

**Linking Banks and (Financial)
Self Help Groups in India
-An Assessment-**

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Preface

Congruity with human nature enhances the relevance and utility of human development initiatives. The core of SHG-bank linkage in India has been built around an important aspect of human nature - the feeling of self worth. Over the last ten years, it has come to symbolize an enduring relationship between the financially deprived and the formal financial system, forged through a socially relevant tool known as Self Help Groups (SHGs). An amazingly large number of formal and non-formal bodies have partnered with NABARD in this unique process of socio-economic engineering. What had started off in 1992 as a modest pilot testing of linking around 500 SHGs with branches of half a dozen banks across the country with the help of a few NGOs, today involves about 20,000 rural outlets of more than 440 banks, with an advance portfolio of more than Rs.1, 200 crore (\$ 240 m.) in microFinance lending to SHGs. Financial services have reached the doorsteps of over 8 million very poor people, through 500,000 SHGs, hand-held by over 2,000 development partners. A brief history of the microFinance initiatives in India will help place the present study report in perspective.

The Background

The high level of dependence of the informal sector on non-institutional sources continued despite a rapid growth of banking network in India in the last five decades. The rural financial system at present functions through an impressively large network of more than 150,000 retail outlets. Despite such phenomenal expansion of the outreach of the formal banking structure, the All India Debt and Investment Survey (GoI), 1981, gave indications that the share of non-institutional agencies (informal sector) in the outstanding cash dues of the rural households was quite high at 38%. It was also seen that households in the lower asset groups were more dependent on the non-institutional credit agencies.

The main hurdle faced by banks in financing the very poor seemed to be the comparatively high transaction cost in reaching out to a large number of people who required very small doses of credit at frequent intervals. The same held true of the costs involved in providing savings facilities to the small, scattered savers in the rural areas. Feelings were mutual among the very small savers and borrowers in the rural areas as well, as they tended to view banking as an institutional set up for the elite; even if they tried to reach the bank branch the long distances and loss of earnings on being away from work while visiting bank branch were hurdles and they were never sure whether they would get any service or not if they did approach the branch. The levels of mutual inconvenience and discomfort made the poor look at banking as an almost inaccessible service, and the banks felt that banking with the very poor was not a 'bankable' proposition.

Role of NABARD

It is in this background that NABARD conducted studies in the mid-eighties that brought out the simple fact that the most important and immediate banking needs of the poor households, in the order of their priority were:

- Opportunities to keep safe their occasional small surpluses in the form of thrift
- Access to consumption loans to meet emergent needs and
- Hassle-free access to financial services and products, including loans for micro-enterprises

Viewed against this demand, there were serious limitations on the supply side, as the existing products and services of the banking system were largely meant for a different type of customer segment. In trying to fulfil the credit needs of the poor for financial services, the banks had to contend with regulated interest rates, high transaction costs and high cost of mobilization of funds.

In cases where credit was made available to the poor through special programmes, absence of an integrated savings component and something to fall back upon in case of any adversity was leading to poor repayment performance. The problem was further confounded, as the users were unable to distinguish between the State support (grants/reliefs) and bank credit as the rural and agricultural banking system was getting identified with the State. The political expediency for 'removing poverty at a stroke' was putting resources for running micro enterprises in the hands of the poor without nurturing them to handle such resources. The high cost of appraisal and monitoring led many banks to jettison those systems in the context of low-value advances, aggravating the already vitiated repayment climate further.

Based on the studies mentioned above and the results of action research conducted, NABARD developed the Self Help Group [SHG]¹ - bank linkage approach as the core strategy that could be used by the banking system in India for increasing their outreach to the poor. The strategy involved forming SHGs¹ of the poor, encouraging them to pool their thrift regularly and using the pooled thrift to make small interest bearing loans to members, and in the process learning the nuances of financial discipline. Bank credit to such SHGs followed. NABARD saw the

¹ A SHG is a group of about 20 people from a homogeneous class, who come together for addressing their common problems. They are encouraged to make voluntary thrift on a regular basis. They use this pooled resource to make small interest bearing loans to their members. The process helps them imbibe the essentials of financial intermediation including prioritization of needs, setting terms and conditions and accounts keeping. This gradually builds financial discipline & credit history for themselves, as the money involved in the lending operations is their own hard earned money saved over time with great difficulty. This is 'warm money.' They also learn to handle resources of a size that is much beyond their individual capacities. The SHG members begin to appreciate that resources are limited and have a cost. Once the groups show this

promotion and bank linking of SHGs not merely as a credit programme but as part of an overall arrangement for providing financial services to the poor in a sustainable manner leading to empowerment of the members of these SHGs.

Fine-tuning Future Strategy

The corporate mission for microFinance set by NABARD envisages reaching banking services to one-third of the very poor of the country, i.e., a population of about 100 million rural poor through one million SHGs by the year 2007-08. The banking system has already reached microFinance services to 40 million poor through SHGs, reinforcing this commitment. NABARD and its partners are all set to traverse the path beyond the mid-mark. This is the right time to fine-tune the strategies for the future, based on the experiences of the past.

The overall strategy adopted by NABARD relies on two main planks: (i) expanding the range of formal and informal agencies that can work as SHG promoting institutions, and (ii) building up capacities of the increasing number of stakeholders. The key to all such initiatives has been training and capacity building of various stakeholders including the SHG members themselves, the range of which is growing at a fast pace. The series of studies undertaken now are oriented in this direction, and are

mature financial behaviour, banks are encouraged to make loans to the SHG in certain multiples of the accumulated savings of the SHG. *The bank loans are given without any collateral and at market interest rates.* Banks find it easier to lend money to the groups as the members have developed a credit history. 'Cold (outside) money' gets added to the own 'warm money' in the hands of the groups, which have become structures, which are able to enforce credit discipline among the members. The members have experienced the benefits of credit discipline by being able to save & borrow regularly without many hassles. The groups continue to decide the terms of loans to their own members. *The peer pressure ensures timely repayments & replaces the "collateral" for the bank loans.*

expected to help NABARD and its partners in this process of fine-tuning their future strategies.

The Present Study Series

These studies provide multi-perspective evaluation of the SHG-bank linkage programme from academics, consultants and practitioners of microFinance from India and abroad. What is germane to all these studies is the rapid growth of SHG-bank linkage into the largest microFinance initiative in the world in terms of its outreach and the need to closely look at the different critical issues related to it. The studies cover the overall programme and its impact, document the different steps taken so far, and evaluate the need and scope for fresh initiatives. These studies were commissioned by NABARD, with financial assistance from the SDC, GTZ, and IFAD. The focus of the five studies is:

- A review of the progress and impact of the overall strategy for scaling up the SHG Bank Linkage Programme over the last decade (by Dr. Erhard Kropp, formerly Senior Economist, GTZ, and Consultant)
- Role and scope of NGOs and non-NGO agencies as SHPI (by Mr. Malcolm Harper, formerly Professor, Cranfield School of Management)
- Study on commercial aspects of impact of SHG-bank linkage programme on bank branches (by Dr. Hans Dieter Seibel, Professor, Cologne University, Germany)
- Evaluation of SHG Bank Linkage Programme based on the economic indicators on the members of SHGs (by NABARD)
- Impact of SHG Bank Linkage Programme on Social Indicators and Empowerment of the members (by Mr. Aloysius Fernandez, Executive Director, MYRADA, India)

In addition, an independent study on 'The role of Self-Help Groups and the Bank Linkage Scheme in Preventing Rural Emergencies' by Ms. Kim Wilson, microFinance Advisor, Catholic Relief Services, Kolkata has also been made available to us. The findings of these studies will be deliberated upon in detail during a seminar organized by NABARD in collaboration with the SDC, GTZ and IFAD on 25 and 26 November 2002 at New Delhi. The seminar would be attended by key stakeholders like banks, NGOs, and government agencies, international agencies like the World Bank, GTZ, SDC, IFAD, ADB, representatives from some developing countries, as also some acknowledged experts on microFinance.

I am sure that the learning points emerging out of the deliberations of the wide range of participants would help NABARD and its development partners to fine-tune their strategy and approach for the next few years.

Y. C. Nanda
Chairman
NABARD

Mumbai
November 2002

ACRONYMS

APRACA	Asian and Pacific Regional Agricultural Credit Association
ARDC	Agriculture Refinance Development Corporation
BASIX	A mFI Group
CEO	Chief Executive Officer
CFSF	Credit & Financial Services Fund
CFTS	Casphor Financial & Technical Services
DCCBs	District Central Co-operative Banks
DDM	District Development Manager of NABARD
DDO	District Development Officer of NABARD
DHAN Foundation	Development of Human Action Foundation
FAO	Food & Agriculture Organization
FWWB	Friends of Women's World Banking
GTZ	German Technical Cooperation
HDFC	Housing Development Finance Corporation
LB	Linkage Banking
MYRADA	Mysore Resettlement & Development Agency
mFDF	microFinance Development Fund
NABARD	National Bank For Agriculture and Rural Development
NGO	Non Governmental Organization
PACS	Primary Agricultural Co-operative Society
PRADAN	Professional Assistance for Development Action

RBI	Reserve Bank of India
RFA	Revolving Fund Assistance
RGVN	Rashtriya Gramin Vikas Nidhi
RMK	Rashtriya Mahila Kosh
RRB	Regional Rural Bank
SDC	Swiss Agency for Development Cooperation
SEWA	Self Employed Women's Association
SIDBI	Small Industries Development Bank of India
SHARE	a mFI- grameen replicator.
SHG	Self Help Group

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SHG-Banking - the Indian Experience

1. Definition of SHG-Banking

SHG-Banking is a programme that helps to promote financial transactions between the formal rural banking system in India comprising of public and private sector commercial banks, regional rural banks and cooperative banks with the informal Self Help Groups (SHGs) as clients. **(SHGs are financial intermediaries owned by the poor).** They usually start by making voluntary thrift on a regular -mostly fortnightly or monthly - basis (contractual savings). They use this pooled resource (as quasi-equity) together with the external bank loan to provide interest-bearing loans to their members. Such loan provides additional liquidity or purchasing power for use in any of the borrower's production, investment, or consumption activities.

SHG-Banking through SHGs and the existing decentralised formal banking network including several organisations in the formal and non-formal sectors as banking partners allow for large-scale outreach of microFinance services to the poor in India. These banking services (depositing savings, taking loans) are made available at low cost, are easily accessible and flexible enough to meet poor people's needs.

2. Programme Initiators

When the Asian and Pacific Regional Agricultural Credit Association (APRACA) presented a platform for policy dialogues to target new banking concepts in the early eighties, the basic concern was that traditional banking cannot any longer ignore the creative human potential of the poor in Asia. They should not remain wasted, as they are potential motor for grass root level development. The following thesis became the entry point of SHG-Banking: Providing them access to saving and credit services may stimulate their self help capacity and can be one essential

entry road to overcome poverty and address some of their crucial social concerns.

2.1 APRACA/GTZ

The APRACA, with special programme support by German Technical Assistance (GTZ, Germany) played the role of a Lead Agency in promoting SHG-Banking in Asia and the Pacific. APRACA is an Association of Central Banks, Rural Development Banks and Rural Commercial Banks, established in 1977 with support from FAO and a mandate to promote innovations in rural finance.

It was at the Fifth General Assembly of the (APRACA) in Bangkok (December 1984) and subsequently in Kathmandu (December 1986) that solutions on how to improve the access of large majority of rural poor and micro-entrepreneurs to a cost effective financial intermediation system were discussed. Special attention was given to the existence and quality of informal financial self help groups providing very cost effective and valuable services to rural people by mobilising their savings and operating a functioning credit portfolio with their members. The key question raised by participants was: What can the rural banking institutions learn from these SHGs and how could they cooperate with them in savings mobilisation and credit allocation in order to improve the quality of formal services and achieve a greater outreach among the rural poor? The emphasis was on indigenous, already existing SHGs.

Finally in Kathmandu in 1986 an Agreement was signed in order to undertake national level studies on existing Self-Help Groups of the rural poor and to initiate project activities on “Promotion of Linkages between Banking Institutions and Self-Help Groups in Rural Savings Mobilisation and Credit Delivery to the Rural Poor”. It was recommended that each member country would form a task force to conduct a survey of SHGs and, in case of

identified potential, to formulate suitable national level SHG-Banking programmes.

2.2 NABARD as Implementing Agency in India and the Strategy adopted

2.21 Preparatory Steps

In India, a Task Force was set up with the Additional Secretary, Ministry of Agriculture, Government of India as Chairman and comprising members of Indian APRACA member institutions to

- Identify the existence of self help groups
- Undertake a survey of a sample of such groups
- Draw up a plan of action for channelling the flow of savings and credit between the rural poor and banks through SHGs, and
- Identify concrete projects for action research in this field.

It was NABARD which led the team, presented a preliminary draft of this report at the 18th Executive Committee Session and 10th Foundation Anniversary of APRACA held at New Delhi in 1987, published the report in 1989 and started the National Level Pilot Project Linking Banks and Self Help Groups in 1992. NABARD was at that time already well geared up to undertake this implementation step.

In 1987 a study team - led by NABARD comprising of other Indian members of APRACA- conducted a survey of about 40 to 50 organisations of varying sizes and representing various activities and regions; one of them was MYRADA which had in place an alternate credit system owned and managed by SHGs of the poor. An action research project on SHGs was started by MYRADA in 1987 with NABARD providing a research and development grant. Subsequently the pilot project of linking 500 SHGs to banks was started in 1992 with the objective of linking and financing

existing SHGs as grassroots intermediaries to banks across the country for both savings mobilisation and credit delivery.

2.22 Facilitation and funding support from SDC

Encouraged by the results from the action research, NABARD launched in 1991-92 a Pilot Project for linking 500 SHGs with banks. The SDC, which had a mutually beneficial & constructive partnership with erstwhile ARDC/ NABARD since 1979, had provided NABARD the necessary encouragement for launching the pilot and supporting the same. It is important to note that the earlier experience of promotional funding support from SDC had enabled NABARD to evolve innovative credit packages and promotional programmes for the development of Rural Non-Farm sector. This experience had positively influenced the launch of the pilot project. In pursuance of an agreement between NABARD & SDC, a Fund styled as “Credit and Financial Services Fund” (CFSF) was set up on 1 April 1995 within NABARD. The objective of the fund is to support banking and financial service institutions for undertaking innovations so as to improve the efficiency of the credit delivery and services to rural borrowers, particularly the unreached poor. The initial funding requirement for promotion, capacity building and NABARD’s refinance to banks was made available from CFSF.

2.23 The Basic Strategy

The basic strategy contained three elements:

- The NGO, which identified the SHG and provided adequate SHG capacity building support including support to build-up capital by regular savings
- NABARD which provided the NGO (MYRADA in this case) the funds under its R&D programme (also to match the savings of the SHGs)
- The Banks which extended **a line of credit directly to mature SHGs (not through an intermediary) without**

determining the purpose for which the members could use the loans, or any other norms like restricting the loan size to tangible assets or determining unit costs for loans coverage. The SHGs could lend for any purpose including meeting various emergency expenses, consumption requirements and productive investment, without any prescribed ceiling on interest rate.

It was NABARD that took the initiative of testing the strategic concept in Indian conditions, and also had the courage, resources and could influence policy throughout the rural banking sector. The Linkage Banking programme was started in 1992 when RBI/NABARD circulated guidelines to banks for financing informal Self Help Groups (SHGs). This was one of the most pioneering acts in target group oriented rural banking in Asia. In fact, the **SHGs benefited** from the comparative advantages of these three strategic elements but to consider SHG as a sound investment opportunity was a bold innovative step. And it was found later that the Linkage Banking-model was by far the most cost effective approach in lending to poverty groups.

In 1996 Reserve Bank of India decided to include Linkage Banking as a mainstream activity of the banks under their priority sector lending. The Government of India awarded national priority to the programme through its recognition in the Union Budget 1999.

The **programme as it is operating today**, requires multiple actors in addition to NABARD and RBI: different promoter organisations to form the SHGs, the participating banks and NGO-Intermediaries to finance SHGs and the SHGs themselves. The programme was designed to initiate linkage processes, in two main dimensions:

- 1. Institutional linkages between SHGs and Banks** (either **indirectly** by involving NGOs and other Self-Help Promoting Institutions as financial intermediaries or **direct**).

2. Financial linkages between savings and credit (in fixed ratios or in dynamic ratios of savings: credit which increases in repeat credit cycles).

Three different models of promoting credit linkages have been found feasible and are since applied in India with special emphasis on forming new SHGs:

Model I: SHGs formed and financed by banks (16% of SHGs)

Model II: SHGs formed by NGOs and formal agencies, but directly financed by banks (75% of all SHGs financed)

Model III: SHGs financed by banks using NGOs and other agencies as financial intermediaries (9%)

2.24 Strategic Support elements of NABARD's Project Promotion

NABARD as Linkage Banking programme initiator and prime mover has developed a detailed strategy for SHG-Banking promotion with the purpose to include, address and familiarize the potential actors with the programme. They were qualified to take over the promotional role in the scheme and to assist in financial groups' formation through NGOs, Bankers, Government officials, Farmer Clubs, Volunteers. Most of the experimentation and subsequent mainstreaming of new non-NGO SHPIs for promotion of SHGs were met out of funding and facilitation support from SDC.

However, NGOs are still playing the most prominent role in group formation and nurturing prior to establishing linkages with banks. With the number of specialised microFinance institutions outside the established banking system increasing rapidly, Model III appears next to Model I - to have a great prospect for the future.

The support from NABARD covers the following main aspects (for details see: NABARD & microFinance 2001-2002: 10 Years of SHG-Bank Linkage):

(1) Financial Support

- Refinance drawn by banks (in 2001-02: Rs. 3,958 million; cumulative refinance up to March 2002: Rs 7,965 million or US\$ 166 million¹);
- Direct Loan Fund Support to NGOs, mFIs, SHG Federations up to March 2002: Rs. 104 million (US\$ 2.16 million)
- Recently, a microFinance development fund was established at NABARD with a start-up fund of Rs 1 billion (US \$ 20.83 million) using contributions from Reserve Bank of India, other commercial banks and NABARD

(2) Capacity Building Support²

- 4,880 training programmes for SHG members benefiting 130,519 members of SHG ;
- 2,234 training programmes for bankers covering 49,709 officials including Chairmen of RRBs;
- 436 refresher and awareness programmes for CEOs and field staff of different NGOs benefiting 10,053 staff members;
- 277 programmes for 13,975 government officers including senior bureaucrats;
- 12 residential and location specific programmes for 362 DDMs; DDOs, Nominee Directors on the Board of RRBs and related officers of NABARD;
- 23 exposure visits to banks and institutions pioneering in microFinance initiatives for 681 bank and NGO officials.

(3) Group Building Support

In contrast to the individual and activity oriented lending that the bankers have been so far involved in, SHG-lending

¹ 1 US \$ = Rs.48.00

² Cumulative figures

is organisation-based. Therefore, facilitating agencies were given support by NABARD to assist in establishing SHGs and to cover the costs involved. As on 31 March 2002, 364 NGOs have been sanctioned grant assistance of Rs. 67.3 million (US \$1.4 million) for promotion and linkage of about 54,000 SHGs spread over 21 States (so far a sum of Rs. 27.8 million has been released for promotion of 36,500 SHGs). Maximum permissible grant assistance for promotion and linkage of an SHG is Rs 2,000 (US\$ 42). This has been computed presuming that the NGO performs the social mobilisation of SHGs as an add-on function only. From the formal banking system, 52 RRBs showed willingness to function as Self Help Promoting Institution (SHPI) being subject of a special grant assistance up to Rs. 1000 per SHG (US\$ 21), which covered the cost of sensitisation of the staff, on the job field training of bank staff by an identified NGO, awareness creation in villages, exposure visits to SHG members and cost of stationery. Payment of grant assistance to RRBs is also subject to specific performance indicators. This group building support is now extended to all RRBs in the country. Each RRB is required to select up to 25% branches with a minimum of 10 branches which would function as SHPI branches. On an average, each branch would ensure promotion and linkage of 15 SHGs every year.

In backward states and districts where organised support from NGOs were lacking, NABARD is also experimenting to include Farmers' Clubs sponsored by bank branches under the Vikas Volunteer Vahini (VVV) Programme and to associate rural volunteers in assisting RRBs and DCCBs in promotion and nurturing of SHGs. A budget of Rs. 6 million (US \$1,250,000) was approved in 2001-02 for promoting 5,650 SHGs through 565 VVV clubs but only 3,643 SHGs were promoted by 346 clubs upto March 2002. The banks normally identify 2 to 3 backward districts and select 25 volunteers in each district who receive special training over a period of 2 years with the objective of promoting about 10 SHGs each. Rs 1.7 million (US \$ 35,400) was sanctioned under this scheme. NABARD's Regional Offices are charged with

handling the promotional work for Linkage Banking in addition to the other routine work and we collected enough evidence to say that ROs are handling this function in a very committed and capable way, besides achieving a great degree of success too.

The growth of the programme was slow during the initial years as it was not mandatory, like other lending programmes supported by Government subsidies, besides the SHG-lending technology was unknown. The bankers in India were practising individual and activity based lending. Organisation-based lending to informal SHGs was a complete new innovative approach. Therefore NABARD -with support of NGOs - had to put in great efforts to get this new lending strategy accepted by the Banking System. Large NGOs, in addition to Mysore Resettlement and Development Agency (MYRADA), like Professional Assistance for Development Action (PRADAN), Development of Human Action (DHAN) Foundation had also pioneered the concept of SHGs and Linkage Banking as essential partners of NABARD.

Finally, with the adoption of SHG-microFinance concept as a primary anti-poverty, self-employment generation programme by the Central Government, this programme received the necessary impetus.

The promotional efforts especially undertaken by NABARD in the last two years have resulted in a significant growth of the programme beyond expectations. Many Chief Executive Officers and Bank Officers were ready to try out the programme. The programme was extended to additional States and Regions. In this way, the adoption of best practices in Linkage Banking and microFinance has been encouraged. The development, training and promotional costs of institutions participating in linkage banking have been partially shared by NABARD. This subsidy also covers the participants' expenses for group formation. NABARD's financial support does contribute to

the profitability of the Linkage Banking portfolio of Banks. The primary stakeholders of the Linkage Banking have not been directly burdened with these costs.

Besides the policy advocacy and promotional role, NABARD had effectively managed the implementation of the programme with enthusiasm and commitment. The milestones of SHG-Banking Programme Development have been summarized in Annexure II. Following the issue of guidelines to banks for financing informal self-help groups the programme has come a long way since its beginning in 1992. The focus of the approach was led by capacity building initiatives of different stakeholders, provision of grant support to NGOs and other SHPIs for promotion of groups, crystallisation of vision to cover one third of the poor, building partnerships with government and technical assistance organisation like GTZ, establishment of separate funds to support scaling up the programme, developing a cadre of master trainers using the distance education programmes, experimenting with a range of self-help promoting institutions and individuals and diversifying the range of capacity building approaches etc.

2.25 Present Level of Programme Performance

Today after a decade of implementation of the “Linkage Banking” or “Self Help Group (SHG) banking”- approach, NABARD has been able to increase the outreach of banking in rural India, substantially. The linkage banking approach of providing financial services to unbanked poor now touches 1/6th of rural poor in India.

As of March 2002 cumulative lending by banks to 461,478 SHGs under the programme amounts to Rs 10.26 billion (US \$ 218.27 million). According to unofficial estimates, the amount of accumulated savings in SHGs exceeds Rs 8.75 billion (US \$ 186.31 million). Of the total number of SHGs financed by banks so far 90% were exclusive women groups. This has every reason for us to state that **linkage**

banking has contributed to the feminisation of microFinance banking in India. In total about 7.8 million poor households got access to credit through 17,085 branches of the formal banking system (see Model I and II) and through NGOs/other agencies as financial intermediaries (see Model III) under this programme. It is already the world's largest microFinance Programme in terms of outreach. Out of the 461,478 SHGs only 16% were facilitated by bank branches exclusively (Model I without any NGO being involved) and 75% were linked with banks by initiatives of their promoting/establishing/nurturing NGOs or the Government, while only 9% of the SHGs were having established financial transactions with NGO financial intermediaries directly (Model III). Some representatives from NGOs maintain that their groups are the most stable and sustainable ones.

It is not only the SHG-Bank Linkage-programme of NABARD that allows the SHGs to obtain loans from formal banking institutions. Other apex development banks in India such as SIDBI, HDFC and government institutions like RMK, as well as private financial agencies such as BASIX also provide special credit facilities to SHGs (but their performance is not subject of this report). They also have started to promote SHG federations as a strategy to ensure the financial viability and sustainability of SHGs as small informal organisations.

2.26 Some Suggestions for Adjustment

The following indicators are presently being used to measure the Linkage Banking-programme performance:

- Number of SHGs linked-which have taken loans from banks (which explains the great effort to form new SHGs) ("groups linked")
- Volume of micro credit extended to SHGs by the Formal Banking System (which explains the credit disbursement orientation of the Linkage Banking programme) ("money disbursed")
- Number of banks or bank branches involved

A financial system is more than a set of channels for disbursing loans! The “credit disbursed by banks to SHGs” as an indicator gives a traditional, one sided and incomplete signal to the Government in regard to SHG-Banking. Banks should not only be seen as a credit disbursement mechanism but also as financial intermediators which attract more savings and stimulate internal banking by SHGs from internal and external bank sources to meet short term financial requirements of their members.

There is no indicator, **which reflects the dimension of financial assets/quasi equity of SHGs created, and the volume of loans provided inside the SHG system in support of the low income people in rural India. Therefore:**

- SHGs which hold only savings in the banking system as well as the volume saved should also be included in the Linkage Banking statistics;
- Total volume of savings accumulated by SHG-members should be assessed/estimated;
- In addition to the amount of loans from the banking system, one should also assess/estimate the total volume of loans extended to SHG members (from SHG-internal as well as from bank sources).

3. The Demand Side: SHGs as Financial Intermediaries in the Villages

An unique feature of “SHG-Banking” is the concept of lending to Self Help Groups as a very effective financial intermediation, for it retails loan funds to the poor members and mobilises regular savings. The initial capacity for self-governance has been found in old as well as in newly formed SHGs. Self Help Groups (SHGs) in the SHG-Banking Programme are quite autonomous in their decision making regarding savings and credit.

SHG-Banking is demand oriented. The poor people’s most urgent needs were to find opportunities for depositing their

small savings and access to additional external funds for loans to meet emergencies and for micro-investments (partly for consumption needs). Forming an own financial SHG was the key to access financial services by the rural poor (who have been outside the fold of the formal financial system).

An SHG is an informal organisation of upto 20 people from the poorer section of the village society, organised, owned, operated and controlled by the members, based on solidarity, reciprocity, common interest and resource pooling. Groups formed by households from the same village range - as we found from our survey - between 7 to 20 participants/members (mostly women) from poorer sections of the village community (richer classes do not like to act in groups and to be subject to very tight group discipline). They are mostly from lower castes, from the neighbourhood, some from the same (extended) family; they know each other, have joined together to get access to banks and are ready to meet together and to save regularly (contractual savings). **SHG is a social design in which people participate by making themselves socially and economically accountable to each other.**

About 90% of SHGs formed so far are women groups. They are supposed to be homogenous, sticking to group solidarity and accepting peer pressure in case a member household does not meet obligations. While men very often leave the village to work outside, makes it difficult to form groups and to meet regularly. They usually end up in heated discussions and find it much more difficult to come to acceptable decisions regarding fund allocation among the members. They face the problem of sustainability to a greater degree than women groups.

Some SHGs have been found to adopt girls of poor families and mentor them to go to school, provide them business skill or even get them married. Some organise feasts for school going children or even take up construction of

village infrastructure. These efforts are often considered to be great achievements of a group and they are appropriately felicitated. (especially seen in groups promoted by government officials).

To increase the number of SHGs who start to make voluntary thrift on a regular basis is the most essential strategic variable in the Linkage Banking system. About 75 % of the SHGs have been formed and are continuously supported by NGO staff (not only exclusively to get access to bank loans but also to achieve other development goals through joint actions: educational, health, family planning, access to land and water, forming a social movement of women, etc). Those SHGs formed on the initiative of the Banking System (by bank staff or agents) have the overwhelming objective to help SHGs get access to banking (saving and credit) services to improve the economic condition of their members and to wean them away from moneylenders. They may be called **financial SHGs**. Also some community based organisations like farmers' clubs, local bodies and field level workers of government agencies are involved in SHG formation as an essential strategic element to fight poverty in India. A multi-agency approach in group formation has been initiated and many questions regarding the quality-outcome of the different kind of "foster-children" groups remain (see study by M. Harper: SHG Bank Linkage Programme - Role and scope of NGOs and non NGO agencies as SHPI, September 2002). As the manifestation of poverty is too variegated in India, agencies involved in social mobilisation of the poor do face problems in targeting the real poor - some standardized approaches such as the housing index could be an enabling tool. NABARD leaves the identification of the poor to its cooperating local partners and the people themselves. The most rigorous selection of poor members is being undertaken by the NGO-replicators of Bangladesh's Grameen Bank model.

From our interviews with groups and very limited evidence in the field we could not identify substantial differences in the financial performance of the SHGs according to the organisational support received for getting established! However, capacities and sustainability of SHGs? - It would largely depend upon the promoters of the group.

4. The Supply Side of MicroFinance

The second key indicator for the success of SHG-Banking is the extent to which the vast network of commercial banks, cooperative banks and regional rural banks with 160,000 retail outlets is ready to cooperate. The following institutions are actually or can be potentially involved in Linkage Banking:

- some 94,000 cooperative societies or branches of cooperative banks,
- around 60,000 branches of 27 public sector commercial banks and
- 196 regional rural banks and
- another 4,700 branches of 55 smaller private banks providing financial services in India) as well as
- other financial institutions (37,000 NBFCs) spread all over the country (partially involved in micro-savings)³.

The density of the formal banking network for SHG-Banking in India is ideal: Today, semi-formal and formal financial services through banks and agricultural cooperatives are within physical reach (less than 5 km) of perhaps 99 % of the population of the country;

Actually 444 Banks (121 RRBs, 209 cooperative banks, all 27 public sector banks and 17 private banks) through their 17 085 branches are now involved in Linkage Banking, with number of SHGs reaching 461478 and the loan volume Rs. 10,263 million in 488 Districts.

The RRBs as an important part of the rural financial system, received specific attention in the financial sector

³ RBI data indicates that 749 NBFCs are presently registered, which can mobilize savings.

reform process and later on in SHG-Banking. The RBI had in a phased manner undertaken the restructuring of RRBs since the early nineties (1993/94). As an institutional development agency for rural financial institutions, NABARD had assisted RRBs in elaboration of its development action plans and facilitated the turn around of this segment of rural financial institutions. The action plans of RRBs also covered SHG financing as an integral part of its lending portfolio.

In order to test the efficacy of RRBs for social intermediation, NABARD partnered with an RRB and an NGO to run a pilot project covering different branches of an RRB. The staff in these branches received in-house & on-the-job training in promotion of SHGs through a renowned NGO. The staff was then expected to create awareness in their respective branch area, initiate new SHGs provide support services to them and finally establish a credit link. As on March 1998, 92 groups were promoted 16 credit-linked with a loan assistance of Rs. 200,000. An independent evaluation taken up later showed that the SHGs showed a good performance and **bank staff could promote, nurture, stabilise and link SHGs in addition to their normal work, with marginal operational costs.**

Sustainability of SHGs has been a concern for some NGOs participating in the programme and a few of them have supported institutional upgradation of SHGs by federating them. Such a development would add to a new people's banking structure and would be a new element in financial system development. NABARD's direct Loan Fund Support to microFinance Institutions (as additional (Quasi) equity and for on-lending on an experimental basis) has been provided with the aim to help them to graduate to levels of commercial borrowing and to reach break-even point very quickly. Meanwhile 28 Agencies like FWWB, CFTS, SHARE, DHAN-Foundation, RGVN and 5 Federations of SHGs in Tamil Nadu have received an amount of Rs. 104 million (US \$ 2.16 million) upto March 2002.

Accumulation of rural savings in financial form at SHG as well as at bank branch and microFinance Agency level may also diminish the present decent patronal relationship that currently exist between NABARD, Banks, NGOs, SHGs and rural borrowers. It also may increase intermediaries incentives to respond more dynamically to the interest of their depositors and borrowers and may reduce the scope for politicisation of rural financial markets.

The result achieved so far is unexpected. The formal Banking System in India has accepted the challenge of incorporating microFinance into their business policy. Formal microFinance services are - not only in theory - available and accessible to low income families. An increasing number of formal financial institutions like branches of RRBs, Commercial Bank branches and Cooperative Banking Institutions (DCCBs and PACS) are offering microFinance services now. In PACS, a Self Help Group can be registered as a member and served like other individual members. The lopsided geographical spread of SHG-Banking is on account of non availability of suitable partners in SHG-formation. In areas (states/provinces) with potential for SHG-banking promotion like Bihar, Madhya Pradesh, Rajasthan, Uttar Pradesh, Orissa, it is the non-availability of capable NGOs which cause serious constraints for a quicker spread of the programme.

The formal financial institutions operating in rural India and applying the financial technology of establishing a line of credit facility to quality-SHG's can be internationally classified as **low-cost microFinance service providers**. They were successful in the introduction and promotion of a formal **banking and credit culture** with saving and credit groups as clients (who maintain a self-organised, owned and self-governed internal lending programme).

5. Operational Aspects of SHG Banking

The SHG-based microFinance is the main form of

microFinance in India today and is well integrated into the formal banking system in India.

Many questions were raised during our field trip:

How does the Linkage Banking-system meet the demand of the poorer sections (predominantly women) for financial support?

What is the strategy of Linkage Banking in regard to number of SHGs served, loans disbursed and repaid?

What have been the guiding principles to meet the demand of the poorer section of the people?

Why is saving and credit so important to fight poverty as compared to all the other supporting activities (rigid SHG formation, educational guidance, micro-entrepreneur training, skill training)?

5.1 SHGs as a Retail Financial System at Village Level

The system is predominantly working with newly formed SHGs. SHGs are initiated by agents (bank clients, Volunteers of farmers clubs, social workers etc) or taken over from NGOs to offer bank services to them. Some group members (sometimes all) are sent for special training. Linkage Banking in India is therefore not exclusively working through existing informal SHG-institutions but predominantly with the formal banking system. Several guiding principles for Linkage Banking are very relevant in India (see features of the guiding principles and product designs - Annexure I)

5.11 Training and Savings first SHG Training

The processes of group formation and training are critical stages for stability of the group. Training includes

teaching rules and regulations governing bank procedures and administrative requirements, maintenance of book of accounts, rules for internal lending and repayment of loans, keeping the group fund intact (trust is essential in relations with the bank and among group members!), knowing in detail the responsibilities of the chairman and the secretary of the group, the potential of own savings or learning to write one's signature. Group organisers do this job during 4 to 5 visits to a newly formed group (as against a 7 to 15 days training under bank staff in BGB). In few cases we found that individual members of groups have been send to Training Institutes for training in financial management of groups. They were all very serious about the tasks given to them. Book keeping remains a particular problem area to be addressed by training. This role is usually given to a knowledgeable and trustworthy person in the village (mostly retired government employee or NGO staff).

Bankers' Training

Bankers ought to know their new functions and responsibilities, decision making powers, accountabilities around the focal point of Linkage Banking loans (including refinance facilities), saving facilities offered, loan procedures, viability of potential loans including repeat loans, checking adequacy of loan amounts within a stipulated business activity, loan disbursement and repayments, issuing loan pass books etc.

Savings

The newly established groups do not start with a loan from the bank. They start as savers' groups with regular fortnightly or monthly small savings targets. Each member saves identical amount (approximately Rs. 20 to Rs. 50). This contractual saving system has been introduced by every group visited in the field with the aim to start developing a basic financial discipline and

to build-up an own capital stock as an internal resource base and to become eligible for a bank loan. SHGs usually discouraged members who voluntarily contributed or saved higher amounts with SHG - this was partly because of the added issues of bookkeeping get more complex as also the fear that they may gain more influence in decision making in the group. They usually were asked to go to the Bank and to put their additional savings into an individual saving account. Some of the members wanted to maintain a purpose oriented saving account for meeting marriage, funeral expenses or for religious functions, holidays.

Among the poor households, the capacity for saving is remarkable and testifies their skill in efficient utilisation of resources and also their ability of setting aside thrift even at extreme low income levels. The savings account of the group was opened at the Bank forging a future relationship with the banker. Each member of the group continues to save a small but fixed amount after receiving the first bank loan. The savings are collected during the regular meetings and entered into individual passbooks and the group passbook.

The two requisites for effective savings mobilisation in SHG-Banking mentioned very often: (a) savings shall not yield negative real returns (relative to the rate of inflation) and (b) savings as a potential source to finance new SHG loans are not undermined by cheap subsidised finance facilities or donor money.

Some of the selected group representatives and group members were receiving special training to manage the SHG financial system. Once the groups have been formed no additional subsidies are required. (Only in some of the SHGs under survey, an additional subsidy support was given by Government or by NGOs but not by banks).

5.12 Promoting Loans at Market Rates

(1) Bank loans to SHGs

After 6 months of normal functioning, “bankability” recognition is given to the SHG (despite being a non legal entity) by the Bank. Then, a loan or an overdraft facility is sanctioned by the banking system to SHGs in relation to the savings amount accumulated and based on the SHG request. Market rates of interest are applied and the participating banks are free to modify according to local conditions. The RBI created the necessary conditions by deregulating the interest rate, enabling application of market rates in this case. NABARD original guidelines on SHG-linkage banking programme recommended that banks start lending with a loan to saving ratio of 1:1 or 1:2 and may gradually increase it to 4:1, keeping in view the resource handling capacities of the poor (based on an experience of the Indonesian Central Bank which operated a similar SHG-Banking programme). Conventional collateral is substituted by group liability and volume of group savings. Meanwhile, increased repeat loans are given to good performing SHGs but the amount of repeat loans is still very small (Rs. 20,000 to 50,000 or US \$ 400 to 800).

Field evidence indicates that **banks have started to put in place proper systems for rating of SHGs or NGOs** before financing or they developed their own criteria to assess the bankability of a group for a repeat loan (savings accumulated, SHG performance etc). The interest rate charged is usually 12% but the SHG members have to come to the Bank branch for services. The banks have to keep their operational costs at a low level and have to control their operating costs of the SHG portfolio very carefully in order to assure its earning capacity within the margin left to them (12% minus 6.5%-8.3% cost of funds for the bank). There is some (but more unscheduled) supervision of SHGs at their doorsteps by the bank branch managers but a continued doorstep service would lead to

a high cost structure, which cannot be covered at the present interest rate structure. The loans from Banks to SHGs are short term or medium term (3years). For many banks it remains to be seen, if the credit linkage with the SHG is to be self-sustained (or the credit links being continued with individual members of a group at a later stage?)

(2) SHG-loans to members

SHGs use this pooled resources together with the external bank loan to provide interest bearing loans to their members. The decision on who gets the loan is being **taken by the group and not by the Bank staff**. Sometimes a loan appraisal of individual loan requirements is made within the group. Members request loans during the group meetings and issue the loans during the group meeting (or beyond at ad hoc meetings in case of an individual emergency requirement) out from the collections during the day or they are issuing cheques on their group account with the partner bank. The system is designed to make sure that the loan fund is reaching them directly in a transparent matter. The interest charged for internal lending to members ranges from 24% - 36% as a flat rate partly to simplify calculation by SHG members. The members keep track of the end use as well. Inappropriate loan utilization and other issues like non-payment of monthly instalments are taken care of within the context of the group. Members take great pride in being honourable and making their payments in fixed equal instalments on time. Flexibility of repayment is also granted if necessary. There is a spirit of solidarity in case an individual member cannot repay in time. A loan loss reserve fund could not be found in any of the SHGs visited.

The solidarity principle in SHGs means that groups are in fact a small collective organisation which guards against individual economic and societal risks and for promoting economic ventures individually or jointly.

(Remark: Using the total volume of SHG money to start a joint enterprise like food processing, food catering, running

a village shop jointly, auctioning the right to organise the village market, manufacturing of milestones etc, with all group members involved, is an indicator for the entrepreneurial enthusiasm created at the beginning; but joint micro-enterprises may not last for long!).

There is no monitoring of loan utilization by the bank staff (branch managers, programme officers). In case of default no legal charges are taken (yet to come across such cases).

The loans are used by them to finance working capital and or meet capital requirements for a micro-entrepreneurial activity, for crop loans etc that is usually not linked with marketing and short term consumption and emergency requirements. The entire transactions are recorded in the loan books.

The loan ceiling for the SHG can be upgraded and can also be fixed on the basis of the total amount of savings of the SHG. Accordingly, the supplementary loan funds are made in a gradual manner (with saving credit ratios actually applied from 1:1 up to 1:4). It may also be worked out on the basis of performance (regularity in repayment, attendance in regular meetings etc). A borrower in the group can enhance her loan size - also subject to a ceiling - by making sure that she and her group continue by increasing the regular savings and repay the group loan to the Bank in time.

All payments - loan disbursement, savings, insurance premium contributions, loan repayments - are made at group meetings. The regular saving is continued fortnightly or monthly and the capital stock for lending is increasing continuously. The loan repayments by members include those on loans issued out of group's own funds as well as from the bank loan without differentiating according to the source of the fund. Peer supervision exists in some SHGs. Inappropriate loan utilization and other issues like non-payment of monthly instalments are

taken care of within the context of the group. Members take great pride in being honourable and making their payments on time. There is a spirit of solidarity in case an individual member cannot repay in time because of genuine difficulties, in which case the group on behalf of the member makes the repayment. It exhibits the existence of peer sympathy, ushering in human face of banking and also flexibility of the system. **It is important to note that peer sympathy co-exists with peer pressure. Both are integral part of group dynamics in SHGs.** Some SHGs pay interest on the savings or dividends from the interests earned or retain their earnings as equity capital. Cash flow management can become a problem.

There were a few reports during our field survey regarding lack of proper book keeping practices and accounting/auditing support to newly established SHGs. Sometimes regular attendance at group meetings and absence from village because of outside employment (mostly males) was reported as a problem. Monitoring/evaluation of SHGs still leaves room for improvements. Internal checks and control of the SHG-loan portfolio and a dual control by an outside agency (NGO, Government or SHG-Apex body) may become necessary. There is only a limited consultancy standby for those SHGs (which do not get direct NGO support) that had to face some internal trouble. But we do not have enough concluding evidence to say that SHG-Banking involving NGOs engaged in financial intermediation as facilitator cum financial intermediary performed better compared to direct Bank-SHG linkages. Higher efficacy as compared to the formal Banking System has been reported from few highly specialised microFinance institutions but cost of lending (per Rs disbursed) at this institutional level as well as the interest charged to the SHGs may be higher (12 % levied by banks to SHGs as compared to 20 % upto 45 % in direct lending by microFinance institution system).

We consider this financial scheme a unique contribution to microFinance. The SHGs are **not “used”** by banks to channel a bulk loan to several poor people in a **“single-size-fits-all” kind of methodology** with all members benefiting equally: Same loan product at a high interest rate, same duration, same repayment instalments, designed to be operated mechanically and easily by the Bank. This was the predominant retail delivery system at the start up phase in which microCredit has been delivered to groups in different countries (see Grameen Bank Bangladesh). In SHG-Banking, the central assumption underlying this banking by the people is: the firm belief that the SHGs of the poor are reliable partners in handling bank funds, they will always pay back their loans and they are much more creative in allocating the loan fund among their members than any outside agency because they know the character and capacity of every person very intimately. Therefore, **full autonomy** is given to them by the Bank to decide, to which member a loan is given and how to make it best fit for them (“tailor made”) in terms of purpose, amount, duration, size of instalments, interest rates etc. The first set of decisions incumbent upon the group is deciding the amounts of the loans and which loanees will receive what amount (subject to a loan ceiling for individuals). They allow for individual or joint enterprise initiatives while committing individual members to a strong social accountability. Some SHGs under survey provided loans for productive purposes to their members but not fully excluding loans for consumption, medical treatment, marriage. Some SHGs were even giving loans to non-members and to the local Panchayat at monthly interest rates between 3 % to 5 % levied as a flat charge.

5.2 Success factors in SHG-Banking

The factors that contributed to successful SHG-Banking under NABARD can be summarised as follows:

(1) The SHG is an organisational framework ensuring members direct access to and control of additional

resources borrowed from the bank. They **participate willingly** (but some not always very regular or only ad-hoc!) because the SHG-system is designed in ways conducive to their active participation, shared interest, responsibility and economic potential. These additional money resources are committed by the banking system without prescription for what purpose the loan is to be used by the SHG members. And SHG members retail the money according to own economic inspiration and preference without any tight supervision by the bank representatives.

(2) The **concept of saving first** had a much more decisive impact than anything else. Saving is the initial source of loanable fund and by transforming their savings plus the loan from the bank into interest bearing loans; the SHGs augmented their resources with retained earnings. But unfortunately the uniform contractual saving product with the same amount saved by everybody does not fully mobilise the existing saving potential of the SHG members with some willing to contribute much more. The propensity to save has increased with Bank access. **Self Help instead of government spoon feeding, autonomy instead of constant bureaucratic intervention, flexibility and spontaneity** may be determining factors for success. Therefore the **SHG-system should and cannot be utilised as instruments of government agencies to implement development schemes of the Government.**

(3) SHGs as clients facilitate wider outreach at lower transaction costs and much lower risk costs. The participating Banks experienced so far **low additional operational cost and marginal loan losses**. Therefore the amount made available to SHGs for loans and the average size of loans was growing quickly.

(4) The SHG-system is working like an **informal insurance system** that allows managing risks and income gaps very

effectively and this was most needed according to member's priority assessment.

(5) The SHG-system covers another urgent need of the poor; it is evolving as an effective people's banking nucleus which **allocates money into the economy of the poor with the purpose of stimulating a self-reliant, indigenous developments tapping the manifold skills that poor already possess.**

(6) The sovereign role of NABARD in policy advocacy and designing SHG-Banking strategy, involving a variety of institutions including RBI and Government, influencing policy, funding and technical support, motivating, training and coordinating with partners, stimulating innovations in financial technology and moulding attitudes is definitely the key to success. No substantial conceptual support from external donors was required as NABARD had the professional capacity to handle the new programme and to select the most appropriate experience from other Asian linkage projects on its own.

(7) Most outstanding is also the role of NABARD in **building commitments through capacity building** by:

- Designing separate training modules
- Developing separate course materials
- Content and delivery enrichment by training tools, training methodologies
- Identifying and developing new training partners
- Organising Workshops, training programmes, seminars at different levels for bankers, for NGO employees including field staff
- Providing selective capacity building support to NGOs, SHGs, Federations of SHGs and related institutions

Training has prepared the ground for SHG-Banking and contributed most to building trust and confidence between the banks and the rural poor. More than 7000 orientation

programmes were funded (CFSF) and guided to establish the new capacity required.

(8) The encouragement and flexible funding support from SDC assisted CFSF had enabled NABARD to experiment with a range of new SHPIs and also meet the major challenge in upscaling exercise by organise diverse training and orientation meets for different stakeholders.

(9) RBI policy support for the banking system to consider mainstream financing of SHGs as a business activity for banks and also make it a component of priority sector lending were both considered the most adequate enabling conditions for the formal banking system to start SHG-Banking.

6. The mFI or the Non-Government microFinance Sector (NGMS)

The NGMS is an alternative microFinance supply system to SHGs that is predominantly self organised and supported by NGOs with no government, government bank or individual agent involved. Meeting saving and credit requirements of the poor is only one facet of a strategy, which facilitates the overall development of the poor. This NGMS system is exclusively designed to meet the financial service requirements of the poor and is strictly target group oriented, trying continuously not to allow other sections of the society to enter as clients. Their products are exclusively designed to meet the financial requirements of the poor and are - because of small transactions and lack of economies of scale - rather highly priced. This is why the NGM -System is often characterised as a **high cost financial service provider** system charging interests for their loans ranging from 20 % upto 45 % per year.

They incur high cost of forming the groups, starting with awareness creation before the group starts to enter into a bank relationship (upto Rs 18 000 per group as against

lower costs in groups formed by banks); the follow-up cost of serving the group regularly at their meetings in the villages is a heavy burden but adequate in order to overcome poverty among all SHG members. But as a result one may expect a more consistent strategy/operation and a higher efficacy towards eradication of poverty among the rural population.

Also SHG-Linkage models involving NGOs as either facilitator or financial intermediary may “perform better as compared to SHG-Banking as a result of direct linkages between banks and SHGs” (Fernandez) because of better and more integrated quality services rendered to groups. But there is not yet a clear evidence for this hypothesis.

Specialised microFinance institutions face a great shortage in qualified staff capable to build up a MFI and to provide appropriate bank services at the doorstep of the SHGs with the result that they have to train young graduates intensively to take up such heavy work load commitments; they are additionally burdened with a relatively high drop out rate among their staff etc and find it difficult to provide quality microFinance services from the very beginning. But the recovery of their loans is nearly 100 %.

Most mFIs established by private initiatives have high institution building costs in the beginning (before costs break even). The financial product - for loans and savings are mostly designed very rigidly, several loan products are also offered side by side. There is a danger of loans being taken for repayment of old loans and loan cascading with constant increase of amount of indebtedness per family and SHG. There is no flexible credit (like overdraft for example) cum savings facility yet offered by the Non-Government microFinance Sector to serve the needs of the poor in a more client friendly manner. Shortage of funds is another primary constraint that impedes significant outreach to the poor. Being externally (mostly donor) funded, these organisations are confronted with

irregular inflows disturbing regular delivery of credit services.

There is a lack of equity and equity-like financing which is a significant obstacle to optimal growth. More traditional avenues of raising pure equity should be pursued including social venture capital and special capital support from NABARD.

NABARD support should also include a special institutional development grant based on a clear understanding of the growth path of a new microFinance institution with particular indicators for each institutional development level and level specific financial support. Also a problem solving advisory service for breeding new microFinance institutions may be required

7. Achievements in SHGs through SHG-Banking

With the introduction of “SHG-Banking” a highly flexible financial service structure has been made available to poor households, which allowed them to stabilise their irregular income flow and to increase their income in most cases. The SHG-System allows members to maintain a more regular financial flow in support of the family and of the microenterprise operated by the family.

It

- enables the conduct of **frequent transactions** both for allocating small contractual saving amounts and for borrowing for a **variety of self chosen purposes at irregular intervals from the SHG**
- tunes the allocation of funds with the needs of group members at local level inside the SHG-dominated financial self help system (without formal requirements)
- provides a very flexible credit line from the banking system at an acceptable interest rate (mostly 12 % p.a.) at bank branch level to the SHGs and also allows small bridging loans internally by members from their SHG-fund.

- offers deposit facilities at the bank and at the group level that enables conduct of frequent saving transactions both individually and on group saving accounts (almost 24 hours a day);
- starts to offer purpose oriented savings accounts in the form of insurance with the Life Insurance Corporation of India;

SHG-Banking is an ideal combination of the formal banking sector's "banking with the poor" and "banking by the people" through informal SHGs. This also shapes the introduction of a basic element of an informal insurance sector with gradual access to the formal insurance sector.

The economic impact of SHG-Banking on poor households has been captured in several studies; some evidences indicate that it:

- Enables increased propensity to save
- Permits enhanced net incremental incomes
- Smoothens income inequalities
- Assists reduction of indebtedness with moneylenders and freedom from bondages
- Enables additional employment (person days) generation
- Facilitates empowerment of women.

The good performance of the SHG-Banking Programme is due to its strategy to mobilize underused capacities of the target group. What are these particular skills and assets of low-income people - particularly women?

They hold non-wage earning activities, they can work on own account, as self-employed person, are self-reliant, more independent, more autonomous in managing their family affairs and household budget, they do business or go into new business on one's own initiative, they think of oneself but it is also the collective wisdom of all group

members which pervades the system. They are more reliable and are able to communicate much better within their self-selected groups as compared to males; they hold a poignant intelligence and are more teamwork oriented than males; they also can lead a group as cooperative or authoritarian than males. They know how to utilize an available resource, money included, in a remarkable variety of ways and combinations to maximise its potential (animal husbandry and cattle fattening, utilization of land for all kind of crops cultivation, use of water, collecting products from the forests, pulse husking, mustard oil manufacturing, betel nut and spice processing, making lime and other building materials like milestones for roads, tailoring, running tiny snack shops, petty trade, preparation of sweets and snacks with chutneys, pitching tents and organising festive entertainments and banqueting, food-catering to schools and distribution of products through trade etc. Male groups are involved in rickshaw or cart pulling, buffalo carting and other transport services, some are involved in crafts hide and skin preparation, shoe making, pottery making, carpentry, broom making, weaving. Their ingenuity in the endeavour to survive appears inexhaustible. Common to them is the competence to make a living from it. Their resource management skill, a fair treatment as respected bank clients, plus access to loans and financial services along with a newly established group oriented saving habit has contributed to a new conscientization of the poor (predominantly women), which allows them:

- To overcome circumstances where nature intervenes frequently and erratically in the economic system, by building up financial resources and use them as social security and risk management system;
- To start to control forces of socio-economic exploitation by landlords, moneylenders, bureaucrats, traders by using credit for extending income generating activities. (These forces were interacting during disaster situations - in a way which had earlier aggravated the distress enormously);

- With additional self-employment and increase of income from investments: To overcome the gap between income flow and consumption;
- The socio economic source for dependence and exploitation relationships (low wages, exorbitant interest rates for loans, bondages etc) along with impacts of natural disasters is gradually controlled and the social process of SHG members escaping from poverty is gaining momentum. SHG Bank Linkage Programme gets through to the poor section of village India; and the SHGs have become gradually very efficient moneylenders (also to non-members, to the village panchayat etc.) earning good interest-income for distribution to their members at every year end;
- New discovery of bankers and the society: Poor people are reliable and honourable they gain pride and dignity. They are aware: The only way to combat their problem of poverty and dependence is by acting together as a group. Their ideas centre around the most rational use of money and on the collective production of goods and services. The most preferred input is credit. **Credit is a catalyst. It comes and goes but leaves behind some changes.**

8. Acceptance of SHG-Banking by the Formal Banking System in India

SHG-Banking has become a **big challenge to the Formal Banking System** in India and has led to a process of **“downscaling” (Seibel) and new capacity building in banks to handle SHG-Banking:**

(1) SHG-Banking looks as an escape from well established banking practices, which required written contracts with individuals, a clearly defined activity for loan use, which has been exclusively one-purpose oriented, required legal character of the borrower, collateral, etc. When it comes to banking with the poor, the most rigid requirements of the formal banking

system have been overthrown; SHG-Banking cannot be described in the usual frame of credit policies and bank management (“Bankers as an instrument of a credit delivery mechanism of the Government” following exclusively Government instruction and not their own professional intuition in doing bank business). SHG-Banking is therefore an extremely innovative approach in banking;

(2) It allowed substantial freedom to operate in the low income client market segment which was not considered bankable so far. SHG-Banking allowed a flexible and more unregulated service design and most flexible credit product design in order to fully meet the requirements of the low income households and particularly of women;

(3) It requires different attitudes and a different motivation of bank staff involved in SHG-finance to do “social banking” with the poorer section of the village society and especially with women. And to do this banking purely under commercial conditions;

(4) Those bankers handling the SHG-Banking portfolio enjoy a complete new banking experience: Very careful and sensitively conceived loan applications by SHGs, near perfect loan recovery, the discovery of financial discipline and money allocation skill of poor people and their reliability, entrepreneurial (including money lending) capacity and dignity;

(5) SHG-Banking gave the participating bankers who we met during our field survey a new dimension of job satisfaction that they never had experienced before in “directed lending regime”!

(6) SHG-Banking initiated a change from supply oriented “directed” loan delivery to demand oriented service structures; but the programme does not necessarily entail provision of advisory services support to low income people

- except in some cases of NGO promoted SHGs - ("Banking by the People")

(7) SHG-Banking made subsidiary attitudes towards autonomous SHGs possible and contributed to challenge the traditional banker's attitude of interference and a belief that the banker has all the solutions for his client;

(8) SHG-Banking is predominantly women oriented (feminisation of microFinance).

The dimension and new flexibility in SHG-Banking as practised now in India is unmatched in the World's Banking System.

Impact on the formal banking set-up

Many formal bank branches and bank branch managers feel comfortable with the SHG-Banking concept; they feel safe in their jobs and seek to continue serving their bank in the new programme. There is less staff turnover. They have accepted the challenge of becoming more flexible and innovative on their own; the "can do" attitude of the staff is becoming very obvious; they are still trying to find own solutions in organising the most appropriate services to the SHGs: be it at the bank branch office level or directly at the doorstep of their village clients or at the group meetings. So far, staff travel time and costs are less as compared to those of newly established MFIs, which normally serve on a weekly basis at the doorstep of the poor. The methodology of covering 12-20 member groups rather than 5 member groups is more acceptable to the staff.

Most important: Deficiencies of the Government directed credit programmes and the frustration of the ordinary bank staff have not been transferred into the SHG Bank Linkage Programme approach. SHG Bank Linkage Programme as a new strategy to provide

microFinance services through the already established Banking System reflects a break from the conventional wisdom of development banking and supply led finance schemes of conventional banks. A conventional commercial bank, or an agricultural credit and extension agency, operate as an entity, as something cognitively different from its social environment. The staff interacts with customers/ individuals in a very limited way and relationship is mostly impersonal. **SHG-Banking in India, however, is formative in the sense that the bank partner after issuing a loan participates in the formation of a new social and economic environment by the SHG members by paying visits to SHGs or by participating at their group meetings from time to time, not regularly!** This social development function by providing financial services to SHGs of poorer families exclusively (and paying them a visit from time to time) has been accepted by the banks and by the new clients.

A new innovative role is given to the formal bankers and this role is highly appreciated by them. Management and staff members work creatively together, comforting themselves with openness, perceptiveness and self confidence. In Linkage Banking staff become good performers by virtue of what their organisational environment allows them to learn and act. The leadership (CEOs, Managing Directors) can be the most serious bottleneck or the motor for inspirational operations of the staff. Social accountability and participation emerges. **Corruption is not reported and transparency of transactions with SHG is assured.** A constant increasing number of new SHGs, an increase of the amount of loans disbursed and an excellent loan recovery performance has created **a new job satisfaction among the bankers.** Many bankers show tremendous satisfaction to report about the socio-economic achievements of their groups.

There are a number of indicators showing that the gap between formal bankers and rural poor has been bridged:

- The number of civil suits have reduced
- Overdue loans outstanding for longer periods are increasingly repaid
- People showing substantial interest in a permanent relationship with **“their”** bank (no evidence for “hit and run”)
- Songs and other PR-relevant measures of people praise the role of bankers
- More and more Chief Executive Officers committed to SHG-Banking
- More job satisfaction among the bankers involved in SHG-Banking
- Concept of cost externalisation of giving micro-loans to poor successfully implemented
- High potential for increased outreach of formal banking shared by the bankers
- Assistance in putting up SHG owned financial assets governed by people as important as continuous feeding with new bank loans of the Government and loan cascading.

The potential of SHG financing is especially seen and the approach accepted by RRBs. They see also other external effects when handling the SHG-Banking portfolio like

- recovery of old outstanding loans in the villages because of greater acceptance,
- new loans to individuals are considered less risky if a family member is member of a SHG.

The cooperative banks are late entrants but they start to realize the latent strengths of the programme in form of profitable transactions with SHGs. They may move into SHG-Banking to a much greater extent now in the immediate future. Similar insights have been gained from very positive achievements in Commercial Banks. They reported neither conflicts nor frustrations when entering SHG-Banking. More commercial banks show increased interest in SHG-microFinance portfolio.

9. Why could SHG-Banking achieve such good results

There are a number of reasons and enabling conditions that support SHG Banking:

(1) 2155 NGOs involved in group formation creating the preconditions (homogeneity, solidarity, discipline and absorptive capacity for loans) in SHGs for linkage with banks;

(2) The concept of SHG-Banking has fully honoured the needs, wisdom and discipline particularly of low income women, who were living under extreme economic pressure and uncertainties, to manage their financial operations according to their day to day as well as business needs;

- they have gained risk management capacities, enjoy now a new dimension of social security.
- Loans allowed them to add new micro-entrepreneurial activities to the family's source of income, to a greater diversification of the sources of income of the household, to smoothening the income stream and building up additional productive and financial assets
- They feel liberated from exploitative labour relationships and financial bondages;

(3) Low cost and interests charged to SHGs: When microFinance through SHG-Banking is taken up as an additional new business proposition in the existing Banking System there is a **substantial institutional cost advantage as compared to the establishment of highly specialised new microFinance Institutions (mFIs):**

- No additional basic institutional build-up cost until break-even are required;
- No expenses for putting up an Apex system for microFinance or a new microFinance institutional network with someone having to cover the cost for the new built-up: clients, government, donors;

- The existing banking system and NABARD can offer the services for introduction of Linkage Banking at cheaper rates.

(4) Excellent human capital already existing in banks and professional banking know how available, which can be additionally used (only marginal additional training required to handle a MF-portfolio and to work with SHG clients) though the rigid mindset of bank officials at different levels and at different banks is still not fully overcome. New mFIs have to spend a big amount of money to recruit, to train and to put new bank staff in a bank position. Most of them are very young and inexperienced; there is a high drop out rate among these youngsters.

(5) The existing banking know-how in the formal banking system in India is appreciated and acknowledged by SHG-clients. Clients and SHGs prefer to put their savings into a formal bank;

(6) Participating banks feel for the first time that this part of banking is not a losing proposition but this portfolio has earning capacity possibly immediately and even more so in the future because it is giving them the chance to extend their client base substantially and to improve their banker's image;

(7) The sensitive programme design by NABARD, the apex funding (and promoting, training and guiding) organisation of the linkage banking approach, has found much appreciation among the banking partners; the promotion of the SHG-Banking-concept by NABARD's regional staff and training staff has been praised and the management of the programme by the whole NABARD-system at Apex and - with some variance - at regional level is very effective; the strong commitment of NABARD CEOs cannot be overlooked.

When asking participating bankers and NGOs, NABARD's following services were most appreciated in addition to its policy advocacy role:

- Refinance to banks at 100 % at a concessional rate of recently changed to 6.75% p.a and financial assistance given to banks to function as promoting institutions
- Workshops, training programmes, seminars at different levels for bankers and NGO employees in order to build trust and confidence between the banks and the rural poor
- Facilitating training of bank officials and field staff of NGOs
- Providing selective capacity building support to NGOs, SHGs, Federations of SHGs, related institutions in form of revolving fund assistance, training facility and other support.

(8) Initial conceptual support from APRACA-programme "Linking Banks and Self Help Groups" the information available from similar externally sponsored projects in Asia. The facilitation by SDC through flexible funding support was also critical for upscaling training and sensitisation approaches and experimenting with other non-NGO SHPIs;

(9) Role of Reserve Bank of India:

A special role in the implementation of Linkage Banking was the policy support of RBI. RBI gave appropriate guidelines and circulars to the banking system to take up the programme. The RBI's initiative of permitting informal entities like SHGs to open savings bank accounts in formal institutions was instrumental in providing the necessary thrust to the programme at the pilot phase itself. Further, it also enabled the banks to deregulate the lending conditions and to allow the interest rate to be fixed according to market conditions. The built-in-flexibility for the start-up period of the programme has not yet been narrowed by restrictive regulations. SHG-Banking was made a component of priority sector lending

for Commercial Banks, for RRBs and for Cooperative Banks. The terms and conditions allowed banks to consider mainstream financing of SHGs as a business activity (not only because of the additional volume of lending).

10. Risks in SHG-Banking as implemented by the Formal Banking System.

The receptivity of the participating Banks as Self Help Promoting Institution (SHPI) by the rural women or poor people in general who hardly had any bank support so far has been remarkable. But certain problems should not be overlooked.

(1) Equal Distribution of Benefits in SHGs with Members not exclusively from very poor Community

Because of restricted capacity of branch staff they tend to implement a simpler SHG-formation concept and are not so much concerned, if the established linkages are self-sustaining or not. They mobilised SHG-members and assisted in forming groups that do not necessarily represent the poorest of the poor in the villages **but those who had no bank access yet**. The first impression we could gain from SHGs organised with bank support and served by bankers is that they may represent a different quality as compared to NGO backed SHGs. All SHGs have one orientation in common: They want primarily access to regular bank services which had been so far refused to the individual poor families and want to start an internal saving and lending activity in support to their members. In comparison with NGO-SHG the Bank-SHG relationship does not carry additional social development oriented tasks to be implemented by the SHG (family planning, eradication of drinking habits, scholarships for orphans or young girls, feeding school children, introducing house-toilets etc, for which the “group approach” is also used today in India). Some of these additional activities are done in NGO supported SHGs with a broader development agenda.

In SHGs, which have been newly formed by Banks to provide them access to bank loans, the question of how to avoid unequal distribution of benefits turns up. Despite the spirit of solidarity it may not completely be avoided over time that the benefits from the SHG-system may not be equitably enjoyed and one member in a SHG may not be as successful when using a new SHG loan compared to another one who may economically lag behind. There may be some buffering mechanisms practised inside the group like delaying the prospering member's new (additional) loan until the others achieve the same standard. There are also other mechanisms like credit prioritisation and non-disbursal of second loan to a member until every other interested member of the SHG takes a loan. In addition the impact assessment of the SHG-Portfolio in regard to achievement of the social development agenda (eradication of poverty) is to be continued. Poverty eradication may hopefully be an indirect outcome of the SHG-Banking strategy (though it is not the exclusive concern of SHG-Banking).

(2) Avoiding diminishing Returns from Microenterprise Investments

Uneven distribution of benefits has been one reason for individual members to leave the SHG at a later stage and form a new group on its own. In villages with already existing and good performing SHG-groups one can observe a constant addition of new SHGs. But with limited know-how and alternatives available for investment within the village economy - diminishing returns from consecutive disbursements of loans for additional investments in existing micro-enterprises for income generating may become unavoidable.

Watershed rehabilitation schemes (like in Maharashtra and Karnataka) and Dry Land and Water conservation schemes (like in Bihar) were creating new opportunities for very productive investment of poor households and have provided best platforms for establishing successful and fast

growing financial SHGs. In this respect, strategies to maintain and establish new innovative business opportunities for SHG-members may become essential in the near future and banks may have to play a more active role in it (**organising up-and downstream contractual arrangements with established enterprises, supporting the organisation for on the job skill training of SHG members** etc).

(3) Stability of Bank-SHG

SHG-Bankers - besides assisting in group formation - do not undertake many more interacting functions besides offering saving and credit services to carefully selected SHGs because of extreme time constraints and lack of personal. There is also no permanent effort undertaken to change the people's attitude and behaviour by constant supportive educational interventions starting from changing traditional attitudes (dowry system, bad drinking habits of husbands etc) to family planning and to new practices in agriculture, horticulture or business management etc. There is no special service offered which is related to the social and economic development of individual SHG members! Within the participating banks no organizational change is foreseen to ensure their optimal suitability for SHG-Banking in regard to SHG capacity support.

But questions do arise regarding the **stability of the groups**, regarding the continuation of the Bank/SHG-relationship and regarding the development of the future business transactions with this client segment? Will the good loan disbursement and recovery performance remain in the future? There is no constant and systematic evaluation of the performance of the existing SHGs. Bankers seem to feel: As long as the loan recovery from SHGs is showing good results (as compared to the "directed loan"- portfolio) there is no need for follow-up or a trouble-shooting service in order to avoid that

something is going wrong inside the SHGs. Formal Bankers - target oriented as they have been in their past performance - are of course oriented to increase the number of new groups as quick as possible and the loan amounts disbursed to them. Saving mobilization is so far only an instrument for making the group bankable as soon as possible. And they may see the present business relationship with SHG only as an interim step in their lending business which also could be continued later with individual group members as already done with depositors who put their additional voluntary savings at their individual account with the Bank. The purpose of additional clients getting access to bank services would be achieved but it may be of great concern, if the same portfolio quality could be maintained as well with individual small former SHG-member clients.

As long as there are no significant identifiable weaknesses yet in SHG-Banking the Banks will be not so much concerned with establishing more SHG internal checks and controls by bank staff or a dual control by NGOs or SHG-Federations. But the need for a problem solving mechanism may arise in future loan transactions when loan amounts outstanding are increasing and internal problems do arise which may require an external moderator! What may be noticed today is a lack of correct book keeping in some selected cases. Management of SHGs, term-lending skills, credit risk management policies may also contribute to the sustainability of financial SHGs in the future- after the first enthusiasm about innovative Self Help Group Banking is over.

The following solutions have been already developed and should be strictly applied:

- (1) NABARD and NGOs have developed instruments for proper rating of SHGs - for self-evaluation of the organisational strength and the participative discipline of the members, which the groups or the bank partner

could use for evaluation. More use should be made of the instrument for credit appraisal, assessing capacity building needs etc and to ensure that corrective actions are undertaken in case the rating instrument shows increasing tensions in the group.

(2) Participating banks may develop organizational tools and problem solving mechanisms for an effective facilitation of SHG sustainability in performing their banking and economic function and for adjusting the Bank's organisation for better management and supervision of the SHG-portfolio as well. The possibility of defaulting, poor fund management and accounting, poor self evaluation leading to SHGs breaking apart etc. can only be countered by intensive supervision of the SHGs and by a monitoring and evaluation system that gives early warning signals. But this is a complex challenge. It requires a high degree of organisational talent, creativity and hard work by the bank staff. And it can become a substantial cost item. New staff could be added to those branches with high SHG-Banking portfolio, interest rates could be increased to reflect higher cost in serving SHGs at their doorstep more regularly and to operate a problem shooting or problem solving mechanism service. More female group organisers and loan officers could be included and a regular quality control or regular reporting of SHGs to the bank could be considered. Group dynamism in maturing groups should be observed and trainers should be included in monitoring and evaluation of the programme. They also should play an active role in group's problem solving.

(3) Based on own initiatives or external support - SHGs could establish SHG-federations, which could attempt to provide support to achieve financial viability and sustainability to SHG banking.

(4) NABARD may gradually support more and more of newly upcoming private microFinance institutions (MFIs) in the Non-Government microFinance Sector (NGMS) which

exclusively target the poor and undertake great efforts to stabilize their groups and undertake substantial development activities with them. But the essence of their bank's mission is to provide a very comprehensive strategy inextricably linked to economic development and social development of the poor exclusively (as for one example: Banks considering dowry an economic burden which the poor can ill afford and working hard to motivate people to marry without it; if not credit will only serve to inflate dowry payments). NABARD support should also include a special institutional development grant (start-up capital, scaling-up capital, additional equity support) based on a clear understanding on the growth path of a new microFinance institution with particular indicators for each institutional development level with level specific financial support. Also a problem solving advisory service for breeding new microFinance institutions may be required.

(4) Availability of adequate Saving Products to SHGs and to their Individual Members

The return on investments are still small for much wealth to accumulate, the family still facing a number of unpredictable events from illness to floods; there is not much except the accumulated SHG-savings to offer them security in the likelihood of emergencies. SHG-Banking as a financial market intervention targeting poorer people should also focus on providing secure and convenient **deposit facilities** to groups and individual members of groups. Our findings from the field made clear that there is substantial scope for introducing new saving products and insurance products for groups as well as for individuals.

It would be desirable that each borrower has access to a personal savings account with the bank (from where a member client can withdraw any amount at the time she desires instead of taking a loan from the SHG). In addition a pension or life insurance saving account should be introduced based on the experiences collected from the GTZ pilot project in Karnataka and from SEWA.

Some members asked for a special saving account to cover the risks of hospitalisation, loss of houses or assets or for meeting dowry expenses. The annual premium of the most popular insurance package of SEWA (covering death, hospitalisation, loss of house to a certain amount) equals Rs. 85 (about US \$ 1.8) and the maximum insurance sum that would be paid out in case of destruction of a house and assets would be Rs. 5000 (US \$ 105). More own financial assets and insurance cover would gradually contribute to a reduction of loan demand of the poor for emergencies and special risks.

In addition to savings for purchasing a life insurance cover, a cover against theft and loss or damage to livestock or crops should be included as far as possible. More own financial assets and insurance cover would gradually contribute to a reduction of loan demand of the poor for emergencies and special risks.

Some SHGs considered the establishing of a loan loss reserve fund as a useful instrument to meet loan losses from members by deducting a small percentage from every loan amount disbursed to members or by requiring from the borrower putting in a small amount of money in a loan insurance saving account at the end of the year.

In SHG-Banking there is also a lack of special saving schemes for specific functions: covering the risk of default of individual members (reserve or emergency fund from special emergency savings), and acceptance of individual savings deposits in addition to the collective saving scheme (individual deposit banking). And acceptance of special savings from individuals (including in future a shareholder scheme for progressive SHGs to ensure equity capital for SHG Federations to start with own banking) could be accommodated in the SHG-Banking Approach.

In addition, the earning capacity of banks from increased SHG savings and individual member savings and future individual lending should be clearly assessed.

(5) Analysis of SHGs not succeeding in Linkage

There may be also groups that could not establish effective Bank linkages and nobody knows their number and the reasons (expecting subsidies only?). An evaluation of the experiences with those groups should be included as well in order to learn from potential failures in the group formation process. Sometimes failure stories tell us more than success stories.

Annexure I

Design Features of the product

1. **Small and fixed savings at frequent intervals:** Small and fixed savings made at regular intervals coupled with conditions like compulsory attendance, penal provisions to ensure timely attendance, saving, repayment etc forms a deterrent for the rich to join the SHG system- thereby enables exclusion of the rich.
2. **Self-selection:** The members select their own members to form groups. The members residing in the same neighborhood ensure better character screening and tend to exclude deviant behaved ones.
3. **Focus on women:** As regular meetings and savings are compulsory ingredients in the product design, it becomes more suitable for the women clients- as group formation and participatory meetings is a natural ally for the women to follow.
4. **Savings first and credit later:** The saving first concept enables the poor to gradually understand the importance of saving, appreciate the nuances of credit concept using their own money before seeking external support (credit) for fulfilling future needs. The poor tend to understand and respect the terms of credit better.
5. **Intra group appraisal systems and prioritization:** Essentials of good credit management like (peer) appraisal for credit needs (checking the antecedents and needs before sanction), (peer) monitoring - end use of credit; (peer sympathy) reschedulement incase of crisis and (peer pressure) collateral incase of willful non-payment etc all seems to coexist in the system - making its one of the best approaches for providing financial services to the poor.

6. **Credit rationing:** The approach of prioritization i.e.: meeting critical needs first serves as a useful tool for intra-group lending. This ensures the potential credit takers/users to meticulously follow up credit already dispensed, as future credit disbursements rely on repayments by the existing credit users.
7. **Shorter repayment terms:** Smaller and shorter repayment schedule ensures faster recycling of funds, greater fiscal prudence in the poor and drives away the slackness and complacency that tends to set-in, in long duration credit cycles.
8. **Market rates of interest:** Self-determined interest rates are normally market related. Sub-market interest rates could spell doom; distort the use and direction of credit.
9. **Progressive lending:** The practice of repeat loans and often-higher doses - is followed by SHGs in their intra-group loaning, thereby enticing prompt repayments.
10. **A multiple-eyed operation:** The operations of the SHG are transacted in group meetings thus enabling high trust levels and openness in the SHG system. The banking transactions are also generally conducted by SHG members facilitating openness and freedom from unfair practices.

The product design features combine the collective wisdom of the poor, the organizational capabilities of the social intermediary and the financial strength of the Banks

Annexure II

MILESTONES IN SHG-BANK LINKAGE PROGRAMME

Year 1992	Launching of Pilot project of linking 500 SHGs with the banking system.
1993	<p>Introduction of bulk lending scheme to NGOs by NABARD.</p> <p>Studies on Transaction Cost conducted by external experts.</p>
1994	<p>Extension of policy Support by RBI - beyond the Pilot phase.</p> <p>Unleashing the concepts of banking with poor.</p> <p>Extension of support for capacity building of NGOs by NABARD.</p>
1995	<p>Setting up Credit and Financial Services Fund (CFSF) within NABARD - to support expansion of the programme.</p> <p>Setting up a working group on NGOs & SHGs - to assess ground realities and identify operational issues in implementation of the programme.</p> <p>Extension of Revolving Fund Assistance to Federations of SHGs by NABARD.</p>
1996	<p>Mainstreaming SHG-Bank Linkage by banks - RBI and NABARD notifications.</p> <p>Tackling operational issues</p> <ul style="list-style-type: none"> ■ Documentation ■ Defaulters ■ Size of group ■ Service Area etc

1997	<p>Organizing National level Training consultation meet - thrust on trainers training.</p> <p>First experiment of RRB as Self Help Promoting Institution (SHPI).</p> <p>Up scaling training and awareness programmes by NABARD and the banking system.</p> <p>Emphasis on interventions winning in cooperative banks.</p>
1998	<p>Recognition of potential of government intervention.</p> <p>Extension RRB as SHPI to other 10 other RRBs.</p> <p>Documentation of rating/grading practices for SHGs' appraisal.</p>
1999	<p>Recognition of potential of SHGs by GOI.</p> <p>Setting up task force on supportive regulatory & policy framework.</p> <p>Refinance requirements out grow CFSF - use of NABARD's normal resources.</p> <p>Extension of RRB-SHPI-experiment to 2 more RRBs.</p> <p>Crystallization of NABARD's vision and Mission.</p> <p>Building partnerships with Governments.</p> <p>Deregulation of interest rates in SHG lending</p> <p>Emphasis on studies documentation and dissemination.</p> <p>Provision of promotional grants to NGOs for SHG promotion- development NGO appraisal tools.</p>

2000	<p>Thrust on widening the range of SHPIs.</p> <p>SHGs credit linked crosses 1,00,000.</p> <p>RBI advises banks to finance Microcredit organizations.</p> <p>Emphasis on flooding market with quality SHGs by NABARD.</p> <p>Thrust on expansion of the programme in Union Budget.</p> <p>Recognition of potential of Farmers Clubs as SHPIs.</p> <p>Roping in Rural Volunteers as potential SHPI.</p> <p>II National Consultation meet on training to redesign training modules, contents and methodologies.</p> <p>Collaboration with Indira Gandhi National Open University - for commencing a distance education programme on women's empowerment and SHGs.</p> <p>Introduction of State level Awards for best performance.</p> <p>Evaluation studies on impact on SHGs.</p> <p>Setting up a separate fund for scaling up the programme-microFinance Development Fund.</p> <p>Technical collaboration with GTZ, Germany commenced.</p>
2001	<p>Crossing 2,00,000 mark of credit linked SHGs.</p> <p>Thrust on backward States & districts.</p> <p>Extension of RRB-SHPI module to all RRBs.</p> <p>Launching of National Level newsletter.</p> <p>Diversifying capacity building approaches - Videos, tools, visits.</p>

	<p>Accelerating promotional grant support to NGOs.</p> <p>Conceptualizing the use of technology in microFinance.</p> <p>Initiating efforts all developing a comprehensive Management Information System for SHG -Bank Linkage programme.</p> <p>Exposure visits to other mF initiatives for clients and banks.</p> <p>Launched studies to assess Savings pattern for the poor.</p>
2002	<p>Intensifying training interventions through exposure visits.</p> <p>Focus on backward states/provinces</p> <p>Encouraging and facilitating internalization of rating and self-rating techniques.</p> <p>Increasing role of Government in internalizing the concept.</p> <p>Launching a pilot in IT in microFinance.</p> <p>Launching studies to understanding the commercial prospects of SHG linkage.</p> <p>Closer look at saving products for the poor-designing pilot project for savings product development through an RRB.</p> <p>Support by way of promotional grants to NGOs closes to 500 nos.</p> <p>About 50% of the 10-year mission covered.</p> <p>Diffusion of knowledge and experience with international mF practitioners.</p> <p>Redefining the role of banks in the programme as enhancing business opportunities NOT mere Service providers.</p>

(Source: NABARD, Mumbai)

Other Studies in the Series

Promotion of Self Help Groups under the SHG Bank Linkage Programme in India - An Assessment
by Malcolm Harper



The role of Self Help Group Bank Linkage Programme in preventing Rural Emergencies in India
by Kim Wilson



Self Help Group Bank Linkage Programme for Rural Poor in India - An Impact Assessment
by V. Puhazhendi
K.C. Badatya



Commercial Aspects of Self Help Group Bank Linkage Programme in India
by Dr. Hans Dieter Seibel
Harish Kumar R. Dave



Impact of SHG Bank Linkage Programme on Social Indicators and Empowerment of the members
by Aloysius Fernandez,
MYRADA



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This image shows a blank page from a notebook or ledger. The page is white and features horizontal ruling lines spaced evenly down its length. On the left side, there is a light blue vertical margin strip containing the number "56". The rest of the page is empty, with no handwriting or other markings.