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The Role of Islamic Financial Institutions in Resource Mobilization and Poverty Alleviation in Bangladesh: An Empirical Study of Rural Development Scheme (RDS) of Islami Bank Bangladesh Ltd (IBBL)

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Abstract

A major portion of rural people in Bangladesh live below the poverty line. Provision of credit to the needy and the hardcore is considered the sine qua non for the poor to involve in income and employment generating activities and thus break away from poverty. But the poor and the landless in Bangladesh do not have access to the formal credit market due to lack of tangible collateral for loan. The Grameen Model introduced in 1976 was the first mechanism to deliver credit to the poor without any collateral. Being inspired by the pioneering success of the Grameen Model in the field of micro finance, many micro finance organizations (MFOs) or micro finance institutions (MFIs) and non-government organizations (NGOs) have come forward to alleviate the sufferings of the poor and elevate their status in the rural society with their respective programs for providing micro finance.

However, one of the serious limitations of all these MFOs and NGOs from Islamic point of view is that they are interest-based, charge a very high rate of interest, and have very little or no focus on human development. Instead of bringing the hardcore poverty group out of the vicious cycle of poverty, the interest-based micro finance rather aggravates the situation further, perpetuating their indebtedness and poverty. It is also held that most of these MFOs are not able to operate at breakeven level without subsidies from outside sources and hence are not able to attain sustainability. As a way of escape from this interest-based system of micro financing and to carry on

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financial operations with no dependence on subsidies from outside sources, a handful of Islamic NGOs have recently come forward to provide interest-free loan based on profit and loss sharing (PLS) in line with Shari'ah principles. Of these Islamic programs, the micro financing program known as Rural Development Scheme (RDS) undertaken by Islami Bank Bangladesh Ltd.(IBBL) to mobilize resources in order to ameliorate poverty is the largest one.

It is held that the Islamic MFOs are better performers than the secular MFOs and NGOs in the field of resource mobilization and poverty alleviation as well as loan repayment. The Islamic programs are also held to be economically more viable and sustainable both in respect of borrowers and lending operations compared to secular NGOs and MFOs since they are not dependent upon subsidy from outside sources, emphasize on moral and ethical values as well as qualitative development of human beings, and operate on profit and loss sharing (PLS) abandoning interest in any of their lending operations and banking transactions.

There are very few studies undertaken so far to establish the superiority or otherwise of micro finance of Islamic banks and other Islamic MFOs over the traditional interest based ones. The present paper, based on an empirical study of the RDS of IBBL, attempts a comparison of the performance of the RDS with that of some well-known MFOs, and NGOs including Grameen Bank, so as to derive lessons for necessary rectification and modifications as well as determining the future course of action in micro financial activities of the Islamic financial institutions aimed at local resource mobilization and poverty alleviation both in Bangladesh and other similarly-placed countries of the world.

1. Introductions

As a way of escape from the interest-based system of micro financing and to carry on financial operations with no dependence on subsidies from outside sources, a handful of Islamic NGOs have come forward very recently to provide interest-free loan based on profit and loss sharing (PLS) to both men and women of hardcore poverty group with necessary modifications in the Grameen Model in line with Shari'ah principles. Of these Islamic programs, the micro-financing program known as Rural Development Scheme (RDS) undertaken by Islami Bank Bangladesh Ltd. (IBBL) to mobilize resources in order to ameliorate poverty is the largest one.

The IBBL was founded to establish equity and justice in the economy. With this end in view, the IBBL in 1995 launched a special program known as "Rural Development Scheme" (RDS) in order to mobilize local resources for alleviation of poverty through the generation of income and employment opportunities and to cater to the investment needs of poor micro entrepreneurs, particularly in the rural areas. The program started its operations in 1996. RDS is funded from IBBL's general investment fund with no subsidy from external or foreign sources. As of June 2004, RDS provided micro finance services in 3700 villages from 83 branches of IBBL. A total of Taka 3523.11 lacs were disbursed so far at 12 percent rate of return to 120087 clients (organized in 29941 groups and 6073 centers) with a recovery rate of 99 percent.

The RDS has chalked out a package program to ensure socio-economic development of the rural poor, marginal farmers and the landless laborers by making them self-reliant so that they are able to meet their basic needs and can contribute to the rural upliftment. The objectives of RDS are to eliminate rural poverty through community development approach. The target group of RDS is the rural poor, defined as landless or households having a per capita farm size of 0.5 acre of cultivable land or a gross annual income of not more than Taka 15000 (equivalent to US $ 250) per household. The investment programs, among others, include provision of loan for investment in crop production, fish cultivation, irrigation, agricultural and irrigational equipments, non-farm activities, rickshaw van and rural transport, hand-driven tube wells for drinking water, materials for housing etc. Other than providing finance for micro enterprises to generate income, RDS also focuses on health, sanitation and education of its beneficiaries. The dominant mode of financing used by RDS is Bai-Muajjal (deferred price-sale). The scheme (i.e., RDS) retains the group-based format of the Grameen Model, but rejects interest on any of its operations.

All operations of the RDS are on PLS (Profit and loss sharing) basis in line with Shariah principles. Small amounts (roughly from Taka 3000 to Taka 25000) are given to individuals and repaid back in small weekly installments. Like Grameen Bank (GB), no physical collateral is required for obtaining funds. Instead, social collateral is introduced by forming groups and centers like GB. The clients save Taka 5 per week as personal savings and have to give Taka 1 per week for the center fund. It should be mentioned here that 2 percent of the 12 percent rate of return charged goes to a risk fund that is used to repay installments of beneficiaries facing unusual problems and in case of emergencies.

Side by side with income generating and employment creating activities, RDS also aims to motivate people, to seek help from Allah (SWT) in all circumstances, to advise for good work and to refrain from evil deeds, to refrain from anti-social activities and to abide by the rule of law, to cultivate vegetables in the fallow land or the vacant compound of dwelling houses, to plant trees in the planting season, to remove illiteracy and to establish night school for adult education, to arrange education for children, to help one another in times of danger and misfortune, to take care of own health and health of the community people, to drink water from tube well, to abstain from giving and receiving dowry, to maintain law and order, to work hard, to practise five times prayer as well as shariah laws in every day life (Hakkullah and Hakkul Ebad), to keep promises to tell the truth and to keep the deposit (Amanah) of somebody under safe custody, and so on.

RDS deals with the family via the women. The Islamic approach of targeting the family and using Islamic modes of financing eliminates to a large extent asymmetric information problems that arise in conventional micro finance programs. This approach seeks to mitigate the adverse selection and moral hazard problems resulting from the fact that the intended use and user are different from the actual use and user of funds.

As Islamic modes of financing involve a real transaction, the moral hazard problem arising from the use of funds for purposes other than those intended is also expected to be eliminated.

1.1 Objectives of The Study

It is held that the Islamic Micro Finance Organizations (MFOs) are better performers than the secular MFOs and the NGOs in the field of resource mobilization and poverty alleviation as well as loan repayment. The Islamic programs are also held to be economically more viable and sustainable both in respect of borrowers and lending operations compared to secular MFOs and NGOs since they are not dependent upon external fund, emphasize on moral and ethical values as well as qualitative development of human beings, and operate on profit and loss sharing (PLS) basis abandoning interest in any of their lending operations and banking transactions.

Based on the above assertions with regard to the Islamic mocro finance some relevant questions are likey to be asked the answers to which need intensive study into the operation and performance of the Islamic MFOs. The questions are:

a) Are the Islamic MFOs institutionally more viable than the secular MFOs?
b) Are the Islamic MFOs financially more viable than secular MFOs because they are not dependent on external fund or subsidies from outside sources?
c) Are the borrowers from Islamic MFOs more viable than borrowers from secular MFOs in terms of group deposit, behavior of the group members, loan repayment, mobilization of savings etc.? If so, why?

d) What are the kinds of resources mobilized by Islamic MFOs and for what purposes and with what result? To what extent do they differ from those of secular MFOs?

e) What is the role of Islamic MFOs with regard to ideological promotion, human development and social welfare activities?

So far known, no intensive study has yet been undertaken to answer the above questions regarding the role of Islamic financial institutions in resource mobilization and poverty alleviation. The present paper is an attempt to find answers to the above questions based on an empirical study of the RDS of IBBL carried out by the author in June, 2004 and compares the findings of the study with the findings of a few other selected empirical studies undertaken so far with regard to the performance of selected well known MFOs and NGOs including Grameen Bank (GB) in Bangladesh.

1.2 Methodology and Scope of The Study

Eighteen villages in 18 districts covered by 18 branches of IBBL (i.e., one village under one branch) operating RDS have been taken for the study on the basis of purposive sampling. The recipients of investment assistance (i.e., the borrower) have been chosen as the unit of study and fifty respondents from each of 18 selected village have been taken as sample size for the study on the basis of random sampling. The primary data have been collected on the basis of a set questionnaire through formal interview of the respondents. Secondary data have been collected from published sources like books, journals, research reports etc. and also from relevant documents/records of IBBL dealing with RDS.

Primary data collected cover a wide range of information relating to different aspects of the investment program under RDS, viz., information on the nature of the activities financed, amount of loan disbursed and recovered, socio-economic costs and benefits of loans received, the nature of generation of income and employment, productivity, literacy, raising of Islamic consciousness in terms of 'Hakkul Ebad' activities, and human development.

The study covers a period of eight years from 1996 to 2004. Both qualitative and quantitative techniques of analysis have been used for the study. Arithmetic mean, ratios, percentages and other relevant statistical techniques have been used.

The paper is organized as follows. Section –1 gives an introduction, including the objectives, methodology and scope of the study. Subsequent sections, beginning with Section 2, discuss the major empirical findings of the study. Section –2 discusses the findings with special emphasis upon sustainability and viability of the RDS both at the institutional and program levels. Section–3 explains branch level viability relating to financial cost-benefit of RDS while Section–4 discusses branch level viability with special reference to outreach and sustainability. Section –5 explains borrower's viability with special emphasis upon mobilization of saving, poverty alleviation and income generation as well as ideological promotion of the borrowers. Section–6 highlights the complementary poverty reduction program of the RDS, while Section–7 makes a comparison between Islamic MFIs and Secular MFIs based on the basis of findings of the present study. Section–8 presents the conclusions and prescribes some policies for further development of RDS and its replication elsewhere.

2. Major Findings of The Study

Sustainability of the RDS

The sustainability of the program is defined as the ability of the program to continuously carry out activities and services in the pursuit of its objectives (Khandker, Khalily and Khan, 1996). The sustainability of the program has been examined in terms of (a) institutional viability, (b) financial and economic viability, and (c) borrower's viability. Each of these is discussed at some length in the following, based on empirical findings.

a) Institutional viability

The institutional viability has been examined in terms of leadership, decentralization, monitoring, evaluation, management style, staff training, incentives and performance, administrative structure and organizational growth or credit delivery, targeting credit, social development program (Hakkul Ebad), coverage and expansion of activities.

(i) Leadership, Decentralization, Monitoring and Evaluation

The leadership in the case of RDS of IBBL is rather institutional rather than personal. Unlike Grameen Bank (GB) or BRAC there is no influence of personal leadership on the operation and performance of the RDS. The leadership is delegated to the bank branches of IBBL in the areas covered by the RDS. The manager and project officer of the relevant bank branches together with the field staff (FS) are empowered to plan, organize and implement the RDS investment program in the areas with little or no supervision from the head office of IBBL. The devolution of many decision making roles to the branch offices and the flexibility in branch operation allow the head office to focus on broader issues of policy and development. Unlike GB there is no participation of the loanees (the recipient of investment assistance) in the management process of the RDS. The decision making function of the branch offices with respect to the implementation of the investment project relies on field level information which are collected by the FS and analysed and disseminated by branch manager together with project officer. The branch manager and project officer in collaboration with the FS in relevant areas does thus the monitoring and evaluation of the RDS. Monitoring and evaluation are crucial to the RDS's operations and expansion, providing continuous feedback from different operational and financial reports. The head office of IBBL monitors loan disbursement made by the branch offices, repayment, saving and default records as well as the flow of funds from information reported by the branch offices and based on the daily statement prepared by branch managers. These reports enable the head office to keep track of each branch's performance and compare it with the aggregate data prepared by the head office of IBBL. This comprehensive reporting forms the basis of the built-in-learning process characterising the decision-making and policies of IBBL relating to the RDS and helps to identify problems in branch or area performance that can be addressed by the head office.

(ii) **Management Style, Staff Training, Incentives and Performance:**

Besides decentralized administration, professional management is an important component of institutional viability. The management style of the RDS has evolved from its effort to provide a whole range of programs to the rural poor. It is observed that the management structure has a built-in-adaptability that has been refined through field level experiences. It should be mentioned here that a combination of learning, innovation and flexibility is the hallmark of style evident at all levels. (Fuglesung and Chandler,1998).The management system is based on an innovative approach to training characterized by a structured learning process which is continuously modified by trial and error. The branch manager, project officer and the **FS** are well oriented to plan, organize and implement the RDS programs without extensive supervision from the head office.

The **FS** of the RDS faces the challenging task of mobilizing the rural poor and helping to make them creditworthy and productive. They are located in remote rural areas where the amenities of modern life are seldom available. The same is applicable to the project officer and other staff including the branch manager of the branches located in the project area. Although employees may be influenced by factors like pay structure, they also require different types of real incentives in order to be more productive. With this end in view, sometimes the **FS** are rewarded for better performance. Needless to say, the decision to choose an area to be covered by the RDS is based on concern for the poor and the nature of risk involved due to agro-climatic and locational characteristics. It should be mentioned here that it is really difficult to start a financially viable project in an area which is largely flood-prone and where seasonality is more pronounced and infrastructure, including the road, is very poor. But the RDS has been started in such risky areas to alleviate poverty in the true sense of the term. This is quite in contrast to the investment projects of the commercial banks and other development finance institutions.

b) **Financial And Economic Viability:** The viability of the RDS depends on its revenue and cost structure. The concepts of financial and economic viability are used to examine the implications of operating efficiency on viability. The RDS is financially viable if revenue is equal to cost. The RDS is economically viable if profits are greater than economic subsidy, if any. In this study, financial or economic viability refers to the program level viability which is evaluated using two parameters: (1) profitability and (2) employee and capital productivity.

Loan recovery enhances profitabilities by turning over loanable funds and minimizing default, thus improving the viability of the RDS. Cost minimization, in addition to other parameters, depends on the composition and sources of funds. Given the availability of fund from own sources, the RDS does not have to depend on interest-based credit from outside sources. An evaluation of the cost structure and the operational performance also requires the analysis of both capital and employment efficiency which may be regarded as the crude proxies for the operational efficiency of the RDS. The financial margin (defined as service charge as a percentage of investment assistance) gives an overall measure of the cost of funds and revenue in relation to total assets or investment assistance. The subsidy dependence is not calculated in this study since all the funds for investment assistance under RDS come from the internal source of IBBL (i.e., deposit, paid-up capital and investment).

Based on the above brief introduction to the concepts relating to program level viability, we will now analyze program level viability of the RDS in terms of loan recovery profile, assets and financial structure, revenue and cost structure, financial margin and program level viability in the following section:

i) **Loan Recovery Profile:** The loan recovery performance of the RDS is an important supply side issue. Defined as the amount of loan recovered as a percentage of the loan due, the recovery rate of the RDS has been 99 percent every year since 1995. The minimum time allowed for repayment is 12 months while maximum time allowed for repayment is 36 months depending upon the nature of the investment project.

ii) **Assets and Financial Structure:** The average asset holdings of the bank branches under study increased from Taka 45 lacs in 1995 to Taka 80.5 lacs in the year 2004. The average earning asset in terms of loan, deposit investment etc. increased from Taka 43.17 lacs to 76.70 lacs in the year 2004. The average fixed asset of the bank branches under study increased from Taka 7.94 lacs in 1995 to Taka 20.17 lacs in the year 2004. The higher amount of capital increases the capacity of the bank branches under the RDS to absorb any losses and to operate with more stability.

iii) **Revenue and cost Structure:** The revenue or income side of RDS includes income from investment at 6 percent rate of return, income from supervision fund at 4 percent and amount of risk fund at 2 percent while the cost of RDS includes salary of field supervisors, other operational costs (i.e., depreciation of motor cycles, fuel cost etc.), salary of project officer and cost of funds (opportunity). When all items of income and expenditure are taken into account to calculate profit of RDS, it appears that RDS operates at a loss. However, the result does not reflect the true picture of the situation because of the following reasons:

a) The rate of return charged by RDS (i.e., 12 percent) is lower than most MFIs that have rates of return / interest rate in the range of 16-

55 percent (Morduch, 1999). By charging a lower rate of return than the market rate, RDS is essentially subsidizing the micro entrepreneurs. As a result, the income from investment is relatively lower than that of MFIs (Ahmed, 2002).

b) A major part of the expenditure is the salary of the project officer. The project officer, however, devotes only a part of the time for RDS activities, as he is an officer of the bank overlooking the activities of RDS. Payment of full salaries to the project officer is an overestimation of the expenditure for RDS (Ahmed, 2002).

c) The opportunity cost of using the funds for micro financing is close to ziro since the Islamic bank (IBBL) has a large amount of liquid assets due to the lack of Islamic money market instruments and since the amount needed for micro finance is miniscule compared to total assets of IBBL (Ahmed, 2002.).

When all the above qualifications are taken into account, then RDS is found to operate at positive levels of profit (i.e., at a profit of Taka 2389 million to Taka 3066 million) (Ahmed, 2002).

There is another point to consider on the income side of the RDS. The income figure calculated by us is based on a rate of return of 12 percent. To cover all the expenditures, however, the breakeven rate of return is estimated at 13.2 percent. The rate of return charged by RDS is much lower than that charged by other MFIs. If the income is calculated at the lowest rate of return of 16 percent charged by other Islamic MFIs, then the profit with this rate of return will be significantly positive (Ahmed, 2002).

iv) **Financial Margin and Program Profitability:** the profitability of the RDS is of critical importance to the operators or the policy makers of the project. It is found that the RDS is able to cover all its costs as a percentage of assets within its financial margin. The financial aim of the RDS is to gradually reduce its overhead cost to accommodate more members and more lending per member.

v) **Employee and capital productivity:** The efficiency of RDS may be analyzed in terms of employee and capital productivity. The productivity of capital and employee can be measured in terms of membership, borrowers, loan disbursement, loan outstanding, savings and deposit mobilization. The average number of increase in male members per bank branches increased from 50 in 1995 to 302 in 2004 while the average number of female members per bank branches increased from 150 in 1995 to 850 in 2004.

A similar pattern also holds for borrowers per bank branches. The borrowers per bank branches increased from 130 in 1995 to 550 in 2004. The total amount of loan distributed by the bank branches under study increased from Taka 43.17 lacs in 1995 to 1.50 crore in the year 2004. So, both the membership and lending criterion show a rising trend in case of RDS.

(vi) **Analysis of Branch level Viability:** As is evident from the field level study, all the branches of IBBL dealing with the RDS have a similar number of staff, members, and amount of assets, loan disbursement and saving mobilized. It is found that loan recovery rate is higher and member dropout rate is very negligible for all the bank branches dealing with the RDS under study.

The financial viability of a financial institution at branch level may be measured under two criteria: (a) Criteria relating to financial cost-benefit of a project; and (b) Criteria relating to assessment of self-sustainability and outreach to target clients. We shall discuss both types of the criteria in some detail in Sections 3 and 4 that follow.

3. Branch Level Viability of RDS based on criteria relating to Financial Cost-Benefit of a Project

i) **Earning Asset to Total Asset:** The earning asset to total asset investment ratios shows how well bank management puts bank assets to work. The estimated result shows that over the years under consideration (i.e., from 1995 to 2004) the ratios have been highly consistent (i.e., 0.96 on average) which implies that the branch banks dealing with RDS are quite successful to put their assets to work of investment.

ii) **Return on Earning Asset:** This is a profitability criterion. The ‘return’ here means income from investment assistance. The return on earning asset (ROEA) has been consistent over the years since 1995, which indicates that earning assets of the bank have been put more effectively.

iii) **Profit Margin to Average Earning Asset:** Profit, which is one of the key determinants of bank profitability, has been found positive for the RDS and consistent over the years under study. Therefore, we can conclude that the branches dealing with RDS have been able to maintain lower spread between profit and the cost of operation of RDS.

iv) **Equity Capital to Total Asset:** This ratio is a measure of the extent of equity ownership in the bank. This ownership provides the cushion against the risk of using debt and leverage. For branches working for RDS, the ratio was 0.10 on average, which is satisfactory.

v) **Deposit-Equity Capital:** It refers to the average deposit to average equity ratio. More capital requires a greater degree of safety while more deposits give a higher return to stockholders since more money is available for investment purposes. This ratio (1.50 on average) has not been very high over the years under study. This indicates higher margin of safety of the deposits.

vi) **Investment Assistance (Loan) to Deposit:** This is a type of asset to liability ratio. Investment assistance (loan) makes up a large portion of the bank assets and its principal obligations are the deposits that can be withdrawn on request within limit. This is a type of debt coverage ratio and it measures the position of the bank with regard to taking risks. The impact of the loans to deposit ratio (6.50 on average) is found satisfactory. The average loans have been always higher than the average deposit, which also measures the ability of the bank in taking risks.

vii) **Loan Loss Coverage Ratios:** This ratio helps determine the asset quality and level of protection of investment assistance plus 10% provision for risk of losses, if any, by net charge off (i.e., difference between bad debt and recoveries). In the case of RDS, not a single case of bad debt has been found.

From the above analysis we can say that all the financial ratios relating to the branch level viability of the RDS are consistent and hence it may be said that the bank branches under the RDS manage their finance well.

The assessment criteria to assess branch level viability of RDS focus on income expansion and poverty reduction. They are also helpful in explaining the cost-effective alternatives such as increased investment in rural infrastructure or in human development to reach the goals. Because of socio-political reasons the Government intervenes extensively in financial markets, especially in rural financial markets of less developed countries both directly and indirectly. The indirect interventions are made to improve the policy environment by addressing incentive problems and regulating intermediaries etc, while direct interventions refer to the steps to increase or supplant credit provided by private lenders. These interventions generally have had a limited outreach and resulted in huge costs, with insignificant impact on the borrowers at household level. As a result, it has become increasingly important to measure self-sustainability or viability based on subsidy dependence index. Fortunately, this is not the case with the RDS. So, an attempt is made here to measure the outreach and sustainability of the bank branches under the RDS with the help of assessment criteria comprising of several indicators other than the subsidy dependence index.

4. Outreach and Sustainability of Bank Branches under RDS

Outreach is measured by a hybrid index comprising several indicators. The main indicators of outreach are (1) market penetration, (2) relative income level, and (3) quality of services offered.

Market penetration is measured by (a) the number and annual growth rate of saving and loan accounts, (b) the value and annual growth rate of loan portfolio and deposits, and (c) the number of branches and staff.

Relative income level is measured by (a) the value of average loan and range of loan securities, (b) percentage of rural clients, and (c) percentage of male and female clients.

The quality of service is measured by (a) transaction costs, (b) flexibility and suitability of services, and (d) distribution network.

The **IMF**'s Executive Board has broadly agreed that the following objectives should provide guideline for strengthening the financial system:

a) to ensure transparency and the role of market forces;
b) to eliminate distortions created by official safety nets;
c) to control risk through regulatory and supervisory measure;
d) to strengthen the broader structural framework;
e) to poster national and international supervisory co-ordination;

A bank or financial system will be unsound if it is characterized by the following factors:

1) If a weak governance of banks leaves the system vulnerable to microeconomic shocks.

2) If financial deregulation, competition and innovation outstrip the capacity of bank to manage risk prudently.
3) If financial deregulation takes place before adequate prudential regulation and supervision are in place.
4) If weak and incompetent financial institutions are allowed to continue operations, thus weakening the entire system.
5) If capital account liberalization occurs before the soundness of the domestic financial system by macroeconomic policy is ensured.
6) If declining business profits together with excessive corporate indebtedness lead to a decline in asset quality.

Although the above mentioned criteria are applicable for purely commercial banks operating in any country, the unsoundness and insolvency of banking systems have some kind of universality for all types of financial institutions. Moreover, some elements such as managing risks, creating official safety nets etc. are more important for those financial institutions, which are vulnerable in managing risks. Since the RDS is not dependent on external finance and since the recovery rate is too high, the question of risk and insecurity of realization of investment assistance is minimum in the case of the RDS, which is based on a sound footing. This fact may be further established if we examine the indicators of outreach index mentioned above in case of the RDS as described below:

(a) Market Penetration

(1) Number and Annual Growth Rate of Saving and Loan Accounts: In case of the RDS of IBBL, investment assistance is given to each member via the group he/she belongs to. Those people receive the investment assistance who maintain saving account with the relevant bank branches of IBBL. Since the bank branch also conducts normal banking services such as receiving deposits at the stipulated rate of profit, the total number of member's accounts and loan (investment assistance) accounts differ. The loanees (recipients of investment assistance) maintain different types of account, namely, individual voluntary provision of saving for an amount of Tk.5, a forced group or center fund, a risk fund, and a personal saving account fund. From the data we have found that the growth of membership has been increasing gradually over the nine year period under study. In the same way the overall growth of saving in individual and group account has also been increasing year by year. This has been possible because like GB the field supervisors of the RDS travel long distance daily to serve their clients from door to door.

(2) Value and Annual Growth Rate of Portfolio: The main type of investment assistance given by the RDS is Bai Muazzal. Side by side with investment assistance from the own fund of IBBL, the RDS has also been assisting the recipients of investment assistance by providing finance from group fund to different categories of social sectors of activities such as social and household need, health and medical expenses, loan repayment, maintenance and repairing, processing, new supplementary investment, trading, farming, joint activities, promotion of Hakkul Ebad_activities etc.

The RDS has contributed a lot to the social development and the promotion of 'Hakkul Ebad'. Due to the RDS assistance, 85.45% of the respondents found an increase in their employment, 19.07% found an increase in their crop production, 74.09% found an increase in the educational level of their children, 94.07% found an increase in their income, 97.36% became self-reliant, 99.34% found an increase in their self-confidence, 99.01% experienced an increase in their Islamic knowledge, 96.38% has become accustomed in honest (halal) earning, and 96.68% became inspired in social welfare (Hakkul Ebad) activities.

From the above discussion, we may conclude the following about the performance of the RDS operated by IBBL:

1) It has been able to maintain a broad based loan (investment) portfolio like GB so that any unavoidable and unforeseen circumstances of any sector can be covered by other sectors.

2) It has been funding almost every sector of rural household economy in such a way that all members of the target group can participate in its activities.

3) It has not only been considering activities that are purely economic, but also some social activities without which no real development would be possible.

(4) The poor people are getting proper direction for the development of the social system.

(5) By and large, the RDS has developed a broad-based investment portfolio with a view to diversifying risks in volatile socio-political situations.

(3) Number of Bank Branches, Staff and Village Covered: The cost and effectiveness of rural credit are dependent on some specific points, of which the number of branches, staff and villages covered are considered as important elements. The growth of the RDS in terms of the number of branches, employees and villages covered have always been increasing. Initially the RDS was started with 48 field supervisors in 198 villages with 3600 people through 21 branches. Now it has become an organization of people with more than 1,49,705 members that covered 3700 villages and employing about 638 field supervisors through 83 branches. It is remarkable that there has been a rapid expansion of membership, but the increase of bank branches has not been proportionate to the increase in membership. This indicates that the RDS has been trying to achieve economies of scale to reduce costs to administer credits/ investment assistance.

(b) Relative Income Level

The second important criterion to measure the outreach to clients is to find out the relative income level by evaluating the value of average investment assistance and the range of the amount of investment assistance, percentage of rural clients, and percentage of female clients to total clients. It should be mentioned here that because of relatively small size of investment assistance and hence very small fraction to be repaid weekly, the repayment rate has been very high over the years. Hence the risks of bad and doubtful debts in such cases are negligible. It should be pointed out here that almost 74 percent of the RDS members are female and this fact has been contributing to:

1) Empowerment of females who are not given due attention by the development process of the country;
2) Provision of social security to the female members of the society;
3) Involvement of females in the household decision-making;
4) Provision of expenditure by females to improve consumption standard of the household;
5) Provision of expenditure by females to help improve child health; and
6) Provision of expenditure by females for Hakkul Ebad activities;

However, females do not always control the amount of investment assistance. The same is sometimes distributed to other members of the family of the females, and the household head controls the expenditure to some extent.

(C) Quality of service

In order to measure quality of service, the third indicator of outreach, indicators like profit, number of field supervisors, number of villages covered, number of members, number of branches, total amount of investment assistance given, total income, total costs, salary cost as % of total cost, client per field supervisor, profit/loss per bank branch, average number of village per employee etc. have been used. The RDS has been earning profit from investment assistance at a consistent rate since 1995. Profit per employee has been satisfactorily increasing, which indicates that the bank is trying to achieve economies of scale. The coverage of recipients of investment assistance per employee also indicates the same fact.

The quality of service provided by bank branches dealing with RDS is found better than other MFOs. The reasons for better quality of service are the following:

a) The RDS can attract better employees since a better benefit package is offered to them. The field supervisors not only get better pay, they also get other benefits associated with working in an established financial institution.

b) All employees in the RDS are trained at the Islamic Bank Training Academy at no extra cost to them. The high quality in-house training provided by professionals in the Training Academy improves the skills of the workers increasing their productivity.

c) The field level workers can perform their banking services more efficiently due to better logistic support. For instance, whereas field workers of most MFIs use bicycles to go to the weekly meetings and visit beneficiaries, those of RDS use motorcycles.

d) RDS employs sufficient workers to keep an ideal employee-beneficiary ratio. This helps them to monitor clients and supervise the funds more efficiently.

e) Since RDS is not dependent on external sources for funds, it can formulate its program in a manner that is suitable to the beneficiaries. For certain activities, an installment repayment schedule that corresponds to the income stream of the funded activity can be arranged. This practice does not burden the beneficiaries when there is no income generated from the investment (Ahmed, 2002).

5. Borrowers' Viability with Special Reference to Resource Mobilization and Poverty Alleviation

The RDS has enabled the poorest of the poor to get interest-free loan without collateral and saved them from exploitation by both the formal and informal money lenders who charge interest at a high rate. This has enabled the investment seekers to utilize their creativity to be self-employed. The most vulnerable and deprived men and women have come under the umbrella of the RDS to form a club of the poor, so to speak. It has united the poor (both man and woman) and created an environment in such a way that the poor can create their own security, for their existence and livelihood. The contribution of the RDS to promote indicators of socio-economic development is found satisfactory. The growth of membership, amount of loan in kind (investment assistance), saving etc. show that the RDS has successfully elevated the poor and mobilized their savings in the best possible productive way.

The average saving fund, average risk fund and average personal saving of the loanees per bank branch under study during 1995 were Tk. 6.95 lacs, Tk. 1.96 lacs and Tk. 15.10 lacs, respectively, which increased to Tk. 20.50 lacs, Tk. 10.15 lacs and Tk. 15.10 lacs, respectively, during the year 2004. A major proportion of the loanees (54%) took investment assistance for business purposes. This fact implies that the investment assistance in most cases was utilized for production purposes, which definitely helped asset formation of the loanees.

From the findings of the study it is evident that the investment assistance under the RDS contributed enormously to the upliftment of the socio-economic condition of the poor borrowers. We also find that 85.45 percent of the borrowers were benefited from increase in employment, 99.34 percent of the borrowers got self-confidence for their work, 99.01 percent were oriented in Islamic knowledge, 98.68 percent were inspired for social welfare activities, 96.38 percent were inspired for halal or honest earning, 97.36 percent became self-reliant, 94.07 percent experienced increase in their income, and 74.09 percent of the borrowers were able to raise the level of education of their children due to the availability of investment assistance under the RDS. It is also observed that 76.31 percent of the loanees were able to repay their loan (investment assistance) out of project income (i.e., income generated from within the investment activities for which investment assistance was sought). Most of the investors got surplus dividend from the investment project financed by the RDS. The provision of investment assistance by RDS generated different economic activities like fish cultivations, handicraft, handloom, betel leaf cultivation, cultivation of vegetables, cane products and rearing of poultry and livestock. From the above brief description it can be safely concluded that borrower's viability increased significantly due to the provision of investment assistance under the RDS.

6. Complementary Poverty Reduction Program

RDS has been successful in integrating other support programs along with the micro finance scheme. Due to poverty, the poor people are usually induced to divert funds to consumption and purchase of other assets. RDS uses funds from Islami Bank Foundation for a complementary program for asset building. The clients can obtain interest-free loans (qard-e-hassana) from this fund to buy assets (like tube wells) and housing. This not only builds the asset base of the beneficiaries, but also affects the repayment rate positively as the funds are not diverted for non-productive purposes. Besides, as default and arrears disqualify beneficiaries to avail of interest-free loans, this facility acts as an incentive for them to repay the installments on time (Ahmed, 2002).

7. Comparison between Islamic MFIS and Secular MFIS based on Empirical Study of RDS of IBBL

1. Islamic MFIs have been managing micro-investment / micro-credit programs with no dependence on external assistance while secular MFIs are implementing the same mainly with the financial assistance of external donors.
2. Both Islamic and secular MFIs are following almost the similar selection criteria to select their program beneficiaries. Both the groups of MFIs select poor people mainly on the basis of land ownership criteria, I.e., the families having maximum of 0.5 acres of land.
3. The secular MFIs include mostly women in their program while Islamic MFIs are including both men and women in their program.
4. Both the secular and Islamic MFIs copied the micro credit mechanism developed by the Grameen Bank (GB) with little or no modifications.
5. Secular MFIs charge interest rate at the rate of 20 to 30 percent on the credit (in cash) provided to the members. However, Islamic MFIs do not provide any cash loan. Their loan is called investment assistance. They apply the concept of 'Bai Muazzal' (sale on credit) and provide commodity adding certain percentage of mark-up on the cost of the commodity. The mark-up is 12%. IBBL divides the income from RDS as follows: profit to the bank is 6%, supervision fund is 4% and risk

fund is 2% and all these make a total of 12%. The equivalent rate of interest in conventional method of interest computation is 24%. Moreover, one distinguishing feature of RDS-IBBL is that it rebates one-fourth of such income, i.e., 6%, to the borrowers if his/ her repayment is regular. That makes the rate charged by RDS-IBBL 10.5%, one of the lowest in the micro credit sector. The minimum amount of saving is Taka 5.00 and members are free to save any amount since every member has to open a saving account in the bank. There is no legal restriction for RDS regarding mobilization of savings since it is a program of a bank.

6. The other terms and conditions of loan, apart from interest rate, are almost similar for both Islamic MFIs and Secular MFIs.
7. Both the groups of MFIs finance almost similar type of activities like poultry and livestock rearing, petty trade, agricultural inputs, rural vehicles, housing material, handlooms etc. However, unlike many MFIs, RDS-IBBL provides credit for both farm and non-farm activities for purchase of tube well and for building houses.
8. The institutional mechanism of credit delivery of Islamic MFIs is similar to that of the GB and other MFIs. The important difference is that the Islamic modes of investment have been proven to be equally applicable in reaching the poor. The duration and ceiling of loan are slightly different from typical micro credit and sometimes overlap the micro enterprise program of some MFIs.
9. To become a member of program of secular MFIs, a client is required to pay a fee of Taka 20.00. He is also required to buy a book of account. But in the case of RDS, a client or an investment seeker is not required to do so.
10. In case of secular MFIs like GB, a loanee is required to repay the 1st installment of the loan money just one week after the disbursement of the loan money whereas a recipient of investment assistance under RDS is allowed to repay the same two weeks after disbursement.
11. Since investment assistance under RDS is on PLS basis, the loss (if any and if it is genuine) incurred by the investment seeker may be borne by the RDS (i.e., IBBL). But there is no such provision in the case of other secular MFIs.
12. The RDS plays a vital role in promoting Islamic values and culture. In every weekly meeting of the center (Kendra), the field supervisors

teach the members about ethics and morality, values, norms, ideals and basic principles of Islam and their application in practice for overall human and material development. This teaching helps members to build their character and make a proper choice of their career. The pious villagers are very much attracted by this teaching of the field investigators. But there is no such religious and moral teaching in the case of other MFIs.

8. Conclusion and Policy Implication

The study presents an overview of the RDS, its style of lending or giving investment assistance, the process of distribution and collection of investment assistance without collateral and the present position of the RDS in sustainability and outreach. From the findings of the study stated in the previous sections, the following conclusions may be made:

a) The RDS has enabled the poorest of the poor to get interest-free loan in kind without collateral and saved them from exploitation by both the formal and informal moneylenders who charge interest at a high rate. This has enabled the investment seekers to utilize their creativity to be self-employed. The most vulnerable and deprived men and women have come under the umbrella of the RDS to form a club of the poor, so to speak. It has united the poor (both men and women) and created an environment in such a way that the poor can create their own security for their existence and livelihood. The contribution of the RDS to promote indicators of socio-economic development is found satisfactory. The growth of membership, amounts of loan in kind, savings etc. show that the RDS has successfully elevated the poor.

b) Although group-based lending is not a new one, the RDS has been successful in breaking all the previous records of loan recovery by both **GO**s and **NGO**s. The RDS has been found relatively less bureaucratic in all cases of its operation.

c) The loans (investment assistance) provided to poor (both men and women) help to empower them since investment assistance given in kind can not be transferred to other members of the relatives and the families. But this is not always found in the case of other **NGO**s.

d) Like the GB, the RDS has developed a broad-based loan portfolio with a view to diversifying risks. But most of its investment portfolio is related to agricultural and household sectors of Bangladesh.

e) The RDS is not dependent on subsidized funds or foreign donations or loans like other **NGO**s including **GB**. As a result, it can run more smoothly and without fear of uncertainty relating to availability of funds.

f) All the empirical findings relating to qualitative and quantitative indicators of sustainability and outreach prove that the RDS program is highly sustainable and effective. It is desirable from both practical and ethical points of view. It will maximize welfare both in the world here and the world hereafter since it serves the cause of both the mundane world and the cause of Allah. So, it is the best system so far as poverty alleviation is concerned.

g) Since RDS does not depend on external sources, its operations can adopt to cater some special needs of the beneficiaries. RDS also operates a complementary support program along with micro financing to target the hardcore poverty group.

h) RDS facilitates wealth creation of the poor through involvement in micro financing. Islamic banks are in a position to play the social role in the best possible way. The social aspect of Islamic banks can be best realized by financing the poor micro entrepreneur. Islamic banks can operate micro finance program at no extra-cost and improve economic conditions of the poor since they are predisposed to provide micro finance in a "win-win" situation. Empirical evidence of RDS of IBBL supports this assertion. However, RDS faces some transitional problems, which however, may be overcome if some effective steps are taken in time. The probable problems are highlighted and their tentative solutions are suggested below:

    1) The RDS has been providing investment assistance to the rural poor, especially women. These women have limited skill in entrepreneurship, marketing and distribution processes. The poor people living in urban areas have more skill in marketing and distributing the products but they are not eligible for investment assistance. The excessive biases cannot solve the real problem. Therefore, a satisfactory combination of male and female members as well as urban and rural poor may be more appropriate than the present one.

    2) The present target base is determined on the basis of land holding of less than half an acre. If the RDS increases this limit of half acre to one acre, it may increase the target base, which will enable more

people to join the RDS, and in the process, its overhead costs will also fall.

3) Relying primarily on the credit demand of poorly educated entrepreneurs may be too costly for the RDS if the investment seekers of the RDS find it difficult to switch over to more growth-oriented activities. The RDS should find out the field of investment in technology sectors in stead of agriculture. The diversification of portfolio in technology and raising the income of the poor may help the RDS to generate revenues and at the same time become more sustainable.

4) Heavy pressure on field supervisor to collect and distribute investment assistance may make them reluctant in overseeing utilization of the investment assistance. The number of field supervisor should be increased and necessary measures for rewarding honest and active field and branch level workers including the **FS** should be undertaken on a priority basis. The job of most of the field supervisors is temporary. They want to be regularized as permanent employees with higher salary and allowances. It is alleged that most of them are not regarded as a bank employee. The regularization of **FS** as permanent employee will give them incentive to work more sincerely and effectively.

5) The recipients of investment assistance often complain that the amount of investment assistance in general and the allocation for sanitary latrine are not adequate.

6) Till now, only one mode of investment (Bai-Muazzal) is practised. IBBL should taka initiatives to practice other modes of investment as well.

7) The RDS should be integrated with the IBBL mainstream banking, as a regular program and a separate department of the bank should be established with regular staff to deal with the RDS on a permanent basis.

8) The program should be replicated by other Islamic banks of the country and by Islamic banks in other countries of similar nature for resource mobilization and poverty alleviation. The secular MFOs, too, should derive lessons from the experience of RDS of IBBL to improve their performance.

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