Indian SHG Microfinance experience - endeavors and Challenges

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ABSTRACT

Microfinance in India presently is too small to create a great impact in poverty alleviation, but if provide new technologies with skills and opportunities for the development of the poor, it holds to change the socio economic face of the India's poor. The self-help group (SHG) model with bank lending to groups without collateral has become an established part of rural finance. SHG-based microfinance look after and supported by NGOs, have become an significant alternative to traditional lending in terms of reaching the poor without increase in operating and monitoring costs. The government and financial institution have accepted this and have highlighted the SHG model and take initiatives to work along with NGOs. Million of SHGs have been linked to banks over the years but still most of the states are not doing well to established the development process of the poor and also do not link up and nurtured the various schemes of the Govt. The paper also discuss the why rural poor easily get the loan from the private players and not with the rural banks.

Keywords: India, microfinance
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Introduction:

The Indian state put stress on providing financial services to the poor and underprivileged since independence. The commercial banks were nationalized in 1969 and were directed to lend 40% of their loanable funds, at a concessional rate, to the priority sector. The priority sector included agriculture and other rural activities and the weaker strata of society in general. The aim was to provide resources to help the poor to attain self-sufficiency. They had neither resources nor employment opportunities to be financially independent, let alone meet the minimal consumption needs.

Microfinance refers to small scale financial services for both credits and deposits-that are provided to people who farm or fish or herd; operate small or micro enterprise where goods are produced, recycled, repaired, or traded; provide services; work for wages or commissions; gain income from renting out small amounts of land, vehicles, draft animals, or machinery and tools; and to other individuals and local groups in developing Countries in both rural and urban areas.

The growth of Microfinance sector in India has been significant over last two decades. There exist different approaches and models of microfinance; the most predominant in operation among them is the Self Help Group (SHG) model. The SHG interventions in the country have reached out to more than 17 million households becoming the largest microfinance endeavours in the world in terms of outreach. The Indian microfinance experience is unique in its diversity and has involved the stakeholders such as NGOs, microfinance intermediaries, donor agencies, NABARD, SIDBI, commercial banks, insurance providers, Self Help Groups (SHGs) and their federations, research and academic institutions and the government. The apex financing institutions and commercial banks have played a critical role in the tremendous growth of microfinance in India through the SHG-Bank linkage programme. The state governments have shown

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keen interest in microfinance as part of their development agenda and they support large scale microfinance programmes. Despite the remarkable growth and feats of the SHG movement in the country, sustainability of the SHGs continues to be a major concern. It has now been well established that access to a range of microfinance services through SHGs can bring about significant changes in the lives of poor. SHGs are proved to be a good tool for organising the unorganised and building social capital. The impact of SHGs has been well demonstrated on the aspects such as arresting leakages in household cash flows, increasing income, enhancing asset status, building selfesteem and confidence of women, improving leadership qualities etc. However it should be understood that these are mere beginnings and there is a lot to be done and accomplished. Considering the complexity of poverty issues there is an enormous need to retain and take these achievements forward through generations for comprehensive poverty reduction. But the SHGs in India remain to be the 'populist' programmes of state governments supported by larger bilateral donors and when there is a setback in these factors the very existence of these groups becomes an issue. There are very few examples in the country on deepening microfinance through federating these SHGs, mainly attributed to diversity of perspectives and institutional capacity among stakeholders on the issue. By many, sustainability is still perceived as mere financial self sufficiency ignoring other vital factors such as governance building, transformation of roles between the promoting organisation and people, creating institutional systems and processes, resource mobilisation and management, building alliances with other partners etc. On the other hand there are quality concerns leading to increase in number of dysfunctional groups and challenges like continuity in linkages with banks, and multiple lending. There is also a serious need for capacity building of SHG promoting organisations to impart 'know-how' on federating SHGs and establish mechanisms for achieving sustainability. There is a need for assimilating the wisdom of successful experiences and issues on sustaining SHGs and charting out way forward for policy advancement.

The credit scheme Integrated Rural Development Programme (IRDP) was launched in 1980. But these supply side programs (ignoring the demand side of the economy) aided by corruption and leakages, achieved little. Further, 'The share of the formal financial sector in total rural credit was 56.6%, compared to informal finance at 39.6% and
unspecified sources at 3.8%. [RBI 1992]. Not only had formal credit flow been less but also uneven. The collateral and paperwork based system shied away from the poor. The vacuum continued to be filled by the village moneylender who charged interest rates of 2 to 30% per month. 70% of landless/marginal farmers did not have a bank account and 87% had no access to credit from a formal source. It was in this cheerless background that the Microfinance Revolution occurred worldwide. In India it began in the 1980s with the formation of pockets of informal Self Help Groups (SHG) engaging in micro activities financed by Microfinance. But India’s first Microfinance Institution ‘Shri Mahila SEWA Sahkari Bank was set up as an urban co-operative bank, by the Self Employed Women’s Association (SEWA) soon after the group (founder Ms. Ela Bhatt) was formed in 1974.

The first official effort materialized under the direction of NABARD.(National Bank For Agriculture And Rural Development). The Mysore Resettlement and Development Agency (MYRADA) sponsored project on “Savings and Credit Management of SHGs was partially financed by NABARD during 1986-87.¹

Section II: MFIs, Self Help Groups, Income Generation and Women Empowerment

Microfinance programs in developing countries have been enormously successful in providing credit to the poor women without any collateral who are largely bypassed by the conventional banks. Their success attracted the attention of both academic economists and policy practitioners around the world, and the flagship microfinance program Grameen Bank in Bangladesh and its founder Muhammad Yunus have been awarded Nobel peace prize in 2006. There is now a voluminous literature analyzing different aspects of the microfinance revolution that swept across the developing world in last thirty years.

The MFIs stress on asset creation by the SHGs and extend loans for production and provides training for the same. If any member needs credit beyond the stipulated limits they are allowed to draw from group funds and the amount is settled in the periodic (monthly) group meetings. SHGs consisting of poor members with identical socioeconomic backgrounds are usually more sensitive to the credit needs of the poor.

¹ Rajarshi Ghosh” Microfinance in India: A critique”
Under the microfinance programme, loans are extended to the ‘Self Help Groups (SHG) who pool a part of their income into a common fund from which they can borrow. The members of the group decide on the minimum amount of deposit which ranges from Rs 20 to Rs 100 per month depending upon the size of the group. The group funds are deposited with a Micro Finance Institution (MFI) against which they usually lend (The deposits are usually placed with a bank by the MFI) at a credit deposit ratio of 4:1 but the ratio improves with account performance record i.e. prompt repayment of loans. The group funds is the way ‘micro savings’ are enforced ,though it may seem like a collateral .The loan ticket sizes are usually Rs 2000/-to Rs 15,000.Though loan repayment is a joint liability of the group but, in reality, individual liability. is stressed upon. Maintaining group reputation leads to the application of tremendous peer pressure.

In India and other Asian countries the majority of SHGs consist of women because, in these countries, Self Employment through Microfinance was perceived as a powerful tool for emancipation of women. It has been observed that gender equality is a necessary condition for economic development. The World Bank reports that societies that discriminate on the basis of gender are in greater poverty, have slower economic growth, weaker governance, and lower living standards.

Loans obtained from MFIs are utilized in agriculture and small businesses. Independent incomes and modest savings have made women self confident and helped them to fight poverty and exploitation. Previously we had to shy away before our husbands to ask for one rupee. They do not have to wear tattered sarees anymore and, today, they have the confidence to come and talk to you without seeking permission from our husbands.

**Empowerment through microfinance :**

- Capacity to save and access loans
- Opportunity must be provide to undertake an economic activity
- Opportunity to visit nearby urban areas
- Knowledge of local issues, MFI procedures to provide loan, banking transactions
- Skills for income generation
- Decision making within the household
- Group support to individual clients - action on social issues
- Role in community development activities

Section III: Financing the SHGs

In India, the adaptation of the new microfinance approach by rural financial institutions assumed the form of the “Self-Help Group–Bank Linkage Program.” After an initial pilot study the RBI set up a working group on non-governmental organizations (NGOs) and SHGs. The working group made recommendations for internalization of the SHG concept as a potential intervention tool in the area of banking with the poor. The RBI was quick to accept the recommendations and advised the banks to consider mainstreaming lending to SHGs as part of their rural credit operations.

The financial needs of the SHGs are catered to by various financial institutions: the Commercial Banks, Co-operative Banks, Co-operative Credit Societies and Regional Rural Banks (RRB). They finance the SHGs directly or route their funds through a Microfinance Institution set up by an NGO (NGOMFI) or Non-Banking Financial Companies (NBFC).

The NGO-MFIs (the major source of MFIs in India) disburse loans from the line of credit which is provided to them by a Financial Institution. The advantages of intermediation of funds through NGOs are manifold: It leads to reduction in time of identification of creditworthy people, documentation and recovery. The fall in transaction costs is not less than 40%.

Along with developing saving and credit facilities, the NGOs engage in:

1) Providing Basic Education

2) Providing education of Health and Hygiene

3) Providing education and encourage on family planning.

4) Awareness about environment protection and biodiversity
5) Fostering an environment of gender equality.

In India, three types of SHG models have emerged:


2. Bank-Facilitating Agency-SHG-Members: Facilitating agencies like NGOs, government agencies, or other community-based organizations form groups.

3. Bank-NGO-MFI-SHG-Members: NGOs act both as facilitators and microfinance intermediaries. First they promote groups, nurture them, and train them, and then they approach banks for bulk loans for lending to the SHGs.

Section 4: Sustainability of Microfinance

Based on the success of new MFIs, India has ventured into official collaboration between NGOs, financial institutions, and the government of India. Collaboration between these organizations has been an outcome of greater emphases on a community approach to development through participatory method. Moreover, the need to be cost effective and sustainable while reaching the poorest was also an important factor in the collaboration of formal structures and NGOs.

In spite of the optimism generated by the expansion of SHG credit and the high recovery rate (According to NABARD 2003-04 report on SHG bank linkage it was more than 95%.) there is a gap between actual per capita credit provided to the poor and the demand.

The distribution of Microfinance in India was highly skewed, with 65% of the SHGs being in Southern India and these SHGs were enjoying 75% of the credit disbursed.

Though there is limited data on the accessibility of the poor in India to Microfinance programmes, available evidence suggests that 80% of the poor do not have any savings and 91% are without any formal credit. The effective rates of interest charged by the MF institutions are in the range of 14 to 36% p.a. In a country of one billion, where 25% of the population (As on 1st January, 2004 as per the CIA World Fact book) are below the national poverty line, and even among those above the poverty line, very few can afford to pay these kinds of interest rates. They may be able to only at a great cost and upto a
limited time. One reason why high interest rates prevail is because timely availability of credit is more important than cost of credit per se.

**Challenges:**

1. In India to Microfinance programmes, available evidence suggests that 80% of the poor do not have any savings and 91% are without any formal credit. The effective rates of interest charged by the MF institutions are in the range of 14 to 36% p.a.

2. Illiteracy and insufficient organizational experience of most SHG group members constrain the governance capacity in SHG group. This constraint, inherent to an organization of poor women, affects the ability of the group members to effectively perform oversight functions. Few group members were able to identify oversight of staff as one of their roles. Insufficient understanding of auditing expressed by the group members also reflected this weakness; group members perceived auditing more as a means to check for accounting errors rather than as a check on management.

3. One of the strengths of SHG group, its capacity to have staff to perform specialized functions. Furthermore, most or all the staff are locally recruited. The long-term strategy has to be in helping the SHG group recruit professionals directly.

4. Good systems provide efficient means to carry out routine functions of an group. Such systems should be cost effective and easy to use, while ensuring sufficient controls and efficiency. The groups needs to improve their systems and processes. Risk management, repayment monitoring, and financial management are some of the systems which need increased attention.

5. Accountability in a member-owned organization depends primarily on ability of the members to hold the organization accountable. One of the major factors influencing this ability is the awareness of SHG members of their rights and duties as members as well as their capacity to use this awareness. As in the case of governance, the high level of illiteracy and lack of organizational experience of most members is a constraint for most SHG members in performing this role.
Learning through experience contributes significantly to SHG members overcoming this constraint.

**Discussion and Conclusions:**

SHG-based microfinance in India has significant achievements: over 10 million people reached, Rs.8 billion (US$170 million) in savings mobilized, Rs.20 billion (US$425 million), and over 95% on-time repayment rate on these loans. However, the financial sustainability of SHGs has not been clear because several of their costs are subsidized by organizations that had promoted them, and because of less than market cost paid by SHGs on loans from banks. Similarly, their organizational sustainability has been suspect because of their small size, which limited the financial and human capital available to them, and thereby the services they could provide themselves.

NABARD has played a crucial role in the development of the SHG microfinance program. It has been focusing, perhaps justifiably given the slow initial progress of the program, on increasing the outreach of SHGs and strengthening their linkage with the banking system. However, given the exponential increase in the program in the recent years and similar trends observed in other microfinance programs around the world (including that of Grameen Bank) (World Bank 2003), the focus needs to shift to sustaining the benefits provided by SHGs. Despite the considerable achievements of the SHG-bank linkage program, sustainability of SHGs has not been clear. The extent of sustainability and factors determining sustainability are not known. Knowledge on impact is also inadequate. The need to investigate these issues is long overdue. Factors those are likely to make the benefits of SHGs sustainable need to be identified. Fundamental questions such as whether SHGs need to be sustainable for the program benefits to be sustainable need to tested. This shows that the SHGs need to be sustainable and suggests that SHG groups have the potential to contribute to this. This suggestion needs to be tested further. SHG federations studied for this paper provide several services to their member SHGs. These services help the SHGs gain economies of scale, obtain value-added services, reduce transaction cost, and enhance empowerment, thereby contributing to organizational sustainability of the SHGs.
References:


