



Social Accountability of Microfinance Institutions in South Asian Region

**Iftekhhar Ahmed^{1*}, Abul Bashar Bhuiyan^{2,3}, Yusnidah Ibrahim⁴, Jamaliah Said⁵,
Mohammed Fuad Mohd Salleh⁶**

¹School of Economics, Finance & Banking, College of Business, Universiti Utara Malaysia, Kedah, Malaysia, ²Faculty of Business, Universiti Selangor, Selangor, Malaysia, ³Accounting Research Institute, Universiti Teknologi MARA, Selangor, Malaysia, ⁴School of Economics, Finance & Banking, College of Business, Universiti Utara Malaysia, Kedah, Malaysia, ⁵Accounting Research Institute, Universiti Teknologi MARA, Selangor, Malaysia, ⁶Faculty of Business, Universiti Selangor, Selangor, Malaysia.

*Email: iftekhharhbs@gmail.com

ABSTRACT

The purpose of the study is to examine the social accountability and argue comparison of outreach level of microfinance institutions (MFIs) in member countries of South Asian Association for Regional Cooperation. The inquiry has employed quantitative research approach to meticulous secondary data that has quantify using financial ratio and multiple regression analysis. Our results expose that gross loan portfolio (GLP) has significant positive relation with the number of clients served. Conversely, the average loan balance per borrower per gross national income per capital and average outstanding balance have significant negative relation to the dependent variable. On the other hand, the yield on a GLP, size of MFIs and operational self-sufficiency has insignificant effect to the number of active borrowers. Eventually the study found no evidence of trade-off between profitability and outreach breadth. However, interest rate, board and ownership structure and outreach depth issue suggested for the further studies.

Keywords: Microfinance, Accountability, Outreach, Mission Drift, South Asia

JEL Classifications: G21, G32, O18

1. INTRODUCTION

Microfinance is the alternative approach of collateral free loan service provider to the poorest populations in rural area. Traditional bank has ignored these populations because the lack of collateral and the weak legitimate practice will be unable to secure loans repayment if the client reneges on loan. The borrowing options, therefore, was shut down for the poor from the traditional credit service provider and the circumstances lead to the continuous poverty and economic inequality. Collateral free micro-credit loan service therefore received enthusiastic acceptance (Beck et al., 2007). Moreover, the innovative approach of micro-lending to the social bottom line (reach out to the poorest) and client's involvement in profit generating micro-enterprise ensure comparatively very high loan repayment (Armendariz and Morduch, 2005).

Nevertheless, the high repayment of loans yet unable to makesure the profitability for microfinance institutions (MFIs). Therefore, MFIs still extensively depend on various local and international donors. As a result, the greatest debate on microfinance profitability and sustainability yet to be solve (Morduch, 1999). In a different perspective there is a call for more commercialization of microfinance program to access the available large asset and finance their further operational expenses, thus greater number of poor populations will be served (Ghosh and Van Tassel, 2008; Morduch, 2000). Once MFIs able to reach their profitability from their own operations they can start borrowing from commercial sector and reduce donor dependency. Pursuing the profitability will increase the poorest populations in loan which is the prime concern of microfinance program.

However, the controversy arise here too on whom to serve (target group), and the level of poor people to serve (poverty level).

Navajas et al. (2000) argued that MFIs lending credit to the households those are nearly to the poverty line, however, most of them are the richest among the poor. There are some families whose income about to poverty line, on the other hand, some living under lower subsistence frontier. Few of them employed, few might involved in setting up micro-venture and others are unemployed. The very poor can realize the benefit of microfinance from its consumption smoothness (Morduch, 1998; Zeller and Johannsen, 2006). Several studies also confirmed that competition in microfinance industry also effects outreach of MFIs in different region (Hartarska and Nadolnyak, 2007; Olivares-Polanco, 2005).

The South Asian Association for Regional Cooperation or SAARC is a geopolitical and economic cooperative organization consist of eight South Asian countries. SAARC comprises 3% of total global land area and contains 21% of total global population. It also has 9.12% of global GDP. Apart from that, SAARC is the home of global top ranked MFIs and the birth place of microfinance. A large portion of the total population in the SAARC region are living under poverty line, thus MFIs are able to create visible impact in the rural community of this region. However, the impact mostly linked to institution's sustainable operation and merely to social accountability.

Number of studies found where social accountability of MFIs has been examine from different perspectives. Among those, few studies identified where outreach has been discussed from the corner side of microfinance objective while most of the studies analyze profitability issue in microfinance industry as concern of sustainability is taking place everywhere. However only minimal study conducted to analyze the social accountability of MFIs though none of them in SAARC region. This study therefore, aims to quantify the result from empirical corner and compare the level of breadth of outreach as a proxy of social accountability of SAARC-MFIs.

2. LITERATURE REVIEW

Professor Yunus invested his idea of micro-lending to the poor who are unserve by commercial bank because of their poverty in Bangladesh. The poor commonly considered as proper client for microfinance because they can involve in profit making venture and repay their interest for loan have taken (Morduch, 2000). Poverty and vulnerability create entrepreneurial spirit in the mind of poor people and influence them to change their destiny (Im and Sun, 2014). But they need law enforcement to protect private properties; thus poor borrower will have incentives to generate wealth and enrich prosperity (Ding et al., 2014; Peng et al., 2009).

From the sustainability perspective, profitability of MFIs could be very close issue to the outreach of social bottom line as it will keep sustain the institutions to serve more client (Yunus, 2007). Conversely profit seeking for MFIs also has negative impact on outreach as it increase operational cost to serve the poorest populations (Cull et al., 2007; Mersland and Strøm, 2010). However, a recent study propose a comprehensive model that include financial sustainability and outreach as endogenous variables and the results disclose that financial sustainability does

not badly affect to the depth or breath of outreach (Nurmakhanova et al., 2015).

Another examination has taken place by Meyer (2015) where she analyze the interaction between social and financial returns in microfinance. A multivariate regression models has ran using 1508 observations on MFIs for the period of 2004 to 2010. The result found strong evidence that MFIs can achieve higher portfolio yields from more social outreach (Meyer, 2015). On the other hand, Quayes (2015) has conducted a panel investigation on possible trade-off between outreach and performance using 764 MFIs from 87 countries. The empirical results of this study revealed that financial performance of MFIs can be boosted by the reach out to the poor (Quayes, 2015). Consequently, both recent studies confirm microfinance institutions can achieve better financial performance from their social outreach, however, some market oriented strategies need to be applied.

A study on Savings and Credit Cooperative Societies of Tanzania revealed that both product development and market development have significant contribution on outreach performance (Jeje, 2014). However, sometime this relationship of outreach and financial performance can be represent negative from the country context. Indeed a study has been taken place with an assumption that financial performance and outreach in Ethiopian microfinance institutions is not related. The hypothesis has tested with three outreach and two financial sustainability indicators based on five MFIs. The study concluded with negative trade-off between financial performance and outreach in Ethiopian microfinance institutions (Gashayie, 2014).

Governance and board composition are new concern of microfinance institutions' performance and outreach. In some region such as Central and Eastern Europe and New Independent Nations, the external governance mechanisms played minimal role in microfinance institutions (Hartarska, 2005). However, sustainability and outreach also has tradeoff based on stakeholders' representation on the board, therefore independent boards with limited employee participation advised (Hartarska, 2005). A recent study identified board composition and outreach to the poor of MFIs appear to be related. If the MFI has independent higher share, foreign, and/or women member in the board then the outreach of that institutions will improve (Mori et al., 2015).

3. DATA AND VARIABLES

The data has used in this study had acquired from microfinance information exchange (MIX) market that is the most extensive online database of cross-country information for MFIs. In the method of obtaining data the study aims to collect MFIs' information that fall into the period of 2008-2012 and related data for the inquiry must be available. Moreover, the study chose MFIs that operate in SAARC region and particularly non-governmental organization (NGOs) with highest number of active borrowers. As a result, MFIs from Bhutan and Maldives were excluded from this study due to their unavailability of required data.

That provides six major NGO MFIs from the SAARC region that hosts prime percentage of the total clients from the respected

country. As the study focus on NGOs therefore, banks, credit unions, rural banks and non-bank financial institutions have excluded. Moreover, institutions with the highest active borrowers assert that the institutions are performing microcredit lending activities as primary operations and that also shows their aim toward social accountability. The list of MFIs chosen to conduct this study has shown at the Table 1.

Performance indicators used in this study will be based on study by Bhuiyan et al. (2011) and Microfinance Consensus Guidelines such as percentage of women borrowers, average loan balance per borrower, average loan balance per borrower/gross national income (GNI) per capita, average outstanding balance (AOB), AOB/GNI per capita, average deposit balance per depositor/GNI per capita and average deposit balance per depositor/GNI per capita (Bhuiyan et al., 2011). The indicators used are the standardized measure of MFIs performance as suggested by the guidelines from the Consultative Group to Assist the Poor (CGAP, 2003). Items and the formula for each indicator are listed at the Table 2.

The number of active clients includes borrowers, depositors, and other clients who are currently accessing any financial services. This indicator is more useful than the cumulative number of loans made or clients served during a period. The AOB includes only loan amounts that clients have not yet repaid, or savings that clients have not withdrawn. Expressing average balance as a percentage of GNI per capita allows for a comparison of how deeply MFIs from different countries reach down in their own national income distributions. Some regard an average outstanding loan balance below 20% of per capita GNI as a rough indication that clients are very poor. The MIX classifies lenders as being MFIs if their average outstanding loan balance is not above 250% of per capita GNI (Table 2).

Furthermore, multiple regression models have been used to measure the outreach performance of MFIs in the SAARC region. Variables used for the regression analysis have been identified from previous literature. It has also found these variables often used to measure outreach in various studies. Number of active borrower represent the number of individual who borrow or/and save with the MFIs. Higher number of active borrower implies the institution’s intention to serve wider poor clients, that also considers as “breadth” of outreach. Conversely percentage of female borrower represent as “depth” of outreach. Women borrower usually borrow smaller loan which is costly for the institution. This study will focus on number of active borrower as the indicator of “breadth” of outreach. Next section will describe more about variables used in this study.

Model for the regression of breadth of outreach:

$$\ln NAB_{it} = \alpha_1 + \beta_1 OSS_{it} + \beta_2 YIELD_{it} + \beta_3 ALBPBG_{it} + \beta_4 \ln SIZE_{it} + \beta_5 \ln GLP_{it} + \beta_6 \ln AOB_{it} + \epsilon_{it}$$

Where, $\ln NAB_{it}$ is the number of active borrower ratio which indicate breadth of outreach of MFI_i at time t (the dependent variable), α_1 is a constant term, β measures the partial effect of

independent or explanatory variables in period t for the unit i (MFI), X_{it} represents the explanatory variables as described in the Table 3, and ϵ_{it} is the error term. The variables, both dependent and independent, denote cross-section unit i at time t, where i = MFI (1 to n), and t = 1 to 5.

4. EMPIRICAL RESULTS

4.1. Comparison of Outreach of MFIs in the SAARC Region

Percentage of women borrowers consider as a core indicator of outreach in microfinance industries. The study found both Building Resources Across Communities (BRAC)-LKA of Sri Lanka and Jeevan Bikas Samaj (JBS) of Nepal have the highest percentage of women borrowers at 100% which represent their highest possible outreach in this region. BRAC-AFG of Afghanistan has the highest average loan balance per borrower at 235.82 with Shri Kshetra Dharmasthala Rural Development Project (SKDRDP) of India coming second highest at 173.35. As average outstanding loan balance below 20% of per capita GNI is a rough indication that clients are very poor, that means five out of six MFIs of South

Table 1: Selected MFIs

Country	Name of institutions	Legal status
Bangladesh	Building Resources Across Communities (BRAC)	NGO
Afghanistan	BRAC Afghanistan	NGO
Sri Lanka	BRAC Lanka (Guarantee) Limited	NGO
Nepal	Jeevan Bikas Samaj (JBS)	NGO
Pakistan	National Rural Support Programme (NRSP)	NGO
India	Shri Kshetra Dharmasthala Rural Development Project (SKDRDP)	NGO

NGO: Non-governmental organization, MFI: Microfinance institutions

Table 2: The outreach measurement indicators and ratios

Outreach indicators for comparison	
Name of ratios	Equations
Percentage of women borrowers (%)	$\frac{\text{Number of active women borrowers}}{\text{Number of active borrowers}}$
Average loan balance per borrower	$\frac{GLP}{\text{Number of active borrowers}}$
Average loan balance per borrower/GNI per capita	$\frac{\text{Average loan balance per borrower}}{GNI \text{ per capita}}$
AOB	$\frac{GLP}{\text{Number of loans outstanding}}$
AOB/GNI per capita	$\frac{AOB}{GNI \text{ per capita}}$
Average deposit balance per depositor	$\frac{\text{Depositors}}{\text{Number of deposit accounts}}$
Average deposit balance per depositor/GNI per capita	$\frac{\text{Average deposit balance per depositor}}{GNI \text{ per capita}}$

Source: Microfinance Consensus Guidelines (CGAP, 2003). GNI: Gross national income, GLP: Gross loan portfolio, AOB: Average outstanding balance

Asia have successfully reach their social objective and they are efficient enough to reach out to the very poor. Those are BRAC, BRAC-LKA, JBS, National Rural Support Programme (NRSP) and SKDRDP and their average value has found 0.1834, 0.0562, 0.1611, 0.1340 and 0.1048 respectively, in percentage it will be 18.34%, 5.62%, 16.11%, 13.40% and 10.48%. Besides, average value of AOB per GNI per capita for BRAC-AFG stands at 0.5308 which couldn't fall in the range to indicate that clients are very poor. Moreover JBS of Nepal has the highest value for average deposit balance per depositor and BRAC-AFG of Afghanistan has the highest value for average deposit account balance but this measurement is not really comparable as NRSP of Pakistan and SKDRDP of India don't exhibit their data (Table 4).

4.2. Regression Results and Discussion

The study found that estimated result of multiple regression analysis is also quite satisfactory level where the adjusted R^2 is 0.985 and observed R^2 value is 0.988 respectively. The value of adjusted R^2 revealed that there are good relationships with dependent variables and independent variables where all independent variables can able explain about 98.5% to the number of active borrower, indicator of breadth of outreach. On the other hand, the ANOVA table also reflected about the goodness of model and F-test estimated that the regression is quite meaningful in the sense that the dependent variable is related to each specific

explanatory variable. The linear relation of the model is highly significant where the value of F-statistics has found at 325.087 which are within acceptance range.

Furthermore, the result of this model also confirmed that there is little multicollinearity problem between size of MFI and gross loan portfolio (GLP). Moreover, this study employed the technique of the collinearity diagnostics to eliminate the problem of the multicollinearity. Besides, the study has found Durbin–Watson value at 1.521 which also falls in acceptance range and shows strong positive correlation. In addition, the linear relation of the model is highly significant where the P value for the $F < 0.001$ percent level. On opposed, the estimated coefficient also denoted from the model that most of variables significantly related at the 0.01 and 0.05 levels, which is significantly different than zero.

The regression result also revealed that only GLP (lnGLP) has significant positive relation with the breadth of outreach. We employed the log form of GLP data to analyze in regression model. Conversely average loan balance per borrower per GNI per capital (ALBPBG) and AOB (lnAOB) have significant negative relation to the dependent variable. Although many previous studies concluded that average loan balance per borrower per GNI per capital (ALBPBG) and/or AOB (lnAOB) have significant positive correlation but this study has found reverse result. On the other

Table 3: Variables of the study

Variables standard name	Description	Variable name in regression model
Number of active borrower	Number of borrowers with loans outstanding, adjusted for standardized write-offs	lnNAB*
OSS	Financial revenue/(financial expenses+impairment losses+operating expenses)	OSS
Yield on GLP (nominal)	Adjusted financial revenue from loan portfolio/adjusted average GLP	YIELD
Average loan balance per borrower/GNI per capita	(Average total loans/average total number of borrowers)/GNI per capita	ALBPBG
Size of MFIs	Size in term of total asset of MFI	lnSIZE*
GLP	Average GLP	lnGLP*
AOB	GLP/number of loans outstanding	lnAOB*

*Variables have presented in their log form for regression purpose. OSS: Operational self-sufficiency, GNI: Gross national income, GLP: Gross loan portfolio, AOB: Average outstanding balance, MFI: Microfinance institutions

Table 4: Comparison within MFIs of the SAARC region

Elements	Benchmark					
	BRAC	BRAC-AFG	BRAC-LKA	JBS	NRSP	SKDRDP
	Bangladesh	Afghanistan	Sri Lanka	Nepal	Pakistan	India
Number of active borrowers	5,434,625	148,524	64,124	42,986	373,418	1,347,824
Percent of female borrowers	96.33	87.44	100	100	64.37	65.68
GLP	659,634,925.9	35,233,981	8,337,373.21	6,314,652.9	52,993,444.94	230,048,238.5
Average loan balance per borrower	125.38	235.82	128.23	136.87	141.11	173.35
Average loan balance per borrower/GNI per capita	0.1925	0.5308	0.0562	0.2825	0.1340	0.1268
AOB	119.06	235.82	128.23	75.76	141.11	138.28
AOB/GNI per capita	0.1834	0.5308	0.0562	0.1611	0.1340	0.1048
Average deposit balance per depositor	37.83	37.51	26.08	47.18	-	-
Average deposit balance per depositor/GNI per capita	0.06	0.08	0.01	0.1	-	-

Source: Authors computation based on data from MIX Market database (MIX, 2015). GLP: Gross loan portfolio, AOB: Average outstanding balance, MFI: Microfinance institutions, GNI: Gross national income, BRAC: Building Resources Across Communities, JBS: Jeevan Bikas Samaj, NRSP: National Rural Support Programme, SKDRDP: Shri Kshetra Dharmasthala Rural Development Project

Table 5: Regression result of the study

Model	Unstandardized coefficients		Standardized coefficients	T	Significant	Collinearity Statistics	
	B	Standard error	Beta			Tolerance	VIF
1							
(Constant)	-1.908	0.983		-1.942	0.064		
OSS	-0.478	0.334	-0.041	-1.432	0.166	0.605	1.653
YIELD	0.701	0.630	0.030	1.113	0.277	0.696	1.437
Average loan balance per borrower	-0.803**	0.304	-0.068	-2.645	0.014	0.758	1.319
lnSIZE	0.288	0.187	0.281	1.537	0.138	0.015	66.106
lnGLP	0.734***	0.183	0.740	4.017	0.001	0.015	66.974
lnAOB	-0.621***	0.160	-0.123	-3.894	0.001	0.511	1.958
R ²	0.988						
Adjusted R ²	0.985						
F	325.087						
Durbin-Watson	1.521						

***Significant at 0.01 level; **Significant at 0.05 level. GLP: Gross loan portfolio, AOB: Average outstanding balance, OSS: Operational self-sufficiency, VIF: Variance inflation factor

hand, yield on GLP (YIELD) and size of MFI (lnSIZE) have identified as insignificant positive effect to the number of active borrower.

However, between this two variables size of MFI has more positive impact toward breadth of outreach, resulted from the regression outcomes. Operational self-sufficiency (OSS) has insignificant negative effect to the dependent variable of the study. OSS and YIELD often use indicators to analyze financial performance or profitability of MFI along with others. Therefore we also included them into our study to justify the trade-off between profitability and outreach, in other word mission-drift. However the study found negative trade-off between profitability and outreach as both of the indicators resulted insignificant level. Furthermore the study tested ANOVA analysis and found it at significant level (Table 5).

5. CONCLUSION

The study attempted to look upon breadth of outreach of the SAARC MFIs and argue their reach out level. Only NGOs have been tested for the study based on the highest number active borrower. The study has concluded that, GLP (lnGLP) has significant positive relation with the breadth of outreach. Conversely average loan balance per borrower per GNI per capita (ALBPBG) and AOB (lnAOB) have significant negative relation to the dependent variable. On the other hand, yield on GLP (YIELD) and size of MFI (lnSIZE) have identified as insignificant positive effect to the number of active borrower. Furthermore, OSS has insignificant negative effect to the dependent variable of the study. Eventually the study found negative trade-off between profitability and outreach as both of the indicators resulted insignificant level. Moreover, based on average outstanding loan balance per capita GNI the results also resolved that five MFIs are able to reach to the social bottom line among selected six MFIs in this region. Alternatively, BRAC-LKA and JBS identified with full percentage of female borrower which also presents their strong reach out to the poor, also consider depth of outreach. There are other relationship also has identified from the study such as competition, interest rate, governance, board and ownership structure issue which we recommend for further study.

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