CHAPTER I

INTRODUCTION AND DESIGN OF THE STUDY

The term ‘Micro’ relates to the size of financial transactions. Micro Finance is the provision of financial services to the poor people like providing small amount of credit and collect tiny amount of savings. Microfinance can be defined as any activity that includes the provision of financial services such as credit, savings, and insurance to low income individuals which fall just above the nationally defined poverty line, with the goal of creating social value. The creation of social value includes poverty alleviation and the broader impact of improving livelihood opportunities through the provision of capital for micro enterprise, and insurance and savings for risk mitigation and consumption smoothing. After the institution of social control in banks and their nationalization, a big thrust was given on provision of credit to the weaker sections by commercial banks while Regional Rural Banks were established to provide credit exclusively to the poor. The policies concerning rural credit through the banking system were hitherto pursued on certain assumptions such as, (i) the rural poor have no capacity to save, (ii) could only be developed through subsidy linked poverty alleviation credit programmes, and (iii) interest rates of credit from informal sources were exploitative, etc.

This chapter deals with the concept, structure and details of Micro Finance, Self Help Group (SHG) and SHG – Bank Linkage Programme such as definition, objectives, approaches, models, products and services offered, trends, progress and its challenges. The chapter also covers the statement of the problem, the objectives, the null hypotheses, the significance and the limitations of the study.
The above policy framework often resulted in excessive target orientation selection of clients and projects and leakages. Poor interest margins practically forced banks to cut down on appraisal and monitoring costs which further resulted in low recoveries. The main constraint with regard to flow of credit to asset less poor borrowers, therefore, seems to be the comparatively high transaction cost to the banks in financing a large number of small borrowers who require credit frequently and in small quantities. The poor also often perceive banks as alien institutions which exist to serve the needs of others.

1.1 MICRO FINANCE

The task force on Micro Finance constituted by NABARD suggested a working definition of micro-finance as “provision of thrift, credit and other financial services and products of very small amounts to the poor to enable them to raise their income and improve their living standards”. The upper limit of amount is fixed at Rs. 25,000 to be categorized as micro-finance.

Rutherford Stuart (2000) defined “Micro Finance” as “the means by which poor people convert small sums of money into large lump sums”.

Microfinance originally established to impel the moneylender out of business and to bridge the capital gap apparently unfilled by the rural co-operatives and commercial banks. It is a collection of banking practice built to provide small loans and accepting tiny saving deposits. Microfinance address one constraints faced by the poor, that is, shortage of capital. Capital investment from savings or borrowing, takes an important place for everyone, regardless of their income. Microfinance performs the service of time shifting; borrow money today to

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1 Rutherford, Stuart. (2000) "The Poor and Their Money". Oxford University Press, Delhi,
solve today’s problem and paying the money back in future, or saving money today for an event in the future.

According to Otero, Maria (1999)², “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 organization building, promoting democratic systems, and strengthening human rights; enables people to move out of poverty. Microfinance enables poor self-employed people to create productive capital, to protect the capital they have, to deal with risk, and to avoid the destruction of capital. It attempts to build assets and create wealth among people who lack them. For the very poor, microfinance becomes a liquidity tool that helps smooth their consumption patterns and to reduce their level of vulnerability”. Microfinance is a logical approach to development because it functions at the grassroots level, can be sustainable, is capable of involving large segments of the population, and builds both human and productive capacity.

Robinson (2001)³ defines microfinance as “small-scale financial services primarily credit and savings provided to people who farm, fish or herd” and adds that it “refers to all types of financial services provided to low-income households and enterprises”.

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² Otero, Maria (1999) Binging Back Development in Microfinance, Journal of Microfinance, Volume 1, number 1,
CGAP (2003)\(^4\) define microfinance as “a credit methodology that employs effective collateral substitutes to deliver and recover short-term, working capital loans to micro entrepreneurs”.

Microfinance is the provision of a broad range of financial services to low income micro enterprises and households. The range of financial services usually includes savings, loans, insurance, leasing, and money transfers. On the other hand, Micro credit emphasizes on providing credit to low income clients. Micro credit is often associated with an insufficient appreciation of the value of savings services to the poor. Microfinance models usually refer to the products and services provided as the method in which they are provided. Internationally, the most well known microfinance models include the Grameen Bank model, community owned village banks, savings and loan associations and self help groups.

The informal nature of microfinance, uncontrolled by governments and donors, allowed the MFOs to freely innovate. The MFOs themselves designed innovations that enabled them to reduce lending costs and risks and serve poor clients without the collateral normally required.

- Small loans mostly for working capital for short periods, sometimes only a few weeks, with frequent repayments;
- Incentives for good repayment, primarily guaranteed access to repeat (and sometimes larger) loans;
- High real interest rates, sufficient to cover costs;

Large loan portfolios per loan officer, frequently 75 to 100 groups or
100 to 500 borrowers, with financial incentives for efficiency and
good loan portfolio performance;

Little or no collateral, with solidarity group guarantees or assets with
high personal use value as collateral;

Decentralized and simple lending procedures and close client
supervision; and

High loan repayment rates, often more than 95 per cent”

OBJECTIVE OF MICRO FINANCE

Microfinance program is typically viewed as an economic development
strategy, where disadvantage groups basically not benefited from involvement with
the formal economic activities. MFO are designed to improve access of the rural
poor to financial services, make them bankable clients and promote savings
mobilization among them.

The primary objective of MFO following welfarist approach is to alleviate
poverty. According to a supporter of welfarist approach, Doocy (2005) mentioned
that, “the primary goal of most microfinance institutes is improving the economic
status of poorest segment of the population, most service provider aim for a broader
impact of enhanced well being”

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microfinance program and management actions to improve services”. Journal of
Microfinance 7(1):70
Satish (2001) mentioned that, “the primary goal of most MFO is improving the economic status of poorer segments of the population, most service providers aim for a broader impact of enhanced well-being. Because households function as social and economic units, micro enterprise programs have a unique opportunity to impact the economic, social, and general well-being of households”

On the other hand, Institutionalist proponents argue that the primary objective of microfinance is financial deepening, the creation of a separate system of sustainable financial intermediation for the poor. Outreach, also known as Poverty Outreach, refers to how well a MFO can reach or being able to provide financial services to the poor or the poorest of the poor.

Schreiner (1999) proposed a framework for outreach in term of six aspects, namely Worth to clients, Cost to clients, Depth of outreach, Length of outreach, Scope of outreach. The most important aspect of Schreiner’s framework is Depth of outreach and Breadth of outreach. Depth of outreach according to Schreiner (1999) “is the value that society attaches to the net gain of a given client. In welfare theory, depth is the weight of a client in the social-welfare function. If society has a preference for the poor, then poverty is a good proxy for depth. For example, society likely prefers that a street child or a widow get a given net gain than that a richer person get the same net gain” Schreiner (1999) mentioned that the “Breadth of outreach is the number of clients. Breadth matters because of budget constraints; the wants and needs of the poor exceed the resources earmarked for

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them. All else constant, the breadth of the poverty approach depends on the level of
donations that it can attract”. In short, depth is the level of poverty outreach and the
breadth is the number of clients. Because of the difficulties to measure and compare
the depth of outreach in different countries, breadth or the number of poor/clients,
are often used in most of the literature and reports to indicate the outreach of
microfinance program.

The last topic of microfinance triangle is “Impact”, which is concerned
with what kind of impact MFO have in their clients, their micro enterprise, their
household and their community. The objective of Institutionalist is to achieve
financial sufficiency. To achieve financial sufficiency, they have to lend more and to
do that, MFO have two options, they can increase loan size and/or they can increase
breadth of outreach. When MFO increase minimum loan size, they will ultimately
create a barrier for the poorest clients which will reduce depth of outreach. The
available alternative for the Institutionalist is to increase breadth or in other word,
increase number of clients. Now, poor people will participate more when there is a
significant positive impact. So for Institutionalist MFO to achieve their primary
objective, they have to increase the number of clients as designing product and
delivery method in a way that will increase the impact.

On the other side, the primary objective of welfarist is to alleviate poverty,
that is increase the economic and socio economic impact of their product and
services on a significant number of poor. To reach the significant number of poor,
providing financial services to them and to continue this service, it is very important
for welfarist MFO to achieve financial sufficiency.

Though the objectives of two approaches are different, but to achieve their
objective, MFO must have to achieve other two issues mentioned on the
microfinance triangle. The most common objective for both approaches will be “improve the economic and socio-economic impact of microfinance on a significant number of poor in a way that leads to financial sufficiency”

**APPROACHES OF MICRO FINANCE**

The concept of Microfinance was influenced by two major schools; the Institutionalist school and the Welfarist school. Institutionalist school focuses on developing a financially sustainable institution in order to serve the poor. The issue of providing financial services to poor is the basic foundation of this approach. In this approach, numerous large scale, profit seeking MFOs that provides high quality financial services to the large number of poor. The Institutionalist position is expressed in nearly all literature published by World Bank, CGAP, USAID, ACCION International and Ohio State Universities Rural Finance Program (Dingue, 2005).

Believers of Institutionalist approach are opposed to the idea of dependency on subsidiaries because earlier attempts on poverty alleviation through subsidiaries credit by development agencies, Non Government Organization (NGO) and the governments of developing countries failed. The reason behind this failure includes; high cost of transactions, lack of assets for poor house holds, institutions lacking in saving mobilization and high level of corruption. The impact was so insignificant and that leads the dried up donor fund. The failure of past subsidized program leads the core arguments of Institutionalist thought; includes,

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• Lower income households desire access to credit, not cheap credit.

• Only financially sustainable programs can have significant impact on poverty alleviation.

• Subsidized programs are inefficient and often end up in the hand of non poor.

According to Institutionalist, a significant impact on poverty can be achieved only if MFOs are financially self-sufficient and independent from any subsidize funding from donor or government.

On the other hand, Welfarist approach focuses on immediate improvement of economic safety for the poor. They focused on providing financial services to the poorest of the poor at subsidized interest rate. MFOs that fall under this approach are heavily reliant on government subsidy and grants as donor commitments. Saving mobilization is not a part of the lending process in this approach. Though they understand and aware of the long term sustainability of MFO is very important, they do not agree that avoiding donor subsidiaries completely will be required to achieve that state. Example of MFO operate under Institutionalist approach includes Grameen Bank Bangladesh, FINCA in Latin America, and most of MFOs in Africa and Asia.

Woller and Woodworth (2001)\(^9\), as cited from Fatukasi, 2005, explained the difference of two approaches in three different ways. First, the difference in service delivery methods of MFOs includes individual verses group based. Second is the difference in Institutional structures; with or without donor fund. Third is the

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difference in population segment. When MFO focus on financial sustainability, the poorest of the poor might become neglected.

According to Dingue (2005), Microfinance is both a development instrument and a business instrument and its success is judged by whether financial services alleviate poverty over time.

1.1.1 Micro Finance in India

Microfinance in India has achieved tremendous growth in the last ten years, due to the progress of the Self Help Group-Bank linkage model and of Micro Finance Institutions (MFIs) using various Grameen Banks. In India, Institutional Credit agencies (banks) made an entry in rural areas initially to provide an alternative to the rural money lenders who provided credit support, but not without exploiting the rural poor. There are three main Factors that count to the bringing up of Microfinance as a Policy in India.

The first of these pivotal events was Indira Gandhi’s Bank Nationalization drive launched in 1969 which required commercial banks to open rural branches, resulting in a 15.2% increase in rural bank branches in India between 1973 and 1985. Today, India has over 32,000 rural branches of commercial banks and regional rural banks, 14,000 co-operative bank branches.

The second national policy that has had a significant impact on the evolution of India’s banking and financial system is the Integrated Rural Development Program (IRDP) introduced in 1978 and designed to be ‘a direct instrument for attacking India’s rural poverty’. This program is interesting to this study because it was a large program whose main thrust was to alleviate poverty through the provision of loans and it was considered a failure.
The last major event which impacted the financial and banking system in India was the liberalization of India’s financial system in the 1990s characterized by a series of structural adjustments and financial policy reforms initiated by the Reserve Bank of India (RBI).

The systems and procedures of banking institutions were emphasizing on complicated qualifying requirements, tangible, collateral, margin, etc., that resulted in a large section of the rural poor shying away from the formal banking sector. The banks too experienced that the rapid expansion of branch network was not contributing to an increasing volume of business to meet high transaction costs and risk provisioning, which even threatened the viability of banking institutions and sustainability of their operations. At the same time, it was not possible for them to allow a population of close to 300 million - even if poor - to remain outside the fold of its business. The search for an alternative mechanism for catering to the financial service needs of the poor was thus becoming imperative.

In India, a variety of micro finance schemes and various approaches have been practiced by both Governmental and Non Governmental Organizations. There are examples of spectacular success and there are also examples of not-so-successful programs which experienced high default rates and are unable to provide financial assistance in the long run. Ultimately, the aim is to empower the poor and encourage them into development.

Variety of micro finance organizations in government as in non government sector exists in India. Leading financial institutions like, the National Bank for Agriculture and Rural Development (NABARD), the Small Industries Development Bank of India (SIDBI) and the Rashtriya Mahila Kosh (RMK) have played a significant role in making micro credit a real movement in India. The size
and types of implementing organizations range from very small to moderately big involved in financing and savings activities for individuals and groups. These groups also adopt a variety of approaches. However, most of these organizations tend to operate within a limited geographical area. There are a few exceptions like Professional Assistance for Development Action (PRADAN), International Centre for Entrepreneurship and Career Development (ICECD), Mysore Resettlement and Development Agency (MYRADA), Self Employed Women’s Association (SEWA) which have been successful in replicating their experiences in other parts of the country and act as resource organizations. Also, many organizations have been involved with SHGs in not only providing credit, but for other purposes like watershed, agriculture also.

Micro Finance interventions can be identified based on their span of activity, source of funds, route through which it reaches the poor or the coverage. However, it seems that one of the most common practices and approaches is providing credit through Self Help Groups. The approach is to make SHGs the main focal point to channelise all credit to members. Almost, all national funding organizations (NABARD, RMK) as other Government organizations advocate forming of SHGs and providing or linking with credit. However, many organizations provide individual finance directly also exist.

**Micro Finance: A paradigm shift in the process for poverty alleviation**

The Indian policy makers’ consistent strive for combat against poverty is barely a new phenomenon every time resulted into the commencement of economic reforms with human values reflects the then finance minister Mr.P.Chidambaram’s support towards microfinance is not at all unexpected. Poverty alleviation being the
prime most criteria for the Indian government, the policy makers are consistently in the process to find out most suitable way to deal with this situation.

Averaging 5.7 per cent per year the Indian economy has steadily increased since 1979. The growth rate of above 8 per cent was achieved by the Indian economy during the year 2003-04 and had maintained the estimated growth rate of around 8 per cent for 2004-05, and has maintained the growth rate well above 8 per cent attaining the level of growth of even beyond 9 per cent for 2006-07. In fact, the Indian economy has posted an excellent average GDP growth of 6.8% since 1994. Even though it has maintained the faster level of growth during these years it has failed to deal with poverty alleviation effectively and efficiently. Even today around 35% of total population of 1.2 billion are still living under the earning of Rs.47 per day and around 80.5% of people live under Rs.94 per day. As per the 60th round of the National sample Survey Organization, during January-June 2004, the unemployment rate for males was 9 per cent (up from 5.6 per cent in 1993-94) in the rural areas and at 8.1 per cent (up from 6.7 per cent in 1993-94) in the urban areas. During the same period, the corresponding figures for females were 9.3 per cent (up from 5.6 per cent) in the rural areas and 11.7 per cent (up from 10 per cent) in the urban areas. The country has touched the level of unemployment well beyond 7 per cent for the year 2006.

During 1974-2000, there was a substantial uniform decrease in poverty across rural and urban areas took place that is the percentage of the population living below the poverty line fell from 55 per cent to 26 per cent. The provisional data of the latest National Sample Survey (NSS) 61st round for the year 2004-05 indicate that the poverty ratio at the national level was 27.8 per cent if the Uniform Recall period (URP) is used and about 22 per cent if the Mixed Recall Period (MRP) is used. To accelerate the reduction in poverty and increase in employment, a number
of poverty alleviation, employment generation and basic services programmes are being implemented. They are as follows:

1. Pradhan Mantri Gram Sadak Yojana.
2. Indira Awas Yojana
3. Swarnjayanti Gram Swarojgar Yojana
4. Sampoorna Grammen Rozgar Yojana
5. DPAP, Dap and IWDP (Drought Prone Areas Programme, Desert Development Programme and Integrated Wasteland Development Programme)
6. Swarna Jayanti Shahari Rozgar Yojana
7. Valmiki Ambedkar Awas Yojana
8. Jawaharlal Nehru National Urban Renewal Mission
9. National Rural Employment Guarantee Scheme

The then Finance Minister P.Chidambaram in Parliament on February 28, 2008 introduced India’s Budget 2008-09 that built on the poverty reduction and social sector schemes begun in the previous year, and added some new ones. Key provisions aimed at reducing poverty and improving the quality of life of the poor are:

1. Bharat Nirman allocation enhanced.
2. More Schools, teachers for Sarva Shiksha Abhiyan
3. Enhanced allocation for midday meal scheme
4. Expansion of Rajiv Gandhi Drinking Water Mission
5. Increase in outlay for Rural Sanitation Campaign
6. Emphasis on supplementary nutrition in Integrated Child Development Services scheme

7. National Rural Health Mission begins work

8. National Rural Employment Guarantee Scheme started

9. Grant for Jawaharlal Nehru National Urban Renewal Mission

10. Pensions increased in National Social Assistance Programme

11. Gender budgeting coverage increases

12. More funds, schemes for scheduled castes/tribes

13. Educational, vocational support for minorities

14. Increased coverage of Kasturba Gandhi Balika Vidyalaya Scheme

15. Increased outlay for irrigation

16. New credit schemes for farmers

17. Microfinance: self-help group (SHG) schemes to be expanded.

The 2008-09 union budget of India for the first time formally accepted the contribution of Microfinance in the procession to alleviate poverty. In specific to Microfinance, the then Finance Minister Mr.P.Chidambaram has opted for a bill to promote, develop and regulate the micro-finance sector in India. In short period of time, 801,000 self-help groups (SHGs) have been linked to credit; banks will link another 385,000 SHGs. A committee will be appointed to suggest a plan to ensure that every household that requires credit gets it.

1.1.2 **Micro Finance Organizations (MFO)**

According to Dr. Yunus, “MFOs are just like any other banks, but doing a completely different kind of job with a very different methodology. Once
governments create the legal framework for microcredit banks, and setup regulatory commissions to supervise them, they can run like any other business enterprises”

MFOs typically offer a variety of loan products and savings services. MFOs are becoming financially viable, moving toward self sustainability, and essential to the communities in which they operate. They have the potential to attract more resources and expand services to clients. The ability of most MFOs to leverage capital and manage external sources is generally limited. To support outreach to poor clients, donated resources are generally leveraged and augmented by borrowing from formal financial institutions or large institutional and individual investors, or accepting limited deposits from the public.

Ownership of microfinance organizations can be many types, such as: Owned by Private investors, owned by borrower themselves, Owned by borrower and Private Investors, Owned by Non Government Organizations (NGO) and Co-operatives.

**Structure of Micro Finance Institutions**

A Micro Finance Institution from the structural point of view can be a trust, registered society, co-operative society, company registered under section 25 of Companies Act, 1956 (not for Profit Company), NBFC or Local Area Bank (LAB), Grameen bank etc. But in India trusts and societies constitutes the vast majority of Micro Finance Institutions. Conversion into a NBFC or LAB gives MFI greater credibility as it brings the Micro Finance Institution under the purview of Reserve Bank of India. Besides, this Micro Finance Institutions as corporate entity are allowed to access the capital markets for generation of funds, have given them an option to solely not depend upon the bank lending, grants or donations. Apart from the
above sources, the MFIs are also allowed to raise savings from the member-borrowers. A Micro Finance Institution may lend to individual beneficiaries, or to partner NGOs or to Self Help Groups (SHGs) or allocate funds among these different categories of borrowers.

**Widespread Product and Services offered by MFO**

A wide range of financial services offered by microfinance to the poor includes; group credit, individual credit, savings, micro insurance and micro leasing. Lending are the most commonly associated in people mind with microfinance revolution. Lending come in two major types: group and individual lending.

In Group lending, which practiced by the followers of welfarist approach, borrowers are asked to form group of three to seven members, most commonly five. Borrowers in a group are jointly liable for all loans taken out; meaning that everyone in the group are liable for other loans and any one of them can be held responsible for an outstanding loan. In the classic Grameen model, payments begin immediately after giving the loan, are due weekly, and are constant over the life of the loan. When a loan is repaid on time, the borrower becomes eligible for a larger loan as all group members are in good standing and approve the individual loan requests. In the classic model, eight solidarity groups are joined together into a larger group called “center” which gathers each week with a loan officer to perform all financial transactions. **Roodman and Qureshi (2006)**\(^{10}\) mentioned that “Given members’ superior knowledge of the character and economic circumstances of friends and neighbors, they can do better than the lender at screening out risky borrowers prior to the loan decision and monitoring loan use after”.

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\(^{10}\) Roodman and Uzma Qureshi (2006), “Microfinance as Business -Center for Global Development”. Massachusetts Ave NW Third Floor Washington, DC 20036 United States
Individual lending was followed by most Institutionalist approach followers. It is build around more straight lending relationships with individual clients. But the difference with conventional lending, individual micro lending offers smaller loans and relies less on traditional sources of marketable collateral. It relies more on informal assessments of borrowers character and business operations.

Savings services offered by MFO, help poor people to save actively whenever they can. This savings is often the only way poor can manage to pay for a major life event such as a marriage or funeral, survive a natural disaster, or take advantage of a business opportunity. Poor can save daily, weekly, monthly or whenever they want based on the MFO’s offer. The amount of savings can be fixed or a flexible amount. Savings are the prerequisite to receive loan from many MFO.

According to Ahuja and Jutting (2004)11, “the optimism that accompanies micro insurance stems mainly from two different sources: the success of micro credit programs in improving the conditions of the poor in different parts of the world by enabling them through asset and/or skill formation to generate sustained income; and the growing recognition of the role that risk plays in the lives of the poor and hence the need to increase the ability of the poor to cope with their various risks”. Micro insurance is the provision of insurance to low-income households. Poor people are extremely vulnerable to risk, both in the form of natural calamities as more regular occurrences of illness and accidents. Micro insurance service includes life insurance, health insurance, disability insurance, livestock insurance, crop insurance and unemployment insurance.

Financial leasing is a contractual arrangement between two parties, which allows one party to use an asset owned by the other in exchange for specified periodic payment. Leasing can be of three types, financial leasing, hire purchase and operating lease. Grameen Banks use the financial leasing. Micro leasing services offered mostly individual basis and basically there is no prior list for leasing item. Grameen bank provides micro insurance to those who receive loans at least and have some additional source of income (Dowla, 1998)\textsuperscript{12}.

1.1.3 Challenges of Micro Finance Organization

MFOs are facing triple challenge: they have to provide financial services to the poor (depth and breadth of outreach), they have to cover costs in order to continue their operation (financial sustainability) and they also have to design their product services; and delivery method, in such a way that will improve the impact. All three challenges must therefore be taken into account in order to assess MFOs performance.

Outreach the Poor

Outreach is generally broken down into six aspects: cost, depth, breadth, length, scope and worth. Among the six, Depth is central to the question of the usefulness of microfinance in poverty reduction. Depth is defines as clients’ poverty level or the percentage of poor reached. Whether microfinance is capable of reaching the poorest of the poor is one of the most hotly debated topics in microfinance at present. The heart of this debate is whether microfinance should be targeted exclusively at the very poor, or whether it has a wider financial system function.

Breadth of outreach is the number of clients served. Breadth is important because it is also related to sustainability of MFOs. Length of outreach is the timeframe of the supply of microfinance. Length is difficult to measure, but profit is a proxy because it signals the ability to sustain the business over time. Scope of outreach is the number of types of financial contracts supplied. Scope depends on market opportunities, available resources, management and legal. Scope matters because credit is not the only microfinance service that is of importance to clients. Worth or quality refers to how valuable microfinance services are for particular clients. And cost is a measure of how expensive these services are for the client, including price and transaction costs. The six aspects data are available about Depth and Breadth of outreach.

The Microcredit Summit Campaign Report 2006, mentioned that “as of 31 December, 2005, there are 3,133 microcredit institutions reported reaching 113,161,390 clients, 81,949,036 of whom were among the poorest (in the bottom half of those living below their country’s poverty line or below US$ 1 a day) when they took their first loan. Of these poorest clients, 84.1 per cent or 68,993,017 are women. 847 of these institutions submitted an Institutional Action Plan in 2006. Together these 847 institutions account for 88 per cent of the poorest clients reported. Assuming five persons per family, the 81.9 million poorest clients reached by the end of 2005 affected some 410 million family members”.

Institutional Financial Sufficiency (IFS)

Institutional Financial Sufficiency is essential for a MFO to obtain the large amount of funds required to reach and benefit a significant number poor and
poorest household. **Christen, Rhyne, Vogel & McKeen, (1995)**\(^{13}\) mentioned that IFS reflects an MFO’s “ability to operate at a level of profitability that allows sustained service delivery with minimum or no dependence on donor inputs”.

The most important reason for moving toward IFS is funding. Reducing poverty by reaching a significant numbers of poor and poorest households requires vast amounts of funds. Where MFOs can have vast amount of fund from? Supports from Donor’s funds?

Microfinance are limited, and probably not from governments either. Grants and soft loans have played, and continue to play, major roles in financing MFOs start ups (Gibbons and Meehan, 2000). Grants and soft loans are particularly useful at that early stage when equity is usually nonexistent and deficits are large. Guarantees and quasi-equity are also very important when MFO seeks to establish relations with banks. These soft loans and grants are always limited in supply and time consuming to secure, for that grants and soft loans are likely to be insufficient for financing MFOs to reach significantly large number of poor and IFS. The only formal financial institutions can provide this kind of vast financial resources. Now this profit oriented, formal financial institutes will likely to provide this fund when MFOs can prove their strength on operational and financial management, on other word, level of IFS. According to Gibbons and Meehan (2000), “it is not a question whether or not MFOs need to pursue IFS so as to be able to reduce extreme poverty in a big way, but rather how best to go about it without losing sight of their overriding concern for poverty reduction”.

Gibbons D. Meehan, J., (2000)\textsuperscript{14} defined IFS as the ability of an MFO “to cover all actual operating expenses, as adjustments for inflation and subsidies, with adjusted income generated through its financial services operations”. Inflation adjustments include: (a) to account for the negative impact, or cost of inflation, on the value of equity and (b) to account for the positive impact of the revaluation of non-financial assets and liabilities for the effects of inflation. Similarly, there are two types of subsidies which must be adjusted for (a) explicit subsidies to cover operating expenses, and (b) implicit subsidies to account for loans received by an MFO at below market rates, and in kind donations. These adjustments allow an MFO to understand the potential commercial viability of their financial operations. This is done by comparing adjusted operating income top adjusted operating expenses. When the operating income is greater than operating expenses indicates that MFO has reached IFS.

**Emergence of SHGs**

Muhammad Yunus (1976) of Chittagong University in Bangladesh introduced this popular approach of Self-Help Group (SHG). The concept of ‘Nijeri Kori’ (which means literally ‘we do it ourselves’ or self-help) for poor women to start small business through Grameen Bank was his initial step. Now the bank has more than 1000 branches and 12,000 workers and a saving fund of $32.92 million. The Self-Help Group movement became a silent revolution within a short span in the rural credit delivery system in many parts of the world. It has been documented that nearly 53 developing countries including India, have taken up this on a large scale. Viewing Self-Help Groups as an effective welfare programme in Ninth five year plan (1997-2002) the Indian Government adopted this approach to uplift the

rural poor. National programmes like Support to Training and Employment Programme (STEP), Training Cum-Production Centers (NORAD), Rashtriya Mahila Kosh (RMK), Indira Mahila Yojana (IMY) etc also focus on promoting SHGs.

1.2 SELF-HELP GROUPS

Self Help Group is a group of rural/urban poor who have volunteered to organize themselves into a group for Eradication of poverty of the members. They agree to save regularly and convert their savings into a Common Fund known as the Group corpus. The members of the group agree to use this common fund and such other funds that they may receive as a group through a common management. The group formation will keep in view the following broad guidelines: Generally a self-help group may consist of 10 to 20 persons. Generally all members of the group should belong to families below the poverty line. However, if necessary, a maximum of 20% and in exceptional cases, where essentially required, up to a maximum of 30% of the members in a group may be taken from families marginally above the poverty line living continuously with BPL families and if they are acceptable to the BPL members of the group. This will help the families of occupational groups like agricultural laborers, marginal farmers and artisans marginally above the poverty line, or who may have been excluded from the BPL list to become members of the Self Help Group. However, the APL members will not be eligible for the subsidy under the scheme. The group shall not consist of more than one member from the same family. A person should not be a member of more than one group. The BPL families must actively participate in the management and decision making, which should not ordinarily be entirely in the hands of APL families. Further, APL members of the Self Help Group shall not become office bearers (Group Leader, Assistant Group Leader or Treasurer) of the Group.
The group should devise a code of conduct (Group management norms) to bind itself. This should be in the form of regular meetings (weekly or fortnightly), functioning in a democratic manner, allowing free exchange of views, participation by the members in the decision making process. The group should be able to draw up an agenda for each meeting and take up discussions as per the agenda. The members should build their corpus through regular savings. The group should be able to collect the minimum voluntary saving amount from all the members regularly in the group meetings. The savings so collected will be the group corpus fund.

The group corpus fund should be used to advance loans to the members. The group should develop financial management norms covering the loan sanction procedure, repayment schedule and interest rates. The members in the group meetings should take all the loaning decisions through a participatory decision making process. The group should be able to prioritize the loan applications, fix repayment schedules, fix appropriate rate of interest for the loans advanced and closely monitor the repayment of the loan installments from the loanee. The group should operate a group account preferably in their service area bank branch, so as to deposit the balance amounts left with the groups after disbursing loans to its members.

The group should maintain simple basic records such as Minutes book, Attendance register, Loan ledger, General ledger, Cash book, Bank passbook and individual passbooks. These could be used with necessary changes/ modifications wherever required. It is highly remarkable to point out that Self Help Groups provided effective coping mechanisms and peer pressure acts as the best collateral and high repayment rates of Self Help Groups run through NGOs was not an inherent structural feature of Self Help Groups but a commitment to group values.
Self Help Groups had substantially increased, mobilizing thrift deposits and receiving timely matching and revolving funds to generate employment activities to earn their livelihood. Increasing awareness among rural women about Government development programmes, beneficial change in social outlook of the women, better sense of equality of status of women as participants, decision makers and beneficiaries in the democratic, economic and social spheres of life sensitized the women members to take active part in socio economic progress of rural areas.

1.2.1 Evolution of SHGs – Bank Linkage Programme

Banking industry has exhibited tremendous growth in volume and complexity during the last few decades. Despite making significant improvements in areas relating to financial viability, profitability and competitiveness, there are concerns that banks have not been able to reach and bring vast segment of the population, especially the underprivileged sections of the society, into the fold of formal banking system. Internationally, also efforts are being made to study the causes of financial exclusion and design strategies to ensure the financial inclusion of the poor and disadvantaged.

In the above backdrop, the National Bank for Agriculture and Rural Development (NABARD) initiated a search for alternative policies, systems and procedures, savings and loan products, other complementary services and new delivery mechanisms that would fulfill the requirements of the poorest, especially of the women members of such households. The emphasis was on improving the access of the rural poor to an integrated micro finance services covering both savings and credit rather than providing just micro credit facilities.

Based on study findings of an Action Research Project, the Self Help Group (SHG) – Bank Linkage model was evolved as the core strategy that could be
used by the banking system in India for increasing access of the poor to the formal banking system. The strategy involves forming small, cohesive and participative groups of the poor, encouraging them to pool their savings regularly and using the pooled savings to make small interest bearing loans to members and in the process, learning the nuances of financial discipline. Bank credit follows and does not precede this stage.

The SHG – Bank Linkage Programme was launched by NABARD in 1992, with the policy support of the Reserve Bank of India (RBI), the Central Bank of the country. The programme has been designed and nurtured by NABARD for over 15 years. The pilot phase was followed by the setting up of a Working Group on NGOs and SHGs by the RBI in 1994 which came out with wide ranging recommendations on SHG – Bank Linkage as a potential innovation in the area of banking with the poor. The programme was mainstreamed with Commercial and Cooperative banks in 1996. The main objective of the programme has been financial inclusion by extending outreach to poor households, making available credit services at their doorstep with easy and self managed access to formal financial services on a sustainable basis and in a cost effective manner.

Objectives of SHGs – Bank Linkage Programme

- To build mutual trust and confidence between the bankers and the rural poor.

- To encourage banking with thrift and credit, in a segment of the population that the formal financial institutions usually find it difficult to reach and serve.
• To evolve supplement credit strategies for meeting the credit needs of the poor with the strength of technical and administrative capacities and financial resources of the formal financial institutions.

1.2.2 Success of SHGs – Bank Linkage Programme

There exists massive potential of the Linkage of SHGs with banks and expects the banking system to take a prompt lesson from the success of the SHG Linkage. There is the need to provide required space for the rural bank branches and MFIs have to work sustainably for making the microfinance success, a driving force in the process to poverty reduction in India. The linkage of SHGs with bank branches has numerous advantages both for the banks and SHGs. In the first case, the recovery performance of the loans through MFIs or SHGs has been found to be highly satisfactory at near 100 per cent as against 50 to 60 per cent in the case of normal rural lending. In the second case, intermediation through SHGs significantly reduces the transaction costs of both the bank and the MFIs, thereby assuring reasonable margins on their operations. And in the third case, bank branches have the opportunity of getting future quality clients, both for deposits and loans. In the last case, the SHGs successfully provide both savings and credit services to the poor with efficiencies comparable to other agencies. Therefore, it is important to encourage such initiatives of MFIs or SHGs. By extending finance to MFIs, the banking system would not only offering credit but also meeting the expense of the poor with an opportunity to keep safe their insufficient savings and leverage and secure their credit with it.

The success of SHG-Bank Linkage model a successful road map for alleviating poverty in India, led RBI to issue comprehensive instructions to banks to treat SHG-Bank linkage as a business opportunity and a part of their corporate plan.
Banks were also asked to treat lending to SHGs as a normal lending activity in the priority sector, service area approach and review and monitoring system. The policy prescription of RBI was also accompanied with intensified programme support of NABARD in the form of 100 per cent refinance and training and sensitization of bank and NGO officials at various levels. As a result, over 3000 bank branches have taken up SHG linkage for expanding their outreach to the poor. Major public and private sector banks the majors like ICICI Bank, Citi Bank, ABN AMRO Bank have also decided to take up linkage banking on a priority basis.

ICICI 2004 report indicates that there is huge gap exists between demand and supply of credit in India as there is the short supply of credit amounted to Rs.9,000 to Rs. 13,500 million against the demand of Rs.135 to Rs.400 billion annually. This huge gap attracted the attention of commercial banks, Development banks, SIDBI, NABARD, RRBs, SHGs/MFIs and NGOs to play a significant role in profit planning which will give an upward surge in the availability of money in the hands of the poor in various ways resulting in reduction of poverty in India. Microfinance in a positive note are changing the lives of the rural poor, re-energizing the poor community, particularly the most suppressed and neglected community of the rural society mainly comprising SCs & STs and women, small and marginal farmers, artisans, tenants and agricultural laborers. MFIs or SHGs gives these sections of population an access to micro insurance through which sudden expenses relating to serious illness or loss of an asset can be recovered.

Studies conducted in India found that the average annual return on investments by micro business ranged from 117 to 847 per cent. This indicates that the interest rates charged by the informal money lenders are much higher than that of the interest rate charged by SHGs/MFIs and NGOs. The generation of income is possible through establishment and running of agro based units. The problems centre
on unemployment, under employment, low wages and illiteracy. This led the backward class to get more affected with social injustice and political and economic powerlessness.

1.3 MICRO FINANCE THROUGH SHGs

Conducive Elements

SHGs have made women to move out of their home limits. It had given them the courage to contact and confront the officials. With the limited functional literacy they have gained the skill of maintaining accounts and registers. Many of them have undergone various training programmes and it has given them the self-confidence to be entrepreneurs. The impressive performances of SHG women have drawn more number of NGOs and Government Organizations to be in the fray to form SHGs. Both the state and central government have come forward to channelise the schemes through SHGs. NGOs, Government machineries, educational institutions, commercial banks and corporate sectors have acknowledged SHGs to be an effective body of implementing the divergent programmes. Invariably they are convinced that SHGs to be an effective body of implementing the divergent programmes. Invariably they are convinced that SHGs are one of the feasible modes to organize the people at the grass root. Though the formation of SHGs is accepted as an essential element of people’s growth and development still there are large numbers of remote villages and under served hamlets that are left without being touched by the SHG movement. These could be accessed at the course of time.

Constraining Elements

There are high competitions among the NGOs in covering more number of hamlets. False promises and instant loans with high interest are given lavishly to attract the people. Consequently, the civic consciousness and sense of social
responsibility among the mushrooming groups are demoralized. Convergence of services of key line departments of Government like health, agriculture, police, education, animal husbandry, fisheries etc with SHGs may provide a wider scope. But it can reduce the significance of SHGs in the major platforms decision making and policy decisions. Each department claims that SHGs are under their purview but seldom anybody cares to take care of their needs and problems.

While strengthening Cluster Level Federations (CLFs), it is essential to consider the caste and class Factors that dominate the Indian society. Even the continuous training and exposure programmes have brought them together in a subtle way. The dominance of caste group may continue and the poor dalits may be neglected.

1.3.1 Progress of Micro Finance through SHGs

Physical and Financial Growth

During 2006-07, the number of new SHGs credit linked with banks was 0.7 million taking the cumulative number of SHGs credit linked to banks at 2.9 million. During 2007-08, 87852 SHGs have been credit linked taking the cumulative figure to 3.01 million. The phenomenal outreach of the programme has enabled an estimated 41 million poor households to gain access to micro finance from the formal banking system registering a growth of 24.16 per cent over 2005-06. Today, Commercial banks with more than 32,000 rural branches have the largest share (55 per cent) in credit linked SHGs followed by Regional Rural Banks (31 per cent) through their 11,900 branches. NABARD is working with more than 3000 NGOs and other development agencies as partners in the process.
Regional Growth and Trends

The year 2006-07 witnessed the spread of the SHG–Bank Linkage programme in resource-poor regions of the country, indicating a marked shift from its initial concentration in the southern region. The cumulative share of non-southern regions rose from 29 per cent as on March 2001 to 48 per cent as on March 2007. In order to reduce the regional imbalance in the spread of the SHG – Bank Linkage Programme, NABARD identified 13 states which have a large population of the poor, for focused attention. The cumulative number of SHGs credit linked in these 13 states increased from 1 million in 2005-06 to 1.4 million in 2006-07. During 2006-07, the number of SHGs credit linked in 13 priority states constituted 53.9 per cent in the all India credit linkage of 0.7 million SHGs.

Promotional Initiatives by NABARD

NABARD through the dedicated Micro Finance Development Equity Support and support from GTZ has been introducing various promotional initiatives to sustain the SHG Bank Linkage Model in India. The initiatives generally include capacity and commitment building programmes, support to inventive outreach ideas, capital equity support to emerging MFIs, piloting micro enterprises by members of matured SHGs and support to SHG federations.

Support for Training and Capacity Building

The various training and capacity building programmes supported/ conducted by NABARD covers the following:

- Awareness creation and capacity building programmes for SHG members in association with identified resource NGOs;
- Awareness-cum-refresher programmes for CEOs and field staff of NGOs;
- Training programmes for officers of Commercial banks, Co-operative Banks and RRBs covering exposure visits to banks and institutions pioneering in MF initiatives for bank/NGO officials;
- Visits to nearby SHGs for Block Level Bankers’ Committee members;
- Programmes for the elected members of Panchayat Raj Institutions to create awareness about the MF initiatives;
- Training-cum-exposure visits for new district officials and exposure programmes on microfinance and SHGs for senior Government officials, sensitization programmes for junior level government officials etc.

Table 1.1
Regional Spread of Credit-linked SHGs

<table>
<thead>
<tr>
<th>Region</th>
<th>2000-01 SHGs credit linked to banks</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Per cent to Total</td>
</tr>
<tr>
<td>Northern</td>
<td>9012 3.4</td>
</tr>
<tr>
<td>North Eastern</td>
<td>477 0.2</td>
</tr>
<tr>
<td>Eastern</td>
<td>22252 8.4</td>
</tr>
<tr>
<td>Central</td>
<td>28851 10.9</td>
</tr>
<tr>
<td>Western</td>
<td>15543 5.9</td>
</tr>
<tr>
<td>Southern</td>
<td>187690 71.2</td>
</tr>
<tr>
<td>Total</td>
<td>2,63,825 100.0</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Region</th>
<th>2006-07 SHGs credit linked to banks</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Per cent to Total</td>
</tr>
<tr>
<td>Northern</td>
<td>182018 6.3</td>
</tr>
<tr>
<td>North Eastern</td>
<td>91754 3.1</td>
</tr>
<tr>
<td>Eastern</td>
<td>525881 17.8</td>
</tr>
<tr>
<td>Central</td>
<td>332729 11.4</td>
</tr>
<tr>
<td>Western</td>
<td>270447 9.3</td>
</tr>
<tr>
<td>Southern</td>
<td>1522144 52.0</td>
</tr>
<tr>
<td>Total</td>
<td>29,24,973 100.0</td>
</tr>
</tbody>
</table>

Source: Annual Report-2007-08, NABARD
Promotional Grant Assistance to Partner agencies

As on 31 March, 2007, cumulative grant assistance of Rs. 475 million has been sanctioned to Self Help Promoting Institutions (SHPI) to promote 310,000 groups.

1.3.2 Challenges of SHGs – Bank Linkage Programme

While the SHGs – Bank linkage programme has attained the status of a national movement, the financial institutions and other stakeholders face formidable challenges in scaling up the programme in a sustainable manner.

Regional Imbalances

The regional spread of the SHGs – Bank Linkage Programme is uneven as about 52 per cent of the credit linked SHGs are located in the southern states of the country. There is a need for a better distribution of group formation and linkage efforts especially in the northern, central, eastern and northeastern states. This is important as these states have a higher concentration of the rural poor. Special surveys and analytical studies need to be taken up in such regions to identify Factors affecting the spread and sustainability of SHGs. There is a need to invest more in capacity building programmes in these areas. For this, it is essential to build training capabilities in these regions by identifying or promoting new training institutions that may be trained and guided by training institutions of excellence in other areas.

Livelihood Promotion among members of SHGs

Of the total groups financed by banks, there are substantial numbers of SHGs which are more than three years’ old and are well established in their credit
and savings operations. Members of these mature SHGs are now in a position to scale up and diversify their income generating activities. Many NGOs are trying to promote micro enterprises among SHG members. But their experience is rather limited. The critical constraining factor is that SHG members face a lot of problems in marketing of their produce besides low level of skills. There is a need to evolve a methodology for promoting micro enterprises to create livelihood and employment opportunities among SHG members besides imparting relevant skills and developing their risk taking abilities. The problem of rural migration which is a cause of concern could, among others, be addressed through this intervention. Pilot projects through professional marketing agencies have shown encouraging results.

**Capacity Building of SHG members**

It has been observed that among SHGs, in case there is withdrawal of promoting institutions, there is a tendency for a slip in performance. The solution lies in nurturing of groups up to a point where it becomes self managed and independent of promoting institutions. This implies setting up of proper system for accounts keeping and auditing, credit management, capacity building, skill up gradation etc.

Currently, there is a significant emphasis on capacity building for bankers, NGOs and Government officials involved in promoting and financing SHGs. The time has come when there is a need to focus on capacity building of SHG members as many of the SHGs are maturing and the business levels of the groups are increasing. There is a need to identify ways and means of improving the quality of SHGs consistent with rapid growth and balancing sustainability with easier financial access.
Low Bank Loan per SHG member

Under SHG – Bank linkage programme, the average size of bank loan per SHG is low at Rs. 61,679 which translates to Rs. 4,405 per member. However, the variation at field level shows that the older SHGs which have already availed multiple loan cycles, the average loan per member is in the range of Rs. 25,000 to Rs. 40,000. In general, small per capita loans do not enable the members to overcome poverty or acquire capital assets. While the criticism is valid, it needs to be emphasized that the clientele under the programme covers the lowest segment of rural society. This segment suffers from various handicaps including low level of skills, illiteracy poor access to information etc. All this manifests in significantly lower credit absorption capacity. Nonetheless, the challenge remains for all the stakeholders’ viz. Government, bankers, NGOs etc to join hands in the collective efforts for the economic upliftment of SHG members through various repeat cycles of credit infusion.

1.4 MICRO INSURANCE PRODUCTS

SHG members still do not have access to insurance services, which are crucial for security and sustainability of these groups. According to a study conducted in 2003, over 82 per cent of households surveyed did not have any insurance cover and practically none of the poorest households surveyed, had any insurance policy. There is a serious need to introduce micro insurance products and bring together various players in the insurance sector for supporting pilots for development of composite insurance products, which cater for life, health, crops, assets and accidents. Such a product which could be subsidized as a welfare measure by the Government for SHG members would be ideal for the poorer segments of the rural population who can not invest in multiple insurance policies.
Emergence of Federations

Another challenge to the SHG – Bank Linkage has been the emergence of SHG Federations. Such Federations represent the aggregation of collective bargaining power, economies of scale, and are a forum for addressing social and economic issues. However, their sustainability is constrained by several Factors, both internal, related to the federations themselves and external, related to the other stakeholders.

Considering the emerging role of the SHG Federations and their value addition to SHG functioning, NABARD has decided to support the Federation of SHGs.

Technology for Financial Inclusion

As a large number of the weaker and disadvantaged sections of rural society suffer from financial exclusion, there is a need to bring about financial inclusion using technological inputs, on a massive scale, over the next 5 years. This means that every rural family will have at least one member of the household with a bank account. This ‘no-frills’ bank account is expected to enhance access to deposit account, low cost credit, micro insurance, safe money transfers, and financial counseling.

Financial inclusion, as envisaged above, will bring in enormous business volumes, large number of additional customers as also manifold increase in banking transactions. This would require application of cutting edge technology to deliver such services efficiently while simultaneously complementing human efforts. Technological innovations such as smart cards, biometric IDs, mobile handsets and
rural kiosks that can help control costs are crucial for a safe and rapid scale up. Pilot projects on various technological interventions in rural areas are already underway.

### 1.5 INDIAN LANDSCAPE RELEVANCE FOR THE STUDY

Before a strategy for study of Micro Financial services is articulated, it is important to be aware of the context in which these services are planned to be delivered. Some of the key aspects of the Indian landscape relevant for the subsequent **Multivariate analytical study of Micro Finance and its impact on Self Help Group members** are as follows:

India has a population of over 1 billion people with approximately 70% living in rural areas and the rest living in densely populated urban centres. There are 600,000 villages spread out within over 6,000 blocks and 600 districts. The average population per village is about 2,000 people giving about 2,00,000 individuals per block and 2 million people per district.

The average size of each household is four individuals. This implies that there are approximately 200 million households in the whole country. More than 70% of the total working population is engaged in agricultural activities of which about 80% are small and marginal farmers. More than 90% of the working population falls in the unorganized sector earning very low wages and not covered by any social security net.

The country is divided into 30 states. There is an enormous amount of variation in the development and growth status between these states. While states like Punjab, Gujarat and Maharashtra demonstrate per capita Gross State Domestic Product of Rs.15000 (USD300) and above, Bihar, Uttar Pradesh and Orissa have
less than Rs.5000 (USD 100). Similar variations can be observed for health and education indicators.

India accounts for a large portion of the world’s disease and malnutrition burden. Over one-third of the world’s chronically poor live in India. India accounts for 23% of world child death, 20% of maternal death, 30% of tuberculosis cases and 40% of under nourished children. It also has one of the highest rates of low birth weight (LBW) incidence with 67.2% due to growth retardation in the womb.

Around 34% of the country’s population is illiterate. Although efforts are being made to improve literacy rates, there are major gaps in the areas of universal enrolment and retention of students in schools.

About 25% of the total rural population does not have access to safe drinking water, 55% of them do not have electricity in their homes and 40% of the villages in rural India are not connected by metal roads.

At a recent conference on Micro Finance, Mr. P. Chidambaram, the previous Finance Minister, acknowledged that almost 60 to 80% of enterprises and individuals within the country lack access even to basic financial services such as savings and credit. In a country as vast as India, this translates to a very large number of (potentially over 500 million) “un-banked” people - two times the entire population of the United States of America. This situation obtains even after over half a century of independence and over three and half decades of nationalization of banks – the express aim of which was to address this very problem.

In this attempts to address this issue the nation has built a massive infrastructure, including an apex institution and dedicated regulator for this sector, the National Bank for Agriculture and Rural Development (NABARD), over 30,000
rural branches of scheduled commercial banks, a vast network of Regional Rural Banks, Post Offices which offer basic banking services and co-operative institutions of all kinds. We started to build a micro finance movement with in the country in 1992, having learnt from the efforts of Grameen Bank in Bangladesh and Bank Rakyat Indonesia (BRI) in Indonesia, and have successfully built our very own versions of this movement. However, even after over a decade of micro finance, we have been able to cumulatively disburse barely Rs.39 billion, against an annual estimated demand of Rs.450 billion. In comparison, countries such as Brazil and South Africa, which started much later, have succeeded in providing basic access to financial services to a large proportion of their population. World-wide awareness and the importance of micro-credit to the upliftment of the poor has been growing over the years as different countries are attempting to devise ways and means to enhance the access of the poor to credit facilities. Micro Finance schemes are adopted in many countries in the world such as Bangladesh, Srilanka, also cultivated the habit of thrift / saving and utilized collective wisdom to tackle their own problem, have attempted to study the efficiency of Micro Financing through Self Help Groups bank linkage programme in Haryana and found that commercial banks facilitated the access of the rural poor to financial services in a cost effective and sustainable manner. According to the World Bank (WB), only 7% of the poor have been covered by institutional credit. Micro Finance has been recognized as an effective tool and viable program for poverty alleviation.

1.6 MODELS OF SELF HELP GROUPS BANK LINKAGE

On the basis of the modes of formation, nurturing and credit linkage Self Help Groups are basically categorized into three models, mentioned as follows:
Self Help Groups Model I - Self Help Groups formed and financed by banks

In this model, financing banks themselves form and nurture the Self Help Groups. They organize the poor to form an Self Help Groups, train the members on record keeping, thrift, managing credit, etc. and also supervise the working of the group. Up to March 2004, 20 per cent of Self Help Groups financed were from this category.

Self Help Groups Model II - Self Help Groups formed by domestic agencies other than banks, but directly financed

Under this model NGOs, Farmers' Clubs, Individual Volunteer (IRVs) and formal agencies other than banks in the field of micro finance, act as facilitators. They facilitate organizing, forming and nurturing of groups, and train them in thrift and credit management.

Banks give loans directly to these Self Help Groups. This model continues to have the major share, with 72 per cent of the total Self Help Groups financed up to March 2004.
Figure 1.1
Models of SHG Bank Linkage

SHG BANK LINKAGE MODEL -1

SHG BANK LINKAGE MODEL -2

SHG BANK LINKAGE MODEL -3
Self Help Groups Model III - Self Help Groups financed by banks through NGOs and other agencies as financial intermediaries

This is the model wherein the NGOs, Self Help Groups Federations, etc. take on the add-on role of financial intermediation. In areas where the formal banking system faces constraints, the NGOs are encouraged to approach a suitable bank for bulk loan assistance. This, in turn, is used by the NGO for on-lending to the Self Help Groups. In areas where a very large number of Self Help Groups have been formed, intermediate agencies like federations of Self Help Groups are coming up as link between bank branch and member Self Help Groups. Banks finance these federations who in turn finance their member Self Help Groups. Other agencies like NBFCs are also coming up to take up this role. The share of cumulative number of Self Help Groups linked under this model up to March 2004 continued to be relatively small at 8 per cent.

The distribution of Self Help Groups Bank linkage programme reveals that Model II is the most popular Model in India. On the contrary Model I is more popular in Orissa than the other two as this model constitutes 48% of the Self Help Groups in the state (Table 1.2). It is mainly because Orissa has a wide network of rural branches and the capacity building among the bankers is high. People in IT general have more faith in the banking industry, so bank branches as SHPI could easily convince the rural poor to form a group for the benefit of their own. Regional Rural Banks as SHPIs have done well for group formation through implementation of various modules for Self Help Groups formation and their linkage. The advantage with RRBs was, these banks employ local people for formation of Self Help Groups and rural people have immense faith on them. Commercial Banks, especially State Bank of India have also rendered its diligent services to accelerate Self Help Groups Bank linkage in Orissa.
Table 1.2

Financial development of a Self Help Groups

<table>
<thead>
<tr>
<th>Phase 1: Savings</th>
<th>Phase 2: Inter lending</th>
<th>Phase 3: Bank linkage</th>
<th>Phase 4: Sustainability</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Group chooses a common amount to save each month (typically between US 5 cents and 50 cents per member)</td>
<td>• Savings continue</td>
<td>• Savings and lending continue within group</td>
<td>• Group manages savings, internal lending, bank credit, and book keeping without subsidized support</td>
</tr>
<tr>
<td>Benefits</td>
<td>• Group lends savings to members (charges interest)</td>
<td>• Group approaches bank for credit, up to four times the amount saved</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Basic bookkeeping begins</td>
<td>Benefits</td>
<td>• Group continues indefinitely (as long as members enjoy benefits)</td>
</tr>
<tr>
<td></td>
<td>• Groups learn to lend and borrow with small amounts of cash at stake</td>
<td>• Group develops relationship with mainstream financial institution for permanent credit access and savings</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Dependence on moneylender reduced</td>
<td>Benefits</td>
<td></td>
</tr>
</tbody>
</table>

1.6.1 SHGs -Bank Linkage: the Indian Experience

- Self Help Groups promoted by the bank are sound and maturing in a healthy manner.

- Bank looks at the Self Help Groups Linkage Project as a business opportunity and uses it as leverage for expanding its good clientele base in rural areas [100% repayment of loans under Self Help Groups Linkage as against 50-60% under other individual loans issued].
• Presence of a good and reputed NGO in the neighbourhood has been one of the positive Factors for promotion of Self Help Groups by the bank.

• Self Help Groups approach has helped in rehabilitating some of the hardcore defaulters.

• Continuous training of bank staff will have to be ensured to enable them function effectively.

• As the volume of Self Help Groups business expected to increase in the identified branches, the project may be sustainable in 5-6 years.

The performance of banks in linking Self Help Groups to the banking system scaled enviable heights during the recent years in India. The banks financed 3.62 lakh new Self Help Groups during 2003-04 and 2.56 Self Help Groups during 2002-03, together accounting for 57.2% of total Self Help Groups formed in India till March 2004. The cumulative number of Self Help Groups credit linked with banks increased to 10.79 lakh as on 31 March 2004 covering more than 167 lakh poor households. NABARD had set a mission of credit linking one million Self Help Groups by 2007 and the mission was achieved 3 years ahead of the schedule of time.

NABARD has disbursed over Rs.2124 crore refinance assistance to various banks against Rs.3904 crore of bank loans under Self Help Groups Bank linkage programme. Though one hundred per cent refinance from NABARD was available to all banks for Self Help Groups lending, refinance assistance to the tune of 54.4% of bank loan could be disbursed because some banks did not utilize the facility to the full extent. Around 90 per cent of the Self Help Groups linked were exclusively women Self Help Groups. The progress in financing Self Help Groups from 1991
onwards, in physical and financial terms is given in. 1.23 As can be seen from Table 1.3, (next page) the growth of Self Help Groups bank linkage programme in India remained rather slow in the twentieth century. The momentum accelerated only after 2000-01. Handholding approach towards capacity building by NABARD, financial institutions, state governments and NGOs working on micro finance activities could generate adequate pace in Self Help Groups bank linkage programme during last five years. The demonstration effect of successful groups was also instrumental to motivate the rural women to accept the principles of Self Help Groups bank linkage programme.

1.6.2 **State Government Initiatives.**

The Tamil Nadu Corporation for Development of Women has been spearheading the Self Help Groups movement in Tamil Nadu in partnership with NGOs and community based Organizations, under “Mahalir Thitttam”. Training in Leadership Quality, Team building, accounting systems are being undertaken by TNCDW. As on 31 March 2008, 3.66 lakh Self Help Groups were formed, 3.12 lakh Self Help Groups credit linked with bank loan of Rs.2673.40 crore. To upscale the programme, Government of Tamil Nadu has started providing revolving fund of Rs.10,000/- to groups in rural areas under SGSY with banks providing cash credit upto Rs.30,000/- per group. In 2008-09, the State Government has decided to provide revolving fund subsidy to all eligible 1.50 lakh Self Help Groups. The State Government is also providing seed money to well functioning panchayat level federations of Self Help Groups in the State. The State Government has now started the "Vazhndhu Kaatuvom project“ forenabliing Self Help Groups to start micro enterprises with financial support.
Table 1.3
Details of SHGs in TamilNadu as on 31.03.09

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of SHGs</td>
<td>3,91,311</td>
</tr>
<tr>
<td>No. of Group Members</td>
<td>62.93 lakhs</td>
</tr>
<tr>
<td>No. of Rural Groups</td>
<td>2,72,092</td>
</tr>
<tr>
<td>No. of Members in Rural SHGs</td>
<td>44,14,895</td>
</tr>
<tr>
<td>No. of Urban Groups</td>
<td>1,19,219</td>
</tr>
<tr>
<td>No. of Members in Urban SHGs</td>
<td>18,78,106</td>
</tr>
<tr>
<td>Total Savings</td>
<td>Rs.2167 crores</td>
</tr>
<tr>
<td>No. of Groups Credit Linked</td>
<td>3,60,160</td>
</tr>
<tr>
<td>Total Credit</td>
<td>Rs.5337.96 crores</td>
</tr>
</tbody>
</table>

Source: Rural Development and Panchayat Raj Department, Tamilnadu

Table 1.4
Year Wise Details of Credit Linkage to SHGs by Banks in Tamilnadu as on 31/3/09

<table>
<thead>
<tr>
<th>Sl.No.</th>
<th>Year</th>
<th>Achievement in crores</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Upto 2001</td>
<td>120.30</td>
</tr>
<tr>
<td>2.</td>
<td>2001-02</td>
<td>97.91</td>
</tr>
<tr>
<td>3.</td>
<td>2002-03</td>
<td>184.65</td>
</tr>
<tr>
<td>4.</td>
<td>2003-04</td>
<td>271.32</td>
</tr>
<tr>
<td>5.</td>
<td>2004-05</td>
<td>490.62</td>
</tr>
<tr>
<td>6.</td>
<td>2005-06</td>
<td>600.44</td>
</tr>
<tr>
<td>7.</td>
<td>2006 - 07</td>
<td>593.00</td>
</tr>
<tr>
<td>8.</td>
<td>2007-08</td>
<td>804.70</td>
</tr>
<tr>
<td>9.</td>
<td>2008-09</td>
<td>2174.57</td>
</tr>
<tr>
<td></td>
<td>TOTAL</td>
<td>5337.96</td>
</tr>
</tbody>
</table>

Source: Rural Development and Panchayat Raj Department
Government of Tamilnadu
The credit extended by nationalized banks to Self Help Groups in the State this financial year stands at Rs.1,888 crore, nearly equal to the sum disbursed in the past three years.

The banks willingness to lend fresh credit has meant sea change in the lives of Self Help Groups.

Till last year, the government gave each new Self Help Groups Rs.10,000 in grant (six months after formation) and the banks chipped in with Rs.15,000. But from fiscal, the banks have increased this sum to Rs.50,000.

Total amount disbursed was Rs.594 crore. The sum rose to Rs.805 crore next year. The cumulative credit linkage for Self Help Groups since the scheme was launched in 1989 till March 2008 was Rs.3164 crore. During 2008-09, the amount disbursed was more than half of what was achieved in the past two decades.
• During 2008-09, sanction was given for the formation of 1.5 lakh groups. Till now, 1.3 lakh Self Help Groups have been formed, and another 10,000 proposals are being considered.

• Project director Vazhndhu Kaatuvom, says the recovery is as high as 99 per cent.

• There is a NGO link to the repayment, so it is also in the interest of the NGOs that the Self Help Groups they mentor pay back the credit.

To encourage the banks to provide more credit to Self Help Groups, the State government has instituted awards for banks that lend maximum credit at the State and district levels.

1.7 STATEMENT OF THE PROBLEM

Poverty has been one of the major socio-economic problems in India since Independence, the policy makers have tried to tackle this problem in many ways from time to time, and poverty alleviations has been on top of the planning agenda of the government. Most of the people are in villages, which have an extremely thin presence of banks and government machinery. It may be because the size of the financial institutions of the poor people are very small; cost of providing services are high; the perceived risk of default in payment is very high; no collaterals; the rural people are geographically isolated from banks.

The major problem with the most schemes for poverty alleviation and channeling credit to the rural areas seems to be that they are not based on realistic assumptions and analysis of the rural credit in the earlier schemes, like IRDP, DWCRA etc. The beneficiaries perceived the loan as a grant. They did not feel the
responsibility of time or the mechanism for monitoring the repayment. This led to the poor loan recovery and resulted in the scheme becoming non-viable. In contrast, the repayment of loans in micro-credit schemes using Self Help Groups is reported to be satisfactory from almost all quarters. This may be due to the fact that the concept of Self Help Groups in Micro-Credit schemes is based on the theory of asymmetric information and peer monitoring.

The credit needs of the rural poor are determined in a complex socio-economic milieu, where it is difficult to adopt project lending approach and where the dividing line between credit for consumption and productive purposes is blurred. Under the circumstances, a non-formal agency in the form of Self Help Groups of the poor could emerge as a promising partner of the formal agencies.

At this juncture, how the Self Help Groups (SHGs) are going to gain the confidence of bankers who consider poor people are not worthy for bank credit, how it impact the life style and livelihood of SHG, and how the banks are going to gain confidence of poor people as a trustworthy partner. A Multivariate analytical study and the impact assessment programme need to be carried out gauge its effectiveness and will become an invaluable tool in the hands of the policy makers in order to improve the poverty alleviation programmes to have better outreach and quicker results. The study is very apt and highly relevant to document the effective experiences of SHGs in promoting the micro enterprises and evaluating its role in the development and empowerment of the poor people and the society at large.
1.8 OBJECTIVES OF THE STUDY

The overall objective is to assess the Multivariate impact of Micro finance on Self Help Groups aligned to bank linkage programme. The specific objectives of the study are:

1. To study the role of Micro finance in the development of Self Help Groups.

2. To study the objectives and implementation of Self Help Group - Bank linkage programme.

3. To study the profile and background of Self Help Groups members.

4. To measure the impact on income, expenditure, employment, insurance, saving and material possessions of Self Help Groups’ members.

5. To gauge the extent of credit outreach against its requirements, utilization, repayments, benefits and sustenance;

6. To suggest some steps for better implementation and results.

1.9 NULL HYPOTHESES

To give a specific focus to the objectives, null hypotheses have been formed to test the objectives on clear terms using appropriate statistical tools. The Multivariate Analytical study is carried out extensively on variables i.e. impact both on stand alone basis and also on collective basis. Most of the results (impact) are shown with the aid of statistical tools with the numbers/figures on various aspects from multiple perspectives. It necessitates the development of hypothesis at each
and every stage of the analysis. The study involves more than 20 hypotheses which are listed down, proved and explained in detail in the fourth chapter ‘Data Analysis and Interpretation’. Hence, few major hypotheses have been listed down and the rest can be referred in the ‘Data Analysis and Interpretation’ chapter. These Null hypotheses have been rejected and proved that there is significant difference.

a) There is no significant difference between Mean Rank of frequency and amount of savings before and after joining SHG.

b) There is no significant difference between Mean Rank of Average Income before and after joining SHG.

c) There is no significant difference between Mean Rank of Food and Non – Food Expenditure before and after joining SHG.

d) There is no significant difference between Mean Rank of Frequency and Size of Loans before and after joining SHG.

e) The Multivariate impact of SHG membership are equal to the average level (Mean=3)

f) There is no significant difference between Mean Rank of Multivariate impacts of Factor – Economic Empowerment

g) There is no significant difference between Mean Rank of Multivariate impacts of Factor – Personality Development

h) There is no significant difference between Mean Rank of Multivariate impacts of Factor – Intellectual Development

i) There is no significant difference between Mean Rank of Multivariate impacts of Factor – Social Empowerment
j) There is no significant difference between Mean Rank of Multivariate impacts of Factor – Political Empowerment

k) There is no significant difference between Mean Rank of Multivariate impacts of Factor – Household Empowerment

1.10 SIGNIFICANCE OF THE STUDY

The multivariate analytical study of Micro Finance and its impact assessment is very essential to know, understand and measure both the positive developments and gaps (negatives) in the framework of Micro Finance programmes and its execution for more effective and better results. It is highly useful in the hands of governments, NGOs, MFO, and other policy makers to improvise and customize the policy and its execution approach to make it more suitable and friendly to the final beneficiaries.

It has been a considerable period of time with the existence and wider implementation of Micro Finance programmes in India, it is high time a) To take a look at its impact and performance and b) To relook and revisit its policies, framework and modus-operandi of execution as the people and environment are highly dynamic and c) Also, to make amendments in the policy and changes in the execution method if necessary.

The analytical study of Micro Finance and impact assessment of Multivariate impact through Self Help Group – Bank Linkage programmes in Tirunelveli District remains hollow. Therefore, in depth and comprehensive study on Self Help Groups is carried out with the objective to evaluate the impact in member’s occupation, income, assets position, savings, indebtedness, housing
conditions, insurance coverage and other socio economic developments. The impact is assessed, measured and shown the ‘after effect’ of SHG membership.

The researcher has chosen this vibrant topic for the study because the present work on certain aspects is like starting from scratch in the subject matter with the application of more appropriate statistical tools. Such studies have not been undertaken so far in the area under study. The statistical tools in the multivariate analysis study establish the ‘cause and effect’ relationship amongst variables/impact and show the extent of impact on varied aspects. In the study, the impacts are referred as variables for the analysis.

1.11 LIMITATIONS OF THE STUDY

1) The study, its findings and conclusions are limited to Tirunelveli district. So it may not hold good for other areas.

2) The SHGs linked with banks alone are considered for the study. Hence, the non-linked SHGs performances are not comparable with this.

3) SHG – Bank Linkage Programme alone is considered. The other micro finance programmes and models are not considered for the purpose of the study.

1.12 SCHEME OF WORK

The present study has been organized under five chapters. The introduction and design of the study chapter discusses the definition, objective and approaches of Micro finance in India, MFOs, its structure, products and services and its challenges in India, the evolution, trends, progress and challenges of SHGs – Bank Linkage,
statement of the problem, Objectives of the study, limitation and period of the study and scheme of work.

Chapter II deals with the reviews of the past and present studies apart from the gap yet to be filled in the concerned subject and also describes the Research Methodology adopted for the present study.

Chapter III discusses the profile of the study area. Further it elucidates the role of Micro finance and Self Help Groups in Tirunelveli District.

Chapter IV deals with the analysis and interpretations of the sample Self Help Groups and its members in Tirunelveli district. The descriptive analysis of the profile is done in the first part and the inferential analysis of Multivariate impact of micro finance is done in the later part of the chapter. The broad categories of impact based on Multivariate technique ‘Factor Analysis’ are Economic empowerment, Personality Development, Intellectual Development, Social Empowerment, Political Empowerment and Household Empowerment.

Chapter V presents the summary of findings, suggestions and Conclusion based on the analysis done.