Knowing When to Stop: The Case of UNDP Bangladesh
by Bonnie Brusky

In 2002 UNDP Bangladesh closed down the microfinance components of its empowerment projects. This action showed rare courage and good donor practice in an advanced microfinance market.

Overview

UNDP Bangladesh began implementing empowerment projects with microfinance components in 1996. Savings and credit were designed to be secondary components to these projects, but quickly became the centerpiece of many. In January 2002, a comprehensive review of microfinance activities confirmed UNDP staff suspicions that the components were not in line with international best practices. Much to the credit of UNDP, swift action was taken to close down the activities. Management then took a hard look at what the organization had to offer in a market like Bangladesh. Engaging in critical self-reflection and shutting down ineffective programs is not easy, but as UNDP Bangladesh demonstrated, sometimes good donor practice is about making difficult but courageous decisions.

Setting the stage

Microfinance in Bangladesh. The microfinance sector in Bangladesh is relatively advanced. Hundreds of NGOs and a handful of financial institutions serve more than 10 million clients across the country. It is estimated that roughly 70 percent of poor households are reached by MFIs and in some regions there is fierce competition for clients. The success” of microfinance makes it a popular intervention for many donors working in the country. However, only two of the largest MFIs have achieved full financial self-sufficiency. These are Association for Social Advancement (ASA) and Bangladesh Rural Advancement Committee (BRAC). The majority of microfinance providers are small, highly-subsidized, and poorly performing NGOs and government programs.

UNDP empowerment projects. Between 1996 and 2001, UNDP launched fourteen projects involving microfinance components in Bangladesh. These projects were all based on or inspired by the South Asian Poverty Alleviation Programme (SAPAP) approach. Although their specific objectives were varied, the projects shared the overriding goal of empowerment and, consequently, poverty reduction.

Microfinance components were implemented in a variety of ways. In some projects, groups of borrowers were organized into village organizations that were managed by locally-trained organizers. In others, credit components were executed through existing Village Centers, NGOs, or government programs. In all cases, credit funds were provided by UNDP grants and local project staff set interest rates. Spread across three regions, the total amount of grants initially budgeted for the projects was US$33 million, of which US$21.6 million was specifically allocated for microcredit.

Problematic Assumption

Including savings and credit services in empowerment projects was based on a real intention to improve the welfare of the population, but the combination turned out to be a mismatch. The inclusion of microfinance components was in part based on a problematic assumption that good empowerment projects would be more effective if accompanied by access to inexpensive credit. The implications of this assumption were many, including:
Microfinance components were seen as auxiliary and their sustainability was not considered. Microfinance was included to achieve a variety of project goals, from supporting fisher communities to improving the welfare of sex workers. While in some cases it was hoped that the components would be maintained by the users after the project ended, in many instances, permanent access to financial services was not mentioned as an expected outcome.

No microfinance specialists were involved in the design, implementation, or monitoring of the projects. At the time the projects were designed, UNDP had no in-house microfinance specialist to oversee the components. Six different program officers managed the fourteen projects, with little coordination among them. And although local project implementers received some training, most had little, if any, experience in microfinance. As a result, reporting was largely ad hoc, monitoring weak, and most performance indicators difficult to obtain.

Cheap credit drew in crowds. At 7 to 8 percent per year, the effective interest rates of some projects were far lower than other MFIs operating in the area and attracted clients. Microcredit quickly became the centerpiece of what were intended to be empowerment projects. Without systems and qualified staff in place, projects deteriorated and cases of misappropriation and misuse of funds emerged. UNDP program officers, not expecting to oversee a full-fledged microfinance program, were ill-equipped to manage the situation.

The consequences. Gradually, UNDP became aware of the problems due to program officers’ observations and mid-term project evaluations. Repayment rates were low in several projects, dipping to 54 percent in one program that had roughly 30,000 active borrowers and US$3.6 million in outstanding loans. This situation led to contamination of neighboring MFIs’ portfolios. In some projects, so much time was spent on microfinance activities that skills training of beneficiaries was neglected. As a result, some of the poorer borrowers, lacking the skills to use their loans, were further impoverished by indebtedness. In trying to empower local populations through inefficient microfinance components, UNDP projects were in some cases having the opposite effect.

“We did not have much expertise on microfinance at the country office, yet we somehow became responsible for financial management and credit operations of the groups. I soon realized that this was not the right thing.”

Program Officer, UNDP Bangladesh

“Monitoring is a glaring weakness ... Most of the Village Organization Managers, while educated, do not have either the willingness or the ability to monitor and record financial transactions regularly.”

Microfinance Review, July 1998

Steps to Exit Ineffective Microfinance Projects

1. Have a clear microfinance policy. A UNDP Operational Policy for microfinance entirely in line with international best practices was made official in 2000. This policy shift led management to put a hold on microfinance components of planned projects. Other projects already in operation saw their allocations for microcredit grants considerably reduced. The original US$21.6 million budget was decreased to US$14.1 million by the end of 2001.

2. Include microfinance expertise in the country team. In October 2000, Nicolas Perrin, a UNCDF Junior Program Officer with technical expertise and field experience in microfinance, was brought in to work as the microfinance focal point at UNDP Bangladesh. To better understand the full scope of microfinance activities being implemented, he proposed a comprehensive review.
Despite suspicions that projects were experiencing problems, the proposal met with internal barriers. Many UNDP program staff did not understand or appreciate why an approach and methodology cultivated over the years were being questioned. Resistance was initially strong enough to impede the review.

"I was not aware that certain types of microfinance activities were not allowed under UNDP policy, so the review came as a surprise."
Program Officer, UNDP Bangladesh

3. Be prepared to ask if projects can be better. Gradually, program staff began to express open support for the review. A growing number of mid-term evaluations and project audits raised questions in the minds of many regarding the effectiveness of the microfinance components. Program officers were witnessing deteriorating situations in the field and starting to question the inclusion of microfinance in community empowerment projects. Many staff wanted to know how the projects could do better.

4. Get everyone on board for the review. Conditions for the review, such as which projects would be included and the identification of an external consultant, were discussed internally for six months. During this time, efforts were made to get the buy-in of all program officers whose projects included credit and savings components. A series of staff meetings were held to talk about the pitfalls associated with project-oriented microcredit schemes, with the newly adopted UNDP Operational Policy providing a framework for the discussions.

5. Hire microfinance experts to undertake the review. The review was conducted in January 2002 by an external expert, microfinance consultant Peter Kooi.

6. Ask for honest assessment of projects and donor comparative advantage in microfinance. Given the level of development of the microfinance sector in Bangladesh, UNDP concluded that its comparative advantage as a service provider was limited. In an environment where microfinance is a popular intervention for many donors working in the country, the UNDP conclusion was a brave one. It demonstrated a clear understanding of what constitutes effective microfinance support and a commitment to good donor practices.

7. Be prepared to take immediate action. The review confirmed staff suspicions that projects were not following UNDP microfinance policies or generally accepted best practices. Problems that had been highlighted in mid-term evaluations had only worsened. The review recommended immediate closure of the microfinance activities and UNDP responded promptly.

8. Involve staff in the close-down strategy. In a vote of confidence, the program officers (POs) were closely involved in formulating exit strategies. The POs could have easily felt that their capacity to manage microfinance components was being called into question. By making sure the POs were essentially responsible for the close-down action, senior management demonstrated their faith in the POs’ ability to rectify the situation.

9. Be transparent about decisions. UNDP was open about its decision to end its microfinance activities. The Local Consultative Group Subgroup on microfinance (MF LCG), a quarterly forum for information sharing and donor coordination, provided an arena to announce the decision. UNDP explained that the saturated microfinance market and limited budget available for microfinance had led the organization to end all microfinance activities for the time being. The issue at stake—what constitutes effective donor interventions in a market like Bangladesh—was one with which many donors in the country could identify.

An ounce of prevention...

A great deal of time, effort, and resources go into project development and implementation. The decision to close down one—let alone fourteen!—can be hard, even discouraging. UNDP Bangladesh’s willingness to do just that is to be commended.

What can be learned from this “successful failure”? The following points may prevent other donors from going in the wrong direction:
• **Ask yourself: Is credit really necessary?** Credit is rarely a binding constraint for many projects. Even when it is, it should still be managed by a specialized entity—evidence indicates that it is better to de-link or to sequence financial and non-financial services. Moreover, as in the case of Bangladesh, ample services may be available already.

• If the argument for introducing a credit component is sufficiently strong, make sure to **analyze the viability of credit components as if they were stand-alone microfinance programs**. Had the underlying UNDP assumption been “good empowerment requires sustainable access to credit,” results would have likely been much different! It is essential that microfinance components be addressed from the beginning in the same way as microfinance-only projects are addressed. Notes former Deputy Resident Representative Yannick Glemarec, “It is extremely difficult to re-design project-oriented credit schemes once under implementation.”

• **Have clear microfinance policies and stick to them.** Having a formalized vision and policy statement can be useful to keep activities on track. Equally important, make sure the policy is disseminated and understood by program staff. In the case of UNDP Bangladesh, the policy shift in 2000 proved critical to identifying ineffective microfinance activities. In response to a recent Donor Peer Review conducted by CGAP, UNDP has gone further and boldly decided to undertake a comprehensive independent study of all UNDP microfinance projects and components in an effort to further strengthen organizational policies.

• **Carefully evaluate the microfinance sector and determine what your organization has to offer.** For example, a sector in the start-up phase will usually require human resources training, whereas one in the expansion phase may need assistance with upgrading management information systems. Recognizing the needs of the sector is the key to defining effective donor interventions.

• **Ensure the presence of an in-house technical expert.** Having an in-house microfinance focal point can greatly improve the chances for success. In the absence of a specialist, it is still important that one person be responsible for overall coordination of all microfinance activities, especially if microfinance components are buried in other projects.

**References**

Clark, Heather, with input from CGAP staff. 2003. **Credit Components. CGAP Donor Brief**, no. 10 (February).


**Contacts and Websites**

UNDP Bangladesh: [www.sapap.net](http://www.sapap.net)

Asian Development Bank: [www.adb.org](http://www.adb.org)

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Bonnie Brusky is an independent consultant in microfinance. The author would like to thank all the former and current UNDP Bangladesh staff interviewed for this publication, for their openness and cooperation.