CHAPTER - I

INTRODUCTION
CHAPTER-1
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India still ranks among the poorest countries in the world\(^1\). Since independence, successive governments have emphasized the link between improving access to finance and reducing poverty, a stance that has had influence globally. The need to improve financial access to the poor of India – the overwhelming majority – who lives in rural areas, motivated the establishment of a huge network of rural co-operative credit institutions in the 1950s\(^2\) and nationalization of 14 major Commercial Banks in India in 1969, and six more in 1980. A network of Regional Rural Banks (RRBs) was also established in the 1975s. India thus has one of the largest banking networks in the world,\(^3\) with a multi-agency approach.

PART-A

In this section an attempt is made to analyse the overall contribution of the commercial banks and cooperative credit agencies to the poor and the needy through ‘Microfinance’ activity.

MULTI-AGENCY APPROACH FOR RURAL CREDIT:

During 1952-87, despite a multi-agency approach, the formal credit institutions have not been able to cover large sections of the rural poor inspite of the massive expansion of the banking network. Efforts were concentrated on developing and strengthening co-operative credit structures by providing refinance and also

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financial contributions to co-operative institutions by the Reserves Bank of India (RBI).

Another step to supplement the efforts of Co-operative and Commercial Banks was the establishment of 196 Regional Rural Banks in 1975 in various states with equity participation by Central, State Governments and Commercial Banks. To further supplement the institutional mechanism, 10 Local Area Banks were licensed from the financial year 1996-97. There are over 1,05,735 Co-operative Societies, 12,590 branches of 365 District Central Cooperative Banks (DCCBs). There are 11,825 Rural, 2,153 Semi-Urban and 445 Urban / Metropolitan branches of 196 RRBs (Pre-merger). And we have 20,253 rural and 12,522 semi-urban branches of 99 Commercial banks. Besides, there are 31 State Cooperative Banks (SCBs) with 885 branches, 20 State Credit Agriculture and Rural Development Banks (SCARDBs) with 863 branches and 768 Primary Credit Agriculture and Rural Development Banks (PCARDBs) with 1,008 branches.

Thus, there are about 1,50,000 retail rural credit outlets for a rural population of 680 million. There is now a reasonably extensive formal banking institution network capable of meeting the financial needs of the entire rural population. But over 45 per cent of the members of Primary Agricultural Cooperative Societies (PACS) are not borrowing members and over 65 per cent of the 1,01,245 PACS are dormant or in poor financial condition due to insufficient recycling of funds and other weaknesses.\(^4\)

Between 1973 and 1985, bank branches in rural areas grew at an average rate of 15.2 per cent each year, about double the growth rate of branches in semi-urban (6.4 per cent), urban (7.8 per cent) and metropolitan (7.5 per cent) areas. Rural branches grew from 1,833 in 1969 to 30,186 in 1985, the increase is 1,547 branches.

By comparison, the increase over the same period in semi-urban, urban and metropolitan areas was to 1,94,315 or a rise of 220 per cent.\(^5\) Today, India has over 32,000 rural branches of Commercial Banks and Regional Rural Banks, 14,000 branches of Co-Operative banks, 98,000 Primary Agricultural Credit Societies (PACS), and 1,54,000 postal outlets that are required to focus on deposit mobilization and money transfers.\(^6\)

Over the years, Indian banking has certainly become more inclusive. But the majority of the rural population still does not appear to have access to finance from a formal source, and the poor face particularly severe problems in getting finance. All India Debt and Investment Surveys indicate that the share of rural household debt of Commercial Banks and Co-operative Banks increased from just 10.7 per cent in 1961 to 22.5 per cent in 1971 and then rose sharply to 57.2 per cent in 1981. In the decade that followed, the share of banks remained more or less stable, while that of the co-operatives declined slightly. The share of money lenders declined over the decades.\(^7\)

The main emphasis in the spread of banking network, introduction of new instruments and credit packages and programmes has been to make the financial system responsive to the needs of the weaker sections in the society comprising small and marginal farmers, rural artisans, landless agricultural and non-agricultural labourers and other small borrowers falling below the poverty line.\(^8\)

The Integrated Rural Development Program (IRDP) introduced in 1978 was designed to be a direct instrument for attacking India’s rural poverty. The IRDP was reputed as one of the largest poverty alleviation programmes in the world with the

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number of loans advanced by banks since its inception reached approximately 45 million Indians with financial assistance worth US $6.17 billion disbursed.

The problem with targeting the rural poverty, that the government identified was, that the subsidy orientation of the scheme created a huge temptation for the non-poor to participate in the program by dishonest means. The subsidy provided by the government varied from 25 per cent for small farmers 30 per cent for Scheduled Castes and Tribal people. The overarching goal of the programme was to enhance the income of the rural poor sufficiently so as to enable them to cross the poverty line. But there was no effective mechanism for enforcing the selection of the poor clientele based on the official ‘poverty line’. Therefore, by this standard the IRDP did not achieve its expected results.\(^9\)

By early 1990s the reach of institutional finance was restrictive. The share of the formal financial sector in total rural credit was 56.6 per cent only compared to the informal finance at 36.6 per cent and unspecified sources at 3.8 per cent. The credit requirement of the poor in India has been estimated to be around Rs. 50,000 crore per annum. Against this requirement, the credit outstanding of the poor with the normal banking sector is stated to be Rs. 5,000 crore or ten per cent of the total demand.

In the states – Andhra Pradesh and Uttar Pradesh of India around 87 per cent of marginal farmers / landless farmers do not have access to credit from formal banking sector. Most of the benefits of the so called extensive banking infrastructure have gone to the relatively better off people; around 66 per cent of large farmers have deposit accounts and 44 per cent have access to credit.\(^10\) At this juncture it was

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apparent that there was an urgent need for financial innovation in the rural credit market in India.\textsuperscript{11}

In policy terms, it appears that the government envisages only one policy instrument to fill the gap left by the formal credit section in the country side - that is the establishment of ‘microcredit projects’ in rural India.

**GENESIS OF MICROCREDIT AND MICROFINANCE:**

The terms ‘microcredit’ and ‘microfinance’ have risen spectacularly to fame in development literature in the last decade and a half.\textsuperscript{12}

Microcredit and microfinance are relatively new terms in the field of development. In the literature the terms microcredit and microfinance are often used interchangeably, but it is important to highlight the difference between both the terms.

After the great success of Grameen Bank of our neighboring country Bangladesh, the concept of microfinance has gained momentum, micro credit / microfinance has been defined as “Programmes that provide credit and other financial and business services (including savings and technical assistance) to very poor persons”. Microfinance has emerged as a powerful tool that provides micro funds to very poor people for poverty alleviation in the economy.\textsuperscript{13}

Especially during the past 10 years, micro finance programmes have been introduced in many developing economies.\textsuperscript{14} The pioneer institution of Grameen Bank, Bangladesh, was developed by Dr. MuhAmmad Yunus in 1976, who was its


former Chairman. Other important institutions are Banco Sol of Bolivia, the Bank of Rokyat of Indonesia, the Bank Kredit Deas of Indonesia and village banks started by the Foundation for International Community Assistance (FINCA) in Indonesia.

In India, microcredit programmes are mostly organized by NGOs.

**GRAMEEN BANK MODEL IN BANGLADESH:**

Grameen Bank adopted a simple but effective system. To obtain loans, the potential borrowers must form a group of five, gather once a week for loan repayment meetings. The formation of groups is the first necessary step to receive credit. Loans are initially made to two individuals in the group, who are then under pressure from the rest of the members to repay.\(^{15}\)

Dr. Mahammad Yunus had developed certain principles for effective Grameen bank system.

- Grameen believes that poverty is not created by the poor, but by the institutions and policies which surround them. In order to eliminate poverty, appropriate changes have to be made in these institutions or policies. Alternatively new ones have to be created.

- Charity is not an answer to poverty. It serves only to perpetuate poverty and create dependency. It takes away the initiative of an individual to break through the wall of poverty. The way to overcome poverty is to unleash the energy and creativity in each human being.

- The Grameen system is built on the belief that there is no difference in the ability of a poor person and any other person. The poor merely do not get the opportunity to explore their potential and so their abilities remain unutilized or underutilized. If they had the opportunity, they would be able to change their own lives.\(^{16}\)

- Conventional banks start with the principle that the more you have the more you can get, which provides a spring board for those who are already well off. Our principle has always been the less the person has, the higher the priority s/he gets.

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A central assumption underlying Grameen’s system is the firm belief that poor people always pay back. For many of the borrowers, it is the first time that they are handling money; no one has ever trusted them with these sums of money before; for this reason they commit to pay back every penny.

Lending to women brings greater benefits to the family than lending to men. If the mother is the borrower, the children are the immediate beneficiaries. Women have greater long-term vision and are ready to bring about changes in their lives step by step.17

Policy makers rarely gave the landless a central place in their plans for rural investment as the poor with no land or collateral are considered a risky proposition.18

The RBI recognized the problem of financial exclusion in the annual policy statement in 2005 and since then it has initiated several policies aiming at promoting financial inclusion of especially pensioners, the self-employed and those employed in the unorganized sector.19 The concepts, ‘Microcredit’, ‘Microfinance’, ‘Microfinance Institutions’ and ‘Various Approaches to Microfinance’ are elaborately discussed in what follows:

MICROCREDIT:

Microcredit as defined by the Grameen Bank and the Declaration of the Microcredit Cummit held in Washington DC in 1997 is “extending small loans to poor people for self-employment projects that generate income, allowing them to care for themselves and their families”.20

Microcredit has been called one of the most significant innovations in development policy of the past twenty five years.21 It deals with a small amounts of money loaned to clients by banks or other institutions. Microcredit can be offered,
often without any collateral security to an individual or through a group lending.\textsuperscript{22} This microfinance system often includes saving facilities, training, networking and peer support.\textsuperscript{23}

Micro credit programmes have brought the vibrancy of the market economy to the poorest villages of the world. This business approach to the alleviation of poverty has allowed millions of individuals to work for the way out of poverty with dignity.\textsuperscript{24}

The major argument against microcredit is its failure to reach the poorest of the poor. The exclusion of the poorest is well known. Indeed, there is often a presumption that the moderately poor are less likely to default than those who are acutely poor. Some important factors resulting in this exclusion are lack of awareness, social exclusion of the poor and collusion of officials of micro-credit institutions with non-poor households. Too much of financial discipline / stringency, that is, strict repayment requirements and penalties for delays, could deter the poor from joining a microcredit scheme or could limit their duration of participation in it. We should move forward with caution, making sure that the bad features of the formal credit delivery system do not creep into microcredit.\textsuperscript{25}

The Self-Help Group - Bank Linkage Programme is the flagship service. The intervention of National Bank for Agriculture and Rural Development (NABARD) in microfinance which was launched as a pilot project on 26 February 1992 could be considered as a landmark development in the banking with the poor. The informal thrifty and credit groups of the poor came to be recognized as bank clients under the pilot phase. The pilot phase was followed by setting up of a working group on Non-

\textsuperscript{22} Anil K Khandelwal, “Microfinance development strategy for India”, \textit{Economic & Political Weekly}, March 31, 2007, P-1128.
Governmental Organizations (NGOs) and Self-Help Groups (SHGs), by the Reserve Bank of India in 1994, under the Chairmanship of the Managing Director of NABARD, which came out with wide ranging recommendations on internalization of the SHG concept as a potential intervention tool in the area of banking with the poor.\textsuperscript{26}

**MICROFINANCE:**

In India, microfinance has been defined by the Task Force on Microfinance as “provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi-urban or urban areas for enabling them to raise their income levels and improve living standards”. As per the definition of International Labour Organisation (ILO), the microfinance is ‘an economic development approach that involves providing financial services through institutions to low income clients’.

Today, the term ‘microfinance’ refers to loans, savings, insurance, transfer services and other financial products targeted to low income clients. That means microfinance generally covers all activities like microcredit, micro-savings, micro-insurance and remittances. There are several Micro Finance Institutions (MFI), Non-Governmental Organizations (NGOs), Self-Help Groups (SHGs), Banks and other Institutions, which are actively engaged in microfinancing activities with innovative methods.\textsuperscript{27}


OBJECTIVES OF THE MICROFINANCE:

The following are the fundamental objectives of microfinance:

(i) to offer cost effective approach to formal institutions for expanding the outreach to the poor

(ii) to develop collateral substitutes

(iii) to focus on the rural and the urban poor generally and women in particular

(iv) to pilot test other micro-credit delivery mechanisms as alternative channels to the formal banks

(v) to effectively pursue the objectives of microeconomic growth

(vi) The Social Empowerment through:

- increased status, participation and powers of decision making of women in household
- increased status, participation and powers of decision making of women in community and village
- breaking cultural barriers for equal development of women
- increased status, participation and powers of decision making of women in democratic institutions

(vii) The Economic Empowerment through:

- greater access to financial resources outside the household
- reduced vulnerability of the poor women to crisis famine, and the like
- increasing access and control over resources at the household level
- financial self-reliance of women

(viii) Capacity building (a strategy and an end in itself) through:

- improvement in functional literacy, innumeracy
- better communication skills
- better leadership skills

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self-help and mutual help

(ix) Political Empowerment through:

- participation in Panchayati Raj Institution
- negotiating political power
- accessing political power
- collective identity

(x) To increasing the consumption for poor

MICROFINANCE INSTITUTIONS:

A microfinance institution is generally defined as “an institution that provides financial services to the poor”. For example, NGOs (Non-Government Organizations), Co-operative Societies, Credit Unions, Banks, Insurance Companies, Post Offices etc. are some of the institutions which provide financial services. These institutions provide poor people with access to credit facilities, which they rarely get through formal financial institutions. Today, there are more than 10,000 institutions engaged in these activities and serving the poor.

APPROACHES OF MICROFINANCE:

In the evolution of microfinance industry there are five models based on different philosophies and target groups. They are:

1. Grameen and Solidarity Model developed in Bangladesh and now popular in South Asia.
3. Individual credit – mostly priority sector lending in India.
5. Credit unions and cooperatives – popular in Sri Lanka. The Self-Help Groups (SHGs) are the latest breeds of the microfinance industries in India.

In India the major institutional initiatives include the SHGs-Bank linkage programme under the overall guidance and supervision of the NABARD.33

**Self-Help Group Bank Linkage Model:** In this model SHGs act as a bridge between bankers and the grass root clients. Banks transfer funds to microfinance bodies that are responsible for disbursal and collection. The intermediation cost could be around 6% of the loan amount.

A majority of these grassroots level customers have no means to produce ration cards, identity card and even the do know how to fill in the application forms, which are the bare requirements to obtain loans in the normal course of bank lending operations.34

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Products and interest rates vary from one (Microfinance Institutions) MFI to other MFI. SHG loans start at Rs. 5,000 with Effective Interest Rate (EIR) usually in the range of 24-27 per cent. Grameen loans sometimes have a lower loan size at the start and the EIR is in the range of 32-42 per cent. MFIs following the Individual Banking (IB) model generally have male clients, higher loan size (Rs. 15,000 and above) linked often to economic activities and production cycle linked with individual transactions, including daily collection.\(^\text{35}\)

The SHG gets loans from an MFI and the responsibility for repayment falls on the group and MFIs do not interfere in the disbursements among individual members. The recovery rate of loans to SHGs ranges from 95 per cent to 98 per cent, which shows the efficiency of these groups. As the percentage of population below the poverty line in rural areas is higher than in the urban areas, the NABARD’s

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microcredit programme accepted the challenge of alleviating the rural poverty, by instituting an overall arrangement for provision of a wide range of financial services (credit, savings, insurance, etc.) to the bypassed and the underserved in a sustainable manner, leading to their social and economic empowerment.

Microcredit to SHGs has been paving the way for opening up of a large number of mini-ventures (production and marketing) in rural areas, which has not only generated gainful occupation but also provided scope for transformation of rural society.³⁶

Three distinct linkage models of microcredit are currently being followed by NABARD in India.

**Model-I: Self-Help Groups formed and financed by Banks:**

Under this model, the banks themselves take up the work of forming and nurturing the groups opening their savings accounts and providing them with bank loans. In March 2001, 13 per cent of the total number of self-help groups was financed under this category. Up to March 2005, 15 per cent of the total number of SHGs was financed under in this category.³⁷

**Model-II: Self-Help Groups formed by Non Governmental Organizations and Formal Agencies, but directly financed by Banks:**

This appears to be the most popular model amongst bankers. Under this model Non-governmental Organizations and formal agencies act as facilitators in the field of microfinance. They propagate the message, organize groups, train them in thrift and credit management and nurture them over a period. Banks, in due course, have link with these groups by directly providing loans for them. Major share in 2001 of Self-Help Groups (linked with banks) being 76 per cent under this model is more when


compared to 70 per cent in March 2000. This model continues to have a lion’s share, with 80 per cent of SHGs financed up to March 2005.38

**Model-III: Self-Help Group financed by banks using Non Governmental Organizations as Financial Intermediaries:**

In this model, Non-governmental Organizations take on the dual role of facilitators and financial intermediaries. They help in formation of self-help groups, nurturing them, training them in thrift and credit management. Eventually, the Non-governmental Organizations approach banks for bulk loan assistance for lending to these Self-Help Groups.

The share of cumulative number of Self-Help Groups linked under this model is relatively small that is, 11 per cent. However, in the years to come, a need may arise for the Self-Help Groups as lending institutions also to look for viable substructures for financial intermediation. This could eventually develop into and effective method to control transaction costs through economics of scale.39

**MODEL WISE SHG BANK LINKAGE POSITION:**

All of the three microfinance models have achieved greater success that was difficult for the main stream-banking sector to achieve. In order to analyze the model-wise SHG-Bank linkage position the relevant data is presented in the following Table-I.1 and Table-I.2.40

Out of the three models emerged under the SHG-Bank linkage programme over the years, about 85.6 per cent of the SHGs were financed by banks under Model-II involving NGOs and Government agencies. Banks under Model-I where the SHGs promoted, guided and financed by banks, financed only 14.4 per cent of the SHGs. Under these models the total bank loan amount was increased by 65.24 per

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cent, whereas the number of SHGs increased by 38.38 per cent during the year 2005-06.41

TABLE-I.1: MODEL – WISE SHG BANK LINKAGE POSITION

<table>
<thead>
<tr>
<th>Model</th>
<th>2004-05</th>
<th>2005-06</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No. of SHGs ('000)</td>
<td>Bank Loans (Rs. Crore)</td>
</tr>
<tr>
<td>(A) Self-Help Group Model</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(i) Self Help Groups formed and financed by banks</td>
<td>343 (21.2)</td>
<td>1,013 (14.7)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(B) Micro Finance Institution Model</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(ii) SHGs formed by NGOs and formal agencies (Government) and directly financed by banks</td>
<td>1,158 (71.6)</td>
<td>5,529 (80.2)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(iii) SHGs formed by NGO’s and financed by banks using NGOs / formal agencies as financial intermediaries</td>
<td>117 (7.2)</td>
<td>356 (5.2)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,618</strong></td>
<td><strong>6,898</strong></td>
</tr>
</tbody>
</table>

Note: Figures in brackets are percentage to total, Source: NABARD.

Table I.2: MODELS – WISE OVER ALL PROGRAMMES UNDER MICROFINANCE DURING THE YEAR 2006-07 TO 2008-09

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No. of SHGs</td>
<td>Amount</td>
<td>No. of SHGs</td>
<td>Amount</td>
<td>No. of SHGs</td>
</tr>
<tr>
<td>A. SHG-Bank Linkage Model</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Savings of SHGs with Banks of on 31 March</td>
<td>Total SHGs</td>
<td>41,60,584</td>
<td>3,512.71</td>
<td>50,09,794</td>
<td>3,785.39</td>
</tr>
<tr>
<td></td>
<td>Out of which SGSY</td>
<td>9,56,317</td>
<td>757.50</td>
<td>12,03,070</td>
<td>809.51</td>
</tr>
<tr>
<td>Bank loans disbursed with SHGs as on 31 March</td>
<td>Total SHGs</td>
<td>11,05,749</td>
<td>6,570.39</td>
<td>12,27,770</td>
<td>8,849.20</td>
</tr>
<tr>
<td></td>
<td>Out of which SGSY</td>
<td>1,88,962</td>
<td>1,411.02</td>
<td>2,46,649</td>
<td>1,857.74</td>
</tr>
<tr>
<td>Bank Loans Outstanding with SHG as on 31 March</td>
<td>Total SHGs</td>
<td>28,94,505</td>
<td>12,366.49</td>
<td>36,25,941</td>
<td>16,999.91</td>
</tr>
<tr>
<td></td>
<td>Out of which SGSY</td>
<td>6,87,212</td>
<td>3,273.03</td>
<td>9,16,978</td>
<td>4,816.87</td>
</tr>
<tr>
<td>B. MFI-Bank Linkage Model</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank Loans disbursed to MFIs during the year</td>
<td>334</td>
<td>1,151.56</td>
<td>518</td>
<td>1,970.15</td>
<td>71.1</td>
</tr>
<tr>
<td>Bank Loans outstanding with MFIs as on 31 March</td>
<td>550</td>
<td>1,584.48</td>
<td>1,109</td>
<td>2,748.84</td>
<td>73.5</td>
</tr>
</tbody>
</table>

Source: NABARD.
The SHG-Bank linkage programme has proved its efficacy as a mainstream programme for banking with the poor. The main advantages of the programme are as follows:

- one-time repayment of loans to banks
- reduction in transaction costs both to the poor and to the banks
- doorstep savings and credit facilities to the poor
- exploitation of the untapped business potential in rural India

But it must clearly be understood that poverty eradication in backward regions of India is impossible without a critical minimum dose of public investments – in natural resources regeneration, sustainable agriculture and a whole range of nature-based livelihoods and infrastructure – that creates the enabling environment for private investments to flourish.

Many allied inputs are required – forward and backward linkages (input-market support), appropriate skills and technologies as well as finance for fixed assets and working capital. Without working out this entire package, micro credit can easily become ‘macro debt’, pushing the poor into traps they find very hard to escape. It is truly ironic that the very same people who sing paeans of globalization are promoting micro enterprises as the answer to world poverty without waiting to reflect on how they expect these micro enterprises to withstand the unbearable pressures of global competition.

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42 Op Cit., Dr. Ramesh, T., P: 818.
PART-B

In this section a modest attempt is made to examine the trends in the growth of the microfinance sector in the Indian context and the shortcomings of the microfinance industry at large.

TRENDS IN SHG – BANK LINKAGE:

The Self Help Group - Bank Linkage Programme has emerged as the major microfinance programme in the country and is being implemented by the Commercial banks, RRBs and Co-operative banks. SHG-Bank Linkage Programme (SBLP) is operational in 20 states in India and is actively channeling credit to the poorer sections of society for mainly non-farm activities. The number of 255 SHGs linked with bank during 1992-93, increased to 81,780 by March 2000. The amount of bank loans routed through SHGs increased from Rs. 0.29 crore to Rs. 135.91 crore by March 2000. In all, 85 per cent of the groups linked with the banks are formed exclusively by women.\(^{44}\)

As on 31\(^{st}\) March 2009, 4.2 million SHGs were operating with an outstanding bank credit of Rs. 22,800 crore went up by 34 per cent when compared to the outstanding bank credit in March 2008. During 2008-09, the banks financed 1.6 million SHGs including repeat loans to existing SHGs to the tune of Rs. 12,254 crores. There were 6.1 million savings accounts with banks as on March 31\(^{st}\) 2009, with total deposits amounting to Rs. 5,546 crores.

The Self-Help Group - Bank Linkage Programme (SBLP) provided a major succor to the rural women folk and helped them in gaining financial access for their livelihood. The launching the SBLP as rural financial innovations in the beginning of

90s for increased popularity of Micro-Finance (MF) is a viable tool for extending credit to the poor.

The programme registered a significant growth both in terms of coverage and the outreach of credit to the poor. Beginning with a modest number of 225 SHGs linked during 1992-93, a cumulative total of 25,84,729 SHGs were linked with banks by February 2007. The cumulative disbursement of bank loans was Rs. 14,479.87 crore and refinance assistance was Rs. 5,326.87 crore by February 2007. Over the eight-years-period (1997-05), the number of SHGs linked with banks grew at a Compound Annual Growth Rate (CAGR) of 102.46 per cent. The number of families assisted rose by 73.15 per cent. The average loan per SHG and per family has increased by 8.8 per cent.45

The SHG - Bank Linkage Programme shows a tremendous growth over a period of 16 years from 1992-93 to 2008-09. The progress is notable in cases of granting bank loan to the beneficiaries, refinance programme and then the number of groups linked. The trend line in all the aspects shows a positive one. The exponential growth rate of bank loan is estimated at 60.97 per cent with the coefficient of determination of 0.96. The exponential growth rate on the refinance programme is 60.37 per cent with 0.93 as coefficient of determination vide graph-I.A, and the same is 55.54 per cent and 0.94 respectively for the number of groups linked. However, the progress of SHG-Bank linkage programme is good.

Table-I.3: PROGRESS OF SELF-HELP GROUP-BANK LINKAGE PROGRAMME IN INDIA (Amount Rupees In Crore)

<table>
<thead>
<tr>
<th>Year</th>
<th>No. of SHGs Financed by Banks</th>
<th>Bank Loan</th>
<th>Refinance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>During the year</td>
<td>Trend %</td>
<td>During the year</td>
</tr>
<tr>
<td>1992-93</td>
<td>255</td>
<td>100</td>
<td>0.29</td>
</tr>
<tr>
<td>1993-94</td>
<td>365</td>
<td>143</td>
<td>0.36</td>
</tr>
<tr>
<td>1994-95</td>
<td>1502</td>
<td>589</td>
<td>1.79</td>
</tr>
<tr>
<td>1995-96</td>
<td>2635</td>
<td>1033</td>
<td>3.62</td>
</tr>
<tr>
<td>1996-97</td>
<td>3841</td>
<td>1506</td>
<td>5.78</td>
</tr>
<tr>
<td>1997-98</td>
<td>5719</td>
<td>2243</td>
<td>11.92</td>
</tr>
<tr>
<td>1998-99</td>
<td>18678</td>
<td>7325</td>
<td>33.31</td>
</tr>
<tr>
<td>1999-00</td>
<td>81780</td>
<td>32071</td>
<td>135.91</td>
</tr>
<tr>
<td>2000-01</td>
<td>149050</td>
<td>58451</td>
<td>287.89</td>
</tr>
<tr>
<td>2001-02</td>
<td>197653</td>
<td>77511</td>
<td>545.47</td>
</tr>
<tr>
<td>2002-03</td>
<td>255882</td>
<td>100346</td>
<td>1022.33</td>
</tr>
<tr>
<td>2003-04</td>
<td>361731</td>
<td>141855</td>
<td>1855.53</td>
</tr>
<tr>
<td>2004-05</td>
<td>539365</td>
<td>211516</td>
<td>2994.26</td>
</tr>
<tr>
<td>2005-06</td>
<td>620109</td>
<td>243180</td>
<td>4499</td>
</tr>
<tr>
<td>2006-07</td>
<td>1105749</td>
<td>433627</td>
<td>6570</td>
</tr>
<tr>
<td>2007-08</td>
<td>1227770</td>
<td>481478</td>
<td>8849.26</td>
</tr>
<tr>
<td>2008-09</td>
<td>807905</td>
<td>316825</td>
<td>4585.45</td>
</tr>
<tr>
<td>Total</td>
<td>4433846</td>
<td></td>
<td>21585.4</td>
</tr>
<tr>
<td>Average</td>
<td>124106</td>
<td></td>
<td>636961</td>
</tr>
</tbody>
</table>

Note:
1) Data for 2008-09 are provisional.
2) Data relates to Commercial Banks, RRBs and Co-operative Banks.
3) From 2006-07 onwards, data on number of SHGs financed by banks and bank loans are inclusive of 'Swarnajayanti Gram Swarozgar Yojna' (SGSY) SHGs and existing groups receiving repeat loans.
4) Figures for 2006-07 and 2007-08 are outstanding number of SHGs and outstanding bank loans to SHGs as on 31 March of respective years.
5) The CAGR is calculated using the formula \((ending\ value/beginning\ value)^{number\ of\ years}-1\)*100
Source: RBI bulletin.
Graph-I.A

TREND LINE SHOWING THE BANK LOAN DISBURSEMENT OVER 1992-93 TO 2008-09

Graph-I.B

GROWTH OF THE PROGRAMME MEASURED IN TERM OF LOANS DISBURSED DURING 1992-93 TO 2008-09.
Table I.4
AGENCY-WISE DISTRIBUTION OF SHGS THAT WERE LINKED WITH EXTERNAL CREDIT
(Amount in Rs. Million)

<table>
<thead>
<tr>
<th>Year</th>
<th>Commercial Banks</th>
<th>Regional Rural Banks</th>
<th>Cooperative Banks</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No</td>
<td>Loan Amount</td>
<td>No</td>
<td>Loan Amount</td>
</tr>
<tr>
<td>1997</td>
<td>5,362</td>
<td>62.79</td>
<td>3,048</td>
<td>35.68</td>
</tr>
<tr>
<td>1998</td>
<td>8,704</td>
<td>60.79</td>
<td>5,192</td>
<td>36.26</td>
</tr>
<tr>
<td>1999</td>
<td>20,155</td>
<td>60.96</td>
<td>11,610</td>
<td>35.19</td>
</tr>
<tr>
<td>2000</td>
<td>51,619</td>
<td>54.54</td>
<td>38,998</td>
<td>41.20</td>
</tr>
<tr>
<td>2001</td>
<td>124,246</td>
<td>52.91</td>
<td>97,824</td>
<td>41.20</td>
</tr>
<tr>
<td>2002</td>
<td>274,247</td>
<td>54.53</td>
<td>188,738</td>
<td>37.53</td>
</tr>
<tr>
<td>2003</td>
<td>361,061</td>
<td>50.33</td>
<td>277,340</td>
<td>38.66</td>
</tr>
<tr>
<td>2004</td>
<td>538,422</td>
<td>49.90</td>
<td>405,998</td>
<td>37.62</td>
</tr>
<tr>
<td>2005</td>
<td>843,473</td>
<td>52.0</td>
<td>563,846</td>
<td>35.0</td>
</tr>
<tr>
<td>2006</td>
<td>11,88,076</td>
<td>53.0</td>
<td>740,024</td>
<td>33.0</td>
</tr>
<tr>
<td>2006-07</td>
<td>15,94,787</td>
<td>55.0</td>
<td>9,10,807</td>
<td>31.0</td>
</tr>
<tr>
<td>2007-08</td>
<td>73,5119</td>
<td>59.9</td>
<td>327650</td>
<td>26.7</td>
</tr>
<tr>
<td>2008-09</td>
<td>1004587</td>
<td>62.4</td>
<td>405569</td>
<td>25.2</td>
</tr>
</tbody>
</table>

Source: NABARD Annual Report of various years.
Note: year 2007-08 and 2008-09 data is in crores

Out of 290 banks reporting data on recovery to the NABARD as on March 31, 2007, nearly 73 per cent of banks had more than 80 per cent recovery on loans given to SHGs.46

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SHG GROWTH IN ANDHRA PRADESH:

Andhra Pradesh finds a prominent place in the movement of Self Help Groups with 8.51 lakh Self Help Groups, covering about 101.82 lakh rural women. It has, in fact, come to be known as the microfinance capital of the country. The Indira Kranthi Padam (IKP) project focused on formation of SHGs of the poorest of the poor and Below Poverty Line (BPL) families. However, while forming the SHGs, some non-poor members have also become members of the SHGs. More than one member of a family has also become members of different SHGs in the same village and sometimes in the same SHG. It is estimated that about 50% of the population of the state is either directly or indirectly impacted by the programmes.

Table-I.5: SHGS IN ANDHRA PRADESH – 31 MARCH 2009

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Andhra Pradesh</th>
<th>% Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of SHGs promoted by:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Govt. Agencies</td>
<td>8,28,028</td>
<td>97.34</td>
</tr>
<tr>
<td>NGO’s</td>
<td>20,148</td>
<td>2.37</td>
</tr>
<tr>
<td>Farmer Clubs</td>
<td>114</td>
<td>0.01</td>
</tr>
<tr>
<td>Individual Rural Volunteer</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Total</td>
<td>8,50,671</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: NABARD

Andhra Pradesh has a prominent place in SHG movement with 8,50,671 SHGs covering 1,01,82,181 rural women. Nearly 23 per cent of the members of the SHGs belong to Scheduled Castes category and 10 per cent belong to the Scheduled Tribe category as shown in Table-I.6. In terms of coverage, 20 per cent of women in the state are members of the SHGs. Majority of the groups in the state have been formed through the Indira Kranthi Padam (IKP) project and the District Rural Development Agency (DRDA). At the end March 2009, the SHGs built a corpus of Rs. 4,025.55 crore including thrift amount of Rs. 1,962.50 crore.
Table-I.6: HIGHLIGHTS OF SHG MOVEMENT IN ANDHRA PRADESH AS ON 31 MARCH 2009

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total number of SHGs in Andhra Pradesh</td>
<td>8,50,671</td>
</tr>
<tr>
<td>Total members covered under SHGs</td>
<td>1,01,82,181</td>
</tr>
<tr>
<td>Average number of members per SHG</td>
<td>12</td>
</tr>
<tr>
<td>Percentage of SC members</td>
<td>23</td>
</tr>
<tr>
<td>Percentage of ST members</td>
<td>10</td>
</tr>
<tr>
<td>Total savings of the SHGs (Rs. In Crore)</td>
<td>1,962.50</td>
</tr>
<tr>
<td>Average savings per SHG (Rs.)</td>
<td>23,070</td>
</tr>
<tr>
<td>Total corpus of the SHGs* (Rs. Crore)</td>
<td>4,025.55</td>
</tr>
<tr>
<td>Average amount of corpus per SHG (Rs.)</td>
<td>47,322</td>
</tr>
</tbody>
</table>

Note: Corpus includes savings of the group, interest earned by the SHGs on internal lending, revolving fund assistance provided by the state government, penalties collected etc.

Source: Department of Rural Development, Government of Andhra Pradesh.

The resources of the SHGs come from the thrift by the members, bank loan, interest earned on internal lending and revolving fund assistance provided by the State Government. The average savings of the majority of the SHG members in the state ranges from Rs. 30 to Rs. 50 per month. Some of the old groups saved up to Rs. 10 per month. The SHGs in the state mostly follow a monthly saving system.

The savings coupled with the bank finance have been used for internal lending among the members at an interest rate ranging from 18 per cent to 24 per cent per annum. The interest charged by the banks to the SHGs is in the range of 8 per cent to 12 per cent per annum with effect from 1 July 2004. The SHGs in the State are getting bank loan at effective rate of interest of 3 per cent per annum as the state government is reimbursing the SHGs the interest charged by the banks over and above 3 per cent for promotion repayment. The thrift collection and the interest differential have helped the SHGs in building a corpus of Rs. 4025.55 crore as on 31 March 2009.
Table-I.7: SHG-BANK LINKAGE PROGRAMME – GROUND LEVEL CREDIT IN ANDHRA PRADESH

<table>
<thead>
<tr>
<th>Period</th>
<th>No. of groups financed</th>
<th>Bank Loan (Rs. In Crore)</th>
<th>CAGR%</th>
<th>Refinance of NABARD (Rs. In Crore)</th>
<th>Average per group finance (In Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1992-93</td>
<td>35</td>
<td>0.09</td>
<td>-</td>
<td>0.09</td>
<td>25,085</td>
</tr>
<tr>
<td>1993-94</td>
<td>102</td>
<td>0.16</td>
<td>77.7777</td>
<td>0.16</td>
<td>16,171</td>
</tr>
<tr>
<td>1994-95</td>
<td>105</td>
<td>0.31</td>
<td>93.75</td>
<td>0.31</td>
<td>29,723</td>
</tr>
<tr>
<td>1995-96</td>
<td>147</td>
<td>0.44</td>
<td>41.9354</td>
<td>0.44</td>
<td>29,932</td>
</tr>
<tr>
<td>1996-97</td>
<td>434</td>
<td>1.40</td>
<td>218.1818</td>
<td>1.40</td>
<td>32,488</td>
</tr>
<tr>
<td>1997-98</td>
<td>1,322</td>
<td>3.18</td>
<td>127.1428</td>
<td>3.16</td>
<td>24,054</td>
</tr>
<tr>
<td>1998-99</td>
<td>6,579</td>
<td>12.75</td>
<td>300.9433</td>
<td>12.72</td>
<td>19,380</td>
</tr>
<tr>
<td>1999-00</td>
<td>29,242</td>
<td>54.95</td>
<td>330.9803</td>
<td>54.89</td>
<td>18,791</td>
</tr>
<tr>
<td>2000-01</td>
<td>84,939</td>
<td>143.17</td>
<td>160.5459</td>
<td>143.12</td>
<td>16,856</td>
</tr>
<tr>
<td>2001-02</td>
<td>1,17,352</td>
<td>267.09</td>
<td>86.5544</td>
<td>197.72</td>
<td>22,760</td>
</tr>
<tr>
<td>2002-03</td>
<td>1,65,429</td>
<td>454.13</td>
<td>70.0288</td>
<td>270.94</td>
<td>27,452</td>
</tr>
<tr>
<td>2004-05</td>
<td>2,61,254</td>
<td>1,017.71</td>
<td>35.1558</td>
<td>391.94</td>
<td>39,955</td>
</tr>
<tr>
<td>2005-06</td>
<td>2,94,341</td>
<td>1,599.43</td>
<td>57.1597</td>
<td>475.97</td>
<td>54,339</td>
</tr>
<tr>
<td>2006-07</td>
<td>3,59,276</td>
<td>2,775.45</td>
<td>73.5274</td>
<td>696.11</td>
<td>77,251</td>
</tr>
<tr>
<td>2007-08</td>
<td>4,15,206</td>
<td>5,573.34</td>
<td>100.8085</td>
<td>1,342.30</td>
<td>1,34,231</td>
</tr>
<tr>
<td>2008-09</td>
<td>5,00,536</td>
<td>6,767.40</td>
<td>21.4244</td>
<td>1,685.23</td>
<td>1,35,203</td>
</tr>
</tbody>
</table>

Compounded Annual Growth Rate (CAGR %) = [(Ending Value / Beginning Value) ^ Number of Years] – 1 * 100.
Source: NABARD.

ROLE OF BANKS IN FINANCING THE SHGS:

In promoting SHG movement as a popular vehicle of microfinance in the state the role of banks is laudable. The banks in Andhra Pradesh have played a proactive role in financing SHGs starting financing 35 SHGs with bank loan of Rs. 0.09 crore in 1992-93, the banks have moved a long way in financing SHGs during the year 2008-09 paying loans to the tune of Rs. 6,767.40 crore was extending the benefit to 5.00 lakh SHGs cumulatively. Then 18.61 lakh groups have been credit-linked in
the state involving outlay of Rs. 19,461.71 crore by the end of 31 March 2009. Some of the Regional Rural Banks have acted as Self Help Promoting Institutions (SHPI) in the initial phase of SHG-Bank Linkage Programme. The loans provided by the banks in Andhra Pradesh are given in Table-I.7.

The formation and nurturing of SHGs and the creating confidence among them will sustain only if they are provided with adequate funds for the chosen economic activities.

**AGENCY WISE PERFORMANCE IN A.P.:**

Commercial Banks and Regional Rural Banks have been the major players in the SHG-Bank Linkage Programme in the State. During the period from 1997-98 to 2008-09, the share of commercial banks in the SHG-Bank Linkage programme has gone up from 55% to 63% in terms of number of SHGs and from 63% to 74% in terms of bank loan disbursed to SHGs. The share of RRBs has come down during the above period both in terms of number of SHGs (from 45% to 35%) and bank loan (from 37% to 25%), the cooperatives have increased their share to 2% in terms of number of SHGs and 1% in terms of bank loan (Table-I.8).

**Table-I.8: AGENCY WISE PERFORMANCE UNDER SHG-BANK LINKAGE PROGRAMME – CUMULATIVE**

<table>
<thead>
<tr>
<th>Banks</th>
<th>No. of SHGs</th>
<th>Bank Loan</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1997-98 Share (%)</td>
<td>2008-09 Share (%)</td>
</tr>
<tr>
<td>CBs</td>
<td>1,173 55</td>
<td>3,12,325 63</td>
</tr>
<tr>
<td>RRBs</td>
<td>972 45</td>
<td>1,76,658 35</td>
</tr>
<tr>
<td>Coops</td>
<td>0 0</td>
<td>11,553 2</td>
</tr>
<tr>
<td>Total</td>
<td>2,145 100</td>
<td>5,00,536 100</td>
</tr>
</tbody>
</table>

Source: NABARD.

Total number of participating banks in the SHG linkage programme increased from 314 in March 2001 to 547 by March 2006. By March 2006, the SHG-Bank
Linkage Programme became a part of business for all the 27 public sector banks and 20 private sector banks leading to the increase in number of commercial banks from 43 to 47 in March 2001.

Out of 4,249 rural and semi urban/urban branches of all the banks in the state, 4,150 branches (93%) were participating in the linkage programme at the end of 31 March 2009. On an average, a branch of a bank in Andhra Pradesh has around 118 SHG accounts. The SHG share of the banks in the state varies from 7% to 30% of the total outstanding loans of the respective banks.\(^{47}\)

**POSITIVE IMPACT OF MICROFINANCE:**

1. **Increased Savings:** SHGs helped to generate and collect small savings from rural women who were hitherto considered incapable of having any capacity to save. The regular savings, though they were small, provided a fund for rural poor women to fall back on when in need otherwise they were depending on handouts from others. The SHGs inculcated the habit of regular savings among poor women.

2. **Access to Credit:** The SHGs have extended the credit facility to the needy women / households who have no assets to pledge. The system of group guarantee combined with individual responsibility is the innovation that has enabled the credit to be expanded to millions of poor and ‘assetless’ women across India. The SHGs have to facilitate the rural women to fulfill their credit requirements both meeting emergent consumption needs as well as small production requirements. This has been achieved without requirements of collateral, complex loan and at a low transaction cost.

3. **Regular Repayment of Loans:** The SHGs have been able to build social collateral and peer pressure to ensure that payments come on time. Non-Performing Assets (NPAs) are a non-issue in SHGs-bank linkage programme. The SHGs have been successful in building an impersonal market relation between financial intermediaries and the clients by breaking the earlier patron-client relation. The ethic of repayment of SHGs has radiated beyond that circle in the economy as there has been an improvement in overall loan recovery of commercial bank branch in areas where SHGs have been functioning. They had large NPAs, mainly out of government’s poverty alleviation programmes. But with the spread of SHGs even these NPAs are reported to have come down by as much as 80%.

4. **Choice of Appropriate Avocations:** The selection of the productive activities by the borrower is as per their own choice and hence the rate of success among SHGs members is very high. This is, perhaps, the main reason for cent per cent repayment of loan and also increase in their living standards.

5. **Commercialization of Economic Life:** In order to earn money the members of SHGs have to necessarily increase commercial production. What was formerly produced for domestic consumption as gifts now began production for marketing after forming the SHGs. The system of loans and repayment invariably encourages production on commercial principle. This has resulted in the growth of market and development of the spirit of capitalism.

6. **Secular Capitalistic Ethic:** The SHG is formed mostly among the women of same religion and intercaste people. The successful SHGs are found among Muslims, Hindus, Christians and Buddhists. Besides, microcredit with its strict discipline of saving and repayments represents a much-needed shift from
patron client relation to impersonal market relation of capitalization. The changed economic climate in the country has articulated new gender relations. Today women are more honored and respected when they are earning income than when they were in seclusion or engaged in household chores.

7. **Changed Life Styles:** The long standing SHGs brought attitudinal changes among their members. By making their activities commercial, the SHGs created a sense of purpose and productive partners among members. They are trained in discharging group responsibilities. Though majority of them are illiterate they have learnt keeping accounts. The SHGs imbibed in them the sense of democratic spirit and secular approach. These attitudinal changes of women have brought perceptible changes in social, cultural and political life of the rural folk.

**PROBLEMS AND STRATEGIES OF MICROFINANCE:**

Although there is a remarkable success in SHGs microfinancing, the movement has its own constraints too.

1. **Small Scale Operation:** The SHGs collect savings and advance loan of a meager amount. As on March 2002 the advances of SHGs formed only 0.15% of outstanding priority sector loans and 0.5% of accounts of schedule commercial banks. There is a need for upscale their activities. The performance of SHGs cannot be measured primarily in terms of the repayment rate continuity and sustainability. The upscaling of their issues like efficiency, productivity, opportunity and cost of using the financial resources is necessary.
2. **Winners and Losers:** The success of a woman is judged by her conformity to norms of SHGs – viz. regular savings, timely repayment, work to earn income, the ability control the household and particularly the husband’s expenditure. This being the case there are many women who may be called as winners and also some women who are losers. Some women are not able to repay their loans and make regular savings. There are instances of women who borrowed at high rates of interest from moneylenders in order to keep up with their SHGs repayment commitments.

3. **Lack of Sustainability and Self Sufficiency:** The majority of the SHGs are too small; scale of their business is not viable as the members are very poor. The groups, which were found to be self-sufficient and sustainable usually, were formed by the rich among the poor people, who clustered just above the poverty line. Hence there is a trade-off between sustainability and heading the poorest of the poor.

4. **No Security:** The SHGs work on mutual trust and confidence of the members. The deposits of the SHGs are not secured and safe. The SHGs are not allowed to accept deposits from non-members. There is no statutory redressal mechanism to resolve disputes.

5. **Poor Impact on Income and Employment:** The SHGs are successful in imbibing banking habits among their members. But the impact of micro financing on the income, employment and levels of living of their members is marginal. Many of them are not able to cross the poverty line. It requires an additional injection of investments.\(^\text{48}\)

6. **Coercive Collection Practices:** The set of accusations that received the most prominence however related to coercive collective practices, leading to borrowers having to “abscond”, or migrate out of the village, and even in some cases, allegedly, commit suicide. The base suicide rate in AP is 14 per 1,00,000.49

7. **Over lending:** One of the criticisms of rural banking, both commercial and cooperative, has been the problem of overdues. While there is no large-scale study of overdues in independent microcredit agencies, two recent analyses published by the RBI, permit some observations on the issues of overdues in microcredit-oriented organizations.50

8. **Lack of Contact and Communication:** A final underlying cause was that the MFIs, in their self-absorption with growth at the cost of other objectives, underestimated the degree to which they were antagonizing several powerful players in the local political economy. Among these were informal lenders such as, reportedly, chit fund organizers, and local girigiri bankers, politicians who were embarrassed by the fact that the MFIs were disbursing much more money in their constituencies than they could lay their hands on themselves through their constituency funds, some bureaucrats who felt uncomfortable about anything major happening in their district, even if it was good, without their ‘blessings’, or at least their knowledge. Even retail traders of consumer durables are said to have felt threatened by the fact that Spandana had earlier set up a consumer store so as to be able to purchase goods in bulk and enable borrowers to benefit from lower prices using vouchers they had the option to

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accept instead of cash loans. And finally of course there were a number of highly discontented borrowers, as noted above, some of who were championed by local politicians. This powerful combination of interests may explain the lack of public support when the crisis hit.\textsuperscript{51}

The following are some of the problems faced by the microfinance industry at present:

- high cost of funds and financing – the cost of fund problem;
- marketing (disbursement and collection) of credit services by the MFIs – high cost of information;
- high cost of operations – operational inefficiency,
- inefficiency in information sharing as organizations fail to communicate with one another leading to high risk and vulnerability of the indebtedness,
- effect of strategies of MFIs: forcing growth neglecting long-term effects,
- unavailability of formal banking and other financial infrastructure;
- lack of physical infrastructure in rural areas which can promote more and innovative profitable ventures,
- lack of marketing facility for rural products;
- competition between subsidized government and private credit;
- lack of social security networks;
- lack of proper regulatory mechanism;
- low levels of technical expertise and entrepreneurial knowledge; and
- credit for non-productive and consumption purposes.\textsuperscript{52}

PROBLEMS OF THE MICRO FINANCE INSTITUTIONS (MFIs):

Among the problems being faced by the MFIs the most constraining is the lack of appropriate legal form and entity. Although NGOs have been largely responsible for the expansion of microfinance services their legal form does not make them the most appropriate type of agency to carry out microfinance on a long-term sustainable basis. Operating as an MFI, an NGO has the following problems associated with its inappropriate legal status:

- More than 90 per cent of the retail providers of microfinance services are established under the Societies Registration Act, 1860 that provides for the performance of activities of a charitable nature. Current banking operations are not clearly specified in the Act as permissible functions. If they earn a substantial part of their income from lending activities, they may violate section 11 (4) of the Income Tax Act and lose their charitable status under section 12 of the Act.

- NGOs do not have the appropriate financial structure for carrying out microfinance activities. Since they are mainly registered as societies or trusts, they are unable to have any equity capital. This in turn, implies that they find it difficult to be ‘capital adequate’.

- An alternative for an NGO-MFI is to become a ‘for-profit’ concern. In the long run, the primary source of on-lending funds for MFIs is the deposits from its members. Till that stage, the MFI has to rely on borrowings. However, to be able to attract borrowings, the MFI needs to have adequate capital base.

- In most states, with the exception of Andhra Pradesh, Maharashtra and Gujarat, cooperatives do not have a satisfactory track record of sustainable credit operations for the poor. They may thus not be an appropriate form of incorporation as MFI.
Alternatively, MFIs can be incorporated as a company and then become a Non-Banking Financial Companies (NBFC) or a Bank. Registration as an NBFC and incorporation as a Bank is difficult as the entry norms are too stringent. However, for MFIs registered under section 25 of the Companies Act, 1956 and not accepting public deposits, the RBI, in its recent announcements, has exempted them from the purview of section 45-IA (registration), 45-IB (maintenance of liquid assets) and 45-IC (transfer of profits to Reserve Fund) of the RBI Act. Although this is a welcome step, restricting the registration of these NBFC MFIs under section 25 would imply non-distribution of profits and would thereby act as a deterrent in attracting private capital.

**Interest Rate Violations:** Even though most of the MFIs are charging low interest rates, there is a growing trend among them that they would set their interest rates in a manner so as to cover their operating costs in due course. As a result, some of them have been charging market driven interest rates and have shown improvement in their self-sufficiency levels. But the fact remains that most of them are incorporated as either Trusts or Societies. And although the RBI has, of late, deregulated the interest rates, these MFIs face two potential problems, viz., (i) they could end up violating the Usurious Loans Act or State Level Money Lending Act, (ii) they could attract the attention of local Income Tax authorities, who may withdraw exemptions given to them under section 12A of the Income Tax Act.

In order to avoid infringement of the law with regard to the Usurious Loans Act and the State Level Money Lending Act, many MFIs are already using innovative pricing of their financial products.
Lack of proper Governance and Accountability: NGOs are also lacking in two important areas viz. governance and accountability – lack of organizational culture internal systems to function effectively and to function as financial intermediaries on a commercial basis. Proper governance structure for business decision making and monitoring at the top level is generally lacking and the leadership of most of these organizations is drawn from the field of development. Managing an efficient microcredit programme requires knowledge of financial management and efficient information systems.

Lack of Commercial Orientation: With their underlying social orientations, many NGOs strive to make credit available to the poor at low cost through accessing grants and subsidized funds. Thus, most of these MFIs achieve a lot of success in their programmes in the initial periods but fail to maintain the same record in the long run because of the lack of commercial orientation thus making it difficult to scale up operations on a sustainable basis.

Sustainability Constraints: The long-term prospects of the microfinance sector depend on MFIs being able to achieve operational and financial sustainability. The constraints and challenges vary with the different types and development stage of MFIs. Most MFIs are currently operating below operational viability and use grant funds from donors for financing upfront costs of establishing new groups and covering initial losses incurred until the lending volume builds. They are generally constrained in achieving sustainability level due to a narrow client and product base, not-so-realistic interest rates and expensive delivery mechanisms.
The key factors which determine the viability and sustainability of microfinance operations are:

- **Volume of lending**: Viability has been demonstrated to improve as the share expands. It is estimated that a loan outstanding of around Rs. 100-250 million is required for a typical MFI to be financially viable.

- **Larger unit loan sizes**: MFIs, which emphasize repeat lending involving larger loan sizes, tend to move faster along the viability continuum compared to those which emphasize increasing outreach to new members. Moving towards a larger unit size loan can result in widening the client base to include borrowers who are to absorb larger amounts of credit by promoting a process, which enables borrowers to gradually progress to larger loans.

- **Pursuing a commercial outlook which countenances charging cost covering interest rates**: Many NGOs / MFIs fail on this score.

- **Reducing credit delivery costs**, through promoting community-based organizations and other innovative and cost-effective systems.

- **By providing a range of products and services**, which meet the requirements of different segments of customers, the MFIs become responsive to client needs and which enable the MFI to create niche in the markets and attract client loyalty.

- **Achieving high recovery rates and reducing risks.**

(i) **Financial Viability:**

MFIs operating on a small scale face financial problems. Meeting administrative overheads and generating surpluses for expansion out of the spread between their interest income and the interest they pay on the bank finance may become difficult. The average borrowing costs coupled with high operating expenses ranging between 4 to 19 per cent impede MFIs’ ability to offer competitive rates to

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the customer-beneficiaries. As against this, public sector banks lend directly to SHGs at interest rates varying between 9 to 12 per cent.

(ii) **Capacity Building of the SHGs:**

Training and strengthening the groups, improving their accounting, increasing their monthly savings to enable them to avail larger loans in successive rounds of borrowing, providing marketing facilities and infrastructural facilities to the products they manufacture are huge challenges before the MFIs.

(iii) **High entry capital requirements:**

MFIs can raise Rs. 2 crore capitals required to become a Micro-Finance Non-Banking Financial Companies. There is a proposal from SADHAN, a network of microfinance institutions that a new microfinance Act be enacted permitting the creation of a joint-stock for profit entity with an initial capital requirement of only Rs. 25 lakh and which will be allowed to raise deposits from the public.  

**NEED FOR THE STUDY:**

Notwithstanding the progress made over the decades, majority of the rural population still does not appear to have access to finance from a formal source, according to the Rural Financial Access Survey (RFAS) 2003. Some 59 per cent of rural households do not have a deposit account and 79 per cent of rural households have no access to credit from a formal source. The problem of access is even more severe for poorer households in rural areas.

Indeed, bank branches in rural areas appear to serve primarily the needs of richer borrowers. Some 66 per cent of large farmers have a deposit account; 44 per cent have access to credit, meanwhile, 70 per cent of marginal farmers do not have a bank account and 87 per cent have no access to credit from a formal source.

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Presently, the microfinance scenario needs to be reviewed for emerging trends, concerns and growth prospect. Since its humble start in the late 1980s, the SHG-bank linkage movement had taken off in 1992 and is today the largest in the world. As per current growth rates, by 31 March 2007, NABARD aims at linking 2.5 million SHGs involving 325 million poor households with the help of 5,000 NGOs and 1,000 microfinance institutions. It is interesting to note that as per government estimates, 25 per cent of the world’s 100 million poor are in India. There will be a tremendous demand for quality NGOs and microfinance institutions in India in the next few years.

The poverty-alleviation and government sponsored schemes in banks have problems in implementation, more with NPAs than the other schemes. Thus, the rural banking institutions are out of step with the changing rural credit requirements and are unable to come up with systems and credit / savings instruments as required by the rural clientele.55

Under these discomforting and pathetic conditions, that the rural poor were facing, microfinance activity has come into force as the saviour to redeem them from the clutches of the poverty and unemployment. However, the question that how best this Micro finance programme has been really benefiting the beneficiaries still remains to be examined. The present study under reference is one such an attempt to assay the performance of the SHG network of the microfinancing programme in terms of its generation of income and employment of the beneficiaries in the sample district in Andhra Pradesh state.

ORGANIZATION OF THE STUDY:

1. The first chapter deals with the introduction.
2. The second chapter deals with the objectives, methodology and review of literature of the study.
3. The third chapter studies the profile of the study area and the sample respondents.
4. The fourth chapter assesses the contribution of various financial institutions in support of microfinance in India.
5. The fifth chapter evaluates the impact of Microfinance on the income and employment generation of the respondents under both Govt. SHGs and MFI SHGs in the study area.
6. The sixth chapter assesses the performance of the loan amounts sanctioned, actual utilization of the amounts sanctioned and repayment of loans by the respondents under both Govt. SHGs and MFI SHGs in the study area.
7. The seventh chapter elicits the views and opinions of the sample beneficiaries with regard to the role and working of the SHGs and the problems being faced by the respondents under both Govt. SHGs and MFI SHGs in the study area.
8. Finally findings, conclusions and suggestions are presented in the eighth chapter.