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Covid-19 and MFIs in Bangladesh: Innovations in Resilience Building

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Abstract

A large segment of the poor households and microentrepreneurs rely on financial and other services offered by the microfinance institutions (MFIs) in Bangladesh. During times of natural disasters or other crises, the MFIs also provide the borrowers flexibility in loan repayment and access to emergency loans to deal with the predicaments. But the Covid-19 pandemic has been unprecedented which has seriously affected the activities of both the MFIs and their members. The study explores the nature and depth of financial and operational constraints faced by the MFIs based on information collected through an online survey during September 2020. The operational difficulties of the MFIs highlight problems in interacting with the borrowers, bottlenecks in nonfinancial service delivery, and constraints in collecting repayments and disbursing new loans. Around 93 per cent of the MFIs experienced a sharp increase in their portfolio at risk (PAR) relative to the pre Covid-19 period and 73 per cent had inadequate equity capital to cope with the Covid-19 crisis. The MFIs face similar financial difficulties due to the pandemic including rising outstanding loan portfolio, high savings withdrawal and difficulties in repaying borrowed capital. About 51 per cent of the large MFIs had to revise their loan distribution policy. Although about a quarter of the MFIs adopted mobile services to disburse loan and emergency grants, medium and small MFIs are more constrained in adopting the mobile technology.The MFIs recognise that their recovery policies should include alternative investment policies and institutional behavioural changes that will reduce the likelihood of future shocks and increase resilience when another covariate shock occurs.

Keywords: Financial and operational challenges, MFIs, Covid-19, Bangladesh

Covid-19 and MFIs in Bangladesh: Innovations in Resilience Building

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1. Introduction

As a sudden shock, the Covid-19 pandemic presents not only a critical threat to human health, but it has also inflicted massive and far-reaching socioeconomic turmoil globally. Massive and prolonged lockdowns have been imposed across countries to limit the spread of Covid-19 with dire consequences on livelihoods and businesses. The question has also been debated as whether to 'save lives or save livelihoods' (Khawar, 2020). Along with this, a hidden question came to the forefront as how to save the institutions that people rely on for basic services (Ogden and Bull, 2020). In Bangladesh, the crisis related to Covid-19 has struck at the heart of most microfinance activities as microfinance institutions (MFIs) staffs and clients are required to maintain social distances and travel restrictions. These institutions are facing difficulties in disbursement of loans, collection of installments and meeting with clients, among others. Repayment of installments has become close to impossible, while new loan applications have dwindled. On the other hand, the operational expenses of MFIs persist due to inflexibility of these outflows.

Still, it is uncertain exactly when the pandemic will be over and how long its effects will last. The key issue for the MFIs is to resume their normal operations at the earliest opportunity. During past emergencies such as natural disasters, the MFIs in Bangladesh have shown remarkable resilience and have turned around within a short span of time. These institutions could weather through all types of upheavals; and the MFIs have bounced back every time with renewed commitment to their vision of serving the poor and disadvantaged. But the present Covid-19 crisis is different from the earlier crises. Earlier crises tended to impact the MFI operations at a regional scale (e.g. in places where natural calamities hit), enabling more vibrant areas to cross-subsidise the negatively impacted regions. The duration of the impact was also much better anticipated, enabling contingency plans to be prepared and funded. However, these flexibilities are mostly absent in the present Covid-19 crisis as it is a universal disaster affecting the entire country.

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As experienced during the past crises, there is always an increased demand for loans in the post-crisis period in order to inject new finances into businesses, buy productive assets, and boost consumption in the hard hit communities. In the informal economy, the MFIs play the important role in financing the households/enterprises and reviving local economies in the post-crisis period. With their long experience of working with the poor households and informal microenterprises, these institutions have the ability to show extraordinary resilience and commitment to support their customers and ensure the stability of their income-generating activities. They apply various techniques at their disposal, such as deferring the repayment of loan installments, credit refinancing, and setting up specific support mechanisms suited to specific borrowers. During the present coronavirus crisis, many MFIs have set up awareness-raising campaigns on basic protective measures for employees and customers. They are also promoting digital transfer systems which limit contacts and allowing teleworking to enable the staff to continue their essential operations.

However, the greatest challenge for the MFIs is to ensure sustainability of their operations after the pandemic. During the past, the MFIs could revive their operations within a short period after the occurrence of the crises. But for the present crisis, it may take 12-18 months for a full rebound, depending on the extent and duration of the crisis, which is highly uncertain. Full normalcy can only be possible if the field staff of MFIs can move freely again. Yet, given the nature of the Covid-19, there is a real risk of repeated spikes and possibly repeated and localised lockdowns. These have the potential to disrupt the recovery process intermittently. The present study aims to explore the specific operational and financial difficulties faced by the MFIs during Covid-19 period. It highlights the changes in the portfolio at risk (PAR) of the MFIs due to the crisis and the operational and crisis management measures adopted by the MFIs as a precaution against Covid-19 impacts. Finally, the study suggests supportive measures that can be adopted for the MFIs to carry out their mission of serving the poor and disadvantaged in a more effective manner in the post Covid-19 period.

2. MFIs and Covid-19: Transmission Channels and Global Impact

The Covid-19 pandemic has impacted nearly everyone across the world, but its impacts are particularly acute for the people in poverty. One ADB estimate in May 2020 shows that: *'The global economy could suffer between $5.8 trillion and $8.8 trillion in losses – equivalent to 6.4 per cent to 9.7 per cent of global gross domestic product (GDP) – as a result of the novel coronavirus disease (Covid-19) pandemic'*

(ADB, 2020). The spread of the virus itself and the containment measures attempting to mitigate it can bring production and consumption to a near standstill (Boone et al., 2020). For example, high mortality and morbidity rates of Covid-19 reduce the labour supply which, in turn, hinders production. Similarly, social distancing rules (mobility limitations and quarantine) aiming to reduce the transmission rate also causes a sharp decline of production in the economy.

The economic impact of Covid-19 is more severe than most past crises and this is a highly infectious disease relative to past major disease outbreaks. As a result, the global value chains have greatly been disrupted, which now account for more than two-thirds of total world trade (Dollar, 2019); and these disruptions are likely to continue to propagate in all directions as countries restrict economic activity to control the disease (Baldwin and Freeman, 2020). The manufacturing sector, in particular, is likely to suffer major disruptions through shutdowns, labour shortages, supply chain and transportation disruptions, and declining demand as customers cancel or delay purchases and investments (Baldwin and di Mauro, 2020). The world merchandise trade is likely to decline by between 13 per cent and 32 per cent in 2020 (World Trade Organization, 2020). Agricultural production and prices have not yet been strongly affected by Covid-19 (World Bank, 2020), and food security is not currently threatened at the global level. However, agriculture and food security are at risk of disruption if barriers on input supply (e.g. labour shortage due to travel restrictions and supply chain disruptions) persist for a longer time.

More importantly, people everywhere are out of work due to the Covid-19 crisis. A large segment of the rural population depends on remittances from the cities or abroad. Their income flows have either been interrupted or stopped and the vast majority of the MFI borrowers have become vulnerable due to the pandemic. The pandemic has affected the earnings of the borrowers which have seriously weakened their repayment capacity. As a result, this has also created a serious threat to the daily activities of the MFIs and also on their sustainability. The poor and low-income households and microenterprises that are traditionally excluded from the mainstream financial services are mostly dependent on the MFIs for finance and business support. A pandemic-induced economic downturn normally puts pressure on the banks' loan portfolios and lead to large withdrawals of deposits, particularly in poor and developing countries (Lagoarde-Segot and Leoni, 2013; Beck, 2020). It is more likely that the socioeconomic disruptions caused by Covid-19 would transmit negative effects on the financial performance of the MFIs. More specifically, the MFIs could experience deterioration in their performance as the small and medium-sized businesses (SMEs) and vulnerable households, which are among the most exposed to Covid-19, struggle to meet their debt obligations.

The effects of the Covid-19 induced decline in economic activities on the financial and social efficiency signify conflicting outcomes for financial efficiency and social efficiency of the MFIs (Zheng and Zhang, 2020). The study shows that the pandemic-induced impact decreases the financial efficiency of the MFIs; while, their social efficiency increases under the impact of Covid-19. To explore the potential channels through which efficiency is influenced by the Covid-19 outbreak, both the supply and demand sides of MFIs' funding are important. The study finds that the lending rate mediates the relationship between the impact of Covid-19 and MFI efficiency, whereas the mediating role of the funding rate is negligible.

Another study on the effects of the Covid-19 crisis on 110 MFIs in 47 countries shows that portfolio and risk managements are among the first short-term challenges raised by the crisis for more than 80 per cent of the MFIs (ADA, Inpulse and the Grameen Crédit Agricole Foundation, 2020). On the operations side, the difficulty or impossibility to collect savings is not an issue for all. This concerns 56 per cent of the surveyed MFIs in Sub-Saharan Africa and 60 per cent in South Asia, whereas the issue is hardly relevant in other regions. This depends on the constitution of the local market, and on the capacity of the institutions to offer the products to their customers.

Despite substantial progress in reducing global poverty over the past thirty years, the apprehension is quite strong that Covid-19 could make 2020 as the first year to show an increase in poverty levels since 1990 (Sumner, Hoy and Ortiz-Juarez, 2020). The anticipated economic downturn will affect people in or near poverty badly, and is likely to result in millions of people falling below the $1.90/day international poverty line (Laborde, Martin, and Vos, 2020). As the MFIs navigate the uncertainties of Covid-19 through injecting cash into the hands of their members, fostering relationships with their members, promoting public health and meeting other challenges, these become the most critical investments in local economies and communities to ensure a quick recovery for the poor and disadvantaged and boost economic growth and community resilience.

[e] Following MRA, the categorisation of MFIs are: very large (more than 500,000 borrowers); large (100,000-500,000 borrowers); medium (10,000-100,000 borrowers); and small (0-10,000 borrowers) Source: http://www.mra.gov.bd/images/mra_files/Publications/vol2015.pdf

3. Study Methodology and Key Results

3.1 Sampling Procedure

For the present study, quantitative data were collected through online survey using Google form to prepare the questionnaire. A detailed questionnaire was developed to understand the impact of Covid-19 outbreak on different aspects of MFI activities in Bangladesh. The response on the questionnaire was received from different categories of MRA-registered MFIs. The survey was conducted during the month of September 2020, and a total of 59 MFIs participated in the online survey. The data captured the status of MFIs during the Covid-19 crisis. The responses to the survey were strictly on a voluntary basis. A total of 59 responses were recorded during the survey covering different size classes of MFIs (Table 1).

Table 1: Size Class of Sample MFIs

Size class of MFIs	Number of MFIs	Number of borrowers in 2019
Very large	2	More than 500,000
Large	8	100,000-500,000
Medium	29	10,000-100,000
Small	20	0-10,000
Total	59	…

Source: http://www.mra.gov.bd/images/mra_files/Publications/vol2015.pdf

3.2 Financial and Operational Challenges

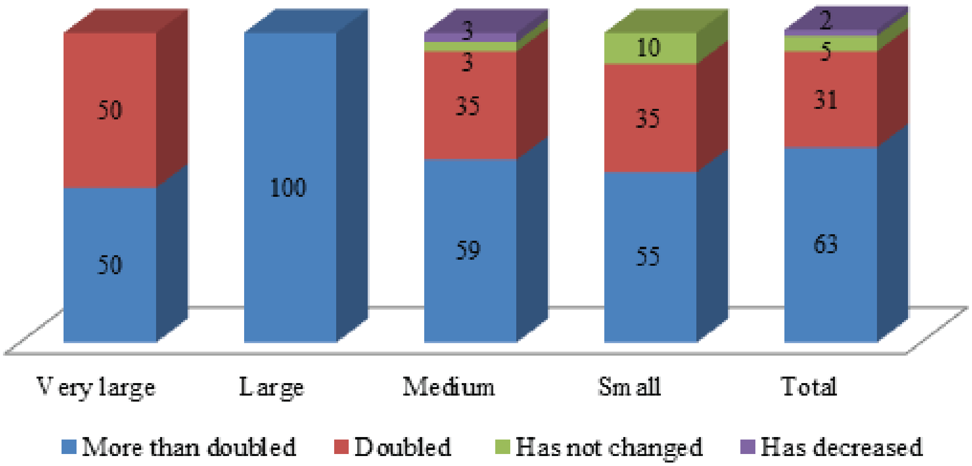
Portfolio at Risk (PAR) of MFIs: The MFIs are faced with diverse operational difficulties due to the Covid-19 pandemic. Among the major problems, the growing portfolio at risk (PAR) is the greatest financial challenge that they have encountered due to the pandemic. Usually, the MFIs measure PAR to assess the quality of their loans and the extent of the associated risk of default. The PAR measures the risk in terms of the share of the loan portfolio that could turn out as default loan when proper breakdown of all loans is made and the loans are grouped in similar risk categories. The PAR is calculated as the ratio of the volume of the loan portfolio that is overdue for a certain period (usually taken as exceeding 30 days) and the total loan portfolio.

All MFIs size classes have been facing rising PAR due to the Covid-19 pandemic (Figure 1). About 93per cent of the sample MFIs indicates that their PAR levels have risen sharply during the Covid-19 period compared with their pre Covid-19 levels.

Among the very large MFIs, the PAR has more than doubled for 50 per cent; while for the rest, PAR has doubled. For all large MFIs, the PAR has doubled. On the other hand, among the medium MFIs, 59 per cent and, among the small MFIs, 55 per cent have experienced a more than doubling of their PAR; while 35 per cent of both small and medium MFIs report a doubling of PAR over their pre Covid-19 levels. Only 10 per cent of the small MFIs have relatively unchanged PAR.

Figure 1: Changes in PAR of MFIs during Pre and Post Covid-19 Period

(Figures in %)



Source: InM Online Survey, September 2020

Operational Difficulties of MFIs

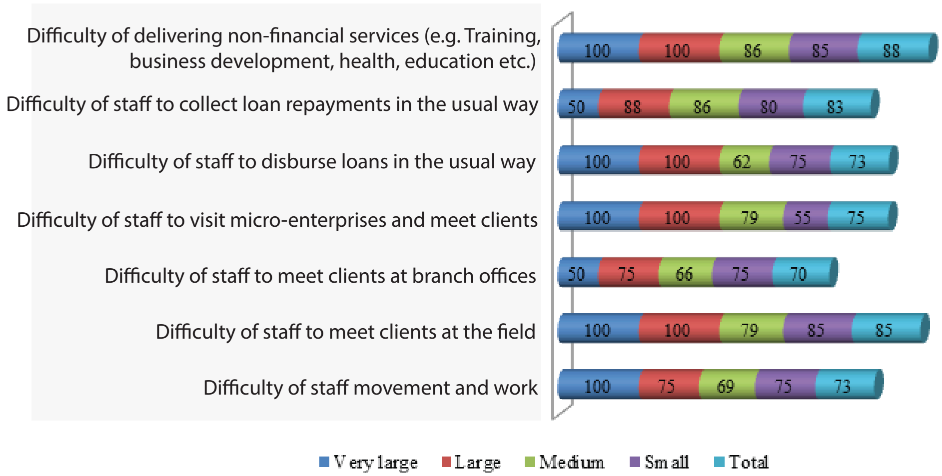
Like other economic sectors, the crisis related to the Covid-19 has disrupted most of the regular activities of MFIs. The evidence shows that most MFIs faced somewhat similar problems (Figure 2). More than 85 per cent of the MFIs have difficulties of their staff in meeting with the borrowers at the field, while 88 per cent face problems in delivering nonfinancial services such as, training and business development, health, education and other services. Around 83 per cent of the MFIs report facing difficulties in collecting loan repayments, while 73 per cent has difficulties in disbursing new loans. Irrespective of their sizes, most of the MFIs face these operational difficulties. It may be seen that the difficulties encountered by the MFIs are closely linked with the financial viability and sustainability of the MFIs. As such, these operational difficulties have also triggered other major short- and long-term financial challenges for all MFIs

In this study, the Covid-19 period spreads from 01 May to 31 August 2020.

including rising PAR, difficulties in portfolio and risk management, mass withdrawal of savings by the members, and worsening liquidity crisis.

Figure 2: Operational Difficulties of MFIs due to Covid-19

(Figures in %)



Source: InM Online Survey, September 2020

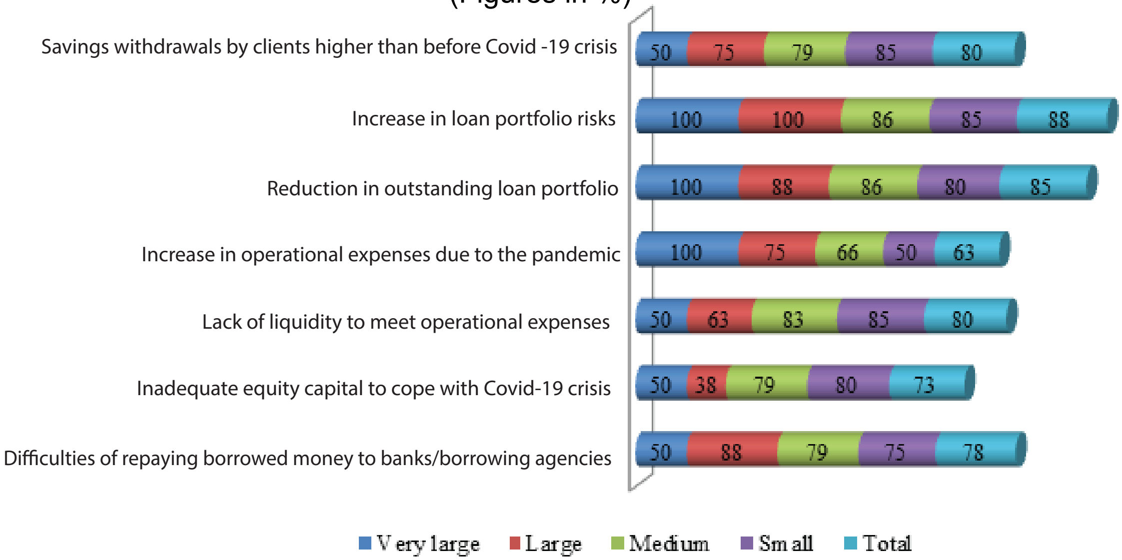
Financial Difficulties of MFIs

Due to the Covid-19, the livelihoods of the MFI borrowers working in the informal sector have been disrupted. Both individual and microenterprise borrowers have faced a serious decline in their average incomes, estimated at more than two-thirds of the normal level. As a result, the vast majority of the MFI borrowers have become vulnerable thereby creating a serious threat to the normal operations of the MFIs and also on their sustainability. The pandemic has seriously affected the workplace and earnings of the borrowers along with seriously weakening their repayment capacity. Regular repayment of loan installments has been disrupted affecting the ability of the MFIs both to maintain their regular operations and repay their loans to their financiers. In short, the MFIs now face a huge cash flow crisis due to the Covid-19.

Irrespective of their size category, most surveyed MFIs face similar financial difficulties due to the pandemic (Figure 3). About 88 per cent of the MFIs report rapidly rising PAR, while 85 per cent face deterioration in outstanding loan portfolio and 80 per cent face the problem of high rates of savings withdrawal by the borrowers. Around 78 per cent of the surveyed MFIs face difficulties in repaying their borrowed fund to the banks and/or other borrowing agencies. More than 73 per cent of the MFIs have inadequate equity capital to cope with the Covid-19 crisis. No doubt, these financial difficulties represent a challenge for the entire microfinance sector for both the short and medium terms.

Figure 3: MFIs Facing Financial Difficulties due to Covid-19

(Figures in %)



Source: InM Online Survey, September 2020

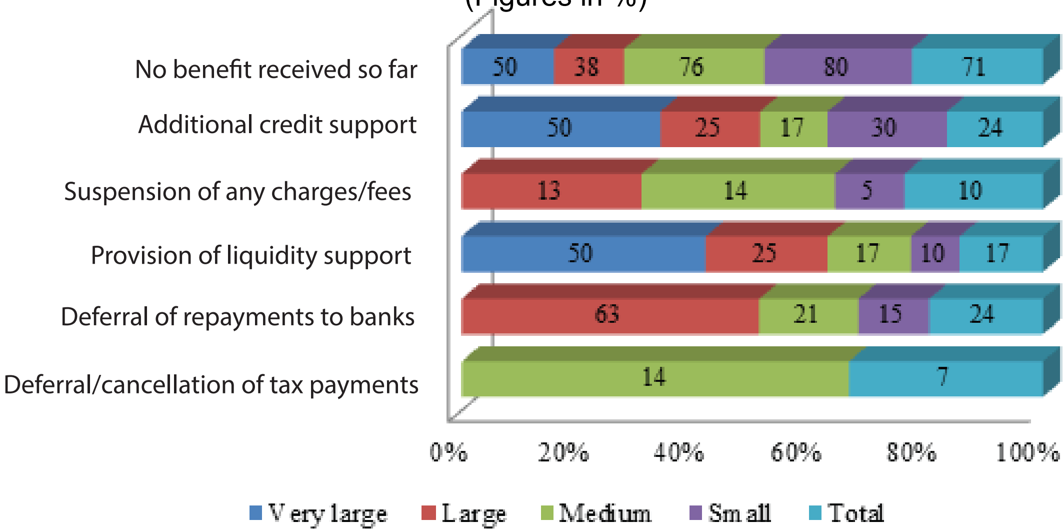
4. Covid-19 Pandemic and MFI Members: Short and Long Term Consequences

Over the years, MFIs have proven their resilience against various odds, like, natural or other disasters. But the current Covid-19 crisis is different from any other crisis that affected the microfinance operations before. With the outbreak of the Covid-19 pandemic, the government has announced a number of fiscal measures targeted to the grassroots level to mitigate the crisis. Around 71 per cent of the MFIs report that they have received no benefits so far and the share is around 80 per cent for the small MFIs, 76 per cent for medium MFIs and 38 per cent for large MFIs (Figure 4). This indicates that large MFIs have managed to procure some support measures but the smaller sized MFIs have mostly been excluded from any kind of recovery measures during the pandemic.

However, the fiscal measures are yet to work fully at the field level; only around 24 per cent of the MFIs have received deferral of repayments to banks and additional credit support. The highest share of receiving deferral of repayments to the banks is by large MFIs (63 per cent), followed by only 21 per cent for the medium and 15 per cent for the small MFIs. Moreover, 50 per cent of the very large MFIs have received additional credit support, which is 25 per cent for the large MFIs, 17 per cent for the medium and 30 per cent for the small MFIs. Only 7 per cent of MFIs have received deferral or cancellation of tax payments.

Figure 4: Assistance Received by MFIs during Covid-19

(Figures in %)



Source: InM Online Survey, September 2020

For the MFIs, loan reimbursement by the borrowers is the major element of cash inflows followed by borrowings from banks or lending agencies. However, due to the national lockdown imposed during the outbreak of the Covid-19 pandemic, the collection of installments faced severe disruptions for all MFIs. The Microcredit Regulatory Authority (MRA) also advised the MFIs to temporarily postpone installment collection on loans from the borrowers and undertake their operations on a limited scale. In view of the pandemic, the MFIs avoided the 'yard meetings' an encouraged the use of digital platforms for making transactions as much as possible, and conducted their activities in the locked down areas in consultation with the local administration to ensure safety of public health. This also reduced the disbursement rate of new loans despite the existence of high demands in the market.

During the period, the lending organisations (e.g. banks) were also on a sit back mode and hesitant to disburse new loan to the MFIs. In contrast, despite sharp decline in their regular operations, the MFIs had to maintain the regular staff, pay their loan installments to the borrowers, and meet coronavirus-induced rising administrative and office expenses. Thus, reduced cash inflows and rising cash outflows seriously affected the net earnings of the MFIs. The situation is especially serious for the small and mid-sized MFIs and the apprehension is that the situation may continue for some time in future. The government has announced a ‘loan package’ for the MFIs and the package should be made available to the MFIs at the earliest opportunity using transparent and effective criteria for distribution among various groups of MFIs to restore their normal activity levels.

For the longer term, the MFIs need to address several major challenges through making adjustments and adopting innovations. Many MFI borrowers will need additional time to repay their current loans. The government and the regulators will have to come up with appropriate stimulus packages, especially for providing easy access to loanable funds with flexible terms and conditions for the MFIs. During the recovery and restoration period, the operational staff especially the branch managers and the field staff of the MFIs will have to play the key role in restoring confidence and discipline in their operations. The MFIs will have to ensure high morale and appropriate support to the field staff to play their due role in the process.

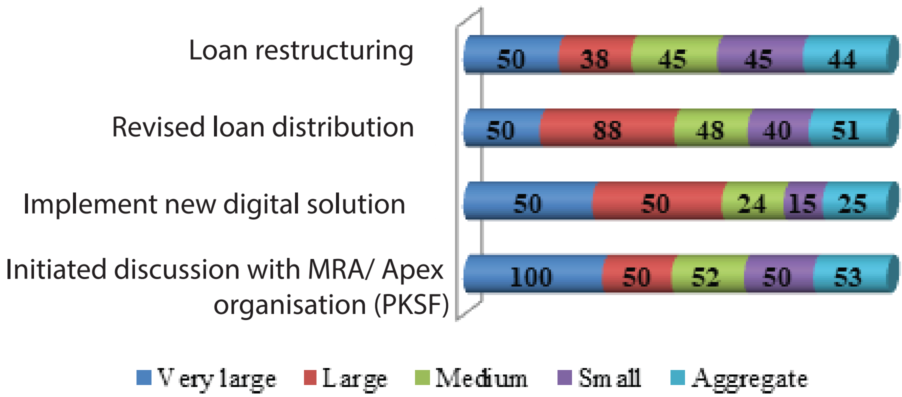
5. Covid-19 Challenges: Path from Crisis to Recovery

The majority of the MFIs have experienced severe disruption in operations and finance. For them, it has become difficult to continue the face-to-face contacts with the clients due to maintenance of social distance. Their portfolio at risk has increased while most of them have been suffering from liquidity crisis to meet operational expenses. Moreover, many MFIs are not able to collect the interest on their loans– but they have to pay the interest on their own borrowings from the commercial banks although at rescheduled terms. On the other hand, loan outstanding has increased, member saving has decreased. As a result, most MFIs have been incurring rising operational costs along with declining revenues.

The survey shows that more than half of the MFIs have initiated discussion with the regulatory authority (MRA) and apex organisation (PKSF) to revise/relax rules and regulation to meet the pandemic situation. It is seen that most MFIs acted on their own to face the Covid-19 challenges since the beginning of the pandemic. For ensuring safety, group meetings were cancelled along with physical repayment collection to maintain social distancing. Protective measures such as masks, hand sanitiser, hand soap, hand washing facilities were ensured for the staff. Around 51 per cent of the MFIs revised their loan distribution policy, mostly by the very large and large MFIs. The medium and small MFIs could exercise little leverage in revising their loan distribution policies. Nevertheless, most of them implemented restructuring in loan repayments. Almost 90 per cent of the medium and small MFIs have restructured the loan portfolio for the benefit of the clients.

Figure 5 : Measures for Dealing with Operational Crisis

(Figures in %)



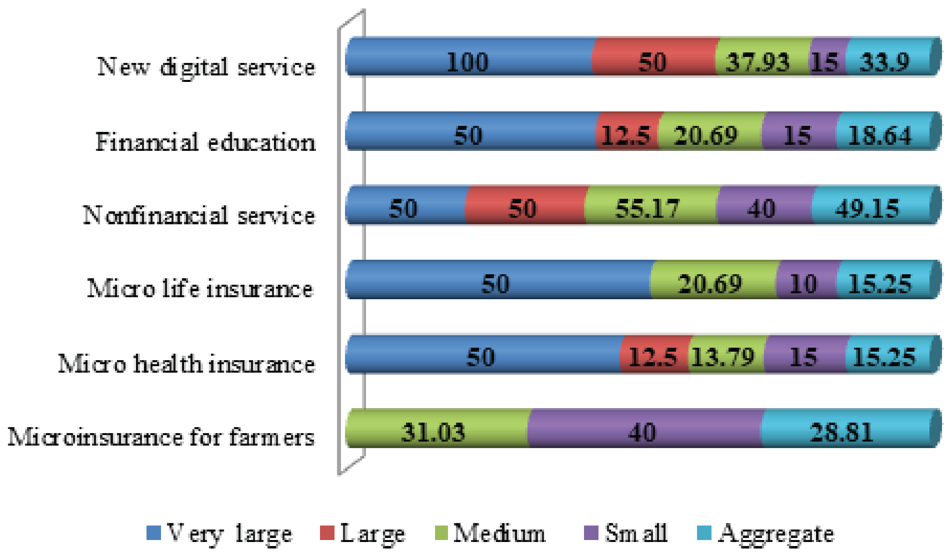
Source: InM Online Survey, September 2020

After the crisis, the loan officers were observed to have informally rescheduled the repayment period for the borrowers providing flexibility where the situation demands before the formal circular came from MRA in May 2020. To deal with the liquidity crisis, most MFIs used their own reserve funds to sustain their operations. They ensured good communications with their clients through phone calls and SMS and continued to disburse loans to farm and nonfarm microenterprises (as per MRA circular no. 57) avoiding selected Covid-19 sensitive risky investments. In addition, the MFIs curbed their operational costs by decreasing other administrative costs but keeping the staff salary/remunerations unchanged. Although around 25 per cent of the MFIs have utilised mobile financial services as the business model to disburse loan and emergency grants during the pandemic situation, medium and small MFIs report additional constraints as their business models are more dependent on human interactions between the staff and their clients and their client-base is less technology-sensitive.

As lockdowns and distancing measures have direct adverse impacts on livelihoods, the borrowers of MFIs face dangers in their survival. Many of these households have already utilised their little accumulated savings, while others have sold their livestock or other assets for meeting basic necessities. With a good track record of working closely with the government during natural calamities and other difficult times, the survey shows that around 60 per cent of the MFIs have provided emergency loans and food to the borrowers to help them get through the Covid-19 recovery process. Moreover, almost all MFIs have initiated health and hygiene awareness programmes in response to Covid-19 on a regular basis. The InM survey further shows that most MFIs are yet to adopt any longer-term recovery strategy against the impact of Covid-19. However, they plan to extend their non-financial and digital services to the clients so that they can cope with the ongoing crisis and enhance their resilience to cope with any such crisis in future.

Figure 6 : Planned Actions by MFIs to Address Covid-19 Impacts

(Figures in %)



Source: InM Online Survey, September 2020

The present survey shows that around half of the MFIs plan to extend training and technical assistance for their micro- entrepreneur borrowers and the trend is similar irrespective of the size of MFIs. It is important to note that MFIs are somewhat reluctant to take insurance product as a recovery option and this is true for all types of MFIs.

During the Covid-19 pandemic, Bangladesh has experienced a digital boom in different types of businesses. Mobile financial services have opened new windows for transferring, transacting and storing money digitally instead of cash. The commercial banks have started offering digital loans without collateral on a pilot basis enabling the entrepreneurs to access financing from their smartphones. The present survey shows that about 34 per cent of the MFIs plan to offer digital products and services to their clients at the earliest opportunity. However, the small MFIs are not too keen to take it as a recovery strategy. Only 29 per cent of the MFIs report that they have received some sort of government support mostly in the form of financial assistance and food and healthcare services for distribution to the target population. Hence, recovery strategy from the Covid-19 crisis should include a feature which is durable and resilient for the MFIs. A return to 'business as usual' without any alignment with the changes of post-pandemic world must be avoided. The recovery strategies need to cover actions that would help the MFIs and their clients to quickly get back to their normal activity levels; additionally, these should also include complementary investments and institutional behavioural changes that will reduce the likelihood of future shocks and increase the resilience of both MFIs and their clients to withstand of the shocks of any such future events.

6. Innovations and Resilience Building: A Framework for MFIs

With the specific portfolio characteristics of the members, the MFIs are prone to serious impacts from any crisis events such as the coronavirus. The portfolios of MFIs usually have a significant share of the informal sector, along with a predominance of trading activities and vulnerable borrowers who have few resources to cushion the impacts of any crisis. These population groups generally save little and invest their resources in limited-scale, low-technology intensive, and low-return economic activities. Many of these microentrepreneurs rely on this daily source of income for meeting their basic needs. Any major crisis and associated containment measures (such as the lockdown) may therefore mean that they are unlikely to pay for food, housing, healthcare, and other basic necessities for themselves and their families. Therefore, any resilience framework for the MFIs needs to create a package to support both the MFI operations as well as the stability of the income-generating activities of the members to ensure sustainability of both the MFIs and their members. Necessarily, the framework has to be comprehensive and the actions must lead to durable and resilient outcomes for the MFIs to align with the new realities of the post-pandemic world. The actions should involve both rapid and longer term policy and institutional responses that will not only generate more effective responses to any crisis when it occurs but also enhance their crisis-coping capacity to withstand any such future shocks. Keeping this in view, the innovation and resilience building framework for the MFIs should possess several key features:

- ***Protect the basic income support to the borrowing households and microentrepreneurs***

The MFIs may undertake social initiatives and actions to help the members in the fight against health and related hazards, such as technology solutions, services for the elderly, volunteering requests, food delivery services for the poor, on-line support services, and other community-based services. In addition, MFIs may launch new products for the members. For instance, new loan products may be launched comprising of loans within (say) the BDT 10,000 – BDT 50,000 bracket aiming to support businesses which have been impacted negatively by the coronavirus. Its main features may be terms typically up to 1-2 years, no interest or repayment for the first six months, no fees and hidden costs/charges, and fixed repayments with no penalty for early repayment. Further, new products such as 'Emergency Livelihood Restoration Loan' may be introduced for the members (with support from the government's assistance package with subsidised fund). The main feature of such a Fund could be a reasonable (e.g. six-month) grace period, reduced pricing, with no guarantor required.

- ***Tailored policy for medium and small MFIs***

Our analysis suggests that medium and small MFIs have been the hardest hit by Covid-19. The sharp increase in their portfolio at risk (PAR) in the Covid-19 period relative to the large MFIs and inadequacy of equity capital have made the situation worse for them to recover from the crisis. Hence, the regulatory authority may go for expanding their efforts in stabilising the medium and small MFIs by providing emergency liquidity facilities to enable them to design their own liquidity management products while designing the recovery strategy.

- ***Designing clear repayment policy***

As MRA has put some restrictions on repayment collection due to the Covid-19 crisis, the terms and conditions of deferred payment are somewhat ambiguous. The MFIs may impose accrued interest on the deferred loan to recover from the liquidity crisis. But will that be fair on poor and vulnerable borrowers? It is an important question to investigate what policies should reasonable lending follow in the aftermath of a pandemic. The MFIs may go for cross-subsidising relatively negatively impacted vulnerable borrowers while designing the recovery strategy. It is also important to mention that MRA should play a regulatory role in designing a clear repayment policy rather than letting individual MFIs decide for themselves.

- ***Exploring alternative financing tools***

It is now time for redesigning the microfinance business model in Bangladesh. In recent times, the capital structure of the MFIs is becoming increasingly dependent on the commercial banks. In the crisis/pandemic situations, banks' own liquidity may become at risk. Moreover, one must also assess the willingness of the banks to invest on the MFIs in the post-pandemic world knowing that the MFIs and their borrowers are particularly fragile to any uncertainty especially a pandemic such as Covid-19. The present experience shows that a well operating MFI can easily incur substantial losses and become financially weak in the face of a crisis. Therefore, it is time to think how the MFIs should be funded sustainably even in the face of a crisis such as the present pandemic. For ensuring sustainability of MFIs operations, it is time for Bangladesh to think of pushing the MFIs to depend more on the financial market for capital along with broad-basing their financing sources through exploring innovative financing options. There exists a wide potential of tapping multiple funding sources from the capital market, such as venture capital, crowdfunding, private equity investment, peer-to-peer (P2P) lending, and many others. The MFIs may also consider non-profit financial tools of Islamic microfinance (such as Zakah, Waqf, Qard-al-Hasan) to attract funds from Islamic multilateral development bank (i.e. Islamic Development Bank) or Muslim philanthropic investors. Just as commercial banks are operating both conventional banking and Islamic banking under the same umbrella, the MFIs may also diversify their financial portfolio along similar lines.

- ***Digital transformation***

Even during this pandemic situation, several MFIs are making transition to digital operations although to a limited scale. The MFIs have a long way to go before digital financial services change operating procedures in the sector. In the present situation, where social distancing is expected to be practiced for a long time, it is high time for the MFIs to go for collaboration with mobile financial service providers for smooth operation of loan disbursement and loan repayment; even if that occur at a limited scale considering the technological illiteracy of both the borrowers and the MFI staff. The key will be to make a beginning.

- ***Regulatory changes in the microfinance sector***

Considering the current situation where the major capital sources of the MFIs are facing liquidity crunch, the MFIs should be allowed to finance their lending by saving mobilisation. Currently, MFIs are allowed only to mobilise member savings and term deposits subject to restriction under rule 28(e) and 29(e). The MFIs should mobilise more member savings and term deposits at a higher level. It is very much desired in the present scenario when the MFIs may not sustain the long run financing of especially of the microenterprises with borrowed fund considering the current situation of the financial market. Moreover, it will also be cost-effective for them as the lending interest rate is likely to be lower.

- ***Implementing collaborative strategies***

The MFIs have developed a strong trust with their customers through face-to-face communication since their operation in the 1970s. The practice of social distancing could somewhat weaken this relationship. The MFIs therefore need to communicate clearly, set reasonable expectations, and work with their members to ensure longer-term outcomes, even if the short-term interactions remain weak. In this respect, the MRA and PKSF can play significant roles in ensuring that the MFIs are not compelled to do away with their most valuable long-term asset – that is, trust – while trying to overcome the short- and medium-term crisis.

7. Summary and Conclusions

In Bangladesh, the Covid-19 crisis has significantly disrupted the regular activities of the MFIs. Most of the MFIs (85 per cent) face difficulties in staff-customer interactions and in delivering non-financial services (88 per cent), while 83 per cent face difficulties in collection of repayments and 73 per cent encounter difficulties in new loan disbursements. These operational difficulties have intensified other financial challenges for the MFIs. Around 95 per cent of the MFIs face rising portfolio at risk (PAR). Among the very large MFIs, the PAR has more than doubled for 50 per cent; while for the rest, PAR has doubled. For all large MFIs, the PAR has doubled. On the other hand, among the medium MFIs, 59 per cent and, among the small MFIs, 55 per cent have experienced a more than doubling of their PAR; while 35 per cent of both small and medium MFIs report a doubling of PAR over their pre Covid-19 levels. Only 10 per cent of the small MFIs have relatively unchanged PAR.

Irrespective of their size category, most surveyed MFIs face similar financial difficulties due to the pandemic. About 85 per cent of the MFIs face deterioration in outstanding loan portfolio and 80 per cent face the problem of high rates of savings withdrawal by the borrowers. Around 78 per cent of the surveyed MFIs face difficulties in repaying their borrowed fund to the banks and/or other borrowing agencies. More than 73 per cent of the MFIs have inadequate equity capital to cope with the Covid-19 crisis. The MFIs strongly recognise that they are probably passing through one of the most difficult times in their long history of existence in the country. To recover from the crisis most of the MFIs have initiated some policy action. Around 51 per cent of the large MFIs have revised their loan distribution policy as per the need of their client. However, most medium and small MFIs do not have the capacity to adopt loan rescheduling measures. Although around 25 per cent of the MFIs have utilised mobile financial services as a business model to disburse loan and emergency grants during the pandemic situation, medium and small MFIs find it difficult to adopt the mobile business model as they consider their personal acquaintance and interactions with their clients as important for success and their client-base not very adaptable to technology. Therefore, recovery strategies need to cover actions that are more than getting the MFIs and clients quickly back on their normal trajectory. The study advocates for the adoption of a set of comprehensive strategies that include both behavioural changes within the MFIs and sector-wide transformations covering organisational and regulatory perspectives. Moreover, an effective response framework for the MFIs should not be a compartmentalised one; rather it should be well-coordinated across all stakeholders linking the macro and micro-developments within the microfinance sector and the overall economy.

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