Resuscitating Rural Financial Institutions in India: Catalytic Role of Micro Finance

Manoranjan Sharma[1]

"With doubt and dismay you are smitten,
You think there's no chance for you, son?
Why the best books haven't been written,
The best race hasn't been run."

Berton Braley

Perspective

Post independent India witnessed the evolution of an elaborate network of rural financial institutions (RFIs) in India and radical changes in their focus, structure and approach in conformity with the changing requirements. However, high transactions cost, absence of physical collateral by small borrowers and inability to submit proper loan proposals hampered increased flow of credit to the rural poor. Despite the mutually reinforcing approaches of focus on overall economic development (through percolation/trickle/ spread effect) and poverty alleviation programmes beneficiary targeted direct intervention), the financial services of the formal banking system remained inaccessible to the majority of the poor people in the rural areas. Cross-country experiences reinforced the view that development pushed from above by the state distorted accelerated industrialization (Korten, 1981: Stohr and Taylor, 1981; Schumaker, 1973). The 'power of finance' (to borrow the title of the powerful book by David Hulme and Paul Mosley) led to the emergence of the concepts of "development from below", "grassroots development", "development as if people mattered", "self-sustaining development", "self-empowering development", etc. In the Indian context, the Report of the Agricultural Credit Review Committee of the RBI (1989) poignantly pointed out: "the aim of serving the poor (through the banking system) has ended up by giving poor service".

Against this backdrop, it was increasingly realised that poverty and social justice must constitute integral elements of the overarching framework for

[1] Chief Economist, Canara Bank, Head Office, Bangalore. The standard disclaimer applies.

national policy formulation. What was needed was a direct assault on the deeply ingrained problems of poverty, unemployment and inequalities in income and wealth, which perpetuated class divisions and gender discrimination. This direct assault on the persisting problems of high illiteracy rate, abominable state of health care and extreme lack of social justice in the Indian economy is impossible without a paradigm shift in RFIs - a paradigm shift which stresses elements, such as, strategic flexibility, e-business strategy, technology management flexibility, streamlined information system, strengthened internal control system, etc. While community organising, training and one-way flow of resources through grant mechanisms may be helpful, the provision of benefits extended might not enhance the ability of the people to act for themselve and thus may not be sustainable in the long-term. This necessitates a shift from welfare-oriented approaches to sustainable, market-based, decentralising authority and local resources.

In the absence of an adequate social safety net for the vulnerable sections of society and the inaccessibility of the formal banking system, the rural masses were constrained to rely mainly on informal sources of credit. Several regions of the country continue to be mired in poverty, unemployment and overall socio-economic backwardness. The credit needs of the rural poor are determined in a complex setting, which makes it difficult to adopt project lending approach as followed by banks and the blurring of the dividing line between credit for 'consumption' and 'production' purposes. While credit is a pre-requisite of any economic activity, credit *per se* may not necessarily lead to economic development for the vast masses of India. We need, therefore, to optimise the use of credit by qualitative deployment in socio-economically-productive channels to sustain development.

Studies on informal groups by National Bank for Agriculture and Rural Development (NABARD), Asian and Pacific Regional Credit Association (APRACA) and International Labour Organisation (ILO) brought out that Self-help, Savings and Credit Groups helped to streamline the existing credit delivery mechanism by increasing the outreach of credit and enhancing the viability of institutions purveying rural credit. While the outreach measures the absolute number of households or enterprises (or relative market penetration) in the target population reached by the population, the depth measures the number of under served (women, minorities, and rural poor) served by it, who were traditionally by-passed by formal credit institutions. In recent years, a concerted attempt has been made to bring about larger coverage of rural clients but there still exists considerable potential for exploitation (Bhupat Desai and Namboodiri 1994 (a) and (b); 1996). Micro credit and poverty alleviation programmes are inextricably linked because of the potentiality of micro credit programmes to link the formal banking structures with the rural poor by stimulation and mobilisation of savings and promotion of entrepreneurial endeavours.

Replication of Western Institutional System

The western institutional system cannot easily be replicated in vastly different Indian conditions because of different institutional environment and the prerequisites of attendant institutional structures. The case for intervention of the Government in the sphere of rural credit emanated from well documented market failures because of the difficulty in achieving allocative efficiency in a competitive and information system (Gamini Herath 1996; Stiglitz 1990). As such, the intervention took the forms of government ownership of banks, branch expansion, subsidisation, selective allocation of credit, etc. But the operation of these policies accentuated 'financial repression' characterised by regulation of interest rates both deposit and lending, large preemption of resources by government at rates lower than even the cost of raising them, cross-subsidisation of interest rates, high level of non-performing assets (NPAs), etc. resulting in gross overall inefficiency of the financial system (Timothy Besley 1994).

Rural credit markets are characterised by high cost of legal enforcement, imperfect information, collateral security, underdevelopment in complimentary institutions and covariant risks. Consequently, a number of alternative strategies have to be devised to attract greater inward investment and unleash latent indigenous potential in the form of entrepreneurship and helping existing business to realise their expansion plans. This requires the active involvement and full support of rural banking in the country. Thus the concept of rural banking has itself become an issue of debate and discussion. The main strands of this debate bring into question the known paradigms of rural banking, direction of development for fostering dispersed industrial growth and the attempt to replicate western models of development without considering the socio-economic conditions peculiar to India.

Institutional Streamlining

Institutions are defined as a set of constraints, which govern the behavioural relations among individuals and groups. Institutional development could be enhanced by strengthening of institutions, promotion of sustainable and equitable agriculture, effective credit support, improving the outreach of the banking system, modification of the regulatory framework and the promotion of competition and privatisation. In conformity with the winds of change sweeping the country, an efficient and performing rural credit delivery system must be an integral part of any design of rural development.

Co-operatives are basically concerned with provision of credit and other inputs to the members to support production, particularly the agricultural production and provision of post-harvest support to farmers. The cooperative credit sector consists of State Cooperative Banks (SCBs), District Central Cooperative Banks (DCCBs), Primary Agricultural Credit Societies (PACS) / Large Size Adivasi Multipurpose Societies (LAMPS) for meeting production credit needs and State Land Development Banks (SLDBs) and Primary Land Development Banks (PLDBs) for meeting investment credit needs. The co-operatives provide the critical forward and backward linkages to their members, enhancing the technical feasibility and in turn the viability of the activities undertaken by them. Their strength lies in the elaborate organisational network extending from village to the national level. Despite these impressive features, the performance of the cooperative banks has been unsatisfactory because of the complex interplay of organisational, financial and managerial inadequacies of the cooperative credit system. This is starkly reflected in the fact that 8 SCBs and 144 DCCBs failed to comply with the basic requirement of minimum paid-up capital, i.e., provisions of Section 11(1) of the Banking Regulation Act, 1949 (As Applicable to Co-operative Societies) as on 31 March, 2003. The floundering of RFIs is, therefore, a cause for concern and forces us to look at the future with some trepidation.

A comprehensive assessment of the Indian rural credit scenario also requires an analysis of both the formal and the informal sector. An elaborate network of the formal sector, as it has evolved in the post-independent India, relates to multi-agency institutional credit structure comprising 91 commercial banks, 196 RRBs and 1,149 co-operative banks. Thus there are today 1,34,000 rural credit outlets, i.e., one branch outlet for every 4,700 population. However, 39 per cent of rural indebted households continue to be served by informal credit sector comprising money-lenders, indigenous bankers, friends, relatives, traders, etc. Non-Governmental Organisations, Self Help Groups (SHGs) / Federations and Credit Unions also play an increasingly important role in credit dispensation.

Dynamics of Credit Dispensation

The basic framework of the credit dispensation attempted to increase the quantum of credit for improving production and productivity without being oblivious to the credit requirements of the vulnerable sections of the society and backward areas. There has, however, been significant changes in the share of various agencies in institutional credit to agriculture and allied activities with the shares of CBs and RRBs rising from 40 per cent in 1987-88 to 50 per cent and from 1 per cent to 10 per cent during 2002-03 and the share of co-operatives declining from 58 per cent to about 40 per cent during this period. This could be explained by an increasing body of evidence, which shows that co-operative banks failed to play their due role in the achievement of avowed objectives of economic development because of duality of control, high incidence of loan delinquencies, mounting NPAs and heavy accumulated losses caused by poor income, high cost of management, injudicious funds management, poor deposit mobilisation, excessive reliance on funds from higher financing institutions, blocking of CCB's funds towards Cadre Fund, etc. Thus such changes in sectoral credit are disquieting because even in the US throughout the 1980s, about 25 per cent of all loans were either originated by government agencies or covered by Government guarantees. Further, as IG Patel (1994) demonstrates cross-subsidisation is a defining characeristic of a civilised society village.

While post-independent India, witnessed a remarkable widening and deepening of financial structure, the period since the post 90s in the Indian economy marks a paradigm shift towards a freer, more competitive and transparent economy. But most RFIs continued to suffer from the seemingly intractable problems of high cost of lending, lower interest spread, mounting levels of non-performing assets (NPAs), poor financial position, non-viability, low profitability, etc. Hence there emerged a discernible need to make these banks sound and vibrant not only to enhance the functioning of these banks but also to provide a stable macro-economic environment. It is imperative for the financial performance of RFIs to be above a certain minimum threshold. This has significant implications for the RFIs, particularly in the post-liberalisation phase, as the prudential norms relating to capital adequacy, income recognition and provisioning require RFIs to be sensitive to the issues of cost effectiveness, commercial orientation, widening of products and services, professionalisation of management, accountability, etc.

Micro Credit- Key to Transformation

To be sure, there are gaps in macro approaches (Kaladhar, 1997). While initially there was cynicism about the possibility of success of innovative micro credit dispensation by non-governmental organisations (NGOs), voluntary agencies (VAs) and self-help groups (SHGs), there are now distinct signs of retooling RFIs in designing financial services for rural poor. The resources of the formal banking system can help overcome difficulties in mobilisation of financial resources for economic empowerment of India's rural population, which will significantly influence India's development process. Economic empowerment is usually defined in terms of access to cheaper credit and other micro-finance services, including savings and insurance. Considering the deposit resources of the formal banking system in India and the annual accretions to such deposits, the requirement of reaching the unreached in the country would perhaps constitute a small proportion of the resources of the formal financial sector. There are also several spin-off effects of micro credit for banks. These could *inter-alia* relate to increase in outreach measured by the number of new clients, volume of lending assessed on the basis of incremental increase in the flow of credit and loan recovery as indicated by the total volume of cash recoveries (RBI, 1998).

Micro finance initiatives have been guided by (a) offering cost effective approaches to formal institutions for wider coverage of poor, thereby supplementing their efforts, (b) testing other micro finance delivery innovations as alternative channel and depending on the prospects and potential, synergise the tested alternative channel with the financial system, (c) reduction in adverse selection in target groups, (d) focus on women, (e) development of collateral substitutions and (f) empowerment of poor. What is basically needed is the strengthening of a mechanism of reaching the poor and the unreached - but by no means unreachable - with the resources of the formal financial sector. It has been demonstrated that micro finance revolution is increasingly demand-led as contrasted to the supply-led, state sponsored rural credit and that micro finance is profitable with banks/Micro Finance Institutions (MFIs) adopting a profit-centre approach with customer-friendly savings and loan products. Innovations by several institutions across countries reveal that the poor are bankable and that micro enterprise activities themselves are sustainable. Loans by MFIs move in the band of US $ 38 in case of BKD (Indonesia) to US $ 1,016 by Credit Union - AECP (Senegal) (Christen 1996). It has also been shown (Yaron 1992) that the average size of micro finance differed from US $ 26 in case of BKK (Indonesia) to US $ 18 in case of Grameen Bank (Bangladesh). In the Indian context, loans up to Rs. 25,000 are covered under micro finance. Evidently, micro credit not only provides the means for an alternative paradigm but also situates the terms of the quest for self-fulfilment in the poor and vulnerable sections of society by providing an appropriate institutional structure for rural banking in India.

It is not our contention that micro credit can bring about a metamorphosis in the given socio-economic situation since development requires a multi-dimensional approach. But we do maintain that micro credit by different agencies does help in developing the sense of autonomy of the deprived sections over their own life-choices. By transcending a simple mechanism of credit delivery to enhancing control over resources, micro credit becomes an effective instrument of strengthening poor in India since the poor need no longer be viewed as objects of charity but as socially productive persons. Contrary to popular impression, the experience of countries like Indonesia, Thailand, Bangladesh, Bolivia, El Salvador and India demonstrates that women do not constitute high-risk clients but are a good banking risk. For, as the Micro Credit Summit held in Washington from February 2-4, 1997 revealed that women were adept at thrift and savings, are highly creative entrepreneurs and ensure that earnings go directly to meeting family needs.

Financing of women also provides avenues for profitable deployment of funds of the banking system. Thus financing of women is a rational, relevant policy entirely in conformity with the interests of the banking system itself because of the well documented efficacy of micro credit in credit dispensation, improved loan recovery and removal of poverty. This is why the US First Lady Hillary Clinton maintained in her greeting to the November 1995 Micro Credit Summit Preparatory Meeting: “Micro enterprise is the heart of development because micro-enterprises work - they lift women and families out of poverty. It is called ‘micro’ but its impact on people is macro; we have seen that it takes just a few dollars, often as little as $10, to help a women gain self-employment, to lift her and her family out of poverty. It is not a handout; it is a helping hand”.

As the term suggests, micro enterprises involve level of operations, which are normally small in size and also unconventional in manner and size of operation. Micro credit is usually defined as “small-scale financial services provided to people who work in agriculture, fishing and herding; who operate small or micro-enterprises; who provide services; who work for wages or commission; and other individuals or groups at the local levels of developing countries both rural and urban” (Robinson, 1996). Subsequently the 1997 Micro credit Summit defined it as “programmes that provide credit for self-employment and other financial and business services including savings and technical assistance) to very poor persons" (Micro Credit Summit 1997, Draft Declaration and Plan of Action). This is why micro enterprises are generally considered more relevant to developing countries and micro credit emerges as a key policy variable in promoting economic development across nations with a salubrious impact on the all round development of women. With micro credit now encapsulating a broad vision of life, we need to aggressively expand it on a macro scale in India to qualitatively improve the lives of the vulnerable sections of society. This requires focused attention on high cost of micro credit operations, limited sources of funds for micro credit, determination of suitable rate of interest for extending micro credit to ensure long-term viable operations, networking with locally feasible integrated development projects and business competence.

Some of the basic elements of the required framework to streamline micro credit in India could be: (a) providing thrust and direction to the credit flow by identifying potential areas/ activities, developing sub-sector approach based on potential refining and broad based existing credit packages, (b) meeting the cost of promotion, training and nurturing of SHGs through convergence of resources emphasising modernisation, technology transfer, etc., (c) development of a sound data based information system and dissemination of information, (d) self-financing of services by SHGs, such as, auditing, enterprise promotion, etc., (e) innovative/ supplementary credit delivery models and (f) conducive policy environment.

Hans Seibel has suggested three main strategies to develop micro finance institutions and sustainable micro financial services in India. These relate to (i) a regulatory reform approach, including interest rate deregulation, revised banking law to facilitate the establishment of local financial institutions and effective supervision over local institutions by an appropriate regulatory authority to improve the policy environment of micro finance; (ii) an institutional transformation approach, including adapting banks to the needs of the micro economy, upgrading non-formal financial institutions, linking formal and non-formal financial institutions and establishing new micro finance institutions to improve the financial infrastructure and the micro economy's access to it ; and

(iii) a sound practices approach, including better market research leading to improved product design and improved product delivery to improve the effectiveness of micro financial services.

Role of SHGs in furthering micro credit

The banks being commercial organisations were initially hesitant to reach the large number of poor strewn all over the country requiring access to credit. Hence, grass root level initiatives on the part of several voluntary organisations/ non-governmental organisations (NGOs) became necessary to overcome the reticence of the banks. The banking institutions could help by utilising the existing voluntary organisations in a selective manner on the basis of an assessment of the capability of each such organisation. In several parts of the world, NGOs have demonstrated that promotion of SHGs of resource-poor persons with some basic traditional skills for undertaking different kind of income generating activities could foster proper grass root level initiatives for motivating the banks to extend credit support to such groups at the appropriate juncture.

Micro credit dispensation by SHGs has evoked discussions and deliberations at various fora since these have brought about a kind of silent revolution relating to the financing of the poor. Accordingly, SHGs can constitute a key element in the strategy of empowering women because of their social multiplier effects. This can be substantiated by the fact that around 90 per cent of groups linked with banks were exclusive women-SHGs. The Indian experience demonstrates that some of the key elements of successful SHGs relate to:

- Formation around ‘felt-needs’ of group members.
- Membership generally based on concept of ‘some common economic interest’.
- Evolution of structure and byelaws in line with development and maturity of groups.
- Emergence of a disciplined group evolving and imposing byelaws and contributing to collective deliberation and action.
- Creation of an awareness and confidence building in the target group.

The remarkable success of micro credit institutions, viz. Grameen Bank of Bangladesh, Bank Rakyat Indonesia (BRI), Bolivia Banco Solidario, Banco Sol encouraged planners and policy makers in India to experiment with this non-formal agency for credit. On the basis of the recommendations of the APRACA Seminar, Mysore Resettlement and Development Agency (MYRADA) promoted credit management groups (CMGs) of the poor, which were similar to SHGs and proved to be effective intermediaries of rural credit dispensation. What sharply distinguishes SHGs from earlier approaches is its focus on the credit needs of the poor, whose capacity to save is extremely limited and thus induces economic development in an area where it is needed most. The formation of SHGs as a catalyst for change was encouraged by mounting overdues of the rural banking system, high intermediation cost, burden of subsidised interest rates, write-offs and implementation problems of centrally controlled structures and mechanisms. Given these constraints operating within the system, the scope for a supplementary credit delivery mechanism was explored to remove these constraints to increase the outreach of RFIs without compromising on their operational viability and sustainability. This led to the issuance of Reserve Bank of India's Circular of July 24, 1991 advising commercial banks (CBs) to actively participate in the project for linking SHGs with banks. Subsequently, RRBs and District Central Cooperative Banks (DCCBs) were also advised to collaborate in this programme in an attempt to mainstream micro credit as a bold, ambitious blueprint for reconstruction on a nation-wide scale. The Reserve Bank of India issued a Circular (February 2000) to scheduled commercial banks including RRBs mainstreaming micro-credit and permitting it to be reckoned towards priority sector lending.

A significant instrument of promotion of micro credit in India in a sustainable manner has been the SHG programme and its linkage with banks. Important components of the policy framework relate to refinance to banks for SHG financing, uniform rate of interest on refinance at 6.5 per cent per annum to all agencies, no insistence on security, encouraging NGOs/VAs in promoting and linking informal groups of rural poor with banks, providing support to NGOs, flexibility in selection of activities, loan for both production and consumption purposes, repayment ethics through peer pressure, timely and adequate credit, low transaction costs for banks as well as clients, better repayment performance than under directed lending and socio-economic empowerment through group activities. With a modest beginning in a992, this linkage has made steady progress over the years in terms of number of SHGs financed, bank loans disbursed, number of SHGs refinanced and refinance disbursed (Table 1).

Table1: SHG-Bank Linkage Programme

Cumulative Progress

(As on 31 March)

Year	**SHGs Financed (No.)**	**Bank Loans Disbursed (Rs. Crore)**	**SHGs Refinanced (No.)**	**Refinance Disbursed (Rs. Crore)**
1999	32,995	57.07	32,995	52.09
2000	1,14,775	192.98	94,645	150.13
2001	2,63,825	480.87	2,13,213	400.74
2002	4,61,478	1,026.34	3,40,131	796.47
2003	7,17,360	2,048.67	4,93,634	1,418.80

Source: Annual Report, NABARD, 2002-03.

True, micro credit still forms a small proportion of the total bank credit in India and may, therefore, seem insignificant at the macro level. But this does highlight the imperative need to bridge the yawning chasm between the demand for credit by poor households and the supply of credit by formal financial and social institutions. This view is vindicated by the remarkable success of SHGs documented in several research studies, including those by Singh (1995), Puhazhendi (1995), Gain and Satish (1996), Girija and Satish (1998). In sum, these studies demonstrate that the methodology of participatory poverty alleviation through SHGs is one of the most effective means in line with the present process of economic reforms based on the policy of decentralisation. SHGs are cohesive and are characterised by a strong sense of ownership, voluntary participation, diversified management, leadership skills and provision of ongoing support services for meeting emergent credit needs of its members as decided by the group. With the extraordinary success of SHGs in several states including Orissa, Karnataka, Tamil Nadu, Kerala, Andhra Pradesh and Uttar Pradesh in setting in motion the socio-economic transformation of the rural poor, SHGs emphasising functional literacy, group building and solidarity, conflict resolution and consensus approach now need to be formed all over the country in a big way and increasingly linked to the banks to be meaningful and effective in the present day context. Such linkage like the Shakespearean quality of mercy is 'twice- blessed': it benefits both the banks and SHGs. While banks benefit by (a) dispensing with pre-sanction appraisal, monitoring and post-disbursement supervision, (b) assured recoveries, (c) reduced transaction cost by eliminating large number of small borrowers at frequent intervals and (d) mobilisation of small savings, SHGs (a) have access to mainstream institutions for augmenting their resource base and (b) shift from non-productive to productive activities with consequential increase in income of its members (Puhazhendi, 1995; Girija and Satish, 1998).

The success of the linkage programme and its use by the formal sector as an appropriate credit delivery mechanism also helps in achieving sustainability of community initiatives. Thus the emerging rural scenario and the changing economic milieu necessitated an approach with difference. Accordingly, RBI vide its circular dated April 2, 1996 instructed banks to consider lending to SHGs as a normal lending activity and such lending with flexible margins, security norms, repayment schedules, etc., now forms part of priority sector lending. The primary characteristics of SHG lending need to be preserved by timely credit delivery, cost effectiveness, responsiveness to needs of members and non-discrimination. While earlier programmes with emphasis on charity and subsidy made the development worker's job difficult, SHGs reverse such a dependence syndrome with stress on empowerment and collective decision-making. They, therefore, eminently meet the test of sustainability - physical and financial. While the former ensures the involvement of the beneficiaries in decision-making, planning and implementation, the latter highlights the self-financing nature of the projects.

Sustainability of operations of SHGs could be defined as the ability of the group to continue to function and grow without financial, managerial and other organisational support from Self-Help Promoting Institutions (SHPI) and others on subsidised terms. In other words, financially sustainable SHGs should be in a position to absorb the costs of group formation and nurturing costs, pay market costs for borrowed funds and manage their funds judiciously without any extraneous help.

Apex institutions like SIDBI and NABARD have initiated several measures to promote equal participation of women in the development process by incorporation of gender concerns in planning, monitoring and coordination of credit. Measures taken to foster wider acceptability of SHGs include issuance of detailed operational guidelines to banks, conduct of training programmes, monitoring and 100 per cent refinance to banks on their lending to SHGs/VAs/NGOs at an interest rate of 6.5 per cent repayable over 3 to 10 years. SHGs can be organised in clusters of blocks or districts either by reputed VAs/NGOs and/or at the initiative of branch managers of CBs/RRBs/DCCBs to identify, analyse and address the felt needs of the people.

Linkage of banks with SHGs

The objectives of SHG Bank linkage programme relate to encouraging banking, thrift and credit among the poor, evolving supplementary credit strategies for meeting the credit needs of the poor, building mutual trust and confidence between bankers and the rural poor, members of the SHG save and contribute to a common fund from which small loans are made to the needy members as per decisions of the group. Thus linkage of banks with SHGs has emerged as an innovative modality with demonstrated potential for addressing the key issues of outreach and sustainability. This approach aims at slashing transaction costs and also bringing about markedly improved recovery performance. The SHG programme could be considered as a pre-microenterprise stage for a majority of rural population. While some groups attempt credit management out of their own savings, others rely on linkages with banks. Such linkages necessitate proper credentials, track record, and system of maintaining accounts and records, regular audits in place and manpower for closer supervision and follow-up. Bank finance could be provided either directly to SHGs in a savings to credit ratio varying from 1:1 to 1:4 depending on the past performance of the group or through bulk lending to NGOs/VAs for on lending to the group on the basis of a credit plan submitted by the group. Credit linkage between the SHGs and the banks forges an alliance between the informal SHGs and the formal banks. The resource endowment of SHGs gets enlarged with the support of formal institutions and simultaneously the banks benefit by externalisation of a part of the items of the credit cycle leading to the emergence of a cost-effective and efficient intermediary for raising deposits and advancing loans. The core objectives of linkage were ably summed up by the S.K. Kalia Group as follows: "gradual transformation of the consumption loaning to production purposes and finally to investment purposes for creation of productive and income generating assets by the group members and the community at large... the success of the linkage programme should not be measured only in terms of number of SHGs linked with banks and/or credit extended by banks to SHGs or refinance provided by NABARD there against but also eventually with reference to other socio-economic indicators like creation of employment opportunities, increase in productivity and income, their impact on the standard of living of the poor, reducing illiteracy, improving health, family welfare, social upliftment, etc. Finally, the SHG linkage programme should emerge in establishing a rural micro financial system owned by the people with technical and financial support from the formal banking system." Despite a strong theoretical and practical underpinning, the upscaling of this programme is hampered by several issues, viz., registration, regulation, legal and organizational aspects.

Impact Assessment

The very nature of SHGs makes it difficult to formulate uniform parameters of viable projects for SHGs and scientific development and systematic organisation of management information system (MIS) aimed at achieving the twin goals of sustainability and outreach. Such a streamlined MIS would help to reduce default and delinquency, optimize rotation of portfolio, help establish sustainable interest rates and improve operational efficiency programmes. What is particularly welcome is that NABARD plans to launch some pilot projects aimed at synergy between the traditional approaches of ‘gramin gola’ or ‘grain banks’ and the SHG-bank linkage programme.

Field studies leave little room for doubt that this approach in India, as indeed elsewhere, leads to profundity of changes in a chain of cumulative causation triggered by credit to the rural poor. More specifically, these relate to definite empowerment of traditionally disadvantaged women in multiple ways by development of self-esteem and confidence in women enabling them to assert their own rights, stress on health, hygiene and education, democratisation of family structure, assumption of decision-making roles by women outside their homes to effectively manage their economic affairs, shift in loaning pattern with emphasis on income-generating activities, reduced incidence of alcoholism in men leading to all-round improvement, reduction in feminisation of poverty and inequalities in conditions of work and wages. This thesis can be substantiated by the findings of a recent study, covering 560 members of 223 Self-Help Groups (SHGs) located in 11 states across five regions, which was recently commissioned by NABARD to assess the impact of micro-finance on living standards of SHG members. The study compared the socio-economic situations in pre- and post-SHG situations spanning an average period of three years. NABARD provides 100 per cent refinance at an interest of 6.5 per cent per annum. The study brought out that the involvement of the rural people in SHGs contributed to improving their confidence in managing their family finance, improved their ability to communicate, enhanced their capacity to protest against social evils, reduced family violence and influenced their behaviour positively towards mutual help. Besides, compared to the pre-SHG situation, the average savings of households jumped three-fold. The average value of assets per household was Rs. 6,843 prior to group formation whereas it was Rs. 11,793 during the post-SHG period. The increased assets comprised livestock and consumer durables apart from other items. Along with savings, the average borrowings per household also doubled from Rs. 4,282 during pre-group to Rs. 8,341 during post-SHG situation. But the majority of the borrowings were for income generating activities and not for consumption as was the case prior to group formation. The study demonstrated that the income levels of the SHG members increased by about 33 per cent. The average net annual income per household from income generating activities where loan amounts were deployed increased from Rs. 20,177 prior to group formation to Rs. 26,889 after group formation.

Cross-section studies reveal that the success of SHGs could be attributed to the sense of solidarity, group size, self-consciousness, self-reliance and transparency, leadership and practical regulations together with peer pressure and group dynamics. As Jagdish Capoor (2001) cogently argued “There is now an urgent need to shift from a minimalist approach-that is offering only financial intermediation-to an integrated approach taking a more holistic view of the client including provision of enterprise development services like marketing infrastructure with direct linkage between the borrowers and potential buyers, introduction of technology and design development”. Banks, therefore, need to play a greater proactive role in SHG-friendly schemes by fine-tuning the size of projects and estimates to the micro situation because of the significant role of individual initiative and entrepreneurship in a group setting in rural development.

While the new paradigm stresses financial intermediation with self-sustainability of institutions and qualitative/quantitative outreach to the poor, it is obvious that self-sustainability alone can not improve the ‘process’ of delivery of micro credit necessitating other attendant measures to mainstream micro credit in India as an effective instrument of empowerment of the underprivileged, particularly in resource poor regions and tribal areas. The spectre of marginalisation of the poor requires a renewed thrust on micro credit to create meaning and value in the lives of a significant section of population. Micro credit by facilitating timely availability of credit, increasing the outreach of the banking system and deepening the rural credit delivery system by operational efficiency and financial viability attempts in a modest way to unleash forces transforming poor people's lives from being debt-driven to self-driven and thus contributes to a structural transformation. In sum, the current focus on micro credit marks a paradigm shift from induced development from above to initiated development from below and highlights the changing role of credit in addressing and adequately meeting the needs of the poor, the deprived and the women.

Recent events and developments have evoked considerable debate about sustainability of micro finance institutions (MFIs). Some of the main strands of this debate relate to the level of cost recovery for MFIs. In the steadily burgeoning literature on development economics in general and micro finance in particular, three levels of cost recovery have been isolated and identified (Christen, 1997):

Table 2: Level of Cost Recovery for MFIs

Level I: Subsidy Dependence	Interest and fee income does not cover cash costs.
Level II: Operational Self-sufficiency	Interest and fee income at least covers cash costs.
Level III: Operational Self-sufficiency	Interest and fee income covers all costs, including inflation and subsidy adjustments.

Sustainability can also be examined from the aspects of demand and supply characteristics, sustainability of the mission of MFIs, organizational sustainability and financial sustainability (Mahajan, 2001). It needs no clairvoyance to perceive that MFIs can make sustainable contribution to poverty alleviation not only by credit but also by adopting combination of savings, credit and insurance services. SIDBI has done pioneering work in enhancing capacity building needs of both the MFIs and the sector. Grants covering all aspects of operational, organizational and managerial aspects are provided by SIDBI to partner MFIs in an attempt to make them sustainable corporate entities. Strengthening of the sector is sought to be promoted by SIDBI through need-based capacity building support to select management and training institutions and use of Capacity Assessment Rating (CAR) made to foster faster and qualitative growth.

NABARD’s Annual Report (2002-03) brought to the fore basic elements, which need to be stressed to accelerate the growth and spread of the programme. These key elements include thrust of quality SHGs on a large scale with accent on comparatively backward and resource poor regions, suitable training and exposure programme for all stakeholders, financial assistance to Self Help Promoting Institutions (SHPIs) for promoting and nurturing of SHGs, credit rating of SHGs, financing of SHGs as a business proposition, SHG financing as ’co-operatives within co-operatives’, widening the range of SHPIs by associating larger number of development agencies and Panchayati Raj Institutions and large scale dissemination of the concept of SHGs among the rural masses.

Sustainable solution of RFIs

The Indian financial system comprises an elaborate network of banks, financial institutions, non-banking financial companies (NBFCs) and a wide range of financial instruments. Despite a considerable widening and deepening of the Indian RFI system, the extension of banking and other financial facilities to a larger cross-section of society and increase in all indicators of financial development such as the finance ratio, financial interrelations ratio and intermediation ratio, the rural banking system continued to be inefficient in terms of low profitability, high and growing non-performing assets and relatively low capital base. But replication of the standard policy prescriptions developed elsewhere to the RFIs would be entirely misplaced. For, as Joseph Stiglitz (1994) cogently argued, the rationale for liberalising the financial markets is “based on an ideological commitment to an idealised conception of markets that is grounded neither in fact nor in economic theory”.

Rural development programmes and policies need to be reoriented in order to help small producers. There is a manifest need for reducing the number of rural development schemes to a few focussed ones and closer interaction at the policy levels by taking a holistic view. In the quest for a sustainable solution to the multi-dimensional problems of RFIs, the bottomline that has to be recognised is that the promotional and developmental role of RFIs would increasingly have to be performed in a competitive set-up in which resources for commercial lending as well as for developmental purposes need to be raised at market-determined rates. The big picture that has been evoked in broad strokes is akin to a tectonic shift in the basic underpinning of the central functions of RFIs. The Narasimham Committee Report II brought into focus the utter futility of fixation of only sub-targets for identified segments for greater credit dispensation to agriculture. Consequently the Committee made a strong case to (a) streamline infrastructure, (b) enforce credit discipline, (c) review and strengthen rural credit delivery mechanism in terms of appraisal, supervision and follow-up, loan recovery strategies and develop the bank-client relationship in view of higher NPAs and eliminate the subsidy element in credit for the priority sector, (d) further deregulate interest rate and slash CRR and SLR.

The Task Force appointed by the Government of India under the Chairmanship of Shri Jagdish Capoor, Deputy Governor of the Reserve Bank of India to suggest a revival and restructuring package for cooperative banks made several important recommendations for strengthening the cooperative credit system in India. But for those involved with the process of rural credit in India, the recommendations could hardly be said to be novel. The Capoor Committee would also have done well to stress active member participation, strengthened link on credit and other aspects of the rural economy like storage, marketing and processing and the positive role of the government through sound development policies and coordination of various programmes of rural development with cooperative credit. Such financial recapitalisation is expected to cleanse the balance sheets of cooperative banks and make them eligible for refinancing by NABARD. The success of this rehabilitation plan is, however, contingent on organisational, structural, operational and systemic reforms.

Strengthening of Core Competencies and Exploration of New Vistas

RFIs can contribute to management and diversification of growth horizons by impacting on employment, productivity and economic growth and their potential to transform economies. Towards this end, consistent attempts have been made to revitalise RFIs by deregulating the interest rate, financing of non-target groups by RRBs, recourse to non-fund business for both cooperatives and RRBs, flexible investment policies and direct financing by SCBs/CCBs (Reddy 2000).

Four critical factors in the contextualisation of credit relate to provision of food security, generation of sustained agricultural growth, creation of gainful employment and exploitation of hi-tech segments in rural credit as growth centres (Mujumdar 1997). Systemic reform of the RFI sector also requires macro-economic stabilisation, support of fiscal and external policies, adherence to prudential regulations and simultaneous implementation of wide ranging reforms in other sectors for optimum results. The resolution of interconnected issues of reduction of fiscal deficits, reform of the banking sector, revitalization of capital and debt markets and the availability of long-term funds for facilitating of India's potential economic growth on a priority basis in the pursuit of second generation reforms would also be helpful to the RFIs in strengthening their core competencies while exploring new vistas of development.

Concluding Observations

Concerted attempts have been made in the last decade to perceptibly improve the functions and working of RFIs to enable them to meet the onslaughts of the emerging difficult macro-economic scenario. These attempts, however, have not been enough to resuscitate RFIs because the viability of RFIs is inextricably linked to business-related factors, viz. low level of deposits with a large proportion of high cost deposits, low level of advances with an unprofitable mix and injudicious funds management. As these problems grow worse, the stakes rise higher, rendering soft options absolutely ineffective and bringing into focus the imperative need for a thorough overhaul of the system. Any strategy to streamline RFIs must necessarily address these basic concerns with the support of all players in the system to bring about a marked improvement for sustainable development.

In a comprehensive examination of various facets of rural credit in India, the Expert Committee on Rural credit succinctly summed up the challenges confronting the RFIs as follows: “It is possible, and indeed helpful to see the system as consisting of many components and analyse their individual problems in details. .. It is, however, more important to also consider the totality of the system and place and its strengths, weaknesses, opportunities threats and remedial measures in an integrated perspective... The well being of rural India’s body economic, and indeed public as well, depends on a vigorous and efficient credit system... In the final analysis, liquidity and credit flow are the life blood of any economic system”.

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