Chapter I

Introduction
1.1 Introduction

The process of economic growth, especially when it is on high growth trajectory, must strive to encompass participation from all sections of society. Lack of access to institutional finance for the poorer segments of our society has been recognized as a serious threat to economic growth process especially in developing countries. Moreover, prolonged and persistent deprivation of banking services to a large segment of the population leads to a decline in investment and has the potential to fuel social tensions causing social exclusion (Mehrotra, Puhazhendhi, Nair G, & Sahoo, 2009). Access to formal financial services is essential to the ability of individuals and households to manage their lives and build their futures. Positive correlation has also been found between increased financial inclusion and lower inequalities, showing that financial inclusion promotes pro-poor growth. Access to financial services is also essential to the ability of businesses to invest, employ people and to grow and is therefore an essential element of an inclusive growth. It is also tied to the financing for development agenda, especially in relation to mobilization of domestic resources, given the direct links between domestic saving rates and long term economic growth (UNCDF, n.d).

It is a well known fact that in most developing countries, poor households rely heavily on informal financial institutions such as moneylenders, neighbours, relatives and local traders for credit, and may not have access to safe and convenient savings services (Ravicz, 1998). This is because of the fact that formal financial institutions such as commercial banks do not serve the needs of the poor households and micro-enterprises because of the high cost of small transactions, lack of traditional collateral, lack of basic requirements for financing and geographic isolation. Mamun and Fontaine (2008) mentioned in their work that the demand of the products and services offered by commercial banks are low among the poor not because of the fact that ‘poor do not need financial services’, but because of the fact that the products and services of the commercial banks are not designed to meet the requirements of the poor.

To fill the void, policy makers throughout the world have actively tried to improve the financial markets in poor regions. Many governments have introduced the delivery of formal credit to rural areas by setting up special agricultural
banks/state-owned development banks or directing commercial banks to loan to rural borrowers. However, these programmes have almost all failed because of the political difficulty for governments to enforce loan repayment and also because of the interest rate restrictions which prevented banks from operating viably in poor areas (Armendariz & Morduch, 2005). Moreover, the failure of these institutions could also be attributable to the fact that relatively wealthy and powerful people rather than the poor people received most of the loans granted by these types of financial institutions.

The recent proliferation of innovative microfinance programmes, often based on a group lending methodology has been largely inspired by the belief that such programmes reach the poor and have positive impact on their economic and social well being (Coleman, 2002). This has been accompanied by the rise of social entrepreneurs, notably in Bangladesh. Using innovative strategies involving groups of women, joint liability, progressive lending, small loans and weekly repayments, they demonstrated that it is possible to lend to the poor and have high rates of recovery and because of that, a consensus on microfinance has developed, broadly within the neo-liberal framework, which highlights the possibility of profitable banking with the poor. Further, other financial services like savings, pensions, etc. can play equally powerful roles in helping poor people pay school costs, respond to health concerns and manage unforeseen shocks. Moreover, the peer pressure exerted by a group and the experience of channeling micro loans, especially to women is seen as an important means of alleviating both rural and urban poverty in most of the developing countries. By delivering financial services at a scale, and by mechanisms appropriate to them, microfinance can reach the poor thereby helping them to make their own way out of poverty. Also by providing loans rather than grants, the microfinance institutions can become sustainable by recycling financial resources over and over again. In other words, microfinance appears to deliver the ‘holy trinity’ of outreach, impact and sustainability.

Microfinance, since its inception in the 1970s, has evolved in astounding ways, incorporating into its practice social and economic development concepts, as well as principles that underlie financial and commercial markets. This combination has led to the creation of a growing number of sustainable microfinance institutions
around the developing world (Otero, 1999). These institutions anchor a movement that is global and growing and have created new opportunities in contexts as diverse as villages along the Amazon, inner-city Los Angeles, and war-ravaged Bosnia. Moreover, these programmes are also well established in Bolivia, Bangladesh, and Indonesia, and momentum is gaining in Mexico, China, and India (Armendariz & Morduch, 2005). According to Robinson (2001), microfinance revolution is the process—recently begun, but under way in many developing countries—through which financial services for the economically active poor are implemented on a large scale by multiple, competing, and financially self-sufficient institutions. In 2003, Khandker states that the microfinance revolution has changed attitudes towards helping the poor in many countries and in some has provided substantial flows of credit, often to very low income groups or households who were hitherto been excluded by the conventional financial institutions.

In the words of Morduch (2000), “microfinance promises both to combat poverty and to develop the institutional capacity of financial systems through finding ways to cost effectively lend money to poor households”. Moreover, there is strong demand for small scale commercial financial services both credit and savings among the economically active poor of the developing countries (Robinson, 2001). Further, the informal and flexible services offered to low-income borrowers for meeting their modest consumption and livelihood needs have not only made microfinance movement grow at a rapid pace across the world, but in turn has also impacted the lives of millions of poor positively (RBI, 2008).

1.2 History of Microfinance

The word microfinance is relatively a new term in the field of development first coming to prominence in the 1970s (Robinson, 2001; Otero, 1999). But the concept is not new. The informal savings and credit groups that have been operating across poor communities for centuries are the SUSUS of Ghana, TONTINES of West Africa, STOKVELS in South Africa, CHIT FUNDS in India, HUI in China, PALUWAGON in the Philippines, TANDAS in Mexico, ARISAN in Indonesia, CHEETU in Sri Lanka and PASANAKU in Bolivia, as well as numerous savings clubs and burial societies found all over the world. These informal groups are also
known as Rotating Savings and Credit Associations (ROSCAs). ROSCAs consist of a group of men and/or women who contribute to a collective fund and decide either by auction or collective decision, to contribute collected money to one of the group members. The other type of informal group is also known as Savings and Credit Cooperatives (SACCOs) (http://www.globalenvision.org; H. R. Singh & Singh, 2011; Seibel, 2005; McKeever, 2009).

One of the earlier and successful, longer-lived, self-sustaining, large-scale microcredit organization that made millions of loans, without collateral, to the poor was the Irish Loan Fund System. The loan funds were an important microcredit institution which operated in Ireland for more than 200 years. The Irish Loan Funds had evolved with the efforts of a notable Irish author and nationalist Dean Jonathan Swift during the early 1700s as a single small fund in Dublin to assist the industrious poor who could not obtain credit from elsewhere and to smooth consumption among the poor. Swift’s idea slowly took root and a network of local, independent, and charitably constituted microcredit institutions or loan funds, arose in the entire Ireland in the face of undercapitalization to provide a form of poverty relief and small scale economic development for the rural poor. But after a century of slow growth, these organizations witnessed a very rapid growth due to a special law in 1823, which legalized financial intermediation by allowing the funds to collect interest-bearing deposits and to charge interest on loans thereby creating the Loan Fund Board in 1836 for their regulation and supervision. By the early 1840s, these funds had grown into a widespread institution of about 300 funds all over Ireland. They made small loans to the poor and at their peak were lending to approximately 20% of Irish households. Loans were given for short period and instalments were paid weekly. Peer monitoring was used to enforce repayment. But unfortunately commercial banks used their power and influence to stop the funds by getting the government to put a cap on the interest in 1843. The loan funds thus lost their competitive advantage, which caused their gradual decline during the second half of the 19th century and finally disappeared in the 1950s. Hamburg established a similar community owned financial system in 1778 but unfortunately this also ended due to outside intervention There were also evidences of several charitable pawnbrokers, Mont-de-Piété, that operated in various cities throughout the Ireland.
Another longer lived microfinance story is the history of microfinance in Germany covering more than two centuries, is one of self-help, regulation and supervision, which have created, relative to its population, the largest microfinance sector of any country. It comprises two networks: one is community savings funds, now referred to as savings banks and the other one is member-owned cooperative associations, now referred to as cooperative banks. The community owned financial institutions started during the latter part of the 18th century. Having learned from the early Irish charities that charity is not sustainable and that there is a strong demand among the poorer sections of the population for savings and deposit facilities. Thus the first thrift society was established in Hamburg in 1778, followed by the first communal savings fund in 1801 (Seibel, 2005).

In the 1800s, various types of larger and more formal savings and credit institutions began to emerge in Europe, organised primarily among the rural and urban poor. These institutions were known as People’s Bank, Credit Unions, and Savings and Credit Co-operatives (http://www.globalenvision.org). But after the hunger year of 1846/47, starvation was widespread, many peasants lost their fields to the money lenders, and also many small businesses went bankrupt. At that time, two men were prominent among those who took action: Friedrich Wilhelm Raiffeisen created the credit associations in the rural areas specially for farmers and Schulze-Delitzsch created the savings and credit cooperatives in the urban areas for the craftsmen and other small entrepreneurs (Seibel, 2005). Their altruistic action was motivated by concern to assist the rural population to break out of their dependence on money lenders and to improve their welfare. From 1870, the unions expanded rapidly over a large sector of the Rhine Province and other regions of the German states. The cooperative movement quickly spread to other countries in Europe and North America, and eventually supported by the cooperative movement in developed countries and donors, also to developing countries (H. R. Singh & Singh, 2011).
In Indonesia, the Indonesian People’s Credit Banks (BPR) or The Bank Perkreditan Rakyat opened in 1895. The BPR became the largest microfinance systems in Indonesia with close to 9,000 units (http://www.globalenvision.org).

Between the 1950s and 1970s, the financial services for the poor was mainly provided by donors or governments and was in the form of subsidized rural credit programmes. These often resulted in high loan defaults, high loses and an inability to reach poor rural households (Robinson, 2001).

1.3 Genesis of Modern Microfinance

The contemporary understanding of microfinance took a big leap in the 1960s and 1970s, when a few scattered Microfinance Institutions (MFIs) or Organisations (MFOs) such as the early ACCION affiliates in Latin America, Yunus's Grameen Bank in Bangladesh, Badan Kredit Desa (BKD) village banks, the Bank Dagang Bali (BDB) and BRI Unit system in Indonesia, the Self Employed Women’s Association (SEWA) Women’s Cooperative Bank in India and various NGOs, credit unions, and cooperatives in a variety of countries began offering small credit solutions to ‘unbankable’ poor people (Robinson, 2001; Tavanti, 2012). During the 1970s, these institutions developed lending methodologies in such a way that suits low-income clients in both rural and urban areas and demonstrated that microcredit could be delivered at an interest rate which covers the entire cost of lending and at the same time can exhibit high repayment rates (Robinson, 2001). By formalizing and expanding the basic concept of sharing programs, these microfinance institutions helped to build capital for small businesses rather than just loaning for basic necessities such as food, water and clothing (http://www.pbs.org). Both BDB and SEWA operated from the beginning without subsidies and emphasized voluntary savings as well as loans, set interest rates to cover all costs and risks, and thereby developed the early models of sustainable microfinance institutions. Robinson (2001) also states that the 1980s represented a turning point in the history of microfinance in that MFIs such as Grameen Bank and BRI began to show that they could provide small loans and savings services profitably on a large scale. The Grameen Bank’s group lending methodology as part of the paradigm shift
in microfinance became widely adopted by numerous institutions in many parts of the developing world.

1.4 Meaning of Microfinance

Microfinance is a term of comparatively recent origin. It has proven as an effective and popular measure in the ongoing struggle against poverty, enabling those without access to lending institutions to borrow at affordable interest rates and start small business (Somanath, 2009). It is reflective of at least two elements which were not captured by earlier debates and concerns on the subject of rural credit. These are: (i) an emphasis on savings and other financial services apart from loans; and (ii) professional management of small loans and savings programmes as part of a perceived need for sound accounting, financial portfolio management and decision making for microfinance institutions (Sa-Dhan, 2005; Indian Institute of Banking and Finance, 2009). Often the term microfinance is limited to the narrow definition of ‘micro-credit for micro-enterprises’. However, microfinance, both in theory and in practice, includes a wider range of financial services that target low-income clients, particularly women. Since the clients of microfinance institutions (MFIs) have lower incomes and often have limited access to other financial services, microfinance products tend to be for smaller monetary amounts than traditional financial services. These services include loans, savings, insurance, and remittances. Microloans are given for a variety of purposes, frequently for microenterprise development. The diversity of products and services offered reflects the fact that the financial needs of individuals, households, and enterprises can change significantly over time, especially for those who live in poverty. Because of these varied needs, and because of the industry's focus on the poor, microfinance institutions often use non-traditional methodologies, such as group lending or other forms of collateral not employed by the formal financial sector (http://www.themix.org). Below given some of the definitions put forward by different experts and renowned institutions.

Robinson (2001) defines microfinance as small-scale financial services — primarily credit and savings — provided to people who farm or fish or herd; who operate small enterprises or microenterprises where goods are produced, recycled, repaired, or sold; who provide services; who work for wages or commissions; who
gain income from renting out small amounts of land, vehicles, draft animals, or machinery and tools; and to other individuals and groups at the local levels of developing countries, both rural and urban.

ADB (2000) defines microfinance as 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 microenterprises. According to ADB, microfinance services are provided by three types of sources:

- Formal institutions, such as rural banks and cooperatives;
- Semiformal institutions, such as nongovernment organizations; and
- Informal sources such as money lenders and shopkeepers.

RBI (2008) defines microfinance as the provision of thrift, credit and other financial services and products of very small amounts to the poor for enabling them to raise their income levels and improve their living standards.

NABARD (2011) refers the term microfinance as extending the whole range of financial services from savings to credit to micro insurance to micro enterprises and a lot more for the poorer sections of society whose scale of operations are so small and hence are generally excluded from the purview of the existing service providers. While definitions differ, microfinance is generally taken to refer to the provision of financial services, primarily savings and credit but also covers other financial services like insurance, leasing, money transfers, etc. to poor and low income households that do not have access to formal financial institutions.

Theoretically microfinance means all types of financial products and services used and/or required by poor section of the society who mostly do not have access to formal financial institutions and are more accessible to the informal financial market. But practically microfinance refers to the small scale financial services offered to poor people by institutions, organisations and enterprises who aim at their sustainability and profitability along with reducing the poverty of their clients (Panda, 2009).

According to Mamun and Fontaine (2008), “Microfinance is a logical approach to development because it functions at the grassroots level, can be sustainable, is capable of involving large segments of population, and builds both
human and productive capacity”. Microfinance creates access to productive capital, which together with two other forms of capital – human capital, addressed through education and vocational training, and social capital, built through creating representative, local organisation building, promoting democratic systems, and strengthening human rights – enables people to move out of poverty. For the very poor, microfinance becomes a liquidity tool that helps smooth their consumption patterns and to reduce their level of vulnerability (Otero, 1999). In other words, we can say that microfinance is a movement that envisions a world in which low-income households has permanent access to a range of high quality and affordable financial services offered by a range of retail providers to finance income producing activities, build assets, stabilize consumption, and protect against risks. According to Ledgerwood (1999), microfinance activities usually involve the following:

- Small loans, typically for working capital.
- Informal appraisal of borrowers and investments.
- Collateral substitutes, such as group guarantees or compulsory savings.
- Access to repeat and larger loans, based on repayment performance.
- Streamlined loan disbursement and monitoring.
- Secure savings products.

### 1.5 Principles of Microfinance

Below given the key principles of microfinance as developed by CGAP

**Box 1.1: Key Principles of Microfinance**

<table>
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<tr>
<th>Principle</th>
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<tbody>
<tr>
<td>1. <strong>The poor need a variety of financial services, not just loans.</strong> Just like everyone else, poor people need a wide range of financial services that are convenient, flexible, and reasonably priced. Depending on their circumstances, poor people need not only credit, but also savings, cash transfers, and insurance.</td>
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<tr>
<td>2. <strong>Microfinance is a powerful instrument against poverty.</strong> Access to sustainable financial services enables the poor to increase incomes, build assets, and reduce their vulnerability to external shocks. Microfinance allows poor households to move from everyday survival to planning for the future, investing in better nutrition, improved living conditions, and children’s health and education.</td>
</tr>
</tbody>
</table>
3. **Microfinance means building financial systems that serve the poor.** Poor people constitute the vast majority of the population in most developing countries. Yet, an overwhelming number of the poor continue to lack access to basic financial services. In many countries, microfinance continues to be seen as a marginal sector and primarily a development concern for donors, governments, and socially-responsible investors. In order to achieve its full potential of reaching a large number of the poor, microfinance should become an integral part of the financial sector.

4. **Financial sustainability is necessary to reach significant numbers of poor people.** Most poor people are not able to access financial services because of the lack of strong retail financial intermediaries. Building financially sustainable institutions is not an end in itself. It is the only way to reach significant scale and impact far beyond what donor agencies can fund. Sustainability is the ability of a microfinance provider to cover all of its costs. It allows the continued operation of the microfinance provider and the ongoing provision of financial services to the poor. Achieving financial sustainability means reducing transaction costs, offering better products and services that meet client needs, and finding new ways to reach the unbanked poor.

5. **Microfinance is about building permanent local financial institutions.** Building financial systems for the poor means building sound domestic financial intermediaries that can provide financial services to poor people on a permanent basis. Such institutions should be able to mobilize and recycle domestic savings, extend credit, and provide a range of services. Dependence on funding from donors and governments—including government-financed development banks—will gradually diminish as local financial institutions and private capital markets mature.

6. **Microcredit is not always the answer.** Microcredit is not appropriate for everyone or every situation. The destitute and hungry who have no income or means of repayment need other forms of support before they can make use of loans. In many cases, small grants, infrastructure improvements, employment and training programs, and other non-financial services may be more appropriate tools for poverty alleviation. Wherever possible, such non-financial services should be coupled with building savings.

7. **Interest rate ceilings can damage poor people’s access to financial services.** It costs much more to make many small loans than a few large loans. Unless microlenders can charge interest rates that are well above average bank loan rates, they cannot cover their costs, and their growth and sustainability will be limited by the scarce and uncertain supply of subsidized funding. When governments regulate interest rates, they usually set them at levels too low to permit sustainable microcredit. At the same time, microlenders should not pass on operational inefficiencies to clients in the form of prices (interest rates and other fees) that are far higher than they need to be.
8. **The government’s role is as an enabler, not as a direct provider of financial services.** National governments play an important role in setting a supportive policy environment that stimulates the development of financial services while protecting poor people’s savings. The key things that a government can do for microfinance are to maintain macroeconomic stability, avoid interest-rate caps, and refrain from distorting the market with unsustainable subsidized, high-delinquency loan programs. Governments can also support financial services for the poor by improving the business environment for entrepreneurs, clamping down on corruption, and improving access to markets and infrastructure. In special situations, government funding for sound and independent microfinance institutions may be warranted when other funds are lacking.

9. **Donor subsidies should complement, not compete with private sector capital.** Donors should use appropriate grant, loan, and equity instruments on a temporary basis to build the institutional capacity of financial providers, develop supporting infrastructure (like rating agencies, credit bureaus, audit capacity, etc.), and support experimental services and products. In some cases, longer-term donor subsidies may be required to reach sparsely populated and otherwise difficult-to-reach populations. To be effective, donor funding must seek to integrate financial services for the poor into local financial markets; apply specialist expertise to the design and implementation of projects; require that financial institutions and other partners meet minimum performance standards as a condition for continued support; and plan for exit from the outset.

10. **The lack of institutional and human capacity is the key constraint.** Microfinance is a specialized field that combines banking with social goals, and capacity needs to be built at all levels, from financial institutions through the regulatory and supervisory bodies and information systems, to government development entities and donor agencies. Most investments in the sector, both public and private, should focus on this capacity building.

11. **The importance of financial and outreach transparency.** Accurate, standardized, and comparable information on the financial and social performance of financial institutions providing services to the poor is imperative. Bank supervisors and regulators, donors, investors, and more importantly, the poor who are clients of microfinance need this information to adequately assess risk and returns.

*Source: Adapted from http://www.cgap.org*
1.6 Meaning of Microfinance Institutions (MFIs)

In principle, Micro Finance Institutions (MFIs) are organizations that provide financial services to the poor. This includes a wide range of providers that vary in their legal structure, mission, methodology, and sustainability but yet share the common characteristic of providing financial services to a clientele poorer and more vulnerable than bank clients. In other words, it can be broadly defined as any organization-credit union, downscaled commercial bank, financial cooperatives that provide financial services to the poor (Fotabong, 2011).

The term Micro Finance Institutions (MFIs) is mostly used to refer to all types of formal and semi-formal institutions that offer microfinance services. These include the following list of Micro Finance Institutions but the list is not exhaustive.

<table>
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<tr>
<th>Table 1.1: Types of Micro Finance Institutions (MFIs)</th>
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<tr>
<td>Banks, Companies that fall under national banking laws with considerable microfinance activities.</td>
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<tr>
<td>Regulated MFIs (Non-Banking Financial Companies NBFCs), Financial intermediaries that are subject to government or Central bank rules and regulation but are not banks.</td>
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<tr>
<td>Micro-credit Companies, Non-regulated companies involved in microfinance.</td>
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<tr>
<td>Credit (and savings) co-operatives and credit unions, Formally registered co-operatives and unions that provide microfinance services to their members.</td>
</tr>
<tr>
<td>Development NGOs and other non-profit organisations, Registered as society or non-profit organisation or trust that acts as intermediary or facilitator in microfinance activities.</td>
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Thus, MFI is a financial institution which can be a non-profit organisation, regulated financial institution or commercial bank that provides microfinance products and services to low-income clients.

Initially microfinance was mostly provided by Non-Governmental Organisations (NGOs) and other development oriented organisations that wanted to do more than just non-formal education, technical assistance etc. In recent years, there has been a tendency for these informal credit providers to transform into a formal and professional microfinance institution. Some countries governments have established separate institutions for micro-finance to be regulated by the Central Bank. Regulation means in many cases that these MFIs are now allowed to capture savings and deposits from their clients and perform other financial services. More
recently, the Commercial banks have taken microfinance into their portfolios more aggressively than before.

As per the accepted definition, MFIs provide financial services to the low-income clients. However, an MFI may also offer other services as a means of improving the ability of its clients to utilise financial services (Ledgerwood, 1999). Based on this, there is much debate in the field of microfinance as to whether MFIs should be Minimalist – that is, offering only financial intermediation or Integrated – that is offering both financial intermediation and other developmental services. In otherwords, poverty reduction focused microfinance service providers/microfinance institutions are divided into two approaches in terms of their view on microfinance products/services: Minimalist and Integrated (Alemu, 2008). The decision to offer nonfinancial services determines whether an MFI is Minimalist or Integrated. But most MFIs offer social intermediation also as part of their business agenda but to a limited extent. A brief discussion on both the approaches is given below:

**Minimalist Approach**

MFIs using the minimalist approach usually offer only financial services, but they may occasionally offer limited social services too. Minimalists base their approach on the premise that there is a single ‘missing piece’ for enterprise growth, usually considered to be the lack of easily accessible short-term credit at an affordable price, which the MFI can offer. While other ‘missing pieces’ may exist, the MFIs recognises its comparative advantage in providing only financial intermediation. Minimalists acknowledge that the poor may need other development and social services, but they have to assume that other agencies will provide these, because provision of such services is not their corporate business. The advocates of this approach restrict their service only to the provision of credit only and the clients are expected to make the best out of the loan delivered. This approach offers the great advantage of having a single focus, which becomes more cost effective with time, so that subsidies that might have been necessary at the initial phase of the programme can gradually be eliminated. This approach is followed by microfinance institutions such as agriculture/farming banks or credit unions (Ledgerwood, 1999; Alemu, 2008).
Integrated Approach

The integrated approach takes a more holistic view and is referred to as the “credit-plus approach” is grounded within the empowerment framework and attempts to attack the structural causes of poverty. It is a comprehensive approach that provides a combination of both financial and non-financial services. The non-financial services include social intermediation like group formation, leadership training, co-operative learning and enterprise development services like imparting of production and marketing skills. Moreover, they also provide training in health, adult literacy, civil and human rights and environmental awareness besides financial services. The supporters of this approach acknowledges that credit alone may not be enough to ensure stable employment and productivity for the reason that the causes of poverty at the grassroots level are multi-dimensional ranging from economic and social problems to lack of marketable skills and managerial knowhow (Ledgerwood, 1999; Alemu, 2008; Sabharwal, n.d.).

An MFI chooses a minimalist or more integrated approach depending on its objectives and the circumstances (demand and supply) in which it is operating. If an MFI chooses to take an integrated approach, it should be aware of the following potential issues as mentioned by the Ledgerwood, 1999 in his book. These are:

- Providing financial and nonfinancial services are two distinct activities, which may at times lead an institution to pursue conflicting objectives.
- It is often difficult for clients to differentiate “social services,” which are usually free, from “financial services,” which must be paid for, when they are receiving both from the same organization.
- MFIs offering many services may have difficulties identifying and controlling the costs per service.
- Nonfinancial services are rarely financially sustainable.

Box 1.2 shows the schematic view of the Minimalist and Integrated Approaches to Microfinance as developed by Ledgerwood (1999).
Box 1.2: Minimalist and Integrated Approaches to Microfinance

MINIMALIST APPROACH
One “missing piece”
- credit

Financial Intermediation
- Working Capital
- Fixed asset loans
- Savings
- Insurance

Social Intermediation
- Group formation
- Leadership training
- Cooperative learning

Enterprise development services
- Marketing
- Business training
- Production training
- Subsector analysis

Social Services
- Education
- Health and nutrition
- Literacy training

INTEGRATED APPROACH
Financial and nonfinancial services

Source: Adapted from Ledgerwood (1999); p 65.
1.7 Microfinance Delivery Models

There are a number of distinctive models of microfinance, reflecting the fact that microfinance has evolved differently in different environments. Some countries tend to rely on one particular model or method, while others exhibit considerable diversity in the range of models used. Internationally, the most well known microfinance models include the Individual Lending Model, Grameen Solidarity Group Lending Model, Latin American Solidarity Group Lending Model, Community-Owned Village Banking Model, Savings and Loans Associations, Credit Unions, and Self Help Groups. In reality, the models are loosely related with each other, and most good and sustainable microfinance institutions have features of two or more models in their activities.

The following is a typology of leading models of microfinance employed by microfinance institutions for the delivery of financial services to low income households.

**Individual Lending**

This is a straight forward credit lending model where micro loans are given directly to the borrower. It does not include the formation of groups or generating peer pressures to ensure loan repayment. This method is famous and popular in the case of microfinance through cooperatives and commercial banks and basically suitable for larger clients in urban areas who are engaged in their own enterprise or running such enterprises that provide self employment to the other poor. It also suits such clients who have some form of collateral or a willing cosigner. Individual lending requires frequent and close contact with individual clients to provide credit products tailored to the specific needs of the business (http://www.grameen-info.org; Jha, Sen & Pattanayak, 2008; Ledgerwood, 1999).

**Grameen Solidarity Group Lending**

This model was initially promoted by the well known Grameen Bank of Bangladesh to serve rural, landless women wishing to finance income generating activities. Under this model, peer groups of five unrelated members are self-formed and incorporated into village ‘centers’ of up to eight peer groups. Within each group
and centre peer pressure is the key factor in ensuring repayment. Each borrower’s creditworthiness is determined by the overall creditworthiness of the group. Attendance at weekly meetings is mandatory. Savings must be contributed for four to eight weeks prior to receiving the loan and must continue for the duration of the loan term. While group members mutually guarantee each other's loans, they are not responsible for paying off loans of other members. However, no further loans are available if any one member does not repay her loan on time. Loans are made to individuals within the group by the local credit officer at the weekly meetings. However, only two members receive loans initially. After a period of successful repayment, two more members receive loans. The final member receives her loan after another period of successful repayment. Because of these restrictions, there is substantial group pressure to keep individual records clear. In this sense, collective responsibility of the group serves as collateral on the loan (http://www.grameen-info.org; Sinha, 2003; Ledgerwood, 1999; Looft, 2007).

**Latin American Solidarity Group Lending**

The solidarity group lending model makes loans to individual members in groups of four to seven. The members cross-guarantee each other’s loan to replace traditional collateral. Clients are commonly female market vendors who receive very small, short-term working capital loans. ACCION is generally credited with introducing the solidarity group methodology into Latin America. Since its introduction, the approach has been adapted by a large number of NGOs and programs. In ACCION, group members collectively guarantee loan repayment, and access to subsequent loans is dependent on successful repayment by all group members. Loan applications are simple and reviewed quickly. Loan disbursement is made to the group leader at the branch office, who distributes it to individual members (group members normally receive equal loan amounts). Loan amounts and terms are gradually increased overtime if clients perform well. Loan approval is the responsibility of the credit officers. Credit officers regularly work with 200 to 400 clients and thus rarely know their clients very well. Loan approval is by the credit officers based on minimal economic analysis of each loan request. Loan disbursement is made to the group leader at the branch office, who immediately distributes to each individual member who normally receive equal loan amounts.
Loan amounts and terms are gradually increased once clients demonstrate the ability to take on larger amounts of debt. Loan applications are simple and are reviewed quickly. Savings are usually required but are often deducted from the loan amount at the time of disbursement rather than requiring the clients to save prior to receiving a loan. Savings serve primarily as a compensating balance, guaranteeing a portion of the loan amount (Ledgerwood, 1999).

**Village Banking Model**

The Village Banking Model was developed by FINCA in the mid-1980s. The Village banks are community-managed credit and savings associations. They are established to improve members' access to financial services, build a community self-help group, and help members accumulate savings. By providing very poor families with small loans to invest in their microenterprises, Village Banking empowers them to create their own jobs, raise their incomes, build assets, and increase their families’ well-being. Membership in a village bank usually ranges from 30 to 50 members, most of whom are women. The groups are self-selecting so default is rare and the savings form the beginnings of an asset base for the borrowers. The financial operation of village banks begins when sponsoring agencies lend seed capital to newly established village banks, which then on-lend the money to their members. Each group member is required to save 20 per cent of the money they borrow and agrees to repay any other member’s default from these savings; there is no other collateral for the loans. All members sign the loan agreement to offer a collective guarantee. The village banks are highly democratic, self-managed, grassroots organisations. They elect their own leaders, select their own members, create their own bylaws, do their own book-keeping, manage all funds, disburse and deposit all funds, resolve loan delinquency problems, and levy their own fines on members who come late, miss meetings, or fall behind in their payments (H. R. Singh & Singh, 2011; Otero & Rhyne, 1994; Ledgerwood, 1999; IFAD, n.d.; http://www.finca.org)

**Self Help Group (SHG) Model**

Initiated in India in the 1980s, an SHG is a group of 10 to 20 people – the vast majority of whom are women and marginal farmers or landless agricultural
labourers. It is an economically homogenous affinity group voluntarily formed to save small amounts convenient to all the members and mutually agree to contribute to a common fund/corpus to be lent to its members for their emergent productive and consumption needs as per the decision of the group. They are facilitated by a diverse set of external organisations like reputed Voluntary Agencies, NGOs, Government Departments, Farmers Clubs, and even banks. The facilitators are collectively referred to as Self Help Promoting Institutions (SHPIs). Normally the SHPIs should provide awareness, training, extension and support facilities to the group and its members in the initial years. Immediately on formation of the SHG, it requires to open an Savings Bank Account in the nearby bank in the name of the group. The concerned NGOs/SHPIs will generally offer introduction for opening the Bank Account. Initially, the SHGs are encouraged and trained to start regular savings, framing rules and regulations, book-keeping and provide small loans to each other for interest out of the group corpus which is ploughed back into group funds. However, within a relatively short amount of time (six to eight months), most of the groups become eligible for accessing credit from banks. In fact, they are essentially credit driven; they save primarily as a precondition for a bank loan. Norms are laid down for the maximum size of the initial and successive bank loans as increasing ratio of the groups own funds. Broadly, the following three models of SHG-Bank linkage have emerged over the past few years in India:

- **Model I**: Banks>SHG>Members.
  
  In this model, the bank itself acts as an SHPI and extends credit directly to the group without any intermediary.

- **Model II**: Banks>NGOs/VAs (as facilitating agency)>SHG>Members.
  
  In this model, SHGs are formed and nurtured by facilitating agencies like NGOs, VAs, Govt. Agencies and other SHPIs. While the bank provides loans to the group directly, the facilitator acts as a catalyst only.

- **Model III**: Bank>NGOs/VAs (as Financial Intermediary)>SHG>Members.
  
  In this model, the NGOs/VAs etc. act both as facilitators and micro finance intermediaries. First they promote, nurture and
train the groups and then approach banks for bulk loans for on-lending to SHGs.

Out of the above three different models, the Model II has emerged as the most popular model under the SHG-Bank Linkage Programme in India. The commercial banks, co-operative banks and the regional rural banks have been actively participating in the SBLP (RBI, 2008; Tankha, 2012; Ledgerwood, Earne & Nelson, 2013; Ghate, 2007).

1.8 Microfinance and Poverty Reduction

Microfinance has generated considerable hope and expectations among the academicians, researcher, policy makers, development practitioners, governments, donors, investors and NGO leaders in all over the world. It has created positive impacts on two vital areas of national development, viz., reduction of poverty and empowering women (Abed, 2000). However, empirical studies on the impact of microcredit are difficult and expensive to conduct and pose special methodological problems. Most impact studies to date have found significant benefits from microcredit. However, only a few studies have made serious efforts to compensate for the methodological challenges. In fact, many studies would not be regarded as meaningful by most professional econometricians. A new wave of randomized control trials are now in process, which should yield a more definitive picture. Other microfinance services like savings, insurance, and money transfers have developed more recently, and there is less empirical research on their impact. Client demand indicates that poor people value such services. MFIs that offer good voluntary savings services typically attract far more savers than borrowers (http://www.microfinancegateway.org).

Though most governments and donor agencies agree that microfinance can contribute to poverty reduction but the debate on the poverty outreach of microfinance continues (Alemu, 2008). Microfinance practitioners have generally accepted that it is not a panacea for poverty, and that it does not reach the poorest of the poor. On the other hand, the practitioners also agree to the point that microfinance can significantly reduce vulnerability and thus prevent people from slipping into extreme poverty. In fact, there is less consensus about to what degree,
how and when poverty can be reduced through microfinance (Gulli, 1998). This debate has given rise to two main ‘camps’ regarding microfinance and poverty reduction: the financial systems approach and the poverty lending approach.

The financial systems approach views the overall goal of microfinance is to provide sustainable financial services to low income people, but not necessarily to the poorest of the poor. In other words, the financial systems approach focuses on commercial financial intermediation among the economically active poor at interest rates that enable the MFIs to cover all costs including the commercial cost of funds. Under this approach, the portfolios of MFIs are financed by savings, commercial debt and for-profit investment in varying mix. Several nationalized banks in India, the private sector banks and the old generation banks predominantly from the South India are at the forefront of the financial systems approach. However, this approach is not suitable for extremely poor people - the poorest of the poor who are badly malnourished, ill and un-skilled or without having any opportunity to gainful employment. They may need grants or other public resources to improve their economic condition (Somanath, 2009; Gulli, 1998; Robinson, 2001; http://www.microfinancegateway.org).

The Poverty lending approach, on the other hand, claims that the overall goals of microfinance should be poverty reduction and empowerment by reaching the poor, especially the extremely poor - the poorest of the poor. Since the overall goal is poverty reduction, complementary services such as skills training and the teaching of literacy and numeracy, health, nutrition, family planning, etc. are often provided and integrated approaches are commonly applied. Under this approach, some donor and government funded credit may be needed because availability of funds is the most binding constraint in expanding the supply of financial services to the poor. Many institutions using the poverty lending approach provide microcredit to poor borrowers at low cost. But these institutions are typically not sustainable, primarily because their interest rates on loans are too low for full cost recovery. In addition, they do not meet the demand among the poor for other financial services. Except for mandatory savings required as a precondition for receiving a loan, savings is not a significant part of the poverty lending approach (Somanath, 2009;
Box 2 below shows the different ways in which microfinance can assist the poor.

**Box 1.3: How can Microfinance Assist the Poor?**

**Promote investment in Assets**

Finance provides additional purchasing power, permitting individuals to exceed the limitations of their current economic situations. For instance, access to financial services provides a means to accelerate accumulation of assets.

**Facilitate activities to earn a livelihood**

Access to financial services enables poor people to manage their economic activities in a more efficient manner. For instance, they can reduce working capital outflows if financing allows them to purchase inputs at lower prices.

**Protect against income shocks**

Access to financial services may reduce households’ vulnerability by providing means to cope with emergency needs and smooth consumption. Access to consumer loans may prevent a sale of productive assets in times of low cash, and thereby increase the economic security of the household.

**Build social capital and improve quality-of-life**

The poor may generate social capital as they participate in solidarity groups (build networks), and establish a credit history and trust. In addition, household members may experience a rise in self-esteem, dignity and a sense of empowerment through opportunities provided by access to financial services.

*Source: Adapted from Gulli, 1998; p 4.*

1.9 Statement of the Problem

The widening gap between rich and poor worldwide is a major challenge to global security and economic integration. About half of the world’s population are poor, living on less than two dollars a day. Poverty is a vicious circle, being both the major cause and the effect of a situation, in which no opportunities seem to exist for the poor to help themselves (UNIDO, 2003). The theory of basic economics suggests that limited access to financial services will prevent consumption smoothing and investments in health, education and income generating activities,
thereby limiting opportunities for the poor. Providing access to financial services has
the potential to significantly help the poor lift themselves from the vicious cycle of
poverty. Its timely availability in the right quantity and at an affordable cost goes a
long way in contributing to the well-being of the people especially in the lower
rungs of society (Jayasheela, Dinesha & Hans, 2008). But India is lagging behind in
this respect so it has become the matter of concern.

India began the process of planned development nearly sixty years back with
the start of the First Five Year Plan in April, 1951. Since then, the successive
Governments in India have emphasized the link between improving access to
finance and reducing poverty (Basu, 2006). This led to the establishment of several
Government institutions and programmes to increase the poor’s access to quality
financial products. Public Sector Banks and other apex financial institutions such as
National Bank for Agriculture and Rural Development (NABARD) and Small
Industries Development Bank of India (SIDBI) have supported and aided the
government in a variety of ways towards this end (Deepti, n.d.). But, most of these
interventions remained unsuccessful due to a narrow focus on credit, combined with
heavy subsidies and poor monitoring (Agarwal, n.d.).

A sizable majority of the population in India, particularly the low-income
groups, continues to remain excluded from the services provided by the formal
financial system (NABARD, 2013). Recent development paradigm suggests that
access to finance by the poor and vulnerable group is a prerequisite for poverty
reduction and social cohesion. In fact, providing access to finance is a form of
empowerment of the vulnerable groups. Through graduated credit, the attempt must
be to lift the poor from one level to another so that they come out of the vicious
circle of poverty. At present, there is enough literature on the issue that banking
with the poor is more viable and profitable. The provision of uncomplicated, small,
affordable products can help bring low-income families into ambit of formal
financial system. Taking into account their seasonal inflow of income from
agricultural operations, migration from one place to another, and seasonal and
irregular work availability and income, the existing financial system needs to be
designed to suit their requirements. Mainstream financial institutions in India such

1 http://pib.nic.in/newsite/erelease.aspx?relid=35141
as Commercial Banks, Regional Rural Banks and Cooperative Banks have an important role to play in this effort, not as a social obligation, but as a pure business proposition.\(^2\) India has, for a long time, recognized the social and economic imperatives for broader financial inclusion and has made an enormous contribution to economic development by finding innovative ways to empower the poor. Starting with the nationalization of banks, priority sector lending requirements for banks, lead bank scheme, establishment of regional rural banks (RRBs), service area approach, self-help group-bank linkage programme, etc., multiple steps have been taken by the Reserve Bank of India over the years to increase the access to the financial services by the poorer segments of society.\(^3\)

The Committee on Financial Inclusion (CFI) constituted by the Government of India in June 2006 under the Chairmanship of Dr C. Rangarajan, submitted its report in January, 2008. The CFI report refers to the data from the National Sample Survey Organisation for calendar year 2003. The report states that about 46 million farmer households in the country, accounting for 51.4 per cent of total farming families (89.3 million) do not access credit, either from institutional or non-institutional sources.\(^4\) Further, despite the vast network of bank branches, only 27% of total farm households are indebted to formal sources (of which one-third also borrow from informal sources). In other words, 73% of farm households do not have access to formal credit sources. Farm households not accessing credit from formal sources as a proportion to total farm households is especially high at 95.91%, 81.26% and 77.59% in the North Eastern, Eastern and Central Regions respectively.\(^5\) In the State of Assam, the percentage of farm households not accessing credit from both institutional and non-institutional sources is 81.9 percent. This figure shows the extent of financial exclusion in the State of Assam whereas the corresponding figure for the country as whole is only 51.4 percent.

It is in this backdrop the problem of very limited coverage of the poor people by the formal banking system in the district of Cachar concerns us. It is more

\(^2\) http://rbidocs.rbi.org.in/rdocs/Speeches/PDFs/FICHI121011S.pdf
\(^3\) http://rbidocs.rbi.org.in/rdocs/Speeches/PDFs/FICHI121011S.pdf
\(^4\) http://www.thehindubusinessline.com/todays-paper/tp-opinion/financial-inclusion-to-overcome-exclusions/article1624022.ece
important to analyse why the problem of poor credit off take originate and aggravates both from the demand side as well as supply side. Why priority sectors which form the core of the weaker sections of the rural Cachar are deprived of microfinance inspite of so many developmental schemes introduced in recent years? The present study is intended to address the issues of poor microfinance penetration in the Cachar district of Assam.

1.10 Review of Literature

In this section, an attempt has been made to review the existing available literature relating to SHGs, microfinance and empowerment of women. The studies were arranged by the year of their publication.

The study conducted by Hossain (1988) analysed the impact of Grameen Bank’s micro credit programme on alleviation of rural poverty in Bangladesh and observed that Grameen Bank has made a positive contribution to the alleviation of rural poverty in the area of its operation. He also pointed out that the bank has successfully reached its target group with credit and has ensured both productive utilization of loans and their recovery in due time thereby helping to improve the standard of living of its clients.

Khandker (1998) reported that microfinance reduces poverty by increasing per capita consumption among the clients and their families. He also reported that poverty reduction estimates based on consumption impacts of credit show that about 5 percent of clients can lift their families out of poverty each year by participating in and borrowing from microfinance programmes.

Pitt and Khandker (1998) reported that microcredit has a larger benefit for the household if it is provided to a female client. They also reported that annual household consumption expenditure increases by 18 taka for every 100 additional taka lent to female clients compared to 11 taka in case of male clients.

The study conducted by Puhazhendhi and Satyasai (2000) evaluated the socio-economic impact of Self Help Group – Bank Linkage Programme on the beneficiary households covering 5 regions and 11 states of India. The findings of the
study suggest that the SBLP is instrumental in improving the both economic and social conditions of the beneficiary households in the post-SHG situation.

Coleman (2002) conducted one study on the targeting and impact of a women’s group lending programme in Northeast Thailand. The study reported that there is strong evidence that households that are participating in the microfinance programmes are significantly much wealthier than those of non-participants. There is also strong evidence that the richest village bank members become committee members i.e. president, vice-president, treasurer, etc. and use their position to borrow significantly more from the village bank at low rate of interest than rank and file members. Regarding impact of village banking operations on committee members, the study reported that committee members had experienced positive and significant impact on many important measures of wealth, savings, income, productive expenses and labour time. But impact on outcomes for rank and file members was largely insignificant.

MYRADA (2002) conducted one study “to establish whether and to what extent membership in Self-help groups and their consequent involvement in the various activities of the group have an impact on the social status and empowerment of the women members of such groups”. The study was carried out in the four Southern states of India viz. Kerala, Tamilnadu, Karnataka and Andhra Pradesh. The findings of the study revealed that the old group members have experienced higher levels of self confidence, increase in awareness about health and hygiene, increase in control over their own lives, increase in their role in the general welfare and decision making matters. The study also reported that the old group members have more professional, technical and managerial skills which they utilise for efficient management of SHGs related matters and SHG led micro enterprises.

The study conducted by Nayak (2002) on the issue of poverty alleviation by IRDP in the Silchar Development Block of the Cachar district of Assam found that IRDP is successful in uplifting 85 percent of the beneficiaries who were poor above the poverty line. The study also reported that although the programme was launched only for targeting the poor people, but in the study area, majority of the beneficiaries were belonged to non-poor group. The reason being the selection bias on the part of the government officials while implementing the programme.
Khandker (2005) conducted one study by using panel data from Bangladesh and examined the effects of microfinance on poverty reduction at both the participants and the aggregate levels. The results of the study revealed that access to microfinance has a positive effect on the reduction of poverty among the clients and also on the overall poverty reduction at the village level. The study also shows that the reduction of poverty is more for the female clients than the male clients.

Kabeer and Noponen (2005) analysed the social and economic impacts of PRADAN’s Self Help Group Microfinance and Livelihoods Promotion Program on the target households. The study also analysed the impact of its program intervention on the capacity of women within its group to exercise voice and influence within the community. The study was carried out in Godda, Dumka and Banka districts of Jharkhand. The study found that PRADAN’s SHG-Bank linkage model has had significant and positive impact in improving their livelihood base, savings and debt position and living and consumption standards of participants. The results also showed that the empowerment gains are not an automatic outcome of targeting women for financial services. While gains in terms of women’s knowledge, awareness and skills were clearly discernible, impact in terms of participation in decision making within the home and in the public domain were far more modest.

Thompson (2006) reported that microfinance services delivered through FINCA Haiti village banks has improved the social wealth among the clients but failed to significantly improve the economic wealth of the clients.

Nathan and Lawrence (2006) investigated the impact of microfinance on poverty reduction in Uganda using panel data for 1992/93 and 1999/2000 with a sample size of 1398 households and observed that microfinance has no significant effect both on poverty reduction and household income growth. The reasons they opined is that movement out of poverty is negatively and significantly influenced by household size, dependency ratio and primary education. They also mentioned that poverty reduction was positively and significantly influenced by transfer earnings, sectoral employment choice and regional location.

Badatya (2006) also suggested that the participation in SHGs has a positive impact on household income and employment generation in the post-SHG situation.
A study conducted by ADB (2007) analysed the impact of microfinance projects in reducing rural poverty and in improving the status of rural women in Philippines, Bangladesh and Uzbekistan. The study reported that in Philippines, the microfinance programme had a significant impact on per capita income, expenditure and food expenditure of the client households. But there was no significant increase in the per capita savings and this can be easily understood since both income and consumption increased. The study also points out that almost all of the survey respondents in Bangladesh reported that their income rose after participation in the microfinance programme. In Uzbekistan also, the majority of the (85%) sample microfinance clients reported increase in their income. Regarding the status of women, the study reported increased self-confidence in managing businesses, improved sense of fulfillment in managing children and improved technical knowledge and skills.

Bhat and Raj (2008) assessed the impact of Prime Minister’s Rozgar Yojana (PMRY) among the beneficiaries in the Union Territory of Pondicherry and reported that the scheme has beneficial effect on the beneficiaries in terms of access to credit, low rate of interest and income generation.

Another study conducted by NCAER (2008) analyses the impact and sustainability of SHG-Bank Linkage Programme on the socio-economic conditions of the individual members and their households in the pre-SHG and post-SHG situations. The study was conducted for India as a whole covering six states – Andhra Pradesh, Karnataka, Maharashtra, Orissa, Uttar Pradesh and Assam – and in effect all the five regions. The overall findings of the study suggest that the SHG – Bank Linkage Programme has positive impact on the rural poor's access to financial services and also had a positive impact on their socio-economic conditions. Specifically, the study revealed that the SHG membership had significant positive impact on annual net household income of the beneficiary households. Also it had found that about 58.3 percent of the total surveyed households were living below the poverty line at the base level, but the percentage had reduced to 33 percent in 2006, thereby indicating overall 25.3 percentage points net reduction in poverty of the beneficiary households.
Jasmine (2008) conducted one study in the Ramanathapuram district of Tamil Nadu to analyse the impact of SHGs on poverty alleviation among the women beneficiaries. The study reported positive impact of SHG led microfinance programme on women’s economic and social status. The study also used the Sen’s Index of Poverty in order to know the intensity of poverty among the beneficiaries before and after joining SHGs and found that the SHG members income level has increased after joining the same and this in turn helped them to move above the poverty line to a certain extent.

Pathak and Pant (2008) conducted one study in the Juanpur district of Uttar Pradesh by comparing clients with non-clients and also using the before-after methodology. They reported that microfinancing through SGSY has not contributed significantly in the change in the level of income of the beneficiaries. But positive results were found on the non-income indicators like improvement in access to safe drinking water, sanitation facility, electricity usage and housing conditions.

Jerinabi and Kanniammal (2008) analysed the degree of poverty alleviation through micro credit and concluded that micro credit helped only the poor beneficiaries to move out of poverty but it has failed to improve the economic conditions of the very poor people and destitute. The reason behind this is that while distributing the credit, this segment of poor class people have been overlooked by the microfinance institutions.

Agricultural Finance Corporation Limited (2008) reported the findings of its seven-year longitudinal study that was conducted in two stages during 2001-2007. The study was undertaken with a view to find out how far the stated goal of its National Micro Finance Support Project (NMFSP) i.e., “substantial poverty elimination and reduced vulnerability in India amongst users of micro finance services, especially women” was achieved. A multi-stage sampling design with cluster based sampling was used to achieve a sample size of 4510 households comprising 3253 client households and 1257 non-client households of SIDBI’s 25 partner MFIs. The study found that the micro finance programme had helped the client households in terms of expansion and diversification of livelihood activities, growth in employment opportunities, income growth, asset acquisition, savings,
access to loans from various sources, reduction in vulnerability and enhancement of women empowerment.

Vasanthakumari (2009) observed that microenterprises promoted by the women SHG members have successful in developing entrepreneurial skill and improving their economic and social status to some extent. But the main aim of eradication of poverty is yet to be achieved.

Panda and Atibudhi (2009) conducted one study to know the impact of group based microfinance programme on the mobilisation of savings by the participating rural households. The study revealed that the average annual savings per household in target group was significantly higher than that of the control group. The study also revealed that the target households had a highly significantly higher savings in commercial banks than that of the control group. The reason behind this is their increased savings habit and increased income due to their participation in compulsory savings led microfinance programme.

Mahajan and Bansal (2009) reported that the microfinance programme has a positive impact on the economic, social, psychological and political empowerment of participating women. The study also reported that the education of the participants, maturity of the group, employment level, household income and mobility of the group members are significant determinants of women empowerment.

Krishnan (2009) analysed the role of microfinance in empowerment of rural women in the state of Kerala. He found that microfinance programme has beneficial impact on the women members to enhance their role in society, family decision making and mobility. He further opined that the microfinance institutions need to take much more initiative to bring women in the fore of economic activities.

Samanta (2009) conducted one study on the impact of microfinance on poverty alleviation and women empowerment. The study reported mixed results in terms of raising of women and their families above the poverty line. According to her, if the microfinance programme is well thought out in advance, then it has a positive impact on household poverty reduction. She also argued that there are several cases where in spite of having longer term membership with SHGs, the
members could not generate sufficient income so that they can come out of poverty. The findings of the study regarding women empowerment suggests that the microfinance programme sometimes empower women to take decisions in some family matters.

The study conducted by Sahu and Tripathy (2009) in the Jagatsingpur and Nuapara districts of Orissa concludes that microfinance is not a panacea to poverty alleviation but it could help to improve the socio-economic condition of the poor by addressing some issues such as income generation and capability enhancement.

Baruah (2009) examined the impact of SHG membership on asset creation in the Deharkuchi Gaon Panchayat of Nalbari District of Assam. He suggested that if the loan taken from SHG is invested in some productive activity or consumer durables like houses, then it helps in alleviation of poverty among the microfinance clients. On the other hand, if the loan is simply invested in current consumption, then it may deteriorate the economic condition of the clients.

The study conducted by Mishra (2009) reported that there is mismatch between the regional concentration of poverty and microcredit participation. The study also reported that the participation of women in the microcredit programme may not necessarily lead to empowerment of women and gender equality within the households. But the microcredit programme helps to some extent in reducing vulnerability through developing crisis coping mechanism, diversifying income earning sources, building asset base and improving the status of women.

Devi and Uma (2010) reported that participation of women in SHGs and NHGs have succeeded in empowering women to some extent but their active participation in local planning and use of their collective bargaining power for improving their status in the society and at home are yet to be achieved. She also reported that the family structure and culture practiced in the society has a significant impact in determining the bargaining power of women.

Kumar (2010) conducted one study in the Hoshiarpur district of Punjab and found that in the post-SHG situation, the SHG member households experienced an increase in their income level, asset base and borrowing level. However the average annual income growth is higher for those households which are linked with SHGs
formed under NABARD sponsored SHG-Bank Linkage Programme than the SHGs formed under Government sponsored poverty alleviation programme i.e. SGSY. He further opined that the members of SHGs under NABARD scheme were financially better than the members of SHGs under SGSY scheme as because the former utilise the micro loan for production purposes whereas later using the micro loan for both production and consumption purposes.

Another study conducted by Sudan (2010) found that the economic activities supported by self-help credit programme have improved the level of empowerment of women. He also found that the women’s role in enterprise decision making, household decision making, their access to assets and their control over self earnings have improved significantly among the client than non-clients.

Krishnan and Silvi (2010) conducted one study to find out the potential of microfinance in transforming the lives of tribal people in the Wayanad district of Kerala. The study reported that the NGO run microfinance programme had a positive impact on the target households income, asset and savings. The study also reported that the target households had significantly higher annual average employment days over that of the control households. The microfinance programme is also contributing successfully in livelihood diversification among the target group households.

Singh, Kaur and Gill (2010) conducted one study to assess the role of Swarna Jayanti Gram Swarozgar Yojana in the socio-economic development of the rural people in the Jalandhar district of Punjab and reported that the programme has a beneficial effect on the economic aspects like better access to institutional credit, less dependence on money lenders, increased savings, reduction in indebtedness and increased volume of asset. The study also reported the beneficial effect of the programme on the social and psychological aspects of the beneficiaries.

De and Sarker (2010) reported that longer period of association with the SHG led microfinance programme yields benefit in the form of higher level of women’s empowerment.

S. K. Kashyap and Kashyap (2010) conducted one study in the Nalbari district of Assam and found that the loans obtained from microfinance institutions
have enabled the members to start microenterprises in almost each and every field which they did not undertake previously. The study also reported that the benefits received from microenterprises helped them to enjoy better socio-economic status, improved standard of living, enhanced leadership quality, regular income and participation in public affairs.

Maurya (2010) found that the increasing access to institutional credit through microfinance acts as an important tool for eradication of poverty in India.

Guha (2010) examined the impact of micro enterprises or income generation activities undertaken by SHG members in the four states of India viz. Jammu and Kashmir, Andhra Pradesh, Himachal Pradesh and Gujarat in 2005-06 and observed that after joining the SHGs, the members experienced a higher level of independence in economic decision making like purchase of assets, other household requirements and management of productive assets. He also observed that the SHG membership has resulted in the overall development of the social and economic status of the members and also it has enabled them to understand the contemporary social issues. There is also evidence of increasing participation of SHG members in the local political process.

Bagchi and Dandapat (2010) reported that the microfinance programme has the potential to improve the conditions of poverty stricken rural people in terms of better self employment, increased income and savings, and enhanced social status.

The study conducted by Natarajan (2010) evaluated the impact of SHG based microfinance programmes on changes in terms of employment level, income and assets of the women SHG members between the ‘pre’ and ‘post’ SHG situation in Madurai and Ramanathapuram district of Tamil Nadu. A multi-stage random sampling was adopted for selecting the sample units for the study. The study found that the mean number of days employed per annum of the respondent increased by 37 percent in the total study area over the pre-SHG period, while the mean income of the respondent increased by 123.1 percent over the pre-SHG period. The mean assets of the respondents increased by 23.5 percent over the pre-SHG period.

Eshetu (2011) conducted one study on the impact of microfinance on women’s economic empowerment in Ethiopia and observed that the microfinancing
scheme has a positive impact on women’s economic empowerment as measured by the increased participation of microfinancing clients in household decision making and also has a positive impact on the living condition of microfinancing clients.

Mitra and Kundu (2011) analysed the impact of microcredit programme through individual liability loan contract system operated by Primary Agricultural Credit Society (PACS) in the two blocks of Hooghly district of West Bengal. The study reported that there has been no economic improvement among the participating households in terms of average monthly income and monthly per-capita consumption expenditure in spite of reducing the rate of interest for the crop loan charged by PACS. The study further reported that the repayment rate is high for such type of crop loans and the households are repaying the same on time even at the cost of their basic consumption need.

Bandyopadhyay (2011) reported that the SHG-Bank Linkage Programme is a strong supplementary credit delivery mechanism that evolved in India around two decades back. The programme is successful in bringing the rural people more particularly the rural women in the fold of banking services and developed the capability of the rural poor in managing and handling the economic and social affairs of microfinance scheme. He further argued that the microfinance programme may not be called directly a poverty alleviation programme, rather it may be called as an income generating programme which facilitates income generation of the poor families and by this process, it helps in empowering the rural people to come out of the vicious circle of poverty.

Rahman, Barua and Sulaiman (2011) assessed the impact of BRAC’s Northwest Microfinance Expansion (NWME) project in Bangladesh on the well-being of the beneficiary households and found that the project is instrumental in improving the housing facility, sanitation facility, stock of physical as well as financial assets. They also suggested that women’s participation in decision making at household level has increased over time and also the domestic violence against women has decreased over time.

Mukherjee and Kundu (2011) conducted one study on the impact of Swarna Jayanti Gram Swarozgar Yojana on health, education and women empowerment in the Murshidabad district of West Bengal. The findings of the study are not
consistent with the view that women’s participation in SGSY improves the status of the women. The result of the study through using pooled regression shows that borrowing from SGSY has significant impact on female agency for all socio-religious communities (SRCs) except for Muslims. But the First Difference (FD) estimation shows the impact of SGSY on women empowerment is significant for upper castes (UCs) only. The reason behind this is that if a time invariant unobserved characteristics like entrepreneurship is removed, then participation in SGSY alone can’t empower the women. On the other hand, the result also shows that the borrowing from SGSY has insignificant impact on the health status and education of the beneficiary households.

The study conducted by Das (2011) focuses on the impact of SHG – Bank Linkage Programme on some economic and social parameters of the SHG member households. The study is based on a field work on 238 selected SHGs drawn from five districts of Assam and Meghalaya and 476 respondents selected from these SHGs. The study revealed that the implementation of SHG – Bank Link Programme significantly contributed to the improvement of asset position of sample households. It also found that SHG membership has also helped the households to increase their income level between the ‘pre’ and ‘post’ SHG situation. The study further revealed that about 22 percent of the total households surveyed moved above the poverty line between ‘pre’ and ‘post’ SHG situation.

Lyngdoh and Pati (2011) analysed the microfinance oriented socio-economic change among the clients in state of Meghalaya and found that there is positive changes in both economic and social conditions of the clients. They specifically reported that the microfinance clients experience increase in income, expenditure and savings, improvement in asset structure, increased access to productive assets and household property. They also reported that the favourable social change noticeable as a result of association with microfinance programme in the areas like education, decision making, health status, family planning decisions, recognition and acceptance.

Rani and Jyothi (2012) reported that women SHG members have less self-efficacy and self-confidence which in turn is an important factor of their personal
empowerment. But the SHG membership has a positive impact on the economic, familial and social empowerment of women SHG members.

Another study conducted by Roy and Dutta (2012) extensively examined the socio-economic benefits of micro financing poor through SHGs in the Karimganj district of Assam. The sample of the study was drawn by applying multistage purposive random sampling technique. The study found that the SHG membership has significant positive impact on the income and asset base of the SHG member households. The study also found that there is significant enhancement in the social status of women SHG members.

Chakraborty (2012) carried out a study in the Purulia district of West Bengal on the impact of microfinancing through Self Help Group on women’s empowerment. The study concludes that the microfinance has the potential to have significant impact of women’s empowerment. The study specifically suggested that microfinance is not always empowering all women SHG members, but most of the women SHG members experience some degree of empowerment and are in the process of empowering themselves as a result of their association with the SHG led microfinance programme.

Mushtaq and Rauf (2012) analysed the social impacts of microfinance institutions in Pakistan with the help of nutrition status, health status and standard of living of the borrower households. It is observed from their study that microcredit programme helps the client household in expanding their existing business or helps in starting a completely new business which in turn contributes greatly towards access to better food, better health facility and better standard of living among the client households.

The review of literature enabled the researcher to gain background knowledge on the topic and identify the research gap. Moreover, the literature review enabled the researcher to find out a suitable research design for the present study.
1.11 Gap in the existing literature

From the above studies, it is observed that though several studies have been conducted in the field of microfinance in the world as well as in India, but no studies relating to microfinance have been conducted in the Cachar District of Assam. So the researcher is intended to undertake the present study in the Cachar District of Assam.

1.12 Objectives of the Study

1. To review the progress of microfinance programme in the Cachar District of Assam.

2. To examine the impact of microfinance through SHGs formed under SGSY on poverty alleviation in the Cachar District of Assam.

3. To examine the impact of microfinance on economic empowerment of women in the district.

1.13 Research Hypotheses

Based on the objectives of the study, the hypotheses are drawn as follows:

**Hypothesis No. 1**

Null Hypothesis ($H_{01}$): There is no significant difference in the change of income of the households during Base Year and Current Year between the Treatment Group and Control Group.

Alternative Hypothesis ($H_{11}$): There is significant difference in the change of income of the households during Base Year and Current Year between the Treatment Group and Control Group.

**Hypothesis No. 2**

Null Hypothesis ($H_{02}$): There is no significant difference in the change of monthly consumption expenditure of the households during Base Year and Current Year between the Treatment Group and Control Group.
Alternative Hypothesis ($H_{12}$): There is significant difference in the change of monthly consumption expenditure of the households during Base Year and Current Year between the Treatment Group and Control Group.

**Hypothesis No. 3**

Null Hypothesis ($H_{03}$): There is no significant difference between the Treatment Group and Control Group in terms of economic empowerment of women.

Alternative Hypothesis ($H_{13}$): There is significant difference between the Treatment Group and Control Group in terms of economic empowerment of women.

1.14 Research Methodology

The approach followed for the study is presented in the following subsections.

**Method of Analysis**

The impact evaluation study of micro finance programme aims ideally at knowing the counterfactual i.e., the situation that would have prevailed had the intervention not occurred or in other words what would have happened in the absence of the programme. But how to know what would have happened without the programme. The key problem is defining a valid counterfactual outcome against which the treatment group (i.e. those people who have received microfinance) can be compared. An impact evaluation is correct only if the estimation of this counterfactual outcome is correct. One of the method of obtaining a valid counterfactual outcome is the use of Control Group (CG) method. But the Control Group may turn out to be completely non-comparable with the Treatment Group and the impact estimates may be biased. The Treatment Group (TG) i.e., borrowers group in general might be more entrepreneurial in nature or might have developed some sort of sanguine attitude or simply be more motivated. But these biases can be easily removed by using new members who have not yet received a loan as the Control Group. The idea behind taking new members as a Control Group is that since both the Treatment Group and the Control Group had chosen to join the programme, so it is assumed that there would be no difference in terms of their entrepreneurial spirit. Otherwise, higher incomes among the Treatment Group might
simply be driven by superior business acumen (Goldberg, 2005). The new members
by hypotheses, are eager to co-operate as a consequence of having been admitted to
the club of borrowers. Accordingly the present study used a quasi-experimental
design that required a both Treatment Group and a Control Group for analysis
purpose. The sample design below shows the sampling technique used to draw the
sample which comprises of both these two groups.

**Sample Design**

A multistage sample design was adopted for selecting the sample SHG members. In the Cachar district, there are total 15 development blocks and out these 15 development blocks, 5 blocks viz., Narshingpur Development Block, Silchar Development Block, Sonai Development Block, Borjalenga Development Block and Udharbond Development Block were selected randomly. From these five development blocks, a total of 236 SHG members were selected by taking 2 to 3 members from each SHGs which were selected by applying judgement sampling technique and based on the fact that they are operational for a minimum period of three years or more and have availed bank loan (these are the old SHGs). These SHG member households comprises the Treatment Group as used in the study. Further an equal number of new SHG members were selected from these five development blocks by taking 2 to 3 members from each SHGs which were selected by applying the same judgement sampling technique and based on the fact that their period of formation has not crossed six months and have not received bank loan (these are the newly formed SHGs). These SHG member households comprises the Control Group as used in the study. Below table shows the block wise classification of sample SHG Members.

**Table1.2: Block Wise Classification of Sample SHG Members**

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Name of the Development Blocks</th>
<th>Treatment Group SHG Members</th>
<th>Control Group SHG Members</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Borjalenga</td>
<td>40</td>
<td>44</td>
<td>84</td>
</tr>
<tr>
<td>2</td>
<td>Narsingpur</td>
<td>50</td>
<td>41</td>
<td>91</td>
</tr>
<tr>
<td>3</td>
<td>Silchar</td>
<td>48</td>
<td>54</td>
<td>102</td>
</tr>
<tr>
<td></td>
<td>Sonai</td>
<td>Udharbond</td>
<td>Total</td>
<td></td>
</tr>
<tr>
<td>---</td>
<td>------</td>
<td>-----------</td>
<td>-------</td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>49</td>
<td>61</td>
<td>110</td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>49</td>
<td>36</td>
<td>85</td>
<td></td>
</tr>
<tr>
<td></td>
<td>236</td>
<td>236</td>
<td>472</td>
<td></td>
</tr>
</tbody>
</table>

Note: 1. The differences in the number of SHG members from each blocks in between the Treatment Group and Control Group is found statistically insignificant as the P-Value for the Chi-Square Test comes as 0.3161 which is more than 0.05.

2. The Chi-Square Test has been performed online in the weblink - http://www.vassarstats.net/newcs.html).

3. For measuring the Economic Empowerment of Women, the sample size for both the Treatment Group and Control Group has been taken as 208.

**Parameters used in the Study**

The impact study of micro finance programme can be carried out at three different levels, i.e., at the Individual Level, at the Household Level and at the Micro Enterprise Level. In this study, the impact of micro finance programme is carried out at the Household Level only. A Structured Interview Schedule was used for collection of primary data during August 2010 to March 2011. The Interview Schedule was pretested during December 2009 to January 2010. The details about the parameters used in the study are mentioned below:

1. SHG member households income relating to Base Year and the Current Year for both the Treatment Group and Control Group (Base Year relates to 2007 and Current Year relates to 2010)

2. SHG member households consumption income relating to Base Year and Current Year for both the Treatment Group and Control Group (Base Year relates to 2007 and Current Year relates to 2010).

3. The parameters used to measure the consumption habit and dwelling structure of both the Treatment Group and Control were taken from the Microfinance Poverty Assessment Tool, Technical Tools Series No. 5 (September, 2003) as developed by Consultative Group to Assist the Poor (CGAP). These are as follows:
3.1 : Number of Meals a Day
3.2 : Intake of Meat/Fish or Other Luxury Food
3.3 : Number of days for which the meal consists of inferior food only (In last 7 days)
3.4 : Number of days for which the household does not have enough to eat everyday (in last 30 days)
3.5 : Number of weeks for which the household have a stock of local staple food
3.6 : Type of roofing materials used
3.7 : Type of External Walls
3.8 : Type of Flooring
3.9 : Structural condition of the main dwelling
3.10 : Type of toilet facility available
3.11 : Number of dwelling rooms
3.12 : Availability of separate room for kitchen
3.13 : Type of electricity supply
3.14 : Type of Cooking Fuel Source Used
3.15 : Source of Drinking Water

4. The following parameters are used for measuring the economic empowerment of women (for women SHG members only):

4.2 : Women’s Work Participation/Freedom of Action and Mobility.
4.3 : Attainment of Economic Self Sufficiency.
4.4 : Decision Making Power in Development Programmes.
4.5 : Ability to Control Resource/Properties.
Sources of Secondary Data

As the study is also based on secondary data, it is being collected from different sources like The Office of the Lead District Manager (LDM), Cachar District; The Office of the Project Director (PD), DRDA, Cachar; The Office of the District Development Manager (DDM), NABARD, Cachar District; NABARD Regional Office (RO), Guwahati; Local Head Office (LHO), State Bank of India, Guwahati; Deshabandhu Club, Behara Bazar, Cachar; Divisional Office, Bandhan Financial Services Pvt. Ltd. (BFSPL), Karimganj; Regional Office, UNACCO Financial Services Pvt. Ltd. (UFSPPL), Silchar; and Regional Office, North East Region Finservices Limited (NERFSL), Silchar.

Data Analysis

Data gathered during the field work was processed, tabulated, analysed and interpreted through MS-Excel and SPSS package by generating information through:

- Cross-tabulation.
- Through percentage, proportion.
- Through Chi-square test.
- Through Mann-Whitney test.
- Wherever possible and feasible, appropriate graphs, diagrams and charts are drawn to illuminate facts and figures.

1.15 Limitations of the Study

Due to the resource and time constraints, the sample survey was carried out in the Cachar district only and also only five developmental blocks have been covered. The sample selected from these five blocks may not represent the entire district and acts as limitations of this study. Moreover, the parameters selected for measuring the progress of microfinance in the Cachar district of Assam is also not exhaustive. Same limitations are there in measuring the poverty and economic empowerment of women.
1.16 Scope of Further Research

Assuming the significant role of microfinance in promotion of microenterprises, further research can be conducted in the areas of microenterprise development through microfinance. Also the accounting and marketing practices followed by the microenterprises can become a suitable area where research can be conducted. Moreover, poverty alleviation and women empowerment aspect of microfinancing clients can be studied to have a re-look into the matter.

1.17 Chapterisation Scheme

Chapterisation scheme followed in the present research work is mentioned below:

1. Introduction.
2. Microfinance - International and Indian scenario.
3. Progress of microfinance programme in the Cachar District of Assam.
4. Impact of microfinance on poverty alleviation in the Cachar District of Assam.
5. Impact of microfinance on economic empowerment of women in the Cachar District of Assam.
6. Findings, Suggestions and Conclusion.
References


