



GLOBAL JOURNAL OF MANAGEMENT AND BUSINESS RESEARCH: C
FINANCE

Volume 15 Issue 8 Version 1.0 Year 2015

Type: Double Blind Peer Reviewed International Research Journal

Publisher: Global Journals Inc. (USA)

Online ISSN: 2249-4588 & Print ISSN: 0975-5853

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GJMBR - C Classification : JELCode : E59



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Contribution of Riba-Free Banking System on Rural Development in Bangladesh: A Projection for Vision-21

Dr. Hossain Shahid Shohrwardhy^a, Md. Alauddin^σ & Mohammad Alauddin^p

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I. INTRODUCTION

Riba-Free Banking System (RFBS) is the most powerful economic factor in the world. In the session 2006-2007, the World Financial Crisis occurred due to the rival of RFBS instead of Conventional Banking System (CBS) (Nizam, 2012). RFBS had passed golden jubilee in 2013. On that time, Bangladesh had also gathered a 30-year experience, knowledge and the existence of RFBS. At present, RFBS in Bangladesh has a strong market share viz. 45.28%. There are 8 full pledged (15.09%) and 16 conventional banks which comply RFBS in branch or window form (30.19%). Islami Bank Bangladesh Limited (IBBL) is the pioneer (IBBL, 1984), and the largest, fastest growing and best performing (Aminuzzaman, 2010) riba-free bank in Bangladesh.

a) Riba-free Banking System (RFBS)

Riba-Free Banking System (RFBS) is a kind of banking which is formed according to the rules,

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regulations and provisions instructed by the Islamic Shariah. Egypt is the pioneer of structurally adaptation of RFBS in the world in 1963 which is also known as Islamic Banking System (IBS). At present, there are 385 commercial banks in 55 countries which have been following their banking operations in riba-free form (GFDR, 2014). Bangladesh has started riba-free banking from 1983. Now a days, Bangladesh has a significant market share (2.08%) i.e. 8 out of 385. Islami Bank Bangladesh Limited (IBBL) is the pioneer riba-free bank which has been passing 30-years glorious journey in the banking sector of Bangladesh.

b) Rural Development

Rural development is defined as the socio-infrastructure development of a nation where rural people are highly encouraged to involve in the economic development. Rural development can be measured by self-sufficiency, productivity and competence to increase financial worth i.e. deposit and investment of rural people (Halimuzzaman, 2014). In Bangladesh, out of 160 million people, 77% people live in rural and urban areas (BURU, 2013). IBBL has been surviving in Bangladesh considering as mass banking (Shohrwardhy, 2015). There are some extrinsic programs taken by various banks and NGOs in private and public level for the development of rural and urban area i.e. Rajshahi Krishi Unnayan Bank (RAKUB), BRAC bank, ASA, Proshika and IBBL etc. Rural Development Scheme (RDS) is a specialized project of IBBL to develop the rural and urban area where more incompetent people are involved in the economic development of Bangladesh.

c) Rural Development Scheme (RDS)

Basic philosophical objectives of Riba-Free bank (RFB), Islami Bank Bangladesh Limited (IBBL) is enhancing the economic system of Bangladesh based on equity and justice in all levels of civilization. In Bangladesh, 38% of the total population maintains their living standard below the poverty line and 18% of the same live in abject poverty (IBBL, 2014). These poverty stricken people are facing a lot of problems like illiteracy, inadequate health and sanitation facilities, discrete of purchase parity, scanty of the sources of income generation etc. Considering the above mentioned problems, IBBL has started a dimension of rural banking

named Rural Development Scheme (RDS) from 1995. The Basic objective of RDS of IBBL is to create self-employment opportunity for income generation and to

reduce the poverty of rural people. Table-1, expresses the basic nature of RDS offered by Islami Bank Bangladesh Limited.

Table 1 : Basic Features of RDS

Contents	Particulars
Target Group	Rural people with 0.50 to 1.50 acres of land. Both men and women
Program	Basically micro-investment.
Criteria Applied for Selection	Land ownership and permanent residence.
Sanction of Investment	Two months after the formation of group
Size of Investment	Core Product- BDT 25,000.00 (For 1 Year) Nursery- BDT 50,000.00 (For 1 Year) Agriculture Implements- BDT 50,000.00 (For 1-3 Years) Live Stock- BDT 50,000.00 (For 1-2 Years) Poultry- BDT 35,000.00 (For 1 Year) Fisheries- BDT 50,000.00 (For 1-2 Years) Rural Transport- BDT 20,000.00 (For 1 Year) Rural Housing- BDT 50,000.00 (For 1-5 Years) Off-firm Activities- BDT 50,000.00 (For 1 Year)
Mode of Disbursement	Goods / Assets: Buy Muazzal (Sale on credit)
Profit Rate	10% (Flat Rate); but 2.50% rebate in the case of regular and timely payment; Profit-Sharing basis: risks are shared by IBBL if loss is genuine.
Repayment- Period Starts	After two weeks of disbursement.
Sources of Funds	Member Savings; Depositor's Savings; PKSf.
Activities Financed	Both farm and non-farm activities.
Savings	Tk. 25 Per week
Collateral	No collateral except
Required	Personal guarantee and savings.

Source: Jahur (2010)

As shown in Table-1, RDS provides various investment modes for development of rural people through financing in the fulfillment process of their basic

needs. The next table provides a brief profile of RDS of Islami Bank Bangladesh Limited.

Table 2 : A Brief Profile of Rural Development Scheme (RDS) of Islami Bank Bangladesh Limited

Areas of performance	Fig. in million BDT No. & Volume/Amount
No. of Branches covering RDS	250
No. of Field Officers	2,492
No. of Project Officers	217
No. of Zone Officers	14
No. of Villages	18,591
No. of Districts	64
No. of Centers	28,122
No. of Groups	176,765
No. of Members	915,209
% of Women members in the Scheme	79%
No. of Clients	580,251
Financial Statement	
Cumulative disbursement (From 1995)	107,307.21
Present outstanding	17,830.10
Overdue	132.00
Recovery	99.30%
RDS Savings	5,992.50

Source: RDS Manual

On the above table explores the involvement of IBBL in the development of rural and urban areas of Bangladesh. The most remarkable mania in 2014 is that the growth of RDS investment is 24.57% over 2013 and recovery rate of its investment schemes is 99.30%.

d) Vision-21

Bangladesh got independence in 1971. Yet, after 40 years of independence, Bangladesh has remained a low-income country (LIC) (GED, 2012), almost two thirds of population remains below poverty line (Bureau, 2013). For improving the situation and recognizing the long-term development challenges, the present Government has adopted the Vision 2021. The Vision 2021 calls for Bangladeshi socio-economic environment to be transformed from a low income economy into the first stages of a middle-income country by the year 2021 (GED, 2012) which also marks as the 50th anniversary of the independence of Bangladesh which is called golden jubilee of the nation. Moreover, Vision 2021 lies down a development scenario where citizens will have a higher standard of living, better education, will have a more equitable socio-economic environment, and the sustainable development will be ensured through better protection from climate change and natural disasters. To achieve Vision 2021, the Government has undertaken "Perspective Plan of Bangladesh (2010-2021): Making Vision 2021 a Reality". The Perspective Plan is a road map for achieving the targets of Vision 2021 and lies down a long-term strategy to make that happen. Thus, it takes two five-year plans: Sixth Five Year Plan (2011-2015) and the Seventh Five Year Plan (2016-2020). Finally, the vision-21 is formed for reaching the country as a middle-income country (MIC) replete with the sign of economic progress.

II. LITERATURE REVIEW

Bangladesh is a growing economic tiger of the third world countries. The majority of the people of Bangladesh live in rural and urban areas (Bureau, 2013) and is contributing to the national economy on the basis of agro-based industry specially small and tinny. According to the statement of Dr. Jahid Hossain, the Lead Economist of the World Bank, Bangladesh is a Lower Income oriented country (LIC) up to 2014. Bangladesh Government has taken sufficient strategic programs to develop our national economy viz. Millennium Development Goals (MDG). In that perspective, banking sector is playing a pivotal role in the economic development in Bangladesh i.e. 1.4% of GDP in service industry (Bangladesh Bank, 2012) but agricultural sector specially crops, animal farming, fisheries, hotel restaurant, community and social service contributions are more significant i.e., 11.4%, 2.7%, 4.6%, 0.7%, 6.9% share of GDP respectively.

Economic development is covered by economic, political and social states of the people of a nation including the economic procedure and policies and social well-being (Wikipedia). Kifle (1997) stated that a strong relationship is existed between poverty alleviation and economic development. The basic principle of Riba-Free Banking System (RFBS) is to realize and ensure the well-being of mankind using equity based economy that is necessary for development economy (Chapra, 1985). RFBS as well as Islamic Banking System (IBS) ensures all kinds of banking activities (Fund collection-Deposit and investment avoiding interest (Riba) (Iqbal, 2001). It is mentioned here with that RFBS ensures steadfast economy considering fair distribution of income, reducing injustice, risk sharing, financial crisis, facilitating production and business activities (Siddiqi, 1985). In the recent world, banking is much more significant than banks (Bill Gate, 2008). Therefore, RFBS always strives itself to ensure its contributions to different aspects of national economy through specialization of its services i.e. Rural development Scheme (RDS) (Ahmed, 2004; Hawlader, 2008; Parveen, 2009; Jahur, 2010 and Bhuyian, 2011).

Islami Bank Bangladesh Limited (IBBL) is the pioneer, the largest and most performing bank in Bangladesh in the field of riba-free banking sector as well as Islamic banking sector. A nominal zero interest rate (Riba-Free) is a required condition for absolute resources allocation (Friedman, 1969). Islamic Shariah based RFBS is playing a pivotal role in economic development contributing a lot to the advancement of the society (Siddidi, 1973). IBBL is providing satisfactory community services through job creation and ensuring consistency in the field of service sector in Bangladesh (Rashid, 2009). IBBL has to deal in equity based profit and Loss Sharing (PLS) contracts that are more suitable for Bangladesh economy but social awareness, rehabilitation, economic and psychological support and strict enforcement of laws are the basic pitfalls for its success (Begum, 2004).

Rural Development Scheme is the specialization of banking expansion aim to incorporate the mass people who live below the poverty level (Hawlader, 2008) in the economic development activities of Bangladesh (RDS Manual of IBBL). A few numbers of scholars engage themselves to explore the different aspects of RDS. RDS is a successful project in retaining the people in the economic development activities (Rahman, 2008). This indicates that riba-free baking sector provides its contribution to the economic progress in Bangladesh through generating employment, earning foreign remittance, strengthening rural economy, promoting ecology and green banking and enhancing industrialization through tiny sector

development using the expansion of RDS (Halimuzzaman, 2014 and Aminuzzaman, 2010).

RDS emphasizes the industrial sector devoting huge investment. Alam (2000) found that industrial development and RDS investment has a strong positive relationship. For enhancing industrialization, banks play vital role to encourage fruitful investment (Iqbal, 2001). Hawlader (2008) proved that RDS positively assets the poverty alleviation existed in Bangladesh encouraging micro scale savings. RDS activities are highly expanded considering the terms of number, investment and deposit (Jahur, 2010). Under RDS, investment is higher than deposit that indicates, investment insecurities are covered by RDS memberships with association (Bhuyian, 2011). Covering all socio-economic factors, RDS is the highest performance oriented micro finance activities in Bangladesh (UNDP, 2012; Ahmed, 2004). RDS plays a vital role in the in the improvement of standard of living through the relationship of household income and expenditures (Rahman, 2008).

Considering the existing literature, it is evident that the contributions of RDS of IBBL are justified by the jurisdiction of scholars' views. Poverty alleviation, socio-economic contributions, high performance oriented micro finance activities were found as scope of operations of RDS. But no evidence has been found regarding the contribution of RDS on the national economy through rural development. Hence, the study attempts to examine the RDS contributions to the development of Bangladesh economy considering the projection of Vision-21 as the golden jubilee of the independence of Bangladesh.

a) Objectives

This study examines the impact of Rural Development Scheme (RDS) of Islami Bank Bangladesh Limited (IBBL) on national GDP of Bangladesh through the contribution on rural development. In light of the basic objectives the study covers the following extensions:

- To measure the contributions of RDS on Rural Development considering vision-21
- To analyze the causality of rural development contributions factors i.e., deposit, investment and GDP
- To determine the impact of RDS on GDP of Bangladesh

III. METHODOLOGY OF THE STUDY

Rural Development Scheme (RDS) of Islami Bank Bangladesh Limited (IBBL) is the organizational sample of this study. It is an empirical research. Therefore, secondary data have been used in this study considering the FY 2002-2003 to FY 2013-2014. The

secondary data are collected from the annual report of IBBL from 2003-2014. Trend line through scattered diagram is used to determine the average existence of different economic contributing factors of RDS i.e. Staff involved in this program for justifying employment, village coverage, members of RDS, savings and investment of RDS. Correlation is used to determine the liner regressive among the variables. Ganger causality test is also used in this study to find out the causal relationship among national GDP, deposit of RDS and investment. Finally, simple regression model is used to determine the individual impact of deposit and investment of RDS on national GDP.

IV. FINDINGS AND ANALYSIS

This section of the study is comprised with three sub-sections considering rural contribution on the basis of various welfare activities, village coverage-employment-members incorporated in the RDS program, and deposit & investment of RDS.

a) Contribution of RDS in the rural development on the basis of various welfare activities

The basic mechanism of RDS is to encourage micro savings in an association formatted by a homogeneous group in a village. This saving tendency has created an economic driven force for their self-consistency of motivation towards the investment. On that prevail, the incompetent people of rural and urban areas involve themselves in the self-income generation activities as well as micro investment modes. RDS creates a wide span of rural investment modes for rural people in various economic activities i.e. service, trading, processing-manufacturing, shop keeping, selling-marketing, rural transport (rickshaw), irrigation equipment, tube well, housing materials etc. (RDS Manual). Formally, RDS encourages the people to retain in a group or association through some significant welfare activities. Table-3 explores the present status of RDS on the basis of its different welfare activities that are complying to the rural development in Bangladesh.

Table 3 : Status of RDS of IBBL on the Basis of Different welfare Activities

Modes of welfare		Beneficiary up to 2014
Graduation Program		71,426
Welfare Activities		2,58,169
Education Program		Education Program
	Scholarship	593
	Academic award	22,190
	Pre-school	18,615
Training Program		Training Program
	Leadership	42,743
	Skill Development	1,14,207
	Self-Employment	184
Health Program		Health Program
	Welfare & sanitation	3,984
	Medical Assistance	49,068
Relief and Rehabilitation Program		6,432
	Waiver	2,029
	Relief-donation	4,403

Source: Annual Report of IBBL, 2014

b) Rural Contribution of RDS on the Basis of Employment Generation, Area Coverage, and Members Involvement

Rural Development Scheme (RDS) is the specialization of project of rural development as well as an integrated factor of Bangladesh economy. This program has been familiarized due to its contribution to poor people living below the poverty level. This program also enhances income generation, moral, social and ethical values of the rural and urban people. For justifying the rural development contribution of RDS, the study uses simple trend equation expressed in the below:

$$Y = f(x) \quad (i)$$

$$Y = \alpha + \beta x \quad (ii)$$

Where

Y = Dependent variable i.e. RDS staff, Village Coverage, members, deposit and investment of RDS

X = independent Variable i.e. year of Operation

The average growth trends mentioned in the table-4 indicate the weighted value of trend equations using scattered diagram and expected value for vision - 21 indicates the forecast value of the Year-2021 when Bangladesh will stand Golden Jubilee of its independence. Table-4 explores the overall performance of RDS in the scale of staff involvement, village coverage and members incorporate in this program.

Table 4 : Contribution of RDS in the Rural Development of Bangladesh

Year	Staff	Village Coverage	Members
2003	639	3700	130465
2004	731	4230	163465
2005	868	4560	217445
2006	1368	8057	409573
2007	1819	10023	516725
2008	1712	10676	577740
2009	1732	10751	492475
2010	1837	11482	523941
2011	2024	12857	608703
2012	2191	15371	735628
2013	2286	17104	816274
2014	2499	18086	891485
Mean	1724	11191	538394
Average Growth Trend	164.40	1303	82541
R ² =	0.939	0.973	0.942
Expected in Vision-21	3696	26824	1319859
Skewness	-0.4105	-0.0468	-0.1594
Kurtosis	-0.7668	-1.1113	-0.9188

Source: IBBL Annual Report from 2003-2014

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Source: IBBL Annual Report from 2003-2014

RDS deposit per year and investment is 1494.00 million BDT. This is very fact that investment is three times greater than deposit but recovery rate of investment is 99% on an average (IBBL, 2014). These trends are emphasized that customers (members) show the trustee with the performance of RDS functions. Therefore, the study states that RDS is the integral part of rural and urban economy in Bangladesh. It is expected that in the Vision-21, deposit of RDS will reach the level of 8092 million BDT while Investment will be 24533.00 million BDT.

d) Correlation Analysis

Correlation expresses the linear relationship between two variables considering direct causation, indirect causality or statistical change (Ferdousi, 2009). Generally, correlation coefficient usually explores the degree of association of defined variables. Table-6 explores the Karl Pearson Coefficient of correlation in two trials with significant value.

Table 6 : Correlation Among the Variables

	GDP	DEP _{RDS}	INV _{RDS}
GDP	1		
DEP _{RDS}	0.986** (0.000)	1	
INV _{RDS}	0.985** (0.000)	0.999** (0.000)	1

Source: Calculated by Authors

Table 7 : Pair-wise Granger Causality Tests

Sample: 2003-2014 Lags: 2, Observation-10				
Null Hypothesis:	F-Statistic	Prob.	Hypotheses	Types of Causality
Dep. \wedge GDP	0.32836	0.7345	$H_0=A$	No Causality
GDP \wedge Dep.	1.97996	0.2326	$H_0=A$	No Causality
Inv. \wedge GDP	0.52090	0.6230	$H_0=A$	No Causality
GDP \wedge Inv.	2.19209	0.2072	$H_0=A$	No Causality
Inv. \wedge Dep.	3.96789	0.0929	$H_0=A$	No Causality
Dep. \wedge Inv.	4.89208	0.0665	$H_0=A$	No Causality
$H_0=A$ Null hypothesis of causality is not rejected since $p > 0.05$				
$H_0=R$ Null hypothesis of causality is rejected since $p < 0.05$				
\wedge = does not Granger Cause				

Source: Calculated by Authors

From the above table, the study has found that GDP, Investment and Deposit of RDS are existed in Bangladesh economy as independent variables since null hypotheses of all causality are not rejected at 5% level.

f) Impact of Investment of RDS on GDP

Investment and industrialization have positive relations (Iqbal, 2001). Industrialization is the basic requirement of economic development which is positively depends on poverty alleviations (Kifle, 1997).

All coefficient of correlations are positive significant at 5% level. This result indicates that deposit and investment of RDS is highly correlated with GDP since all coefficients are more than 0.90 at significant level.

e) Granger Causality Test

In the time series data correlation do not absolutely imply causality since there is a chance to existence to ignore common factors in correlation (Lin, 2008). Therefore, causality test can be used to find out causal influence (Granger, 1980). Generally, causality measures the supernatural representation of data and make interpretations more informative and useful by extending frequency domain. In this study, we use EvIEWS version-7 for pair-wise Granger causality test expressed in the Table-7.

This indicates that investment and national GDP have a significant relation. Hence, the study attempts to justify the impact of investment of RDS on GDP. Simple regression equation is used to analyze the impact between investment of RDS and GDP considering the growth model due to no causality. The relationship between GDP and Investment of RDS is expressed in the below:

$$GGDP = f(GINV_{RDS}) \quad (iii)$$

$$GGDP = \alpha + \beta GINV_{RDS} + \varepsilon \quad (iv)$$

Where,

GGDP = Growth of GDP

$GINV_{RDS}$ = Growth of Investment of RDS of IBBL

ε = Sampling Error

α, β are constant of the model

SPSS version 21 is used to run the simple regression modeling expressed in the Table-7 incorporating constant, standard regression weight (β), standard error (SE), t -value, P -value, F -statistics, R^2 , DW statistics etc.

Table 8 : Regression Effect of Growth of RDS Investment on the Growth of GDP of Bangladesh

Variables	Standardized Weight (β)	S.E.	t-Value	P-value
Constant	0.24	0.04	6.6124	0.00
INV _{RDS}	0.76	0.12	3.6451	0.00
R ² =		0.571		
Adjusted R ² =		0.528		
F-Statistics		13.287 (0.000)		
D-W=		1.973		
Dependent Variable: GDP				
Independent Variable: Investment under RDS of IBBL (INV _{RDS})				

Source: Calculated by Authors

The measurements values of the Table-7 indicate goodness of fit of the model. So finding is expressed in the following equation.

$$GGDP = 0.24 + 0.76 GINV_{RDS} \quad (v)$$

It should be mentioned here that growth of investment of RDS has positive impact on the growth of GDP of Bangladesh i.e., $\beta_{GDP-GINV_{RDS}} = 0.76$ ($t = 3.6451$ and $P = 0.000$). More significantly it is mentioned here that constant of the model is significant at 1% level. Therefore, the study states that the contribution investment of RDS of IBBL is fairly justified to the national GDP of Bangladesh.

g) Impact of Deposit of RDS on GDP

Generally, Deposit is defined as the blood circulation of an organizations and unique elixir (Shohrwardhy, 2015) of investment. The study attempts to determine the impact of RDS deposit on GDP of Bangladesh. Due to the no causality (Table-7), simple

regression equation is used in this section. The relationship between the deposit of RDS and national GDP considering the growth model expressed in the below:

$$GGDP = f(GDEP_{RDS}) \quad (vi)$$

$$GGDP = \alpha + \beta GDEP_{RDS} + \varepsilon \quad (vii)$$

Where,

GGDP = Growth of GDP

$GDEP_{RDS}$ = Growth of Deposit of RDS of IBBL

ε = Sampling Error

α, β are constant of the model

SPSS version 21 is used to run the simple regression modeling expressed in the Table-9 incorporating constant, standard regression weight (β), standard error (SE), t -value, P -value, F -statistics, R^2 , DW statistics etc.

Table 9 : Regression Effect of Growth of RDS Deposit on the Growth of GDP of Bangladesh

Variables	Standardized Weight (β)	S.E.	t-Value	P-value
Constant	0.15	0.04	4.254	.002
DEP_{RDS}	0.89	0.08	6.022	.000
$R^2=$		0.784		
Adjusted $R^2=$		0.762		
F-Statistics		36.270 (0.000)		
D-W=		1.717		
Dependent Variable: GDP				
Independent Variable: Deposits under RDS of IBBL (DEP_{RDS})				

Source: Calculated by Authors

The measurements values of the Table-9 indicate the proper justification of the model due to justification measurements are in the standard level. So finding is expressed in the following equation.

$$GGDP = 0.15 + 0.89 GDEP_{RDS} \quad (viii)$$

From the equation-8, it is found that growth of deposit of RDS has positive impact on the GDP of Bangladesh since constant of the model is found significant at 5% level ($C=0.15$, $t= 4.254$, $P=0.002$). The impact of RDS deposit on GDP is found through the significant value of standard regression weight i.e., β $GDP-GDEPRDS = 0.89$ ($t= 6.022$ and $P=0.000$).

V. CONCLUSION

Riba-Free banking is one of the leading micro finance private sectors in Bangladesh. Specially, Islami Bank Bangladesh Limited is the pioneer of riba-free Banking in Bangladesh. Rural Development Scheme is specialized project of IBBL for rural and urban development. The study has found that RDS is competent to integrate people who live below poverty level and absolute poverty level in the economic development activities especially in the rural areas. RDS encourages these people to save money and investment their savings in a cooperative environment for economic development of Bangladesh. This study has found that deposits of RDS collected from the people (below poverty level and absolute poverty level) and investment have positive and significant relationship with national GDP. It is mentioned here with that impact of deposits and investment of RDS of IBBL on national GDP is significantly positive. Generally, it is mentioned that if more un-scattered people of a country are involved in the economic development activities than percapita income must be increased. It is proved that RDS is the most significant effective factors in the economic development of Bangladesh.

Now, Bangladesh is lower middle income oriented country (LMIC) due to increase per capita income in \$1085. In 2021, if, Bangladesh will be established as a middle income oriented country (MIC), below poverty and absolute poverty level people must be incorporated in the economic development activities. This study is proven experiment of economic development that RDS of IBBL is sample project by which below poverty levels people are contributing themselves to the economic development of Bangladesh. Using the experiences of RDS of IBBL for rural development, it may possible to establish Bangladesh as middle income oriented country in the world which is the basic goal of Vision-21.

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