

Grameen model: Problems and Prospects

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1. Introduction

Grameen Bank concept was born in the village of Jobra, Bangladesh, in 1976. Professor Yunus, nobel prize winner for peace in 2006, had a field visit with his students. He watched a lady called Sufia working with bamboo. He was surprised to know that her status could be bonded labor if she was not able to manage five taka (US22 cents) to buy raw materials. Sufia explained local money lenders charge 10 percent per week and even 10 percent per day and people who start borrowing with them only get poorer. The next day Professor Yunus lent 856 taka (\$US 27.00) to 42 people of the Jobra village and told them to repay without interest. This emotional support of Prof. Yunus was institutionalized by establishing Grameen Bank in Bangladesh in 1983. Today Grameen Bank has 2,475 branches. It works in 80,511 villages and has 7.4 million borrowers and recently passed the \$US 6.6 Billion mark in loans to the poor.

Grameen bank system was introduced in Nepal during 1990s by the central bank establishing five Rural Regional Development Banks, one in each development region. Nirdhan and Center for Self Help Development (CSD) were two NGOs initiating Grameen replication in the private sector. The other prominent MFIs-NGOs replicating Grameen in Nepal are Chhimek, DEPROSC, and NRDSC. With the initiation of Nirdhan to promote Nirdhan Utthan Bank, other MFI NGOs also promoted Microfinance Development Banks like Swabalamban Bikas Bank, DEPROS Bikas Bank, and Chimek Bikas Bank. The five private sector microfinance development banks and five regional level rural development banks are Grameen replicates having coverage over 60% in the microfinance market in Nepal. The Grameen bank program, has been found fast growing and has substantive share both in breadth and depth of outreach. Experience shows it has high prospect of growth in Nepalese microfinance market to address the financial need of the unprivileged groups.

2. Objectives

- The first objective of this paper is to trace out Grameen banking system in the Nepalese context. How it has been started and why Grameen is important in the Nepalese context.
- The second objective of the paper is to share the experiences of Grameen in Nepal, analyze the major opportunities and challenges, and suggest how Grameen can be more inclusive, users' friendly and financially sustainable model.
- The third objective is how Grameen bank can be expanded in hills and remote areas. What needs to be done considering the situation in the hills.
- The fourth objective is to make recommendations to the policy makers, donors and implementing agencies on the basis of lessons learned for the growth of Grameen bank in Nepal.

3. Why Grameen

The following characteristics define why Grameen is a popular and leading model in the Nepalese microfinance market.

Targeted to poor: This model targets the poor based on certain criteria such as: size of the land holding, condition of the house, and income of the households.

Door step service: Bank goes to clients instead of clients to bank in this system. All the financial services are delivered through regular meetings in the community. This has opened the door to all the poor for financial services.

Collateral less: Loans are generally disbursed without collateral. Clients who are unable to give collateral or fulfill the several documents required by other banks can get loans from Grameen. It believes that poor are bankable, so it rather focuses on the cash flow and client's repayment history, not on the physical collateral such as land and building.

Repeated and increased volume of loans: The loan disbursement procedure of Grameen is in cycle. Each cycle contains 1 to 1.5 years time period. The loan cycle is repeated and the volume of the loan increases in each cycle. This makes possible for the clients to repay the loan in different installments.

Good repayment: Repayment rate above 95% in Grameen. It is because of the methodology and strong discipline in the system.

Focus on women: Grameen clients are exclusively women. This has contributed to women empowerment and is an inclusive system.

Fast growing: In Nepal, Grameen has been found fastest for outreach growth. This is due to methodology (easy access to loan, easy repayment schedule, door step service, etc.) and strong financial discipline adopted by the system.

Managed by banking professional: In contrast to cooperative and CBO model, Grameen is managed by banking professionals. Grameen have banking culture which ensures sustainability and viability of the program.

Impact on marginalized groups: Grameen program has positive impact on the lives of the poor. Grameen has increased awareness on health and education among the community people. It has been found supportive on improving living condition of the marginalized groups. The access and control over resources and participation of women on decision making has improved through Grameen program.

4. Grameen Model in Nepal: Key Issues:

4.1 Policy

NRB Directives and Government tax

In Nepal microfinance development banks are regulated by the Central Bank under the Bank and Financial Institution Act, whereas financial intermediary NGOs are regulated under the Society Registration Act and the Financial Intermediary Act. Each of these has its own reporting requirements. Nepal's microfinance institutions are playing the key role in delivering financial services to the socially excluded segment. Most of the microfinance institutions are working in tarai region because of population density, easy access to market and the availability of basic infrastructure. Yet there is no easy access of microfinance program for hilly poor. To operate microfinance program in hill region is very expensive. When MFIs open a branch in the Terai it becomes viable within 2 years of operation but in the hill region it take 4 to 5 years for its viability. The government has to support the microfinance sector by formulating better policies and developing infrastructure across the country.

4.2 Operational

Cost related

The major problem of the Nepalese MFIs is the excessive overhead cost. When a MFI starts its new branch, it incurs various costs such as; group formation cost, training and awareness cost, higher interest rate for the deposit and the other costs related to additional support programs to the client. It takes minimum 1 to 2 years for the branch to reach operational break even in terai and almost 4-5 years in hill areas. In fiscal year 2004/05, 31 partner organizations of Rural Microfinance Development Center [RMDC] have total financial and operational expenses ratio at 20.40 % compared to average gross outstanding loan. Financial Expenses Ratio is 6.72 %, Loan Loss provision ratio 2.32 %, Staff Expenses ratio is 7.26 % and Other Administrative Expenses ratio is 4.09 %. In Fiscal year 2005 the Eastern and Western regional rural development bank earn profit of NRP 11.5 million and NRP 9.3 million respectively. The three Far western, Mid-Western and Central regional rural development banks had a loss of NRP 201.9 millions. In Fiscal year 2005 the eastern and western bank had 2% and 1% return on assets respectively and other three bank had negative return on assets at -7 %. Nevertheless, the private sector bank had average return on assets at 3.2 %.

Governance in 5 GB

Grameen Bikas Bank is a government initiated bank. Among the 5 government initiated Grameen Banks, the two are privatized. Its board of directors are exclusively recruited from government institutions: NRB, the Ministry of Finance and the state-owned commercial banks. The chairman (so far from NRB) and the executive director (from one of the commercial banks) are elected from among the board members - with prior government approval. The Chief Executive Officer changes frequently so he/she can not implement long term plan and program for the sustainable development of the institutions. To the contrary, the bank finds itself under political pressure to lend to the poor at low interest rates at which it cannot cover its operational costs.

Institutional Capacity

Nepalese MFI working system is conventional whereby it lacks expertise in information technology and human resource management. The bookkeeping and other accounting systems are manual. It becomes time consuming and uninteresting for the staff. There is no proper IT system. Moreover IT system is expensive and it is not affordable to all MFI's. Some MFIs are seeking the proper IT system by which they can develop the professionalism.

One can evaluate the organization strength from its management information system. It is the system which processes the raw data and prepares the required information on desired format. With the application of proper information system, MFIs will be able to cut down its transaction cost though it has large number of borrowers of small loan size. The cost of Software, Networking of all branches through V-Sat, Internet and Anywhere Banking are very high and all MFIs cannot afford it by themselves. Choosing the appropriate software package is so hard. It needs regular technical support and need to be modified to accommodate new institutional structures, higher volumes of activity, new pricing methods, new reporting standards or any number of changes. So the availability of MIS package with regular support, perfect manpower for handling and the cost are one of the major issues in Nepalese MFIs.

Resource Management

Resource for the MFIs to deliver financial services include nominal fees, share subscriptions, regular compulsory savings and, voluntary savings to some extent, which is quite limited. A wider range of savings products and collection services is generally lacking. Government run programmes are subsidy based in nature, which have greatly undermined the motivation of the MFIs to mobilize their own resources. The loan demand of MFIs is increasing day by day. The cumulative loan disbursement and loan outstanding of partner organizations of Rural Microfinance Development Centre Ltd.[RMDC] as of mid-December 2007 is 22,17,49,19,000 and 3,523,588,000 respectively [status of RMDC's Partner Organizations]. RMDC have 50 partner organizations. The borrowings of partner Microfinance Development Banks [Nirdhan, Swabalamban, Chhimek, Madyamanchl Grameen Bannk and Paschimanch Grameen Bank] from RMDC is only 23.08 % of total outstanding loan on F/Y 2004/05. Similarly, it is 61.55 % and 69.87 % of RMDC's total outstanding loan in case of partner FINGOs and cooperatives respectively It is seen that RMDC has fulfilled only 32.53 % loan demand of its partner organizations. The other two wholesale lender are Rural Self-reliant Fund[RSRF] and Sana Kisan Bikas Bank, they have limited fund to provide wholesale fund to MFIs.. The deprived sector lending of Commercial Bank is another source of funding for MFIs. Newly established MFIs and those who are in bearing losses are not getting loan from commercial banks.. To solve the long term resource problem Microfinance Development Bank should be allowed to collect public deposit. If Finance companies with small capital are allowed to accept public deposits, why not it can be allowed for MFDBs which provide services to poor

Subsidized Program

Nepalese government has launched the subsidized program called Income generating Activities (IGAs) in selected areas. Now the government implements IGAs program through PAF (Poverty Alleviation Fund) in some areas. For income generating activities PAF provides 90 percent grant to limited Community Organizations(COs) to launch activities. Bisheshwor program is another government subsidized IGAs program. It covers only few peoples. The people can get free service in subsidized programs. Subsequently, the expectations of the people become high. The Principle and ideology is different in microfinance with subsidized programs. The microfinance program and the subsidized program operating in the same area will be the challenge for MFIs. They want the subsidized loan from MFIs which it is not financially possible and thus distorts the market.

Insurgency and Terai Conflict

The Terai conflict and insurgency has greater effect to the microfinance institution. Due to this insurgency some branches have closed and some were relocated. MFIs have to bear extra cost for this. The indirect effect of insurgency on microfinance operation will be on the operational and financial performance and portfolio quality. As MFIs are stable by nature they will not choose to withdraw from the financial market which is practically not possible, but will gradually develop coping strategies to provide continuity to microfinance services or during the conflict. Many MFIs have prepared head office and branch office security guidelines, fund management guidelines, portfolio management guidelines etc. which has thereby added extra burden to the institutions.

Micro-Insurance

Now the MFIs realize that providing credit is not enough for the sustainable development of the people. A range of other non financial services are required to be provided along with saving and credit services. The poor are vulnerable to different types of risks .MFIs should adopt the various strategies to reduce the impact of the losses. Insurances services are very essential on microfinance sector to recover the uncertainties and emergencies like illness, injury, death,

natural disasters, theft, and life cycles needs. Formal insurance services are not accessible to the poor because of high premiums and complicated procedures. Most of the MFIs have launched their own insurance services like livestock, and loanee insurance to minimize the risks of the people. It can minimize the risk on certain level yet there remain the other risks as well. There is an absence of effective insurance company for microfinance affiliated people, re-insurance company in the country and micro-insurance policy and act.

Interest rate

Public relation, transparency, honesty and integrity of leadership, management and staff are essential to retain the confidence of depositors and the value of their savings. Interest rates should be set competitively to give the highest possible rate of interest on savings and a low rate on loans such that the interest rate spread exactly covers the total operating costs of the institution. In the context of Nepalese microfinance, the interest rate is not the problem but rather the easy availability of the loan is the main problem. The interest rate of Nepalese microfinance is around 18 to 25 percent. The interest rate should be fixed considering financial cost, operating cost, administrative cost, future growth projection and inflation rate. The clients must not be the sufferer of inefficiency cost. In Nepal most of leading institution have fixed their interest at around 20 to 25%. The private owned MFIs have covered their cost but the government initiated Grameen banks are not able to cover their cost and are running on losses. The private sectors MFIs have recorded profitability at 20% interest rate and Government initiated Grameen banks are in loss by charging the same interest rate. It shows that effective management system is the main cause of the sustainability of the MFIs. The suitable interest rate in Grameen system is 20% to 25% with effective management system for future expansion.

Operational Procedure

Most of the MFI's are replicating the Grameen model. Chhimek Bikas Bank, Depros Bank, some NGO's and the Co-operatives are using modified Grameen model. Among these, Chhimek Bikas Bank has introduced a number of innovations in the program. Most of MFI's have included 40 to 50 members in one centre. But in Chhimek there are 25 members in one unit, with regular monthly meeting and monthly collection system. Some of the MFI's have applied weekly and fortnightly collection system. The monthly model is suitable in the area with scattered and low density population specially hills.

5. Prospect of Grameen Model

Potential for expansion

It is estimated that 2.4 million households require microfinance services in Nepal. However, data reveals approximately 730,000 microfinance clients have been served so far (a paper prepared on “Linkages of self help groups with MFIs, jointly organized by NRB and UNDP on July 12, 2007). The data reflects that only 30% of the microfinance clients have been enrolled in the program. A large mass is still not deprived of formal financial services. Furthermore, these groups include households living below poverty line. There exists a big gap between demand and supply in the microfinance sector. Of the several models working in the country, data reveals that Grameen bank system has been growing fast and able to reach bottom poor. The professional players of microfinance are 10 Microfinance Banks, some NGOs and some co-operatives. Duplication is very high in terai. Due to the scattered nature of households in the hill, microfinance is very costly. It takes 4 to 5 years recover the operational cost.

Inclusive Impact

Microfinance program is dedicated to the women and other marginalized segment of the community. But there is much to be done as still there is low outreach of microfinance service to the ultra poor from excluded community. They are very poor socially and economically. If the government supports such community on social sector (health, education & others) MFI will provide them financial services to economically uplift them. Hence these socially and economically deprived communities can be uplifted by forming alliance with the government sector, donors and microfinance institutions.

Viability and Sustainability of Microfinance

The sustainability is very important for the qualitative and durable service of microfinance. Microfinance provides service at the door-step of the poor based on the principle that the people should not go to the bank, bank should go to the people. It promotes credit as a human right. Most of MFIs are charging around 20% to 25% interest rates, which is usually not sufficient to cover the costs and risks of micro loans. The bank's delivery system is expensive - a second factor impeding viability. Salaries expensed for 40% to 50% of total expenditures. While office expenses accounted for 30% to 40%. Interest rate on savings deposits is around 10% to 12% and interest rate on borrowings is around 5% to 6%. In the case of government initiated Grameen Bank the cost is higher than this. Most of the Grameen bank are in loss due to low interest rate and lack of other fee income in comparison to other similar institutions. The politicians always claim that microfinance institutions charge high interest rate. The Government and the Central Bank should

CASE STUDY OF SUMITRA GIRI

Sumitra Giri was an ordinary woman living in Hetauda Municipality of Makawanpur District, Nepal. She and her family had a normal life while her husband worked as a truck driver. However, financial difficulties began to erupt when her husband had suffered from the disease and cut his right leg above from knee. Now, Sumitra had the only one option to go beyond her roles as a mother and wife to recover her family from extreme poverty. Sumitra had heard about the microfinance program of Chhimek Bikas Bank from her neighbors. She became the member of Chhimek Bikas Bank and utilized the microcredit, she received on her tailor shop.

With a first loan of Rs.10000.00, Sumitra Giri bought a sewing machine and some pots needed for tea stall. Her husband Dol Raj Giri help her to run the tea stall and her major involvement is tailoring shop. To expand her growing business, Sumitra finally decided to take a second loan of Rs.15000.00 and eventually took up a third loan 20000 and Discipline loan (additional loan) 10000. With a successful and prosperous business, Sumitra was able to keep her three children in school and repair her house with adding three rooms.

make favorable policy for the microfinance institution and the donor should financial support to the MFIs to lunch microfinance in the hill area.

Credit Plus

Loan product alone is not sufficient to uplift poor. The poor are not only poor financially but also poor in education, awareness, social, health and sanitation. The overall developments of the poor people are not possible from single microfinance institution. The basic infrastructure like health and education sector can be supported from the government .The donor can support other part. The microfinance can provide platform for development activities. For the coordination of such activities local level government agency, donor's representative and MFI's representative can form a committee.

Product diversification

Product diversification is very important in the context of Nepal. In the last twenty years or so, the microfinance institutions have greatly modified the Grameen Bank's methodology and devised appropriate financial service technologies to serve success and have become known worldwide. Many MFIs have taken up microfinance as core activities and some people maintain that there is a need to review whether microfinance programs should be separated from other, development programs and conducted independently.

The diversification of product may be in various sectors like in saving product, loan product, insurance product, money transfer, marketing sector etc. Grameen Bank has introduced product diversification through establishing Grameen Shakti for the development of renewable energy resources for poverty alleviation. This is most successful program in Bangladesh. It has 700,000 beneficiaries and 3.85 MW installed power capacity up to the year 2006. Grameen has not only diversified it's loan product but also diversified marketing, saving, insurance etc. In the context of Nepal few microfinance institutions have diversified it's loan, saving, insurance, money transfer etc. Chhimek Bikas Bank is a pioneer bank in the context of product diversification. The diversification is in loan[consumer loan, irrigation loan, renewable energy loan, Foreign employment loan etc], saving [unit house saving and pension saving] and internal remittance service etc.

6. Conclusion

Professor Yunus, nobel prize winner for peace in 2006, institutionalized his vision by establishing Grameen Bank in Bangladesh in 1993. This system was introduced in Nepal during 1990 by the central bank establishing five rural regional development banks. Grameen model is popular in the microfinance sector because this is targeted to poor, provides door step service, delivers collateral less loans, has good repayment rate, focuses on women, is managed by banking professional and has good impact on marginalized groups. To date Nepal has 11 microfinance development bank, 47 FINGO's(NRB Licensed) and some Co-operatives that are replicating the Grameen model.

A huge number of the populations are excluded from the micro financial services in the hill region. Government and Central bank's Policies, institutional capacity, overhead cost of MFIs, resource management are the major issues in the sustainable implementation of Grameen model in Nepal.

The government has to support the microfinance sector by formulating better policies and developing infrastructure across the country. The nature of the business of microfinance bank is

quite different with other financial institutions. So tax bracket should be reduced for microfinance bank. MFBs will be allowed to take public deposits for resources mobilization. There should be some incentive programs to the MFIs from government, donor and wholesale lenders to expand the microfinance in hill area. Besides this, donors can support the MFIs to strengthen the institutional capabilities through technical assistance, IT development and covering the 4 to 5 years overhead cost. The donors should monitor the MFIs whether they are using this fund for the sustainability of the program or just bringing attractive return for the investors. The MFIs associations and other regulation agencies should keenly watch such activities and help to take action to the government for the betterment of the objectives.

7. Recommendations:

7.1 Policy

Government

The government has to support the microfinance sector by formulating better policies and developing infrastructure across the country. The following are the major recommendations.

- Create the technical assistance fund to help potential MFIs to develop appropriate product and procedure and to recognize the best performer.
- The government should make the proper policy and channel for the integrated development to ultra poor on which the microfinance institution can serve them by providing financial services.
- The tax brackets for microfinance institutions are similar to commercial bank and finance company. The nature of business for commercial bank, finance company and microfinance bank is quite different. So tax bracket should be reduced for microfinance banks.
- The government should bring micro insurance policy and act.
- The Government should create the microfinance development fund with the collaboration of donors and provide it for meeting operational cost and technical assistance for the hillside coverage. The cost coverage mechanism must be simple and channelized through Nepal Microfinance Association. The Government should not launch unsustainable subsidized program in the areas where microfinance is implemented.
- The Poverty Alleviation Fund can be used to increase the microfinance outreach in hill area and ultra poor people.

NRB

The following section outlines some specific recommendations for NRB.

- Additional NRP 2,500,000 paid up capital is needed to expand the program in new district. It should be made NRP 1,000,000 for one district for MFBs in hill area.
- MFBs will be allowed to take public deposits. But there should be a limit upto which public deposit can be accepted; for example, balance of public deposits should not exceed the amount of total loan outstanding by a certain percentage.
- Reporting formats for commercial banks and microfinance banks are same. It is suggested to separate for MFIs considering its nature of business.

7.2 Wholesale lenders

Rural Microfinance Development Centre (RMDC), Sana Kisan Bikas Bank (SKBB), Rural Self Reliant Fund (RSRF) and commercial bank's deprived sector lending are the existing wholesale lenders of Nepal. But these institutions are not easily accessible as they are situated only in the capital. The size of their loan is very small to meet the complete requirement in future. The interest rate of these wholesale lenders is high. It should be reduced. There is no any incentive to the MFIs to run there microfinance in the hill. The personal guarantee of FINGO's board of director's demanding from commercial bank is unreasonable. The loan should be providing at institutional guarantee.

7.3 Donors

Hill area Operational cost and Institutional Capacity

Microfinance provides service at the door-step of the poor based on the principle that the people should not go to the bank, bank should come to the people. It promotes credit as a human right. The loan size is small and door-step service makes the transaction cost high. The major players of the MFIs are concentrated in Terai. Due to the scattered households, the microfinance service becomes very costly. Donor should support the MFI's by providing technical assistance, IT development and 4 to 5 years overhead cost for increase the microfinance outreach in the hills and mountains area. The donors should also watch the MFIs whether they are using this fund for the sustainability of the program or just bringing attractive return for the investors.

Implementing Agency [MFI's]

The MFI's mission is to help the poor families to help themselves to overcome poverty. It is targeted to the poor, particularly poor women. Reaching the poor is a must and a non-negotiable mission. Getting sustainability is a directional goal and it must be reached as soon as possible, so that it can expand its outreach without fund constraints. We implementing agencies have responsibility to proper use of the fund for the deprived people. The MFIs associations should keenly watch such activities and help to take action to the government.

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ANNEX

Major Actors in Nepal's Rural Micro Finance Sector and their outreach as of Mid January 2008

S. N	Name of Microfinance Institutions (MFIs)	No. of Members	No. of Borrowers in	Savings Mobilization in NRS	Loan Outstanding In NRs	Remarks
1	Eastern Rural Development Banks	58891	58891	179622405	748062999	Mid Jan. 2008
2	Central Development Banks	44014	42872	128455540	379163780	Mid Jan. 2008
3	Western Development Banks	36786	32971	109655000	468691000	Mid Dec.2007
4	Mid-Western Development Banks	19457	14510	76864000	215711000	Mid Jan. 2008
5	Far-Western Rural Development Banks	12165	8941	39182854	147330428	Mid Jan. 2008
6	Rural Development Bank (Sub Total)	171313	125214	1520679799	1958959207	
7	Nirdhan Utthan Bank (MF Bank)	89879	64728	202301341	666750032	Mid Jan. 2008
8	Swabalamban Bank (MF Bank)	76999	58383	226519356	431582819	Mid Jan. 2008
9	Chhimek Development Bank(MF Bank)	69009	55680	194806590	517661240	Mid Jan. 2008
10	Deprosc Bank (MF Bank)	25226	20244	59600603	239525318	Mid Jan. 2008
11	Nerude Bittiya Sanstha	28905	25943	56131173	147362718	Mid Jan. 2008
	Sub Total Private Sector Dev. Bank	290018	224978	739359063	2002882127	
11	Micro Finance bank (Sub Total)	461331	350192	2260038862	3961841334	
12	Financial Intermediary NGOs and Co-operative	272661	204658	446013000	1267715000	RMDC's 50 Partner Organizations As at Mid December 2007
13	Grand Total	733992	554850	2706051862	5229556334	

Source: 1. Rural Microfinance Development Centre [RMDC] and Nepal Microfinance Banker's Association [NMBA]

