

# Facilitating Access to Finance for Household Investment in Sanitation in Bangladesh

August 2016

## Summary Overview

**Location:** Bangladesh, South Asia

**Approach to Blended Finance:** The provision of an output-based aid (OBA) subsidy to microfinance institutions (MFIs) in Bangladesh is used to help MFIs develop sanitation products and extend their reach to poorer households.

Microfinance (the provision of financial services to low-income people) is emerging as a viable avenue to facilitate increased access to finance for households to water and sanitation products, and for small-scale water service providers' business development. OBA is a form of results-based financing where subsidies are paid to service providers based on verification of pre-agreed water and sanitation project targets defined during project design, thereby offering a strong incentive for the delivery of results. Combining an OBA subsidy with a microfinance loan helps reduce households' cash constraints by spreading repayment over time, and makes investment in improved sanitation more affordable overall.

## Context

Bangladesh has made progress in improving sanitation nationwide, with an open defecation rate reduced to one percent of the population. However, as of 2015 only 61 percent of Bangladeshis relied on improved sanitation facilities according to JMP statistics.

In Bangladesh, households primarily invest their own financial resources in latrine purchase and installation. Many have the ability (and often willingness) to invest in building improved sanitation facilities but they are often cash-constrained. The upfront costs of a toilet or piped



water connection can be prohibitive. Businesses operating in the rural sanitation sector are very small, which inhibits their ability to develop better-suited latrine models and to access credit. These businesses are unable to offer poor households the option of paying in installments and of spreading purchase costs over time. Microfinance institutions (MFIs) are well positioned to help on this front, as they provide financial services across their client networks, and can tailor loans to meet local needs.

Over the last few years, the World Bank has been working in partnership with the Government of Bangladesh to support its sanitation initiatives and encourage private sector involvement in rural sanitation. A pilot sanitation marketing initiative to leverage private sector resources and help households adopt improved sanitation was implemented in Bangladesh in 2009, and was scaled up in 2011 after successful results.

## Financial Structure and Approach to Blended Finance

In 2016, the World Bank approved funding to an output-based aid (OBA) program which channels OBA subsidies to two leading MFIs, the Association for Social Advancement (ASA, the second largest microcredit lending institution worldwide) and the Palli Karma-Sahayak Foundation (PKSF, the Government of Bangladesh’s wholesale microfinance facility).

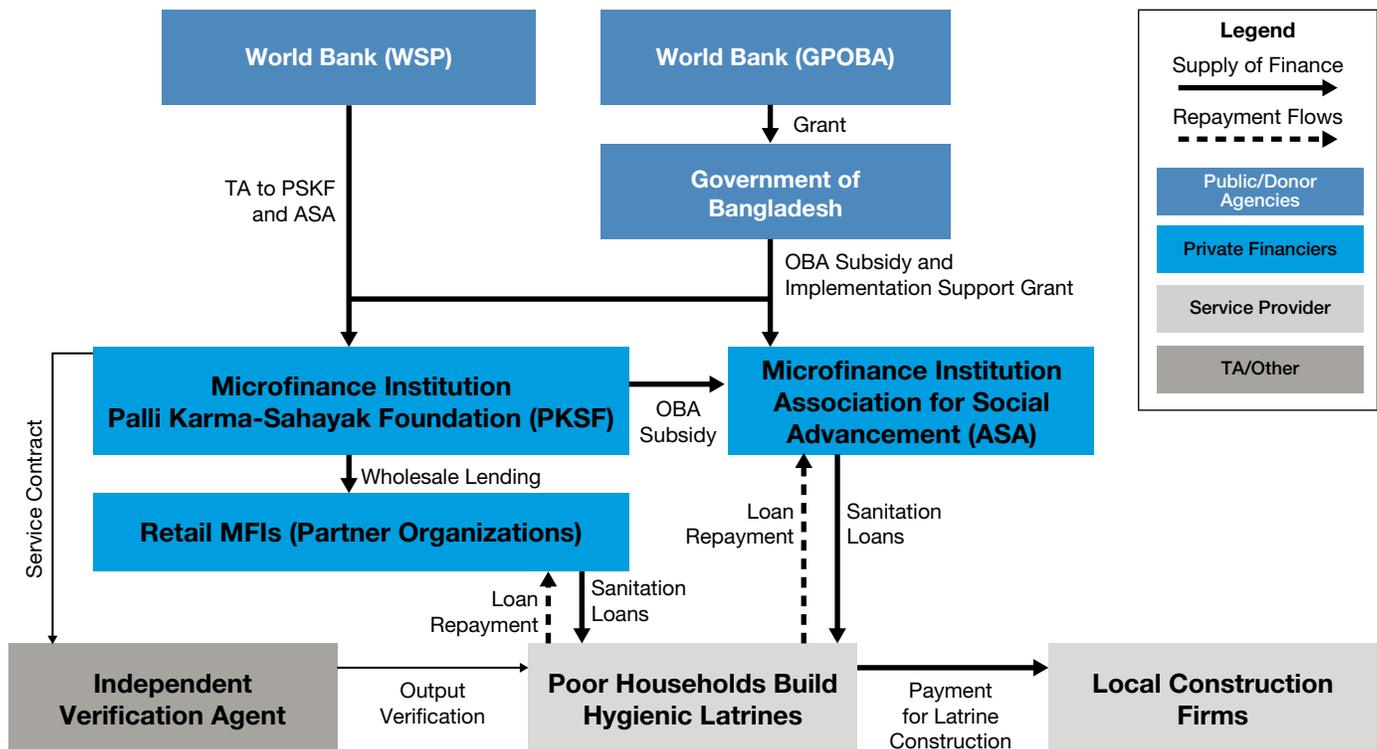
The World Bank is facilitating the provision of loan products to the two MFIs through a US\$3 million OBA subsidy to target poor households. Blending of concessional and commercial financing occurs as the grant is provided directly to the MFIs, ASA, and PKSF, both of which use their own funds to provide pre-financing to households. PKSF provides wholesale loan financing to retail MFIs (partner organizations) to finance household sanitation loans and ASA provides sanitation loans directly to households. Households use the loans to pay trained and pre-certified local construction firms for hygienic

latrine construction. The cost of the latrines built under the program range between US\$45 and US\$220, but the subsidy only applies to loans up to US\$128, as a way to ensure that comparatively richer households do not divert the subsidy to finance more expensive installations.

Figure 1 shows the financial structure for the OBA program.

The OBA subsidy will amount to US\$5-16 per household, and will be paid upon independent verification that the agreed outputs have been achieved. The subsidy will effectively reduce households’ weekly repayment by 11 percent. Loans can be paid off in weekly installments over a period of 55 weeks, allowing households to more easily spread the cost of purchasing materials over time. The partial subsidy both enhances the attractiveness of borrowing by increasing access and affordability of higher-quality options for poor households, and reduces lending risk for the MFI.

**FIGURE 1** Facilitating Access to Finance for Household Investment in Sanitation, Bangladesh: Financial Structure



Complementary technical assistance will be provided through the Water and Sanitation Program of the World Bank under the GPOBA project. WSP implemented an earlier technical assistance program in Bangladesh to help poor households in rural areas access affordable, high-quality sanitation facilities from small firms. The new program will maintain features of the original, and will support demand creation and market promotion through awareness raising activities. It will ensure follow-up support to trained entrepreneurs to guarantee quality construction, and help MFIs reach the poorest households. Such technical assistance is likely to be critical to scale-up the approach and for sustainability.

## Results

The OBA project is expected to start implementation in late 2016, so there are no concrete results to date. The selected MFIs are in the process of developing specialized loan products for low-income rural households to help them finance the purchase of sanitation systems, and to extend loans to microbusinesses trained on hygienic latrine construction and sale.

The intervention aims to expand product availability by targeting the traditional constraints that limit access to finance for households. Projections indicate that approximately US\$22 million in household contributions will be leveraged.

## Lessons Learned

**Providing OBA subsidies to microfinance institutions is one way of facilitating the expansion of sanitation microfinance by increasing the size of the client base that can afford to borrow.** The resulting increase in sector investment allows sanitation entrepreneurs to increase their earnings, thereby enhancing sustainability, and in turn, expanding their offerings and services.

**The leveraging of grants helps cash-constrained households.** Many households are willing and able to invest in improved sanitation solutions, but they are not able to mobilize sufficient funding to invest, and need assistance to be able to spread the costs of such an investment over time. The blending of OBA with MFI loans targets reducing this affordability constraint

through: (1) lowering the latrine cost; and (2) spreading repayment out in weekly installments over the course of a year, making it more manageable.

**Well-designed subsidies can be catalytic for the development of rural sanitation markets.** The strategic use of subsidies, for example for sanitation marketing or to expand the reach of sanitation microfinance, can help create a demonstration effect for sanitation lending at scale via other MFIs.

## References

- Ikeda, J. and H. Arney. 2015. *Financing Water and Sanitation for the Poor: The role of Microfinance institutions in addressing the water and sanitation gap*. Water and Sanitation Program: Learning Note. World Bank: Washington, DC.
- Ikeda, J. and R. Ahmed. 2015. *Building Markets for Rural Sanitation: Lessons Learned in Bangladesh*. Water and Sanitation Program. World Bank: Washington, DC.
- WEF OECD. 2015. *Blended Finance Vol. 1: A Primer for Development Finance and Philanthropic Funders*. Geneva: World Economic Forum.
- World Bank. 2016. *Bangladesh OBA Sanitation Microfinance Program (Project Paper)*. Washington, DC: World Bank Group.

This case study is part of a series prepared by the World Bank's Water Global Practice to highlight existing blended finance experiences in the water sector.

Blended finance refers to “the strategic use of development finance and philanthropic funds to mobilize private capital flows to emerging and frontier markets,” as per the OECD definition (WEF OECD, 2015). Concessional funds can be used in a catalytic manner to open up new opportunities for commercial financing, by providing technical assistance to borrowers and lenders to help them become more familiar with each other, help structure transactions, provide credit enhancement mechanisms, etc.

Private capital flows can help with meeting immediate financing needs for investment in the water sector but ultimately need to be repaid. Repayable financing from private sources to the water sector can come in various forms, including as commercial bank loans, bonds or equity. To obtain such financing, water-sector actors need to be able to repay the borrowed amounts and the associated funding costs, which means that they need to be deemed “creditworthy” by providers of finance.

#### Contact Us

For further information please contact Joel Kolker ([jkolker@worldbank.org](mailto:jkolker@worldbank.org)) or Sophie Trémolet ([stremolet@worldbank.org](mailto:stremolet@worldbank.org)).

#### Disclaimer

© 2016 International Bank for Reconstruction and Development / The World Bank. Some rights reserved. The findings, interpretations, and conclusions expressed in this work do not necessarily reflect the views of The World Bank, its Board of Executive Directors, or the governments they represent. The World Bank does not guarantee the accuracy of the data included in this work. The boundaries, colors, denominations, and other information shown on any map in this work do not imply any judgement on the part of The World Bank concerning the legal status of any territory or the endorsement or acceptance of such boundaries. This work is subject to a CC BY 3.0 IGO license (<https://creativecommons.org/licenses/by/3.0/igo>). The World Bank does not necessarily own each component of the content. It is your responsibility to determine whether permission is needed for reuse and to obtain permission from the copyright owner. If you have questions, email [pubrights@worldbank.org](mailto:pubrights@worldbank.org).