

**Micro Finance – Institutional Sustain to Bhutan Progress Bank**

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**Abstract**

Progress banks are influential institutions in financing improvement. They have played a leading role in the economic upliftment of the weaker sections of the society. The paper explores the loan disbursement to agricultural and small scale industries by Bhutan Development Bank Ltd. (BDBL) and limits of the grants by Asian Development Bank to support the primary activities in the economy. The aim of the paper is to drive suggestions to support the economy from the internal resources when Bank of Bhutan Ltd. (BOBL) can play a vital role.

**Key words:** Small Scale Industries, Asian Development bank Bank of Bhutan Ltd., Bhutan Development Bank.,

**1. Introduction**

The range of cultivation, live stock and forestry is the highest in the GDP of the economy of Bhutan. Alone crops were bring Nu.12, 177 million in 2010 which increased to Nu.20, 050 millions in 2014. The percentage share of agriculture was 16.8 per cent in 2010 which increased to 16.77 per cent in the GDP of the economy, making its highest share among all the economy activities in the country (National Accounts Statistics, NSB, and Annual report2014). To save guard the existing Gross National Income and to further grow it more, banking institution includes Bank of Bhutan Ltd. (BOBL) and non banking financial institutions includes Bhutan Development Bank Ltd (BDBL) are established to inculcate the saving habits among people and to mobilize the funds to cater to the needs of rural and urban public. Modern commercial banking made its beginning in Bhutan with the setting up of the Central Bank, Royal monetary Authority (RMA) in 1982 and prior to this, functions relating to central banking were conducted by ministry of finance (1968), State Trading Corporation of Bhutan (1969), Bank of Bhutan (1968). Further in November 2007,Druk Holding and Investment (DHI) was established to hold and manage the existing and future investments of Royal government of Bhutan for the long term benefit of its shareholders, people of Bhutan (DHI, Annual Report, 2008). To support agricultural infrastructure and development in rural areas these financial institutions float short-term. Medium-term and long-term loans.

**1.1 Bank of Bhutan Ltd. (BOBL)**

Bank of Bhutan is the oldest and the largest bank in Bhutan established by Royal Charter in May 1968. The bank has monopoly until 1997. The Bank's branch sheet showed the increase in total deposits by 7.23 percent in 2013 as compared to 2012when total deposits were Nu.23.69 billion (BOBL, Annual Report,2013). This percentage increased in deposits continued to grow in 2014 by 31.15 per cent from Nu. 25.54 billion in 2013 to Nu.33.49 billion in 2014 (BOBL, Annual Report, 2014). The mentioned figures again support the saving habits of the people and the trust on the government bank. The reason the success of BOBL is basically the catering of the market from urban to rural, from educated to uneducated, from student to entrepreneurs and from industrial to agricultural sector. They try to provide their service to almost all the needs of public. The bank has 47 offices including main branch and head office. They are scattered in all 20 Dzongkhangs, Dungkhag and major townships. The bank provides various kinds of loans in different sectors of the economy from short-term to long-term loans and agriculture to personal loan. To support agricultural activities it provides loan for maximum of 6 years to finance purchase of tractors, power tillers or any other farm machinery and for orchard plantation/maintenance.

**1.2 Bhutan Development Bank Ltd. (BDBL)**

BDBL is the non banking financial institution of Bhutan incorporated by the Royal Charter, in January 1988, with the assistance of the Asian Development bank (ADB) to function as Development Financial Institute (DFI). Prior to this year BDBL was working under the name of Bhutan.

Development finance corporation ltd (BDFCL) registered under company act of kingdom of Bhutan, 2000 and financial institution act, 1992. After obtaining its banking license in March 2010 (BDBL, Annual report, 2010) it started mobilizing funds for the development of infrastructure and cottage and small scale industries in the rural sector. In 2010 the value of the total assets was Nu.3937 million which is almost the value of reserves of the bank with Royal Monetary Authority (RMA) amounting to Nu. 3802 million in 2014. The saving habit of the people and the trust in bank can be seen from the growth of demand deposits (current and saving deposits) increasing from Nu. 338 million in 2010 to Nu. 2,288 million in 2014(annual Report, 2014) but on the other hand increase in Non-performing Loans (NPL) cannot be denied which to 7.77 per cent in 2014 from 7.22 percent in 2013. There are certain constraints like rugged terrain, technology, road connectivity, scattered nature of settlement, lack of adequate market and business opportunities in rural areas which hurdles the growth path of development of industries. The above problem can be solved by the Bank Of Bhutan if it becomes a supplementary or beneficiary to the activities of BDBL.

## **2. Literature Review**

The number of development banks has increased rapidly since the 1950s (post World War 2), having been encouraged by the international bank for reconstruction and Development, IBRD (usually called the World Bank) and its affiliates. Many national development finance institutions (DFIs), as development banks were also called, were established in many countries across the globe during this period. Some of the large regional development banks include the inter-American Development Bank, established in 1959; the Asian Development Bank in 1966; and the African Development Bank in 1964 were established. The International Bank for Economic Cooperation was established in 1963 with the Soviet Union, Bulgaria, Czechoslovakia, East Germany, Hungary, Mongolia, Poland, and Romania as members. Cuba and Vietnam joined later. The core reason to establish such institutions was to finance trade and industry among its members. These nations also belonged to the International Investment Bank, established in 1970, which came into existence to loan for economic development. Development banks are local, national, regional or multilateral financial organizations that eradicate capital constraints in productive sectors and infrastructure. They are among the most widely used tools of funding and assisting in the jobs that demand long term maturity ( Mazzucato, 2011). Thus, development banks solve market imperfections that would leave either profitable projects or projects that generate positive externalities without financing (Bruck,1998; Yeyati, Micco and Panizza, 2004). Moreover, these banks can alleviate capital scarcity and promote entrepreneurial action to boost new or existing infrastructure and manufacturing (Armendariz de Aghion, 1999; Cameron, 1961; Gerschenkron, 1962). According to such industrial policy view, development banks do more than just lending to build large infrastructure projects. They also lend to companies that would not undertake projects if it was not for the availability of long-term, subsidized funding of a development bank (Rodrik, 2004; Yeyati et al., 2004). Furthermore, development banks may provide firms with capital conditional on operational improvements and performance targets (Amsden, 2001). In such circumstances, it is suggested to see the firms who borrow from development banks increasing capital investments and overall profitability after they get a loan. Bank credit is important for the growth of an economy but excessive leads to inflationary gap (khudairi, 1987) so (Catheart, 1982) said that bank credit is an important tool in financial sources. The development bank includes: a) policy banks which directly support the nation's economic policy and plans of the government as in Japan, china, Korea and Malaysia. b) Special-purpose DFIs which support focused sectors of the economy, eg., SMEs in Thailand, agriculture in India, infrastructure in Malaysia, etc. c) multi-purpose DFIs (sometimes called universal banks, in some context) which support both development projects as well as commercial businesses as can be seen in the Philippines, Indonesia, India, etc. and d) commercially-oriented development banks which support development through commercial banking services such as in Singapore. A development bank does SWOT analysis to employ project appraisal tool to find out the opportunity or threads to the project submitted for financing. Project appraisal looks at the technical, financial, marketing, management, environmental and economical aspects of the project. Loan repayment is based on the cash flow to be generated by the project. A commercial bank uses risk asset management as tool to assess the borrower. It looks at the so-called 5 C's of credit, i.e., character, capacity, capital, collateral and condition. It bases loan repayment on the capacity of the borrower to repay the amount of loan borrowed (even from other sources) than from the 'project' itself. Therefore financing is project oriented as compare to commercial bank where financing is borrower oriented.

### **3) Objectives of the study**

The aim of the is to work on the problems of scattered nature of settlement, lack technological skill, lack of managerial skill, lack of transport, lack of adequate market and business opportunity for the rural mob and to bring out the appropriate solution to boost the economy toward the growth and development. The study takes into consideration the limits of the aid by ADB and the way commercial banks can be a supporting institute to enhance and uplift the agriculture and landless farmers and to grow the number of SSI units. They can even support cottage and small scale industries.

#### **3.1 Importance of the study**

As the economy of Bhutan is not very developed and is dependent more on grants from international organizations, an internal solution can be thought of to boost the rural sector of economy where 70 per cent of the public lies (NSB, Annual Report, 2014). If properly worked on the above problems than it will not only boost employment and entrepreneurship but even can stop heavy migration towards urban area which further gives birth to lot many other problems.

#### **3.2 Credit Distribution**

- ADB, UNDP, UNCDP, IFAD, SNV are the international bodies providing different kinds of assistance for the up gradation of the Bhutan economy.
- ADB has been supporting Bhutan since 1982 with loans, grants, and technical assistance amounting to nearly \$764 million. It has approved and equity investment of \$3 million to assist mountain hazelnut, an organization promoting hazelnut production by small holder farmers in Bhutan to help them diversify and boost their incomes. They are also getting technical assistance fully financed by government of Sweden and Canada. For the financing of hazelnut project other assistance is being provided by international financial corporation (IFC), a member of the World Bank group with \$3 million from the global agriculture and food security program. It is being expected that as much as 15% of Bhutan's total population is eventually being benefited from the project but all this activities have limit of US \$5 million from ADB approved by RGoB.
- ADB gives for MSME Nu 22,690,000 @ of 4 per cent interest rate for 20 years (including 5 years grace period). Based on the annual reports of BDBL from 2009 to 2014 and national statistical year Book, 2014.
- It was found that bank had increased its total client by 14 per cent from 40712 in 2013 to 46,326 in 2014 in which rural client were 37,569 in number in 2013 and this number is increase by 14.5 in 2014 and reached to 43,009. In terms of granting loans it was Nu.6.23 billion in 2014 and as compared to previous year. A change is seen in the ratio of amount to rural and urban public. It was 53:47 in 2013 and the ratio changed to 57:43 in 2014 which shows the demand of agriculture in rural sector. In the overall lending in 2014, 24 per cent is to agriculture sector and client wise the sector has 47 per cent of total client. The bank has started its services in six Gewogs out of 205 Gewogs in the country.
- The bank also established business opportunity and information centre (BoiC) in august, 2014 to boost cottage and small scale industries.
- The main branch has the highest deposit amounting to Nu. 9,628 million in 2014 from Nu. 4769 million in 2013 but as far deposit accounts are concerned; it is highest in western region followed by eastern, central and main branch simultaneously in both the years. The percentage of credit accounts for agriculture is the highest with 47 per cent in 2014 from 21 per cent in 2013 and lowest in manufacturing and industry with 1 per cent only in both the years. When it comes to repayment of loans, agriculture again stands at the top with 24 per cent outstanding in 2014 but manufacturing and industry has only 7 per cent in 2014 which is 1 per cent less as compared to 8 per cent in 2013.
- The overall NPL of BDBL increased to 7.77 per cent during 2014 from 7.22 per cent in 2013.
- In the year 2008, 17.03 per cent was the loan given to manufacturing/industry and the percentage of nonperforming asset (NPA) was only 4.39 per cent.

### **5. Suggestion to the problems**

- The international organization providing grants to the country is limited and restricted to the certain sectors, areas and activities. They provide loans for capital establishment and infrastructure but for day to day transaction BOBL can support the working capital need of BDBL. The growth NPA for BOBL has decreased to 4.96 per cent from 6.88 per cent as an outcome of the connectivity with the people of Bhutan. BOBL has its branches in almost in all the 205 Gewogs of the country and the demand for development bank is more in rural areas with the change in the ratios of urban and rural demand.

- The banks can play an important role by bringing out special integrated rural development programme which can act as a strategic step taken to eradicate poverty from the rural societies. Based on the consolidated progress report supplementary assistance can be given to those who are still under poverty line and new beneficiaries can be selected to be assisted by the bank in such a way that they are able to come out of poverty.
- RMA can give flexibility and discretionary powers to the bank managers of lending bank in term of collateral, margin, security, introduction of composite cash credit limits to cover farmers' production, post harvest and household requirements, etc. they can simplify the applications for farmers.
- Commercial banks can be expected to enlarge credit to the priority sectors and can ensure a minimum of fix percentage to be directed towards the advancement of weaker sections of the society. BOB's annual report, 2014 did not show any kind of loan advancement to agriculture and trade had a very small share of only 6 percent.
- Cooperative farming can be suggested for the problem of the scattered nature of land which does not result into economies of scale. It can further solve the problem of risk being shared of many people and an individual is not burdened with the cost. To aid such activities country can have the concept of cooperative societies by pools the resources at one place.
- There are certain places which are still not connected with small scale industries. Places like Trashigang having population of around 56,200; Monggar region with 44,300 populations has negligible amount of industries. The mean annual household income in Trashigang is around 9,623 and for Monggar it is 13,063 only (NSB,RgoB, Annual Report, 2014). So equitable distribution of resources is another suggestion which can be given for the allocation of funds based on population and mean average income.

## **6. Conclusion**

It has been seen that cottage and small scale industries make up an overwhelming (approximately 98%) of all industries in most countries, including Bhutan. Therefore, the need arises to take strategic steps to uplift the weaker section of the society which is to be motivated by providing sufficient funds for technical, marketing and managerial assistance. The government can safeguard itself from bad debts by framing proper policies of invigilation and guidance so that appropriate steps are taken before the industry is declared sick or agricultural loan is converted into NPL.

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