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SUBJECT II

WORKING AND IMPACT OF RURAL SELF-HELP GROUPS AND OTHER FORMS OF MICRO FINANCING

An Informal Journey through Self-Help Groups*

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1. *Economy, Finance and Financial Institutions*

Finance is one of the most crucial inputs for economic activity, growth and development. If finance through own accumulated resource or equity is neither available, nor sufficient, debt assumes a major significance. Financial institutions (FIs) play an important role in this regard by channellising funds from surplus sector (savers) to deficit sectors (investors). However, these institutions do not show much enthusiasm to put their resources in rural and backward areas for the benefit of poorer people as these are commercial organisations and are basically interested in profitability and sustainability, for two reasons: (i) incentive for functioning, and (ii) for safeguarding the interest of stakeholders. Besides, the transaction in credit market is different from the transaction in goods market (Llanto, 1990). Unlike in the latter where transaction ends with the sale of goods and receipt of payment, which are more or less instantaneous, in the former what is important is the future endowment of the borrower which depends upon the purpose of the loan, viability of the project and creditworthiness and the strategic skill of the borrower. As these rural backward areas lack infrastructure, entrepreneurship, opportunities, and people are victims of exploitation and ignorance, the transaction cost of investment by the financial institutions and credit risk are high, and return on capital by the borrowing investors is not attractive.

Besides, rural economic agents find the formal urban institutions alien and inaccessible; the attributes, characteristics and personal circumstances of the rural agents are not very much acceptable to the Formal Financial Institutions (FFIs). For both an information gap exists. This accentuates the problem for the FFIs to locate both a good borrower and a good project. Borrowers know themselves better than the FFIs, but do not desire to fully disclose all relevant personal and project information (Leland and Pyle, 1977). The information transfer is hampered by serious moral

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hazard and incentive problems (Llanto, 1990). Verification of true credentials by an outside lender may prove to be costly if not impossible (Leland and Pyle, 1977). When market imperfections persist, lenders face the problem of managing the risk of loan default (Von Pischke, 1992), and raising the interest rate does not resolve the problems either (Stiglitz and Weiss, 1981). On the other hand, the rural borrower and informal lender literally know each other quite well. The information wedge is easily eliminated because both transactors operate within the same or familiar socio-cultural and economic milieu. At the same time both the parties are able to draw up a very flexible and easily comprehensible loan contract. And the informal financial market continues to function in the same local environment. In the process both the FFIs and the rural borrowers continue to be the losers. Whereas the former loses a new credit market and potential surplus sector, the latter loses access to much larger and cheaper resource.

As a result, capital formation, and, hence, development process takes a back seat in the rural areas. Besides, if land, labour and money market are interlocked, there arises a vested interest among the powerful class to thwart the development process and perpetuate indebtedness and poverty (Basu, 1984; Bhaduri, 1973).

2. *Government, Development and FFIs*

Any modern government, however, does not like to deny economic development to the rural areas because of either strong linkage between agricultural and industrial development or political advantage. Credit reform becomes imperative as credit programmes are easier to implement than other policies (Braverman and Guasch, 1989). Therefore, if the FFIs lack the Schumpetarian entrepreneurial quality to innovate in the rural areas on their own, they are directed to operate there. Whatever be the reason for entry, formal institutions during the course of economic development are likely to expand faster than informal institutions and are expected to take over the part of the latter's function (Holst, 1985); hence informal financiers and loan associations become redundant (Drake, 1980). Policy makers try to provide cheap credit as an alternative to moneylenders or informal institutions in order to curb their monopoly power and high interest rate charged by them (Hoff and Stiglitz, 1990). It is however doubtful whether such a policy either improves access to credit for the poor or eliminates moneylenders or reduces interest rates (Bell, 1990) charged by them.

In India banks were nationalised in 1969; consequently, priority sector for the rural areas, agricultural sector and weaker sections was defined with 40 per cent of mandatory credit and interest concession along with the offer of licenses for new urban branches linked to the number of rural branches opened. An ambitious credit scheme: `Integrated Rural Development Programme' (IRDP) with a considerable element of subsidy was launched to alleviate poverty. It is doubtful whether alleviation of poverty and creating a strong rural market were the major motives

behind it. So corruption and leakage became the central point. The IRDP borrowers were considered as 'passengers' in the banking bandwagon, and less than 10 per cent of them have been found to be still associated with the banks after their loan 'repayment' was over (Pulley, 1989). Besides corruption, the programme was ill-conceived to boot. It was a supply-led, not demand-led credit programme so that the clients did not have choice over `purpose' and `amount'; entrepreneurial skill was assumed which was not there; backward and forward linkages were never of any concern during implementation. Credit target was the main concern and bureaucratic machinery was in charge of ensuring the credit achievement for which they did not have any professional respect. The FFIs were not allowed to apply the principle of three Cs: (i) Character, meaning how a person has handled past debt obligations, (ii) Capacity, meaning how much debt a borrower can comfortably handle, and (iii) Capital, meaning current available assets of the borrower, such as real estate, savings or investment that could be used to repay debt if instalment/income should be unavailable. It is not that the public sector financial institutions were very unhappy about the situation as they did not disburse these loans with a sense of commercial viability but dispensed it with disdain as a `social obligation' and to attract government's favour elsewhere. So the top management never accepted this as a challenge and rural branch managers disbursed credit with indifference. These loans were written off from the psychological ledger of the bankers on day one. Agriculture and Rural Debt Relief (ARDR) scheme further hardened the attitude of the bankers towards rural credit, and the rural borrowers towards repayment. As one story goes, on one occasion a woman borrower in response to a Minister protested that she had not taken a *sala* (loan in Kannada, an Indian language) from a bank but agreed that she had taken a bank loan. Whereas a *sala* is a loan bound by traditional sanctions and norms and is always returned, the bank loan is a 'gift' from the government (Fernandez, 1998). Distribution of cheap and easy loans without any respect for repayment seemed more important (Bouman, 1989). All these only weakened the strength of the financial institutions to serve the poor and the rural areas, and further reduced their interest to transact such business. Although moneylenders became less important after Independence due to government intervention, they have started reassuming an important role in recent years largely due to the poor quality of institutional credit (Rajasekhar and Vyasulu, 1990). Besides, there was an urgent need for financial innovation in the credit market as there was no certainty about the completion of a credit transaction (Bhatt, 1987). This is a story not only of India but of many of the developing countries.

3. *Re-discovering Informal Systems*

The failure of formal institutions to serve the rural poor effectively led to a review and a look at the informal financial systems and lending groups (World Bank, 1983; Huppi and Feder, 1990; Holt and Ribe, 1991). "The traditional assessment of

the informal sector has been that it is exploitative, usurious and dysfunctional and newly established institutional credit is thus often aimed at dismantling the informal sector. Such an approach .... may result in policies which displace informal lenders without offering alternate sources of institutional credit. In these circumstances, rather than substitute for these informal arrangements, supplement and strengthen informal credit sources, and compete with informal lenders. Moreover newly introduced systems could also learn from the informal sector" (World Bank, 1983). "The informal sector as the oldest centre of enterprise preceding the arrival of formal institutions, is a natural and legitimate part of rural financial markets and it is better policy to acknowledge than to deplore the fact" (Bouman, 1989).

It thus seems clear that informal financial system and informal lender are not on the same footing. Whereas the latter may be exploitative charging usurious rate of interest, the former minimising information gap and offering flexibility may be appropriate and efficient for the rural sector. There was thus a need to study the informal systems rather than informal lenders. What has thereafter been discovered are informal financial groups.

Tontines or Hui with 10-15 members involved in financial activities in cash or in kind have been in existence in Vietnam for generations (Abiad, 1995). Bishi which is short form of 'Bishimandal' or 'Chitfund' are old institutions in India in which members made periodic contributions that are pooled into a fund from which money is 'given' to members (Bouman, 1989). Credit unions, fishermen groups, village-based bank-like institutions, irrigation groups, etc., were in existence in Indonesia (Koch and Soetjipto, 1993).

In the international lexicon these informal groups have been termed as Rotating Savings and Credit Associations (ROSCA) and Regular Savings and Credit Associations (RESCA). In both, regular savings are made by a fixed set of members for an agreed period. In ROSCA the total fund is given to each of the members in rotation until everyone has had a turn. Only one loan is made each time. After everyone has had a turn, the old cycle ends, and a new cycle may begin with the same or new members. In RESCA which is a non-rotating ROSCA, several loans are made from the pool of savings. Whereas in ROSCA the fund does not grow during the life cycle, in RESCA the fund grows because of periodic contribution and repayment of loan. At the end of the period there is nothing to be distributed at ROSCA; accumulated fund is distributed among the members at RESCA. In ROSCA, generally three methods, viz:, (i) lottery type, (ii) lottery with discount, and (iii) auction, are used to distribute the fund. In the latter two there is incentive for saving and late winners earn a higher rate of interest (Bouman, 1989).

Whereas the encouraging feature of these RO(E)SCAs is that there is negligible information gap between the lender and the borrower and little transaction cost involved for both the parties, the problem is that they lack access to banks and external credit sources as well as consultancy services and most other modern inputs

which just maintain a status quo by encouraging a near-stationary economy going rather than expanding or modernising it (Kropp *et al.*, 1989).

4. *International Effort in Linking Formal and Informal Systems*

To bridge the gap between the formal and informal systems, Mohammad Yunus started a research project in Bangladesh in 1979 and established Grameen Bank (GB) in 1983 (Khandker *et al.*, 1995). The lending programme of GB depended basically on external fund although the members' savings fund has increased substantially over time.

In 1984, the main conclusion in the third international symposium on the mobilisation of personal savings in developing countries organised by the United Nations was that "the main means of improving the performance of the non-institutional sector were policies directed to enhancing its links with the institutional financial sector" (United Nations, 1986). In the final resolution the participants agreed that (i) internal savings must provide the basis for credit programmes, (ii) state control of interest rates must be relaxed in favour of market or near-market rates, (iii) for effective service, financial services need to be more decentralised, (iv) both formal and informal financial institutions are necessary for the financing of development and (v) linkages between formal and informal financial institutions seem to be more promising than separate development.

In 1984, the Federal Ministry of Economic Co-operation and the Agency for Technical Co-operation of the Federal Republic of Germany undertook a series of studies and workshops on rural finance in developing countries resulting in a new policy for promoting Self-Help Groups (SHGs), different from Grameen Bank Model, and Self-Help Promotional Institution (SHPI) as a financial intermediation between the rural poor and the microenterprises in the informal sector, on the one hand and formal financial institutions, on the other (Kropp *et al.*, 1989).

At the Asia and Pacific Regional Agricultural Credit Association (APRACA) regional workshop of May 1986 in Nanjing, the participants decided on a co-ordinated programme for "the Promotion of Linkages between Banks and SHGs for rural savings mobilisation and credit delivery to the rural poor".

The project "Linking Banks and SHGs" (PHBK) in Indonesia started in 1988 as a pilot project of the Central Bank of Indonesia through the involvement of SHPI which would provide either training and consultancy services to the SHGs and in some cases additionally act as financial intermediaries (Koch and Soetjipto, 1993).

5. *Indian Initiative in Linking Formal and Informal Systems*

First official interest in informal group lending in India took shape during 1986-87 when National Bank for Agriculture and Rural Development (NABARD) supported and funded an action research project on ‘Savings and Credit Management

of Self Help Groups' (NABARD, 1995) of Mysore Resettlement and Development Agency (MYRADA). In 1988-89 NABARD undertook a survey of 43 non-governmental organisations (NGOs) spread over 11 states in India to study the functioning of SHGs and possibilities of collaboration between the banks and SHGs in the mobilisation of rural savings and improving the delivery of credit to the poor (NABARD, 1995).

Micro financing by 'non-formal' financial organisations had already started. SEWA (Self Employed Women's Association) owned by women of petty trade groups was established on co-operative principle in 1974 in Gujarat. Working Women's Forum (WWF) started promoting working women's co-operative societies in Tamil Nadu since 1980. Shreyas in Kerala actively got involved in micro finance operations since 1988 with the objective of promoting people's co-operatives, habits of thrift and self managing people's bank (HDFC, 1997).

Encouraged by the survey results, NABARD impressed upon Reserve Bank of India (RBI) to come out with a circular on July 24, 1991 advising the commercial banks (later RRBs and co-operatives also) to extend credit to the SHGs under the pilot project of NABARD (500 SHGs to be covered). During the project period, the Association of Sarva Seva Farms (ASSEFA), Madras, promoted 214 groups, mobilised Rs. 1.4 million of thrift and disbursed credit of Rs. 2.3 million; People's Rural Education Movement (PREM), Behrampur promoted 829 groups, mobilised Rs. 1.9 million of thrift and disbursed credit of Rs. 1.9 million; Professional Assistance for Development Action (PRADAN), Madurai, promoted 313 groups, mobilised Rs. 1.3 million of thrift and disbursed credit of Rs. 3.9 million; Community Development Society (CDS), Alappuza promoted 350 groups, mobilised Rs. 2 million of thrift and disbursed credit of Rs. 4.7 million (NABARD, 1995). The results were thus quite encouraging.

To formalise the mechanism further, RBI constituted a working group in November 1994 (NABARD, 1995) to review the functioning of NGOs and SHGs and make suitable recommendations for expanding their activities and deepening their role in the rural sector. Accepting the recommendation, in April 1996, RBI advised the banks that lending to the SHGs should be considered as an additional segment under priority sector advances and integrated with the mainstream credit operation.

6. *Self-Help Groups*

The SHGs thus became a regular component of the Indian financial system since 1996. These SHGs are small, informal and homogeneous groups of not more than 20 members each. The groups have been recommended to be informal to keep them away from bureaucracy and corruption, unnecessary administrative expenditure and profit constraints. The size of 20 has been made mandatory because any group larger than this would need to be registered under the Indian legal system. There is however something beyond this. These groups are expected to foster true (direct) democratic

culture where all the members participate actively by taking part in the debate and decision-making process which is possible only in small groups. Otherwise when the groups become bigger direct democracy tends towards indirect democracy - a coterie of decision-making and formation of vested interest within the group. Groups are expected to be homogeneous so that the members do not have conflicting interest and all the members can participate freely without any fear and adverse consequence. When financial transaction starts, there is no subsidy if the groups are identical (Stiglitz, 1990). The repayment rate tends to be lower in large groups (Mosley and Dahal, 1985; Owusu and Tetteh, 1982) as the magnitude of free-rider problem is high in larger groups and the propensity to default is high among heterogeneous groups (Rajasekhar, 1996). These are the features which distinguish small, homogeneous and informal SHGs from large, heterogeneous and formal co-operatives although both are found on the same principle of co-operation. Because of the heterogeneity and bureaucratic interference the co-operatives in so many poor countries have been hijacked by the less poor, the landowners and by allied political interests (Harper, 1998). Several countries including India have had problems with credit co-operatives, although it has succeeded in some other countries (Yaron, 1992).

The SHGs after being formed (generally by an external agency) start collecting a fixed amount (rarely variable amount) of thrift from each member regularly (mostly monthly). For about six months, it only collects thrift; no loan is given to any member. Firstly, the working fund generated out of small thrift is negligible in the initial period; secondly it tests the patience and tries to instill mutual trust among the members. During this period the groups are expected to open a savings account with an FI which would like to extend credit. After accumulating a reasonable amount of resource, the group starts lending to its members for petty consumption needs. Claimants may be large, but resource is small. This forces them to take appropriate decision to identify the most needy person with regard to endowment level and the purpose of the loan. A free and fair discussion removes the element of subjectivity from the decision-making process, makes the borrower understand the value of the credit and the importance of repayment and accountability to the group. The repayment of the loan along with interest and regular thrift enlarge the working fund and increase the scope of lending. Notwithstanding this, the working fund generated by the group may not be adequate to meet all types of credit needs of all the members. The group then approaches the FI where it had opened the savings account. If the bank is satisfied with the group in terms of: (i) genuineness of demand for credit, (ii) credit handling capacity of the members, (iii) repayment behaviour within the group, and (iv) the accounting system and maintenance of the records, it extends a term loan of smaller amount to the group. The group in turn continues to take decision as in the past, the only difference being it has now a higher amount of resource. In addition, the group is jointly liable to the bank for repayment. The group's responsibility in monitoring the members therefore increases. This joint liability however provides incentives or compels the group to undertake the burden of

selection, monitoring and enforcement that would otherwise fall on the lender (Hoff and Stiglitz, 1990).

This joint liability, decision-making process and pressure at the group level are the most important aspects for the banks to do business with the poor, illiterate and informal groups. There is a huge demand for credit in small amounts for consumption, health, education, marriage, petty production, petty trade, etc., for very short to long durations which does not match with the supply menu of banks which consists of large amounts of loan for production proposes but not for very short periods. It is not the rigidity of the banks but their constraints due to high transaction costs and risk because of asymmetric information that they cannot extend such credit to individual borrowers. Individual borrowers, on the other hand, face the problems of absorbing large amounts of credit for some unwanted purpose. Loan contract therefore does not take place between an individual small borrower and a formal lender basically because of mismatch of demand and supply of credit structure. Instead when the FI extends credit to the SHG, (i) the transaction cost for the FI is minimised because the group takes the decision to borrow on behalf of the members, and also the responsibility to repay; (ii) the transaction cost of the individual member is reduced because the member transacts at the group level only; (iii) the mismatch between demand and supply is reduced because the bank extends credit in lumpsum amount and the group uses the amount according to its own needs; also repayment pattern of the members to the group and of the group to the bank need not be the same. When both the lender (FI) and the borrower (SHG) grow in mutual trust and the borrower honours the previous contracts, the lender expresses its willingness to extend higher amount of credit and even provides cash credit facility implying more flexibility and lesser interest burden for the borrower; the SHG in turn increases its capacity to manage higher amount of finance, develop entrepreneurial and communication skills and logical ability, co-operative sense and finally income and employment generating confidence. A sustainable financial relationship between the FI and the poor (SHG) people develops for their mutual benefit.

This is not confined to a single group of about 20 people. Either because of the efforts of the SHPI or demonstration effect, more groups start forming and functioning. A linkage among the groups also evolve. Some of the old leaders themselves take the role of facilitators for promoting other groups. The role of SHPI worker in a particular area then declines. He/she is now available for promotion of groups in other villages/areas. In some cases a number of nearby groups are federated. This federation is nothing but a co-ordinating mechanism and is not expected to assume any hierarchical role. Crucial decision-making process for sanctioning loan to individual members remains with the SHG. The federation is basically supposed to: (i) channelise funds from surplus to deficit SHGs, (ii) promote more SHGs and act as facilitator for weak SHGs, and (iii) perform entrepreneurial jobs like helping the grassroot SHGs for backward and forward linkage and liaisoning with external agencies for the benefit of groups. The SHGs pay some

membership fee for the sustenance of federation. Banks may sometimes find it more convenient and economical to deal with the federation rather than individual SHGs. It is however far better if the banks have direct links with the SHGs individually so that they can monitor their portfolio more closely. The federation may have strong hold over the SHGs, if the latter surrender substantial amount of management rights over their resources to the former which is against the principle of SHG promotion - a concept different from the existing co-operative structure. The peer pressure which is inversely proportional to the distance is much less at the federation level than at the village or group level. Nevertheless, the federation has an important role in the SHG framework, more as a development rather than a financial intermediator for the FIs.

7. *Grameen Bank Groups*

Alternative to the SHGs, the other type of group lending, although in smaller number, is through groups of Grameen Bank Group (GBG) model of Bangladesh. The groups are much smaller, i.e., of five members to start with thrift. However, unlike in the SHGs, the GBG does not manage its resources. The individual savings is deposited in the bank, and the members get loan directly from the bank. The GBG only helps the bank in screening the borrower and assuring repayment. Although the bank benefits, the GBG does not develop much skill in financial management. In fact it does not have much financial resource to manage. Although 0.5 per cent of loan amount is deducted to develop a group fund, it is negligible in comparison to at least 2 per cent per month of rate of interest. As propensity to save (voluntary) for the poor people is much less than the compulsion to pay interest (involuntary), the forced saving in the GBG is much less than in the SHGs. The interest earned in the group after all belongs to its members. The GBG groups permanently remain dependent on the banks or promoter NGOs. But so many SHGs have been found to become independent of banks for their credit requirement (Dasgupta *et al.*, 2001).

A majority of the NGOs in India promote SHGs only, and the commercial banks lend to the SHGs or to the NGO or federation for 'on-lending' to the SHGs. Very few NGOs like ADITHI in Bihar, ASA (Activists for Social Alternatives) in Tamil Nadu, RDO (Loylam Bank of Rural Development and Organisation) in Manipur and SHARE (Society for Helping and Awakening Rural Poor through Education) in Andhra Pradesh follow the Grameen Bank model for group lending (HDFC, 1997).

Besides these NGOs, one public sector bank, viz., Oriental Bank of Commerce (OBC) is experimenting with GBG model in Dehradun in Uttaranchal and Hanumangarh in Rajasthan (Rao *et al.*, 2001) which is called Oriental Bank Grameen Project (OBGP). Eight to ten groups in a village have been federated as a centre. To start with, a completely dedicated branch in Rudrapur is transacting with such groups only. Interestingly, this branch has started showing profit from the second year of existence despite heavy expenditure on group formation in the initial period; it has been found to be more efficient than similar branches in that area; it has been found

to be not only viable but also sustainable considering the business growth. Besides, a culture of subsidy-less credit has taken root in these villages (Rao *et al.*, 2001).

8. *Interest Rate*

These SHPIs along with others who promote the SHGs get refinance from different national financial institutions like NABARD, SIDBI (Small Industrial Development Bank of India), FWWB (Friends of Women World Banking), HUDCO (Housing and Urban Development Corporation), RMK (Rashtriya Mahila Kosh), HDFC (Housing Development Finance Corporation) and a host of other international institutions. Most of the above institutions except RMK and commercial banks, do not fix a ceiling on interest rates on the loan amount for lending to the members of the group. The groups are the best judges to determine the rate of interest. It should be as close to the market rate as possible. This excludes the possibility of moral hazard as an influential heterogeneous element in the group does not have any incentive to borrow from the group to lend at higher (market) rate of interest outside the group. Secondly, this interest amount goes back to the group fund which is owned by the members themselves. So this interest amount can be considered as deferred income which is forced saving in the current period. This acts as insurance substitute; increase the resiliency of food-insecure households and also the risk bearing capacity which facilitates adoption of new technology (Zeller *et al.*, 1997). Net interest paid by the members varies between zero and bank rate of interest depending upon the composition of the working fund: (i) group saving and (ii) bank credit.

9. *Financing SHGs in India: An Overview*

There is not yet any formal official publication on different statistics of SHGs. NABARD however has brought out a publication on some basic data on SHGs (NABARD, 1999-2000). According to this, the number of SHGs availing credit has increased from 3,841 in 1997 to 81,780 in 2000. The total number of SHGs linked to the banks stand at 1,14,755 in March 2000. Eighty-five per cent of them are women groups. The number of FIs extending credit to the SHGs has increased from 120 in 1997 to 266 in 2000. Out of the 266 FIs, 27, 13, 165 and 61 are public, private, regional rural and co-operative banks respectively. These SHGs are operating in 362 districts of 24 states and union territories. The number of NGOs dealing with the SHGs has increased from 220 in 1997 to 718 in 2000. Bank loans to these groups has increased from Rs. 118 million in 1997 to Rs. 1,930 million in 2000. The number of families assisted increased from 0.15 million in 1997 to 1.90 million in 2000.

Three broad models of bank-SHG linkage which have emerged are: Model 1 in which the bank itself acts as SHPI and forms and nurtures the SHG, Model 2 in which the NGOs act as SHPIs and banks lend to the SHGs directly, and Model 3 in

which the NGOs act as both SHPI and micro finance intermediaries (mFIs). In Model 3 banks lend to the NGOs for on-lending to the SHGs. Disbursement under Model 1 remains more or less the same: 13 per cent in 1997 and 14 per cent in 2000. The major change that has taken place is with regard to Models 2 and 3. Whereas the share of Model 2 has gradually increased from 45 in 1997 to 70 per cent in 2000, that of Model 3 has been continuously declining from 42 in 1997 to 16 per cent in 2000. Lending institutions are thus becoming more comfortable in dealing with grassroot SHGs which is a positive development.

Average credit per SHG extended under Models 1, 2, and 3 are Rs. 25,056, Rs. 20,415 and Rs. 16,190 respectively. Bank's preference of the SHGs in descending order is thus quite clear; (i) SHGs formed by themselves, (ii) SHGs to which they lend directly, and lastly (iii) to 'invisible' SHGs which they finance through the NGOs. Models 2 and 3 together account for 85.7 per cent of the SHGs and 82.4 per cent of disbursement indicating a substantial involvement of the NGOs in the credit business of the SHGs.

Three sets of FIs, viz., commercial banks, regional rural banks (RRBs) and co-operatives account for 55, 41 and 4 per cent of the SHGs and 66, 30 and 4 per cent of credit respectively. The average amounts of credit per SHG by these institutions are Rs. 24,765, Rs. 14,734 and Rs. 19,091 respectively. The co-operative sector's involvement in SHG is quite negligible except in the eastern region (especially in West Bengal) where it accounts for 21 per cent of credit. Unless the State Governments change the laws, it is difficult for them to lend to the SHGs outside the framework of Primary Agricultural Co-operative Societies (PACS). The RRBs are more active in North-Eastern, Central and Eastern regions accounting for 82, 53 and 48 per cent of credit respectively; commercial banks which are the major players, on the other hand, are more active in Western, Southern and Northern regions accounting for 76, 70 and 59 per cent of SHG credit respectively. Commercial banks and RRBs disburse about 1 and 2 per cent of their rural credit (agriculture and allied) to the SHGs respectively. With regard to rural business, the RRBs are thus more involved with SHG credit.

What is however of concern is the skewed growth of the SHGs across the regions. The Southern region accounts for 67 per cent of the SHGs and 78 per cent of the SHG credit. This is mainly because of presence of large number of NGOs there. Sixty-one per cent of the NGOs operate in the Southern region where 74 per cent of NGO-linked SHGs function. The poorer regions like North-Eastern, Eastern and Central, which are credit starved areas, account for only 0.2, 4.1 and 6.9 per cent of SHG credit respectively. Only 1, 12 and 9 per cent of SHPI-NGOs are in these three regions. In the Eastern region 64 out of 82 NGOs (78 per cent) are in Orissa alone, indicating a further skewness within a region. In the Southern region Andhra Pradesh accounts for 60 per cent of the SHGs and 57.3 per cent of the SHG credit. In the Central region Uttar Pradesh accounts for 82 per cent of the SHGs.

Besides the availability of NGOs, the ability, integrity, experience and finally their acceptability by the FIs are the other factors which help the SHGs in getting credit. Whereas in the Western and Southern regions the average number of SHGs per NGO having availed bank credit is 92 and 66 respectively, in other regions these figures are below 30. Among the states, Andhra Pradesh, Gujarat, Maharashtra, Karnataka, Bihar, Tamil Nadu and Uttar Pradesh fare better with 145, 109, 76, 62, 59, 55 and 53 credit-linked SHGs per NGO respectively. Among these, Bihar, Maharashtra, Uttar Pradesh and Gujarat have 8, 18, 23 and 25 NGOs which have been accepted by the FIs.

10. *Field Level Observations on SHGs*

Recently, NABARD has studied SHGs in 22 districts of 11 states {Puhazhendhi and Satyasai (PS), 2000} and National Institute of Bank Management (NIBM) has studied SHGs in four districts of Maharashtra {Dasgupta *et al.* (DE), 2001} promoted under Maharashtra Rural Credit Project (MRCP). All these are women groups.

The average size of the groups are found to be 16 and 17.5 by PS and DE respectively. DE further observed that 69 per cent of the groups are of the size 11-20. In both PS and DE about 50 per cent of the members are illiterate (including those who can sign only) and 25 per cent of them are with secondary level of education. DE however observed that 55 per cent of office bearers are having at least secondary level of education. Agricultural labour, and marginal and small farmers constitute about 85 per cent of the SHGs' membership. PS observed that homogeneity of the group is mostly in terms of similar standard of living and proximity of residence.

According to DE, the average savings or thrift rate of the SHGs in MRCP is Rs. 24 per month per member. This rate for newer groups is more than that of the older groups. Newer groups are thus more confident about the group dynamics and ready to start with larger amount of thrift. Older groups, however, after starting with smaller amount of thrift have increased the rate. A few groups, on the other hand, could not sustain and reduced the rate. About 30 per cent of the groups of the age of 3 years or more have changed the rate at least once. The average amount of savings mobilised is Rs. 10,658 per group. Eleven per cent of the groups (mostly older) however have mobilised more than Rs. 20,000, a significant achievement for those who are not expected to have savings capacity!

The SHGs in MRCP have generally been found to start internal lending with their own thrift capital on the eighth month of their formation. Newer groups have started internal lending much earlier than the older groups re-emphasising the growing confidence among the poorer people in the SHGs. Older groups waited for a longer period to gain enough mutual trust to start lending to their peers. Majority of the SHGs extend loan at a rate of 2 per cent per month, followed by 3 per cent. Nine per cent of the groups reduced the rate of interest over time. May be the members have been moving from small, short, consumption loan to large, long, production loan -

implying a larger interest burden and cost disadvantage in the competitive market. Whereas the average loan for some members is Rs. 100 or less, for some it is more than Rs. 20,000.

Around 50 per cent of the groups in MRCP have taken credit from banks. Ten per cent of them have taken loan three times or more. Recently, banks have started providing cash credit facility too to the SHGs. At the same time, about 20 per cent of the older groups have not yet taken any loan. Some have not yet graduated; some have formed groups with thrift as the prime motive. Also, among the borrowing groups, all do not like to take bank credit indefinitely. There is a clear evidence from the talks with members and also the financial data of the SHGs (Dasgupta *et al.*, 2001) that the groups like to either reduce the quantum of further bank loan or completely stop borrowing because of adequate finance of their own. For increasing the credit absorption capacity, vocational and management skill and backward and forward linkages are extremely important. Presently, most of the loans are taken for agricultural activity, followed by petty business, allied activities, medicine, family need, marriage and house building.

This credit process has tremendous effect on informal moneylending. Only 7 per cent of the SHG members in comparison to 54 earlier continue to take loans from the moneylenders. The decline in the interest rate however is negligible (Dasgupta *et al.*, 2001).

Besides, there has been a significant social impact too. These 'mute' members earlier can now organise meetings, discuss and communicate with others, liaison with different agencies and take larger decisions. These members are able to take up socio-economic issues of the villages, viz., alcoholism, problems of road, lighting and water supply, non-functioning of schools, etc. For all these they face criticism and adverse comments too (Dasgupta *et al.*, 2001).

Banks too are gradually realising the significance of SHG credit in terms of: (i) credit according to the need of the clients, also according to the affordable framework for bank; (ii) gradual improvement of credit handling capacity by the poor; (iii) credit-discipline; and (iv) lower transaction cost. It is interesting to note that repayment rate for bank loans for three types of clients, viz., (i) typical weaker section borrower, (ii) SHG member borrowing directly from a bank, and (iii) SHG are 58.1, 66.7 and 83.1 per cent respectively, indicating an unambiguous superiority of bank-SHG-client relationship (Dasgupta *et al.*, 2001).

Banks have gradually increased their exposure to SHGs. The percentage of savings-linked SHGs financed by a branch has increased from 7.1 in 1995-96 to 33.1 in 1999-00 because of the growing confidence. The average size of a bank loan has increased from Rs. 11,050 to Rs. 23,100 in MRCP command areas. Although the share of SHG deposit to total deposit in the MRCP branches has not improved, the share of SHG disbursement to total disbursement has marginally increased.

11. *Oriental Bank Grameen Project (OBGP)*

In a span of 4 years, since 1997, Oriental Bank of Commerce (OBC) has expanded the OBGP model to 64 villages with 769 groups and 3,845 members. Rs. 10.2 million in savings has been generated and Rs. 35.1 million has been disbursed, out of which 64 per cent has already been repaid. Otherwise the recovery rate with regard to actual demand at any point of time is 100 per cent. All group-level accounts are maintained by a facilitator who is paid honorarium by the group members (Rao *et al.*, 2001).

As in the case of SHGs, several loans were taken by the OBGP members. Forty per cent had taken loans three times or more from the bank. Five per cent had taken loans as low as Rs. 500 at a single time. But because of multiple loans 34 per cent had taken cumulative loans of Rs. 15,000 or more. Since the loan is made available at the doorstep, transaction cost for the OBGP members is 0.8 per cent whereas for other typical weaker section borrowers of an OBC branch it is 9 per cent. Like SHG members elsewhere, these OBGP members too experienced a tremendous social improvement (Rao *et al.*, 2001).

12. *Role of NGOs and SHPIs*

The major factor behind the satisfactory growth of SHGs is the role of NGOs and SHPIs. It is the Development Manager in the case of OBGP. These SHGs have not cropped up overnight. Whatever gain the SHG members have got or the benefits banks have received is because of hard work of field workers (FWs) who are generally women. These FWs require 5-6 visits to the village in a span of 3-4 months to form a group. Subsequent groups in the same village however take much less time for formation, if the earlier groups were successful. The FWs face lot of problems from different quarters while promoting these groups. The first problem while entering the village is the resistance they generally face. The second problem is related to work hazard which include (i) inadequacy of training; (ii) attracting unhealthy attention from the male world; (iii) need to work late into the night; and (iv) travelling through isolated areas in infrastructurally backward places. The NGOs which can support their FWs under these hazards can succeed in linking their SHGs to banks.

All these however are not free. The costs include: (i) salary of field workers, (ii) travel cost of FWs from one village to another, (iii) training cost for FWs and other staff members and SHG members, and (iv) monitoring, controlling and supervision. For the village level framework, only the first item is most important; training cost is required for the long-term growth; travel cost is important for the operation in a cluster of villages; and supervision costs become significant when operational area is spread over more than one block, or more than one district. For operation in one district, the district level monitoring is enough. Another tier of

supervision is required if the SHG network covers a large number of districts or states.

Based on the data available from Mahila Arthik Vikas Mahamandal (MAVIM), a parastatal organisation and the most important SHPI in MRCP, the average cost per SHG per annum (Dasgupta *et al.*, 2001) in the first year ranges between Rs. 620 to Rs. 3,513 depending upon the items included in the cost calculated. The cost however declines over time as the SHG members themselves take up some of the responsibilities. In the fifth year the above cost on the basis of current price ranges between Rs. 555 and Rs. 2,868. This decline depends on the strategy of concentrating on a fewer villages at first, stabilising a large number of groups there and then moving on to other villages.

13. *Concluding Observations*

What has been observed here is that micro financing through informal group approach has effected quite a few benefits: (i) savings mobilised by the poor; (ii) access to the required amount of appropriate credit by the poor; (iii) matching the demand and supply of credit structure and opening of new market for FIs; (iv) reduction in transaction cost for both lenders and borrowers; (v) tremendous improvement in recovery; (vi) heralding a new realisation of subsidy-less and corruption-less credit; and (vii) remarkable empowerment of poor women.

The major factor behind the limited success is the absence of any target approach but at the same time it is due to the consistent efforts by NABARD, SHPIs and their donors. Government agencies have not been involved very prominently. But the irony is that the government with the zeal of poverty alleviation has announced Swarnjayanti Gram Swarozgar Yojna (SGSY), with SHG at the core. Unfortunately, it has all the usual ingredients like (i) target, (ii) subsidy, (iii) both bureaucratic and political involvement in the credit process, (iv) insistence on entrepreneurial income generating activity, and most importantly, and (v) lack of understanding of the nuances of rural financial requirements. What is ignored is that these areas lack profitable investment opportunities (Zeller *et al.*, 1997). These opportunities need to be created first before thrusting upon anyone investment credit.

The government instead is required to create an environment where genuine NGOs can perform effectively as SHPIs and banks can conduct business with SHGs on their own. The right type of incentives for banks in terms of grading, income-tax benefit, performance appraisal and reward and punishment, etc., are the better tools and should be tried first. Government can promote SHPIs in NGO-lacking regions through well-established and well-accepted SHPIs, and continuation of support depending upon their performance. Banks, on the other hand, should be left free to evaluate SHPIs and SHGs for conducting business with them. The subsidy amount may be used for infrastructure, training, backward and forward linkages and other requirements of the poor, not the poor-borrowers alone.

All these are likely to improve the opportunity for investment by the poor. Simultaneously, the poor will improve their savings potential, credit-handling capacity and access to financial institutions, inculcate entrepreneurial skill, develop an urge for investment and also increase the risk-taking attitude through SHGs. Only then will investment credit fructify. Government needs to ensure adequate flow of credit to the poor according to their needs and facilitate opportunities of income generation. Along with monitoring mandatory credit, government needs to monitor efficacy of the credit through appropriate tools (Dasgupta, 1994). The SHGs should be considered as one of the best means to counter social and financial exclusion and enhance economic, political and social citizenship (Rogaly *et al.*, 1999) not an end in itself.

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