The way forward

Microfinance has been hailed as the panacea to solving rural poverty in the 21st century. Microfinance however had a humble beginning in the 1970s when Professor Mohammed Yunnus lent $27 USD to 42 women in a remote village of Bangladash. Only 30 years later, the Grameen Bank he started has 3. 2 million borrowers, 1, 178 branches, services in 41, 000 villages and assets of more than $3 billion[1]. I first started to take an interest in microfinance when I visited a village in remote Buriram Province of Thailand. The village underwent a major transformation after it joined the Village Development Partnership organized by the Mechai Viravaidya Foundation. The programe was based on a microcredit scheme that lent loans to the villagers to engage in productive activities. It may seem cliché to say instead of handing the poor a fish on a plate, it is more useful to give them a fishing road. However once you walk into one of the villages transformed by microcredit, you really do feel that microcredit is more than just talk. What left me with a deep impression is seeing first-hand how micro-credit has a real impact on the villagers. In the village of Nong Phulong, many villagers have taken up loans to raise silk worm and weave silk clothes. Some villagers have even started a motor bike repair shop or started a recycling business. This has been an important additional source of income to the villagers in addition to cultivating their land. This source of income is especially important to them during the drought season, which helps carry them to the next harvest. Objective of EssayIndia has been one of the countries with the fastest growth of microfinance industry. Given its huge population, its potential for growth of the microfinance industry is enormous. What this essay aims to study is to compare the traditional form of MFI modeled after the Grameen Bank and the design of Self-Help Groups in India

under the form promoted by the National Bank for Agricultural and Rural Development (NABARD). The essay will first give an overview of the development of the two forms of microfinance institutional design in India. The set of data I use for analyzing the SHG will be from the official website of NABARD of India. As for the data on MFIs I will be using data provided by Microfinance Information Exchange (MIX). In the end I hope to assess both the weakness and strength of both systems and provide recommendations to improving the delivery of microcredit in India. Through this process I hope to utilize some of the knowledge such as I gained at AIT when designing capacity building programmes for microcredit practitioners. The Idea of MicrocreditMicrofinance aims to offer poor people access to basic financial services such as loans, savings, money transfer services and micro insurance[2]. Micro-finance is the provision of a broad range of financial services such as deposits, loans, payment services, money transfers, and insurance to poor and low-income households and, their micro-enterprises[3]. Traditionally commercial banks viewed the poor as an unreliable client that is not bankable as they had no collateral. Microfinance institutions pioneered by the Grameen Bank however believed that the rural poor, although owning no collateral can nevertheless repay their loans through their own productivity. It is believed that with proper support they can be productively engaged in income generating activities, such as processing and manufacturing, transportation, storing and marketing agricultural produce, and raising livestock. Moreover, the Grameen Bank maintains that if the poor are provided credit on reasonable terms, they are able to make entrepreneurial decisions to maximize their income. Based on these notions, Grameen Bank creates the social and financial conditions that

enable poor men and women to receive credit and lift themselves out of poverty. Microfinance in India- SHGs v GrameenThe microfinance industry has gone a long way since Professor Yunnus started his first loan. As of December 31, 2008, there were 1, 395 MFIs globally with an estimated borrower base of 86 million with a total outstanding portfolio of over $44 billion as reported by the MFIs to the Microfinance Information Exchange or " MIXMarket".[4]India has 400 million people who qualify to as being very poor, living on less than $1 per day. Microfinance has proven itself to be a way to provide a means for the poor to lift themselves out of poverty. What also need to be noted is that there have been a number of different forms of designs to provide microcredit. Among the various modes of microfinance institutions in India, the traditional form of Grameen Banks originating from Bangladesh and Self-Help Groups that are home grown have been widely adopted in India[5]. The Indian microfinance sector has two major models for microfinance delivery, which is the SHG Bank Linkage Programme (SBLP) and the MFI Grameen model. Both these models are very different from each other in methodologies adopted and their legal form of institution. A detailed comparison of the two models will be presented in the following chapter. SBLPAs the name suggests, an SHG is a group of people who have congregated to help themselves. According to The National Bank for Agricultural and Rural Development NABARD, an SHG consists of an average of 12-15 members, from a homogenous economic or social class to deal with common problems. The scaling-up of the SHG model started in the mid 1990s when NABARD launched the SHG-Bank Linkage Programme (SBLP) model in 1992[6]. The programme is designed to integrate informal savings and credit groups with the mainstream banking system. Under the SBLP,

NGOs usually act SHG Promotion Agencies (SHPAs) in which the role of the NGO is to provide developmental support to the SHGs. (NABARD) is the main promoter of SBLP, which also conducts various training for staff members from banks or NGOs[7]. Members of the SHG collectively deposit savings and members can then take turns borrowing from the Bank. The group usually first lend among themselves with the pooled savings. They keep records and accounts of such these transactions and when they become confident in their ability to handle larger volumes of credit, they approach banks for more sizeable loans. Under the SBLP, a bank lends to a group after evaluating the group's operations, maturity, and capacity to absorb credit[8]. Grameen Style BankThe Grameen style of microfinance consists of banking units which are usually groups of give, with separate groups for men and women[9].. Individuals receive loans, but the entire group is liable for repayment. If one member defaults, other group member will not be able to receive additional credit. This group pressure helps to ensure social and financial discipline among Grameen Bank members. However, in order to mitigate the entrenchment of vested interests and constellations of power, and to prevent individuals from taking antigroup actions, six to eight groups are organized into a community called the " center" [10]. Such two-tier peer monitoring and transparency in transactions eliminate possible problems of group collusion among self selected groups. Grameen Bank usually lends small amounts of loans to an individual member for a year. The loan is repayable in fifty equal weekly installments to ease the pressure on the poor to pay at once[11]. The loans are provided for activities identified and selected by each member of the five-member group, and members help each other in selecting the activity. Both selection activities and amounts of loans are

discussed in group and center meetings. To enable smooth operations and to oversee the group activity, a Grameem Bank worker will visit each center on a weekly basis. A comparison between the two modes of deliveryOutreach of ModelsIndia in recent years has seen a substantial growth in the outreach of microfinance. This is partly due to the phenomenal growth of Bank –SHG linkage programme promoted by the NARBARD, but also the growth of MFIs pioneered by Grameen organizations. Yet there is still room for growth in the sector as the combined efforts of SHG and MFIs cover around 20 million of the poor out of the 70 million poor in India[12]. In terms of model and legal forms, Grameen organisations have accounted for an increasing amount of memberships, reaching to 78% of total membership of microfinance in 2008[13]. In 2003 the SHGs linked with NGOs accounted for the majority of microfinance coverage as in the initial microfinance experience in India, most organisations such as IRDP, SGSY and later NABARD's SBLP started off as multi-service NGOs to support government initiatives. However in recent years microfinance institutions are starting to realize the potential for greater growth through transforming to for-profit entities and adopting the Grameen model to meet their growth requirements and to become self sufficient. Many lenders that began as non-profit organizations such as ASIX, SHARE, SKS, and Spandana have transformed into commercial microfinance institutions. As compared to SHG-Bank Linkage, these institutions have posted faster growth rates and reached far more borrowers[14]. The for profit legal form has the advantage that it can attract both equity funding from venture capitalists and loans from commercial banks which helps to facilitate their rapid growth. A reason for the slow growth of SBLGs is that there are no clear margins built into the program to take care of the cost of

building, managing, and scaling the program, except through grants, subsidies and other provisions made by government[15]. It is up to NARBARD operating on grants and NGOs to set up and promote SHGs. Another factor that has lead to the relatively slower growth of SBLG is that it takes around three years for a healthy SHG to develop self-governing capabilities. SHG themselves have to be responsible for book keeping and rotating loans among a relatively larger group than that of the Grameen system. Figures have shown that, the percentage of SHG programmes lending to clients through SHGs rather than the joint liability groups of the Grameen methodology has declined from 63% of membership in 2003, to 47% in 2005, 32% in 2007 to just 19% in 2008. MIX Data 2008Staff ProductivityThere are two key indicators to measure the efficiency of human resource utilization. One is the staff productivity ratios, which is the clients to member of staff. The other ration is the outstanding portfolio per member of staff. In 2008, it is the Grameen model in which per staff serves the largest number of borrowers (252) and a portfolio of Rs 11. 5 lakh ($28, 800). Grameen institutions have shown that it can become one of the most competitive MFIs in India by becoming more efficient. Staff productivity has increased from 146 in 2003 to 252 in March 2008. SHG are relatively inefficient serving just 175 borrowers per staff member who services a portfolio of Rs 8. 2 lakh ($20, 000). However it has to be noted that this figure incorporates only the clients that are currently borrowers, but not those who are savers and dormant clients. The SHG groups are usually two times larger than that of the Grameen system, which accounts for a larger amount of dormant clients. The average staff productivity of SHG programmes is much higher than that of the Grameen mode in terms of total

client members served when including both borrowers and savers. Moreover, the relatively low productivity of the SHG model is also due to the intensive staff inputs required in the initial years of developing the self-governance capabilities of client groups. This cost however decreases after the SHG is on track and able to govern itself.