Country Focus Note:

Bangladesh

The objective of this note is to provide readers with an overview of financial inclusion in Bangladesh. The note begins with an examination of the current state of financial inclusion in the country. It moves on to recent trends that have been driving usage in the financial sector. The note concludes by a view of the challenges that limit financial inclusion, and the opportunities that exist to unlock the potential of fintechs.

163 Million
Population

51.3 Million
Population with income <USD 2 per day

148 Million
Population with income <USD 10 per day

65%
Rural population

61.5%
Adult literacy level

81.8%
Mobile penetration

31%
Banked population

8.9%
Gender gap in ownership of bank accounts

Key Trends: Savings	Key Trends: Credit
• Less than a quarter of the population save money, of which less than a third save at a formal financial institution. • Low disposable income, high transaction costs, large distances from financial institutions, and complex documentation are some of the key barriers for low-income customers.	• Ranked at 85 globally in terms of ease of access to loans • Less than half of the population avail credit, of which less than a fifth avails credit from formal financial institutions. • Lack of customised products exclude the poor and push them towards informal sources of credit.

General Business Environment

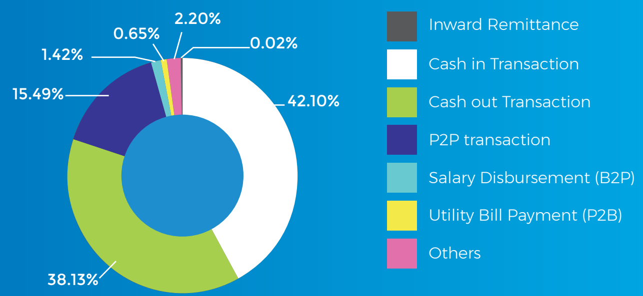
#177
Ranked on ease of doing business index

#107
Ranked on availability of venture capital

99.2%
of the population has access to electricity

46.5%
of the population has access to the Internet

Distribution of transaction amount of various MFS activities for December, 2017



Key Trends: SME Sector

25%
Contribution to GDP

80%
Contribution to employment

30%
SME claim access to finance as major barrier

USD 1.84 Bn
Total credit gap in SME sector

USD 2,288
Average credit gap per SME

Status of Financial Inclusion in Bangladesh[1,2]

Bangladesh is both an inspiration and a challenge for policymakers and development practitioners. While efforts in poverty reduction to date have been extraordinary, Bangladesh still faces daunting challenges, with nearly 51 million people living below the poverty line. With about 58 million (36%) of its residents between the young ages of 15–35 years, there is a massive opportunity for technology-driven interventions in Bangladesh.

According to World Economic Forum (WEF), Bangladesh is one of the top performing economies in Asia. It has maintained an average annual growth rate of over 6% between the 1960s and the 1990s. Bangladesh is the world's eighth most densely populated country and is home to more than 163 million people or around 2.2% of the world's population. The 2017 WEF Global Competitiveness Report states that out of 137 countries, Bangladesh ranks 77th based on the availability and 86th on the affordability of financial services.

Banking penetration in Bangladesh remains low, with over 70% of its population having no bank account. Data from the World Bank reveals that there were only 8.2 branches per 100,000 adults in the country in 2015, explaining in part the low account ownership. Efforts by Bangladesh Bank to increase include the 'Taka 10' no-frills accounts, introduced in 2010. These accounts targeted to promote Direct Benefit Transfers (DBT) and aimed to include the financially excluded. However, by 2015, only 14,000 accounts had been opened.

On the other hand, mobile phones saw rapid adoption. As of April 2017, Bangladesh had over 117 million mobile phone subscribers. Given the rapid adoption of mobile phones in the country, Bangladesh Bank issued guidelines for Mobile Financial Services (MFS) in 2011 to ensure access to financial services to the unbanked. Since then, the MFS sector in Bangladesh has experienced significant growth in terms of the number of users, as well as the number of agents that provide mobile money services.

Bangladesh now accounts for more than 8% of total mobile money accounts worldwide. However, the pattern of transactions suggests that the MFS market in Bangladesh is yet to move beyond basic transactions, such as cash-in, cash-out and payments – many of which are conducted over-the-counter by unregistered users. Over-the-counter transactions those that customers perform through an agent's mobile money account. However, over-the-counter (OTC) is declining - the proportion of OTC users reduced to 70% in 2016 from 77% in 2014. As of September 2017, there were over 770,000 agents in the country with more than 57 million registered MFS users. Of the registered customers, 52% are active users.[3]

The government has shown a firm commitment to introducing policies aimed at advancing financial inclusion. In 2011, Bangladesh signed the Maya Declaration – an initiative for developing frameworks for financial inclusion, and Access to Information (a2i), a think-tank of the Prime Minister's Office (PMO) is currently in the process of drafting a National Financial Inclusion Strategy (NFIS) document. The NFIS will lay out an actionable roadmap for various stakeholders to achieve financial inclusion objectives. Bangladesh Bank is in the process of releasing revised, comprehensive guidelines on MFS. We expect these guidelines to clarify the central bank's vision on MFS, interoperability, entry of non-bank players, ways to promote competition, and contours of a risk management framework.

1. The *MicroSave* report, titled Leveraging Technology for Meaningful Financial Inclusion in Asia, provides a detailed status on financial inclusion and usage of financial services in Bangladesh.
2. This document contains a few hyperlinks and readers are advised to read the document in conjunction with them.
3. An MFS user who has conducted at least one financial or non-financial transaction in three consecutive months (90 days) is considered an active user.

Key Trends in Financial Sector Usage[1]

We can summarise the current use of the key financial products in Bangladesh as follows.

1 Limited Savings at Formal Financial Institutions

The Global Findex Database suggests that by 2014, around 7.4% of adults had been saving at a financial institution[4]. This had halved in three years, as around 16.6% maintained a savings account with a financial institution in 2011. In contrast, approximately 17% of adults prefer to save using informal means[5]. Access to the formal financial system remains a challenge particularly for the rural poor in Bangladesh. Saving at a financial institution[3] for the rural Bangladeshis witnessed a steep decline from 16% in 2011 to 5% in 2014.

2 Complicated Process to Avail Credit Products

Out of 137 countries, Bangladesh ranked 85th in terms of ease of access to loans. Less than half of the population use credit services. Credit availed from formal financial institutions[3] witnessed a steep decline from 23.3% in 2011 to 9.9% in 2014. In Bangladesh, banks are often reluctant to lend money to poorer borrowers in the agricultural sector — where nearly half of the population earns its income. Collateral-based loans and complex application and authorisation processes are the two main constraints that limit low-income customers from using formal credit services. One-fourth of the population borrow from friends and family. The lack of customised and affordable formal credit products exclude the poor and push them towards friends and family and informal lenders to meet their credit demand.

Bangladesh has a long association with microfinance that has led the way to reach out to low-income people in rural and urban areas. The growth in the microfinance sector, in terms of the number of microfinance institutions (MFI) as well as total membership, was phenomenal during the 1990s and continues until today. As of June 2014, the microfinance sector comprised of 33.73 million clients (including 8.62 million clients of Grameen Bank) with a total loan outstanding of BDT 403 billion (~USD 4.8 billion) and savings of BDT 237 billion (~USD 2.8 billion).

Four types of institutions are involved in microfinance activities, which include Grameen Bank, non-governmental organisations (such as BRAC and ASA), commercial and specialised banks (such as Bangladesh Krishi Bank and Rajshahi Krishi Unnayan Bank), and government-sponsored microfinance projects (such as Bangladesh Rural Development Board and Swanirvar Bangladesh). These MFIs mostly provide small, collateral-free one-year term loans to individuals belonging to joint liability groups. Though there are more than a thousand institutions that offer microcredit services, the top-10 large MFIs and Grameen Bank have cornered 87% of total savings of the sector and provided 81% of the total outstanding loan in the microfinance sector.

3 Prevalence of and Preference for OTC Services for Payments and Transfers

In Bangladesh, there has been an increasing shift towards mobile money for internal remittances. About 50% of remittances are through formal channels. However, customers continue to conduct around 70% of all mobile money transactions using OTC services. Most customers prefer the OTC service, which is how the product was introduced, and because it is easier for those who struggle with literacy, or find it difficult to navigate the mobile money menus and fear they will mistakenly send money to the wrong mobile money account.

4. Financial institutions include Banks, MFS providers, MFA regulated microfinance institutions, credit unions and cooperatives.
5. Informal financial institutions include ROSCAs or Lottery Samitis (informal women groups or networks), moneylenders, or other unregulated financial access points, or both.

Challenges that Limit Meaningful Financial Inclusion

Sectoral Challenges

- Access to Capital: High interest rates for bank loans pose a problem for the emerging fintech sector. Challenge fund grants are either not significant enough to support scaling up or are restricted to the development of specific donor objectives that do not match business priorities. Angel investors are the best available option, but this sector remains immature.
- Need for Interoperability: The Bangladesh Bank is seeking account-to-account interoperability, which would enable seamless money movement across MFS, banks, and other platforms. Their goal is to incentivise more commercial payments receivers and providers to come on board, which would increase use cases, and reduce friction and inconvenience for customers.
- 'Cash is King' Market: Though there is high penetration of mobile phones, people depend on cash-based transactions and assisted OTC transactions. This is due to a strong preference for cash and a lack of awareness of, and trust in, DFS.
- Digital Literacy: Despite a high penetration of mobiles, people are using them either to communicate or to access social media platforms or both. Complex processes and User Interface coupled with a limited trust and understanding of technology for financial services has marred the uptake and regular usage of MFS among low- and middle-income customers.
- Distribution or Spread of FSPs: Agency banking is yet to pick up in Bangladesh. Banks have not built relationships with private players, such as MNOs or MFIs, which have a deep penetration in rural areas. Limited interaction between key regulators, such as Bangladesh Bank and Bangladesh Telecommunication Regulatory Commission, has also impeded the growth of MFS.
- Lack of Innovation: Banks often rely on traditional products and services and could focus more on product innovation. This has resulted in an immense competition in the market over a handful of products. Bancassurance, in particular, is yet to take off, despite its massive potential.

Challenges Related to the Design and Delivery of Financial Services

Product	Outstanding Constraints
Payments and Transfers	• Limited internet connectivity and high costs of mobile internet access have restricted the uptake of MFS among low-income customers. • Regulations prevent players such as MNOs, which have a country-wide footprint, from entering the MFS space, limiting access to 65% of the population. Currently, MFS platforms in Bangladesh are sponsored and led exclusively by the scheduled commercial banks, as they are members of the payments system.
Credit	• Low-income customers and microenterprises cannot avail formal credit services because they are unable to offer the necessary collateral or navigate the complex documentation processes. • The high cost of credit and "hassle factors" such as poor quality of service, delays in approval and disbursement result in informal service providers dominating the supply, especially for the lower-income segment. • The absence of a credit bureau makes it difficult for suppliers of credit to understand the needs of borrowers with multiple loans and their indebtedness.

Product	Outstanding Constraints
Savings	• LMI customers save little with the formal sector. This is because of deterring factors, such as the small size of their savings and irregular timing of such savings, the need to walk great distances to the branches, and long waiting times coupled with either with complex processes or a mandate to maintain minimum balances or both. • Most of the savings from low-income families go towards the purchase of gold and livestock. Moreover, the savings products offered by MFIs are not very customer-friendly with conditions such as lock-in, partial withdrawal, among others.
Insurance	• Bangladesh's insurance penetration at 0.5% remains one of the lowest in South Asia where other countries record a rate of 3.5%. Most insurance companies are located in urban areas and there are a very few branches in rural areas, leaving the large majority of the population unserved. • There is still considerable unmet demand for traditional and microinsurance products among LMI customers as current insurance offerings are concentrated on the higher end of the market. • Despite the growth of microinsurance in the country, many low-income customers lack awareness of insurance products.

Opportunities to Unlock the Potential of Fintech

In Bangladesh, licensed MFS players primarily lead the fintech ecosystem. Activities such as cash-in, cash-out, and P2P transfer constitute almost 95% of MFS transactions. Other activities like salary disbursement and utility bill payments, among others, constitute a mere 5%. Other players in the ecosystem include IT platform or solution providers, such as CloudWell and SSLCommerz. There are a few financial service providers (FSPs) who use the technology provided by the MFS players or IT platform or solution providers to distribute their products and services, such as Shakti Foundation for Disadvantaged Women. In addition, organisations like MicroEnsure, in partnership with local institutions, has introduced micro-insurance to the lower-income segment.

The fintech players in Bangladesh have a huge potential to address most of the constraints highlighted before. Outlined in the following section are some ways in which fintechs can address product-specific challenges.

Digital Literacy and Meaningful Financial Awareness

Limited digital literacy and financial awareness in the target market remains a significant challenge. Poor financial awareness limits the ability of the lower-income segments to make informed decisions concerning their household and business finances. In reality, digital literacy, to varying degrees, is a constraint even in countries such as China and Malaysia that have developed financial systems. Fintechs in Bangladesh can gain tremendously by creating intuitive interfaces and use-cases to help people learn how to use technology to manage their finances.

Customised Products to Suit Cash-flows of the Low-income Segment

Fintechs can develop mobile applications that link to a goal-based savings account. Customers can use such applications to set aside funds typically used to meet vital welfare or consumption needs. Examples include 'Save 4 School' from Econet in Zimbabwe, which helps smallholder families plan ahead for their children's school fee payments and 'Goal+' from Amret in Cambodia. The Goal+ product allows customers to save for long-term goals, such as purchasing cows, meeting wedding expenses, and education. Customers sign up and deposit via mobile tellers or third-party agents equipped with a smartphone or tablet app.

SAJIDA Foundation, an MFI of Bangladesh offers Astha, which is a voluntary savings deposit scheme. Astha allows SAJIDA Foundation members to save toward a purchase or financial goal. Members can deposit small amounts for a specified length of time while earning at-market interest. SAJIDA redesigned the Astha product with multiple features such as minimum balance, multiple term lengths, tiered interest rates, and support in setting goals. With these features, the adoption of Aastha accounts has increased.

Credit Risk Assessment for Low-income Segment and SMEs

Many active fintechs have been using non-traditional data to enable credit-scoring. Types of such non-traditional data include payment transaction data, insights based on psychometric tests, telecom data, and geo-position information. These alternative data sources help fintechs assess the credit risks of individuals who may lack credit history, established formal banking relationships, or verifiable sources of income. As a result, the fintechs can tap into the market of previously excluded potential borrowers who rely on informal sources for loans.

Credit Delivery through Alternate Channels

Peer-to-peer (P2P) lending fintechs can be an effective alternate channel that can address the credit demand of borrowers. These digitally enabled players bring in borrowers – typically SMEs that seek capital injection and lenders interested in competitive returns. A key advantage offered by P2P solutions include the flexibility to offer capital in variable amounts at lower interest rates compared to informal sources of loans, in an effective and transparent manner.

Customised Microinsurance Product Delivery and Servicing for Low-income Segments

Microinsurance services offered through mobile phones – mobile microinsurance – offers increased process efficiency through reduced turnaround times and lower paperwork. Mobile microinsurance makes low-value, high-volume transactions more viable. Fintechs such as BIMA and MicroEnsure act as end-to-end providers. They have tied up with MNOs that enable mobile money platforms or airtime used as a payment mode, if applicable. Fintechs, such as TongJuBao, use Internet-based platforms that allow groups to vote on premiums.

Looking Ahead

While basic access to banking services and products remains a challenge in Bangladesh, the government has shown firm commitment through conducive policies aimed at advancing financial inclusion. The microfinance movement has led the way in terms of reaching out to the masses. However, since the poverty remains acute in Bangladesh, the importance of microfinance is crucial especially for the lower-income segments located in the northern and southern part of the country Bangladesh.

Mobile financial services has the potential to be a game-changer in Bangladesh but reliance on OTC poses concerns. Technology-driven and innovative solutions are expected to emerge which will further augment meaningful financial inclusion in the country and facilitate the integration of underserved segments into the formal financial services sector.

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This note is part of a series highlighting the findings of a ***MicroSave*** study supported by MetLife Foundation. The study focused on understanding how technology could be meaningfully leveraged to advance financial inclusion across six markets in Asia – Bangladesh, China, Malaysia, Myanmar, Nepal, and Vietnam.