bank officers outside of the technical unit, and others as appropriate, the methodology of interest rate rationalization. The workshops will be conducted after the methodology is established and operating.

G. Short-term Training

The Contractor will recommend short-term training for members of the technical unit and others as appropriate. Methods of training will include but not be limited to: observation training at other central banks and specialized training courses at financial or academic institutions.

H. Required Reports

The Contractor will submit a written report at the conclusion of each consultancy. The report will describe work accomplished, problems encountered, recommended tasks to be accomplished by the Bank before the next consultancy visit, and items to be undertaken during the succeeding consultancy visit. Each report will have attached to it any reports or documents prepared in performance of tasks.

These reports will be submitted in the English language to the Governor of the Bangladesh Bank with copies to the chief of the Advisory Committee Technical Unit, Agricultural Credit Department and UN ID. Reports will be submitted immediately prior to completion of each consultancy.

IV. WORK SCHEDULE

The Contractor will perform a total of six person months of services in a series of five visits. The first visit is estimated at two months, to start about September 1, 1983. The second visit is estimated at one month to start about February 1, 1984. The succeeding three visits, estimated at one month each, will start at approximately six-month intervals after the second visit.

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PIO/T	UNITED STATES INTERNATIONAL DEVELOPMENT COOPERATION AGENCY AGENCY FOR INTERNATIONAL DEVELOPMENT	BANGLADESH	Page 1 of 1
	PROJECT IMPLEMENTATION ORDER/TECHNICAL SERVICES	2. PIO/T No.	3. Original or Amendment No.
		4. Project Activity No. and Title Rural Finance Project (388-0037)	

DISTRIBUTION

5. Appropriation Symbol

6. Allotment Symbol and Charge

7. Obligation Status
 Administrative Reservation Implementing Document

8. Project Assistance Completion Date (Mo., Day, Yr.)
June 30, 1988

9. Authorized Agent
SER/CM (AID/W)

10. This PIO/T is in full conformance with PRO/AC
388-0037 Date

11a. Type of Action and Governing AID Handbook
 AID Contract (HB 14) PASA/RSSA (HB 12) AID Grant (HR 13) Other

11b. Contract/Grant/PASA/RSSA Reference Number (if this is a Amendment)

12. Estimated Financing (A detailed budget in support of column (2) is attached as attachment no. _____)

Maximum AID Financing	A. Dollars	(1) Previous Total	(2) Increase	(3) Decrease	(4) Total to Date
				-0-	500,000
	B. U.S. Owned Local Currency				

13. Mission Reference

14a. Instructions to Authorized Agent
SER/CM is requested to negotiate and execute a PASA with the Federal Reserve System. Statement of Work and schedule is provided in Attachment No. 1.

14b. Address of Voucher Paying Office
Controller's Office, USATD/Dhaka

15. Clearances—Include typed name, office symbol, telephone number and date for all clearances

A. The project officer certifies that the specifications in the statement of work are technically adequate	Phone No.	B. The statement of work lies within the purview of the initiating and approved agency programs	Date
RDE/C.W. Reece	Date	PRO/W. Boehm	
C. RDE/T.R. Tiffit MGT/M. Taylor	Date	D. Funds for the services requested are available	
		CON/W.A. Miller	
E. DD/W.R. Joslin	Date		

16. For the cooperating country. The terms and conditions set forth herein are hereby agreed to

17. For the Agency for International Development

Signature: James A. Norris Date: _____
Title: Director

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4. 10551 (10-79)	1. Cooperating Country BANGLADESH	2. P/O/T No.	Page 2 of Page
P/O/T	4. Project/Activity No. and Title 388-0037 Rural Finance Project		

SCOPE OF WORK

10. THE SCOPE OF TECHNICAL SERVICES REQUIRED FOR THIS PROJECT ARE DESCRIBED IN ATTACHMENT NUMBER 1 WHICH IS ENTITLED "STATEMENT OF WORK".

11. SPECIAL PROVISIONS

- A. LANGUAGE REQUIREMENTS (SPECIFY) E.g.
 UNMARKED TESTING MUST BE ACCOMPLISHED BY AID TO ASSURE DESIRED LEVEL OF PROFICIENCY
- B. ACCESS TO CLASSIFIED INFORMATION WILL WILL NOT BE REQUIRED BY TECHNICIANS.
- C. DUTY POSTS AND DURATION OF TECHNICIANS' SERVICES AT POSTS (MONTHS) Dhaka - 24 work months
- D. DEPENDENTS WILL WILL NOT BE PERMITTED TO ACCOMPANY TECHNICIAN
- E. WAIVER(S) HAVE BEEN APPROVED TO ALLOW THE PURCHASE OF THE FOLLOWING ITEM(S) (COPY OF APPROVED WAIVER IS ATTACHED)
- F. COOPERATING COUNTRY ACCEPTANCE OF THIS PROJECT (APPLICABLE TO AID/W PROJECTS ONLY)
 - HAS BEEN OBTAINED
 - HAS NOT BEEN OBTAINED
 - IS NOT APPLICABLE TO SERVICES REQUIRED BY P/O/T
- G. OTHER (SPECIFY)

20. BACKGROUND INFORMATION (ADDITIONAL INFORMATION USEFUL TO AUTHORIZED AGENT)

- a. Report of Charles M. Lucas, Federal Reserve Bank of New York, to Governor, Bangladesh Bank, dated November 24, 1982
- b. Project Paper: Rural Finance Project (No. 388-0037)

21. SUMMARY OF ATTACHMENTS ACCOMPANY THE P/O/T (INDICATE ATTACHMENT NUMBER IN BLANK)

- 2 DETAILED BUDGET IN SUPPORT OF INCREASED FUNDING (BLOCK 12)
- EVALUATION CRITERIA FOR COMPETITIVE PROCUREMENT (BLOCK 14)
- JUSTIFICATION FOR NON-COMPETITIVE PROCUREMENT (BLOCK 14)
- 1 STATEMENT OF WORK (BLOCK 18)
- WAIVER(S) (BLOCK 19) (SPECIFY NUMBER)

AIC 1350-1 (10-79)	1. Cooperating Country BANGLADESH	2. PID T Num	Page 3 of 4
	4. Project Activity No. and Title 388-0037: Rural Finance Project		

22. Relationship of Contractor or Participating Agency to Cooperating Country and to AID

A. Relationships and Responsibilities **The Contractor will work under the general supervision of the Governor, Bangladesh Bank.**

B. Cooperating Country Liaison Official **Mr. Nurul Islam, Governor, Bangladesh Bank
Mr. Kasaluddin Ahmed, Chief Officer, Agricultural Credit Department, Bangladesh Bank.**

C. AID Liaison Officials **Mr. Claude W. Reece, Project Officer
Ms. Mildred Taylor, Management Officer**

LOGISTIC SUPPORT

23 Provisions for Logistic Support	IN KIND SUPPLIED BY		FROM LOCAL CURRENCY SUPPLIED BY		TO BE PROVIDED OR ARRANGED BY SUPPLIER
	AID	COOPERATING COUNTRY	AID	COOPERATING COUNTRY	
A. Specific Items (Insert "X" in applicable column as right. If entry needs qualification, insert asterisk and explain below in C "Comments")					
(1) Office Space		X			
(2) Office Equipment		X			
(3) Housing and Utilities					
(4) Furniture					
(5) Household Equipment (Stoves, Refrig., etc.)					X
(6) Transportation in Cooperating Country					X
(7) Transportation To and From Country					X
(8) Interpreter Services/Secretarial					
(9) Medical Facilities	X				
(10) Vehicles (official)					X
(11) Travel Arrangements/Tickets					
(OTHER SPECIFY)					
(12)					
(13)					
(14)					
(15)					

B. Additional Facilities Available From Other Sources

- APO/FPD
- PX
- COMMISSARY
- OTHER (Specify, e.g., duty free entry, tax exemption)

Commissary privileges to be available to U.S. Federal Reserve System staff on same basis as USG employees.

STATEMENT OF WORK**A. OBJECTIVE**

The Contractor will provide advisory services to improve efficiency of Bangladesh Bank (Bank) operations. The first four tasks originate with the report of Mr. Charles M. Lucas, Federal Reserve Bank of New York, dated November 24, 1982 (Report). The fifth task is associated with one of the key phases (i.e., loan recovery) of AID Project No. 368-0037: Rural Finance Project.

B. SCOPE OF WORK**1. Review of Accounting and Related Systems**

The Contractor will perform an in-depth procedural review of the accounting and related areas (including branch operations). The objective of this task is to identify ways in which present systems can be simplified and simultaneously strengthened, to identify opportunities for and an orderly sequence for the introduction of automation, and to formulate a medium-term strategy for the automation of these operations.

One aspect of this task which is important to the Bank but was not emphasized in the Report is maximizing use of manual accounting systems instead of automated accounting systems. This task is described in the Report under Recommendation I.

After completion of this task, the Bangladesh Bank may wish to proceed with tasks described in the Report under Recommendation II, III, and IV.

2. Project Development, Planning, and Evaluation Training

The Contractor will provide assistance in identifying and obtaining training to support the highest priority projects of the Bank. A few selected Bank officials currently in line positions, with potential in project development, planning and evaluation, and with long-term senior management potential, will be nominated for these courses.

This task is described in the Report under Recommendation V.

3. Foreign Exchange Training**a. Course in Bangladesh**

The Contractor will conduct a course on foreign exchange markets for two to three weeks in Bangladesh. This course will be made available to officials of the Bangladesh Bank, the scheduled banks, and

Faculty of the Bank. The purpose is to increase the operational and the technical understanding in Bangladesh of such markets and to enable the more efficient execution of transactions and improve advice to the government and others in the efficient use of foreign exchange resources.

b. Courses in the U.S.

The Contractor will provide assistance in obtaining training in foreign exchange markets for one or two senior level officials. Training will be of four to six weeks duration, will include both practical and theoretical elements, and will be based on a seminar in foreign exchange given by a central or major commercial bank with additional institutional visits at both of the latter types of institutions.

This task is described in the Report under Recommendation IX.

4. Note Issue Advisory Services

The Contractor will provide services of a central bank currency processing expert who will thoroughly review current operations, identify specific ways to simplify complicated procedures without loss of security, and propose introduction of statistical sampling techniques.

This task is described in the Report under Recommendation XI.

5. Bank Inspection Advisory Services

Bangladesh Bank wants to strengthen the Agricultural Credit Department's Inspection Division which examines rural branches of financial institutions. This Division will monitor new standards of accounting for interest earnings, loan classification, overdue debt reserves, and writing off of bad debts.

a. Inspection System Review

The Contractor will review the present system of inspecting rural bank branches including but not limited to: method of selecting branches for inspection; organization, staffing and management of inspection teams; method of performing inspections; preparation and review of reports; recruiting and training of inspectors; and training of trainers. This review will recommend improvements suitable for Bangladesh, to be implemented on a phased basis, including but not limited to modifications in procedures and training in Bangladesh and overseas.

b. Inspection Manual Revision

The Contractor will review the present inspection manual (which was prepared before Independence with assistance from the Federal Reserve) and will recommend modifications, including changes

Attachment 1-3

required or reflect (a) the new accounting standards for interest earnings, loan classification, overdue debt provisions, and writing off of bad debts; and (b) recommendations of the Inspection System Review task force.

C. REQUIRED REPORTS**1. Monthly Progress Reports**

Each of Contractor's advisors will submit a brief monthly progress report describing work accomplished and problems encountered.

2. Final Report

Each of Contractor's advisors will submit a final report at the conclusion of each consultancy. The report will describe work accomplished, problems encountered, and recommendations regarding further work required.

All reports will be submitted in the English language to the Governor of the Bangladesh Bank with copies to the chief of the Bank unit concerned, the Agricultural Credit Department and USAID.

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BUDGET

Attachment No.2
PIO/T No. _____

Category	FY 84		FY 85		FY 86	
	\$	LC(\$ Eq.)	\$	LC(\$ Eq.)	\$	LC(\$ Eq.)
<u>1. Review Accounting and Related Systems</u>						
a. Adviser - Review (3 months)						
International travel	4,000					
Living and per diem		5,600				
Support costs	3,000	1,500				
b. Adviser - MIS (4 months)						
International travel			4,000			
Living and per diem				8,800		
Support costs			4,000	2,000		
c. Adviser - Automation Plan. (3 mos)						
International travel			4,000			
Living and per diem				6,600		
Support costs			3,000	1,500		
d. Automation T.A. and management						
Adviser - Training (3 months)					4,000	
International travel						5,500
Living and per diem					3,000	1,500
Support costs						
Training in U.S. (6x. months)					24,000	
International travel					24,000	
Per diem and miscell.					3,000	
Tuition						
<u>Project Development Training</u>						
Training in U.S. (3 persons x 3 mos)					16,000	
International travel	8,000		3,000		24,000	
Per diem	12,000		12,000		30,000	
Tuition	15,000		15,000			

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Category	FY 84		FY 85		FY 86	
	\$	LC(\$ eq.)	\$	LC(\$ eq.)	\$	LC(\$ eq.)
3. Foreign Exchange Training						
Advisor (3 months)						
International travel			4,000			
Lodging and per diem				6,600		
Support costs			3,000	1,500		
Training in U.S. (2x3 mos = 2 trips)					3,000	
International travel			8,000			
Per diem			12,000			12,000
Tuition			15,000			15,000
4. Note Issue						
Advisor (3 months)						
International travel			4,000			
Lodging and per diem				5,600		
Support costs			3,000	1,500		
5. Inspection						
Advisor - Review (3 months)						
International travel	4,000					
Lodging and per diem		6,600				
Support costs	3,000	1,500				
Advisor - Manual (2 months)						
International travel	4,000					
Lodging and per diem		4,400				
Support costs	2,000	1,000				
Training in U.S. (4 x 3 months)						
International travel			8,000		3,000	
Per diem			12,000		12,000	
Tuition			15,000		15,000	
Sub-Total	55,000	21,600	134,000	35,100	225,000	8,100
Total					\$ 478,800	
Rounded To					\$ 500,000	

বাংলাদেশ সরকার
ঢাকা, বাংলাদেশ

REQUEST FOR TECHNICAL PROPOSALS
FOR
ADVISORY CONSULTING SERVICES

ফুড ফিউচার প্রকল্প
(AID PROJECT NO. J8E-0017)

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BANGLADESH BANK-ADVISORY SERVICES

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ADVISORY SERVICES
FOR
BANGLADESH BANK

SCOPE OF WORK
AND
INSTRUCTIONS FOR PREPARATION AND SUBMISSION
OF TECHNICAL PROPOSALS

The People's Republic of Bangladesh, acting through the Bangladesh Bank (Bank) plans to contract with a qualified U.S. management consultant firm for advisory services in developing activities to improve rural financial markets including: savings mobilization measures, a comprehensive plan for improving loan recovery, training course development, branch rationalization plan, lending efficiency review, and a financial sector review.

I. GENERAL

A. Purpose

The purpose of these advisory services is to assist the Bank in undertaking several changes which will create an economically viable rural financial system to provide reliable savings and credit facilities for private farmers and entrepreneurs. The Scope of Work provides for performance of variety of advisory services which will support policy changes in the areas of savings mobilization and loan recovery, other tasks provide assistance to strengthen the rural financial system, and to conduct a financial sector review. These advisory services will complement activities being separately undertaken by an interest rate advisor and by the Federal Reserve System. AID is financing all three advisory services contracts under an agreement with the Government of Bangladesh. The Scope of Work is described in Section II below.

B. Rural Financial Markets in Bangladesh

Rural financial institutions in Bangladesh predate independence in 1971. The chief participants are Bangladesh Krishi Bank (an agricultural development bank); Bangladesh Rural Development Board and Bangladesh Samabaya Bank Ltd. (two cooperative systems), and the six nationalized commercial banks. In addition, money-lenders play an important but little known role. Rural financial institutions substantially increased their activities between 30, 1978, and June 30, 1981: loans tripled to Taka 4 billion, deposits doubled to Taka 5.5 billion; and rural bank branches increased by 50% to nearly 3,000.

The system, however, is dependent upon subsidies because interest rates do not cover costs of lending. Many banks have become reliant on central bank refinancing facilities instead of mobilizing savings, and high reserves drain capital which should be directed towards new loans. The Government is making changes in the areas of interest rates, savings mobilization and loan recovery. Background documentation on the rural financial sector in Bangladesh is limited. Copies are attached of the AID Project Paper on the Rural Finance Project (386-0037), the paper of the IDA-Bangladesh Government National Review Committee on Agricultural Credit, and the final evaluation of the AID Rural Finance Experimental Project.

C. Consultant's Performance.

The Consultant shall work directly with the Bank and in close consultation with USAID retaining, however, full responsibility for its own work. The consultant may associate itself with other firms or individuals in performance of the Scope of Work without, however, abrogating its primary responsibility for satisfactory completion of each task. In its proposal, the firm should state the extent to which it intends to associate itself with any such firms and individuals and, if applicable, the nature of association contemplated.

The Consultant will be expected to perform much of the work with its own staff. However, in certain areas, a high degree of international, specialized experience is required, and the Consultant is expected to associate itself with such suitably qualified expert institutions or individuals. Many task items will take a relatively short time and may be performed by short-term experts. However, the Consultant will assure adequate control and integration of work performed.

D. Approach to Work

The Consultant is expected to approach the work to be performed under Tasks A (Rural Savings Mobilization) and B (Loan Recovery Improvement) in sequence. The Consultant is expected to start work on Task A approximately one month after contract signing, or about April 1, 1984, and work on Task B is expected to start immediately after completion of Task A. Work on Task C (Policy Change Impact Monitoring) is expected to be performed concurrently with Tasks A and B, as relevant. In contrast to the sequential approach of Tasks A and B, work to be performed under Task D (System Strengthening Activities) is to be performed throughout the project life and is to be scheduled so that performance of this work does not interfere with Tasks A or B including requirements for Bank manpower and/or facilities. The final task to be completed will be Task E (Financial Sector Review) which is tentatively expected to start about December 1, 1985.

In addition to the Consultant's work to be performed, two other contracts for advisory services will be performed under this project. The first contract will be for services of an interest rate adviser who will advise the first phase of the project, as described above. The second contract will be with the Federal Reserve System which will provide experts to assist in strengthening the Bank's Inspection Division, which is associated with loan recovery. The Federal Reserve System is expected to complete most of its work before the Consultant begins work on Task b. In addition, the Federal Reserve System will perform advisory services and training for other departments of the Bank which will not be directly involved with the Consultant's work. Consequently, the Consultant will not depend upon nor conflict with work performed under these two contracts. The Consultant should plan its work to be independent of these two contracts.

II. SCOPE OF WORK

A. Rural Savings Mobilization

Rural savings mobilization is the first task to be performed by the Consultant. Work will be initiated soon after the contract is signed.

1. Savings Mobilization Action Plan

The Consultant will review the Bank's preliminary savings mobilization plan and will develop a comprehensive Savings Mobilization Action Plan. This Plan will describe a broad series of activities to be undertaken to improve savings mobilization in rural branches. Activities to be undertaken are expected to range from research studies to recommendations for immediate implementation. Activities will include but not be limited to the following tasks.

2. Market Research

The Consultant will undertake a marketing research study to develop improved strategies for mobilization of additional deposits and savings. This study will assess depositors' and savers' needs, wants, and attitudes towards bank deposit services. The study will recommend appropriate advertising and promotion schemes, changes in packaging and delivery of loan and savings services, and types of services offered.

Part of this study is expected to be subcontracted to a Bangladeshi firm; however, the Consultant will supervise the study particularly design, monitor risk of performance, and preparation of the report and recommendations.

The report will be distributed to the Bank and also to individual banks for use in developing savings mobilization programs.

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3. Study of Savings Restrictions

The Consultant will conduct a comprehensive review of deposit regulations and procedures to see whether they can be relaxed to encourage mobilization of rural savings. This review will cover all classes of accounts (Demand, call, savings, and time). Restrictions to be reviewed include but are not limited to such items as: minimum size of account, frequency of withdrawal, frequency of interest payments, method of interest payments, and variety of accounts offered. In addition, deposit procedures will be reviewed to see if they can be simplified, including documentation required for deposit/withdrawal, number of bank counters visited, processing time, and tax stamp requirements, etc. The review will include recommendations for change, if any.

4. Innovative Savings Campaign Fund

The Consultant will consider desirability of establishing a fund to partially reimburse banks for conducting innovative rural savings mobilization campaigns. If acceptable, the Consultant will design a simple mechanism for obtaining Bank approval and establishment of a fund which may be considered for initial financing from AID funds.

5. Bangladesh Bank Savings Promotion

The Consultant will review the Bank's present promotional activities for rural savings mobilization and will recommend appropriate modifications. These promotional activities are conducted on an "institutional" basis and should complement savings promotion campaigns of individual banks.

6. Monitoring System

The Consultant will design and assist in implementing a system for constant, or frequent, monitoring of increase in savings mobilization, as described in Task C below.

B. Loan Recovery Improvement

Loan recovery improvement is the second task to be performed by the Consultant.

It is expected that the Bank will have undertaken several activities to improve loan recovery prior to start of work by the Contractor, including: accounting changes, revision of penalty interest

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rates, initiation of a new incentive plan, and strengthening of Bank inspection departments.

Poor loan recovery is a complex problem which will require careful analysis and development of a comprehensive strategy for improvement. Many factors contribute to poor loan recovery and must be improved or effects must be mitigated, including: lending practices, bank branch staffing, borrowers' attitudes towards loan forgiveness, legal procedures and many other factors.

1. Plan for Comprehensive Review

The Consultant will prepare a plan for a comprehensive review of loan recovery problems and submit it to the Bank at least three months prior to initiation of work. This plan will describe areas of investigation to be undertaken, methods for conducting each investigation, and results expected from each investigation together with an assessment of potential impact on improving loan recovery. This Plan will describe data bases needed for each investigation and how such data will be obtained. The Plan will be accompanied by a work plan showing timing and staff, including staff to be furnished by the Consultant, sub-contracted, Bangladesh Bank, and others to perform this review. It is expected that the plan will require cooperation of the Bank and financial and other interested institutions.

2. Comprehensive Review and Action Plan

The Consultant will undertake the comprehensive review including but not limited to: changes in banking practices, revisions needed in applicable laws and regulations, survey of borrower attitudes, methods to speed court disposition of bank recovery cases, and borrower education programs.

Based upon the results of this review, the Consultant will prepare an action plan of recommended changes to improve loan recovery. The action plan will describe specific measures to be undertaken; methods of undertaking them together with recommendations for needed advisory assistance either domestic or expatriate; the estimated time to complete each change; and estimates of impacts on improving loan recovery. The action plan will also include an evaluation plan, as described in Task 2.1.

Certain measures to improve loan recovery may be identified before completion of this review. Such measures will be recommended for implementation prior to completion of the action plan.

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C. Policy Change Impact Monitoring

The Contractor will develop a system for monitoring of the impacts of policy changes (interest rate rationalization, savings mobilization, and loan recovery improvement). The purpose of this monitoring system is to provide senior officials of Bangladesh Bank with nearly continual information on the impacts of policy changes. Development of this system will require coordination with work to be performed by the Interest Rate Advisor, who is being separately contracted, and with work tasks A and B under this contract. The system will include but not be limited to two principal types of monitoring.

1. Statistical Reporting

The system will provide statistical reports which will measure various parameters of policy changes (e.g., increase/decrease in volume, value, customers). The Contractor will define the required data base, relying to the maximum extent on existing data bases; design reporting formats; and train Bangladesh Bank staff in preparation of reports.

2. User Surveys

The impact monitoring system will also include user surveys which will provide a more qualitative perspective of impacts than the quantitative measurements provided in the statistical reports. The Contractor will develop a system for periodic sampling of opinion about policy change impacts on bank customers and non-customers in rural areas. The Contractor will design and perform studies and will, to the extent feasible, assist the Bangladesh Bank and financial institutions in developing their own capabilities to conduct similar studies as part of their own marketing/monitoring activities.

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Procedural Matters, Activities

The Consultant will perform several tasks related to strengthening of rural financial institutions. These tasks are not associated with any specific / and are to be performed throughout the life of the project. Timing of each task is to be scheduled so that it does not interfere with performance of the priority areas (i.e., interest rate rationalization, savings mobilization improvement, and loan recovery improvement). The tasks to be performed include but are not limited to the following.

/policy change

1. Rural Branch Training

The Consultant will develop three standardized core curricula for individual banks to use in their own training programs for rural branch officers and supervisors. The three core curricula will cover courses in: rural credit for branch officers (about two weeks duration), a refresher course in rural credit for experienced branch officers and supervisors (about one week's duration), and a course in management and supervision for rural branch managers and other mid-level officers. The Consultant will review a sample of present courses for content, develop core curricula and test them for effectiveness. The Consultant will train financial institution training officers in using the new core curricula including modifications in teaching methods. Subsequent evaluations will be performed and may show the need to modify course content.

The Consultant will develop these courses in cooperation with a counterpart institution to be nominated by the Bank. The three core curricula may be developed sequentially.

2. Branch Rationalization Plan

The Consultant will assist the Bank in developing a branch rationalization plan to expand the availability of banking services in rural areas. This plan is presently expected to be developed in several stages. First, the Consultant will conduct a brief review of existing bank branch licensing policies and their effectiveness. This stage will include articulation of Bank goals and also problems as perceived by the Bank and financial institutions. Second, the Consultant will prepare an outline of alternative strategies for the Bank to review. This outline will describe alternative patterns of branch systems (including estimated capital costs and staffing and training requirements; it will also indicate chief advantages and disadvantages of each alternative under Bangladesh geographic, social, economic, and banking conditions. Third, after the Bank has selected a limited number of alternatives for further investigation, it will visit foreign countries which pursue such strategies to learn firsthand of benefits and problems. Fourth, after discussion with the

///

Bank, and the choice of priority alternatives will be prepared for Bank review, together with recommendations. The Bank will select its preferred alternative(s) for implementation.

5. Lending Efficiency Studies

The Consultant will perform studies of lending efficiency and will make recommendations for changes to improve efficiency and reduce costs of administration to bank branches and transaction costs to borrowers, without sacrificing integrity of the banks.

These studies will include but not be limited to the following areas:

a. Relaxation of Lending Restrictions

The Consultant will review lending programs to see whether restrictions can be relaxed on loans for non-farm purposes so that loans for all types of purpose are available in rural areas. The review will cover major lending programs and will describe restrictions on loan purposes, particularly those programs which reduce availability of credit to nonfarm rural enterprises.

b. Standard Loan Application System

The Consultant will review rural loan application procedures to determine whether they can be simplified or standardized to speed loan processing time and to reduce costs. This review will describe all steps in the loan application process including but not limited to: application forms, collateral requirements, usage or purpose requirements, establishment of repayment capacity, and other requirements and fees.

c. Loan Sanctioning Procedures

The Consultant will review loan sanctioning procedures with the objective of providing greater authority to rural branch managers. Loan sanctioning authority is reportedly still centralized in some financial institutions at regional or Dhaka headquarters. Decisions regarding delegation of authority to sanction loans are made by individual financial institutions and such authority is sometimes withheld for good reasons such as lack of experience. The Bank cannot directly influence bank decisions to delegate sanctioning authority; it is limited to exercising moral suasion. Consequently, the Consultant may have to conduct workshops or use other media to convince financial institutions to delegate appropriate authority.

4. Training Programs

a. Short-term Courses

The Consultant will identify short-term training courses in rural financial markets and related subjects in the U.S. and third countries which would be appropriate for senior staff of the Bank and financial institutions. These courses are generally expected not to exceed three months duration.

The Consultant will also assist in making arrangements for selected officers to attend these courses at financial or academic institutions.

b. Observation Training

In undertaking various tasks, the Consultant will develop short-term observational training programs for appropriate senior officers of the Bank and financial institutions. Some of these training programs may relate to rural savings mobilization, loan recovery improvement, branch rationalization plan tasks and strengthening of the Bank's Agricultural Credit Department. Others may be developed as appropriate.

F. Financial Sector Review

1. Data Base Review

As an initial step to be undertaken shortly after initiation of work under the contract, the Consultant will conduct a short review of the available data base to select information bases which will be used in the financial sector review.

2. Review

The Consultant will design and perform a financial sector review in cooperation with the Bank, financial institutions, and other interested entities. The purpose of this review will be to evaluate whether this project has accomplished its purpose. The review also assess whether additional policy changes and supporting activities are desirable and, if so, will identify specific areas and tasks. This review is expected to start after most activities have been completed under this project. The Consultant will prepare and submit to the Bank a detailed work program at least three months prior to initiation of work on this review. The work plan will include: a description of individual tasks, their sequencing and inter-relationships; a work schedule showing the number of people to be assigned, their functions, estimated person-months of effort, period of assignment and location of work to be performed; and other relevant information.

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F. Other Tasks

The Consultant may be asked to assist the bank in accomplishing other tasks under this project, such as level, in an incentive system for bankers to encourage savings mobilization and loan recovery, establishing a penalty interest formula, and evaluating further accounting changes. Such tasks, if required, will be defined in contract amendments from time to time.

G. Reports

1. Consultant's Monthly Reports

The Consultant shall submit a monthly progress report in letter form to the bank and USAID not later than the 10th of each month, listing field personnel, indicating progress towards completion, citing any constraints on progress, recommending corrective actions, and setting forth contract status relative to expenditures of person-months of effort and contract funding.

2. Submission of Reports

All reports and correspondence shall be in English. Copies of all reports shall be submitted as follows:

- a. Three copies to: Mr. Kamal Ullin Ahmed
Chief Officer
Agricultural Credit Department
Bangladesh Bank
P.O. Box 325
Dhaka, Bangladesh
- b. Two copies to: Mr. Claude Reece
USAID Mission/Bangladesh
G.P.O. Box 2503
Dhaka, Bangladesh

III. TECHNICAL PROPOSAL

A. Content of Technical Proposal

In general, the technical proposal should demonstrate by the quality of its contents a knowledge of the advisory services requirements and an understanding of the requisite tasks set forth in the Scope of Work. Its contents should include but not be limited to the following:

1. Advisory Services Overview

Information demonstrating an understanding of the advisory services requirements, including actions taken to become familiar with the bank's requirements, views on the adequacy of the Scope of

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Work and any suggested modifications or comments on these or other important aspects.

2. Work Program

Details of the proposed approach to the planning and performance of the advisory services, describing individual tasks, their sequencing and inter-relations. A time schedule, in bar chart form, indicating start and end dates (from notice to proceed) for such tasks, and CPM analysis indicating interdependence among tasks should be included.

In regard to the Scope of Work Task B (Loan Recovery Improvement) and Task E (Financial Sector Review), the proposal will include a preliminary work plan. The actual work plans will be submitted prior to initiation of work, as described in the Scope of Work.

3. Organization and Level of Effort

An organization chart showing relationships among all professional level personnel assigned to the advisory services tasks and division of duties. A work schedule indicating, for professional, technical and clerical positions, number of people to be assigned, their functions, estimated person-months of effort, period of assignment and location where work will be performed. Information concerning the workload of the Consultant and its ability to complete the described tasks should be provided. In regard to the Scope of Work Task B (Loan Recovery Improvement) and Task E (Financial Sector Review), a preliminary estimate of organization and level of effort will be submitted with the proposal. The final work schedule will be submitted prior to initiation of work, as described in the scope of work.

4. Staffing

Resumes of work experience and biographic data of every professional and key technical staff member and outside experts to be assigned including: nationality; education, professional qualifications and registration; chronological experience record indicating years, job title and description, employer and level of responsibility; overseas experience by years and country; and work performed relevant to the tasks described in the Scope of Work.

5. Qualifications

The Consultant may resubmit basic information concerning itself previously submitted as prequalifying information. Any additional information or elaboration which fully demonstrates the Consultant's particular capability to perform the tasks described in the Scope of Work, should be provided. Full information, including

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Standard Form 255 or WB Form 1420-6 should be provided for any firm proposed as a subcontractor or associate which was not proposed in the prequalification information. Full information must be provided concerning any Danish firm or associates proposed to participate in this contract.

B. Basis for Evaluation of Proposals

Proposals shall be evaluated on the basis of the following factors:

- Quality of the proposal as demonstrated by its scope, detailed planning and technical content.
- Understanding of the services to be performed as demonstrated by the proposal content and task coverage.
- Intention and ability to assign experienced, qualified personnel, both technical and managerial, preferably from its own organization or joint-venture. In certain areas requiring a high degree of specialized international experience, the Consultant will be expected to provide such expertise by association with outside individuals or firms.
- Intention and ability to perform the work in a realistically timely manner, utilizing appropriate staff levels.

Selection of a Consultant to perform professional services will not be made on the basis of price. Therefore, prices must not be included in the proposals.

C. Selection and Negotiation

The bank's evaluation of proposals and selection of the Consultant shall be final and not subject to further appeal. The Bank and USAID reserve the right to reject any or all proposals.

Upon completion of the evaluation, the proposals will be ranked in order of evaluated capability to perform the required services. Upon approval by USAID, negotiations will be started between the top-ranked proposer and the Bank to establish contract provisions and costs. In the event an agreement is not reached, negotiations will be terminated prior to initiation of negotiations with the second-ranked firm.

D. Submission of Proposals

1. Technical proposals should be received by the addressee named below not later than sixty (60) days from mailing date of this request. Proposals shall be forwarded in an envelope marked "Technical Proposal for Advisory Consulting Services."

2. Copies of the proposal should be addressed to each of the following:

- a. Three copies to: Mr. Kamal Uddin Ahmed
Chief Officer
Agricultural Credit Department
Bangladesh Bank (Head Office)
P.O. Box 325
Dhaka 2, Bangladesh
- b. One copy to: Mr. Claude Koczo
USAID Mission/Bangladesh
C.P.O. Box 2303
Dhaka, Bangladesh
- c. One copy to: Mr. Ray Hooper
ASIA/TR/ARD-Room 3327A New State
Agency for International Development
Department of State
Washington, D.C. 20523

IV. PROPOSED CONTRACT

The proposed contract shall be a cost-plus-fixed-fee type and shall conform to the standard type of agreement used by AID for engaging professional and technical services. Dollar and local currency costs of the contract will be financed by AID.

The nationality of the contractor shall be AID Geographic Code 000 (United States). The contractor may, however, subcontract with firms and/or individuals from countries listed in AID Geographic Code 941 (Selected Free World) and Bangladesh. Nationality and source rules are described in AID Handbook 11, Chapter 1 (Procurement of Professional and Technical Services.)

Execution of the contract is expected by approximately April 1, 1984. It is expected that contract services should begin within thirty (30) days of contract signing. Subcontracting of contract services will not be permitted without the prior, written approval of USAID.

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DIRECT CONTRACT - PROJECT REVIEW ADVISORDRAFT TERMS OF REFERENCEI. OBJECTIVE

The purpose of these services is to assist USAID and the Bangladesh Bank in performing various reviews of project activities to assess performance in meeting the project purpose.

II. BACKGROUND

The Bangladesh Bank is undertaking a project to create an economically viable rural financial system which mobilizes savings and provides credit facilities to private farmers and entrepreneurs. To assist the Bangladesh Bank, USAID is financing technical assistance to speed implementation of policy changes and related procedural changes. During project implementation and also near project completion, USAID and Bangladesh Bank will conduct several reviews of the project to assess whether it is meeting its purposes and, if not, how it can be restructured to accomplish these purposes.

III. SCOPE OF WORK

A. The Contractor will assist USAID and Bangladesh Bank in conducting reviews of project performance to assess whether the project is meeting its purpose, particularly with respect to major policy changes to rationalize interest rates, mobilize rural savings, and improve loan recovery.

B. The Contractor will submit a written report at the conclusion of each consultancy. The report will describe work accomplished and make recommendations as appropriate for each period of consultancy.

IV. WORK SCHEDULE

The Contractor will perform up to six person-months of services. The first two consultancies are estimated at one month each, to occur concurrently or close to, project reviews presently scheduled to begin on March 1, 1984, and March 1, 1985. Also, the Contractor will participate for up to two person months near the conclusion of the project's Financial Sector Review, presently scheduled for completion about March 1, 1986. The remaining two person-months of services will be undertaken as mutually agreed.

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LANGKATANG RURAL FINANCE PROJECT

INDICATIVE EQUIPMENT LIST

		<u>US\$</u>
(1) Sedans, 1200 cc	2	\$ 8,000
(2) Microbus, Diesel	1	7,500
(3) Calculators (with printer)	10	2,500
(4) Calculators (without printer)	10	1,500
(5) Typewriters	20	10,000
(6) Duplicating Machine	1	5,000
(7) Photo Copiers	2	5,000
(8) Mimeograph Machine	1	3,500
(9) Training Aids and Equipment		15,000
(10) Microcomputer including equipment, software and installation, air-conditioning and dehumidifiers	2	50,000
(a) Accessories and peripherals including quality dot matrix, framed character printers, monitors, external floppy disk and hard disk drives, and modems for telephone communications.		
(b) Advanced programic/communications software.		
(11) Maintenance & Spare Parts		10,000
(12) Books and Periodicals		17,000
Total:		\$ 135,000