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**The Shifting Trajectories in  
Microfinance Discourse: A critical reading  
of the Anti-Poverty Dimensions of  
Microfinance programmes**

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# **The Shifting Trajectories in Microfinance Discourse: A critical reading of the Anti-Poverty Dimensions of Microfinance programmes\***

**K. Kalpana**

## **Abstract**

This paper attempts to trace the paradigm shift away from an earlier conviction in the presumed ability of microfinance to function as a silver bullet that lifts poor households above the poverty line through a virtuous cycle of ‘more income, more credit, more investment’, towards a more cautious approach emphasizing the protectional, as opposed to the promotional, dimensions of microfinance. The discussion begins by distinguishing the current generation of microfinance programmes and institutions from an older generation of rural credit programmes for the poor, based on differences at the level of transactional technologies and ideological perspectives in the underlying conceptualization of credit. Much of the literature reviewed in this paper pertains to the experience of Bangladesh, home to some of the earliest and oldest microfinance programmes and institutions. The paper ends by reflecting on some of the issues that the shifting conceptualization of microfinance poses for the practice of Indian self-help group-based microfinance.

## **Introduction**

The paper attempts to analyze the shifting contours of the conceptualization of microfinance as a poverty alleviation strategy within the dominant development discourse over the 1990s. In particular, it attempts to trace the paradigm shift away from an earlier conviction in the presumed ability of microfinance to function as a silver bullet that lifts poor households above the poverty line through a virtuous cycle of “more income, more credit, more investment”, towards a more cautious approach emphasizing the protectional, as opposed to the promotional, dimensions of microfinance. In Section I, the paper offers a definition of microfinance as popularly understood and attempts to address the issue of how the current generation of microfinance programmes and institutions may be distinguished from an older generation of rural credit programmes for the poor, by outlining the differences at the level of transactional technologies and ideological differences in the underlying conceptualization of credit. Section I also includes a brief outline of the global institutional pressures that have led to the widespread dissemination of microcredit and micro enterprise programmes as key components of anti-poverty development initiatives in the 1990s.

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In Section II, the paper undertakes a brief review of the literature on the poverty and income impact of microfinance programmes across the globe, especially in Bangladesh (home to some of the oldest and best known programmes). The focus here is on the processes by which global donor pressures on institutional viability have influenced programme design and the organizational structure of microfinance programmes and on how these have, in turn, provoked, or reinforced, exclusionary dynamics that work against the interests of the poorest or relatively poorer clientele of microfinance programmes. In Section III, we see how the downsizing, or the toning down as it were, of the claims advanced on behalf of microfinance have led to changes in the projection of microfinance between the World Bank's World Development Report "Poverty" of 1990-91 and the World Development Report "Attacking Poverty" of 2000-2001. These changes are argued to be symptomatic of the shifting representation of microfinance within the anti-poverty discourse and are epitomized by the emergence of microfinance as a central component of social security and social protection concerns that have gained global prominence in the development community in view of the repercussions of policies of globalization, structural reforms and international financial flows. Section IV reflects on some of the issues that the shifting conceptualization of microfinance poses for the practice of Indian self help group based microfinance.

We note that much of the literature on microfinance programmes reviewed in this paper pertains to programmes that are operating in Bangladesh or are located in other parts of the world but have incorporated some of the key design features closely associated with and popularized by the Grameen Bank of Bangladesh. The focus on Bangladesh is warranted by the prominence of Bangladeshi NGOs such as the Bangladesh Rural Advancement Committee (BRAC) and the Grameen Bank in development literature. The Bangladeshi experience in microfinance, and the Grameen Bank in particular, has captured the imagination of a wide spectrum of institutional actors comprising the global development community, donor organizations, commercial banks, government bodies and the international media. It may also be added that the scale attained by microfinance institutions and the magnitude of their outreach has been outstanding in countries such as Bangladesh, where the growth of the NGO-financed microcredit movement has been so massive that even the formal financial sector has been overtaken and pushed to third place, with the informal sector comprising moneylenders, friends and family occupying first place. It is estimated that the semi-formal sector or the NGO financed microcredit sector provides 17 billion taka in microcredit in Bangladesh, while agricultural banks and nationalized commercial banks (including the Grameen Bank) provide 11 billion taka (World Bank, 1996). Further more, we note that Grameen styled microcredit programmes have also invited substantial research attention critiquing the poverty and empowerment impacts of such programmes.

A caveat is in order right at the beginning. The focus of this paper is on debates within the microfinance literature on issues pertaining to social security and poverty alleviation. This paper will not engage with the literature that has been provoked by the

near-exclusive targeting of female clients by microfinance programmes. In other words, debates around the empowerment claim and potential of microfinance programmes and their impact on gender relations, at the household and the community levels, are not dealt with here.

## **Section I**

### **I. 1. Towards a definition of “microfinance”**

Attempts to formally define microcredit / microfinance programmes usually refer to the objective of such programmes viz, reaching small amounts of credit and other microfinancial services to the poor so as to promote income generating activities. The Declaration of the Micro-Credit Summit held in Washington, D. C. in 1997 defined micro-credit programmes as those that “extend small loans to poor people for self-employment projects that generate income, allowing them to care for themselves and their families” (Microcredit Summit, 1997). The Task Force on Microfinance established by NABARD defines microfinance as the “Provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi urban or urban areas for enabling them to raise their income levels and improve living standards” (NABARD, 1999). While these definitions essentially seek to foreground the purpose of microfinance programmes (“income generation through self employment”), the size of the financial services offered (“very small amounts”) and the target clientele of such programmes (“the poor”), the terms “microfinance” and “microcredit” have, in the course of popular usage, come to signify not only the goal of reaching financial assistance to a designated target population, but also to encompass a particular set of lending methodologies and transactional technologies, that set them apart from an earlier generation of credit programmes for development of the agricultural sector. Tara Nair (2001) notes that microfinance actually refers to a system of decentralized credit delivery marked by the substitution of individual banking by social intermediation, where people’s organizations are financial intermediaries. According to the Microfinance Handbook produced by the World Bank’s Sustainable Banking with the Poor Project, while the term microfinance refers to the provision of financial services to low-income clients, many Microfinance Institutions (MFIs) provide social intermediation services comprising group formation, training in financial literacy and management capabilities and therefore the *definition of microfinance encompasses both financial and social intermediation*. (Ledgerwood, 1999).

The current consensus, aggressively propagated by some of the leading development organizations including the World Bank, the USAID and the DFID, which holds that microfinance based programmes constitute the single most effective development intervention that can be universally adapted, may be attributed to the close association of microfinance with lending technologies that reduce transaction costs to the borrower and the lending institution by lending to neighbourhood based “primary groups”, “self help groups”, or “solidaristic groups” (as they are variously called in different contexts). It is important to note that the organizational structure of the peer group based channel of

delivery of microfinancial services is remarkably heterogeneous, assumes diverse forms across the globe and ranges across a spectrum including the Grameen type groups of Bangladesh, the Indian self help groups, the village banking model prominent in Latin America etc. As the Microfinance Handbook of the World Bank points out, the MFIs in turn, could be nongovernmental organizations, credit unions, savings and loan co-operatives, government banks, commercial banks, and non-bank financial institutions (Ledgerwood, 1999). Although microfinance and microcredit are often used as interchangeable terms in the literature, it is generally agreed that microcredit or small loans for income-generation or consumption purposes refer to one component of a larger array of microfinance services that could include savings, insurance and other related business development services as well.

## **I. 2. Differences in transactional technology**

Differences in transactional technology that primarily entail innovations in lending and repayment methodologies constitute an important marker of difference between an older generation of credit for development of the agricultural sector and the contemporary generation of microcredit programmes. Microcredit programmes, in which small, neighbourhood based groups of borrowers substitute the earlier focus on the individual, appear to have been able to provide a workable solution to some of the more intractable problems inherent to rural credit programmes for the poor - whether undertaken by state or private channels - as identified by scholars working within the framework of New Institutional Economics (Stiglitz, 1990; Hoff and Stiglitz, 1990). The joint liability, peer monitoring and peer pressure that are built into the organizational structure of small borrower groups are identified as the key features of the innovative institutional design credited with addressing the critical problems of *screening* (screening potential defaulters from those with lesser probability of default), *incentive* (inducing borrowers to repay) and *enforcement* (compelling repayment) at reduced transaction costs to lenders. Small borrower groups are perceived as effectively addressing problems of adverse selection and moral hazard deriving from informational asymmetries between lenders and borrowers<sup>1</sup> (Wenner, 1995; Hoff and Stiglitz, 1990). In addition to intra-group peer monitoring and peer pressure, residence-based groups also bring to bear the threat of community level sanctions upon potential defaulters so as to ensure conformity to repayment schedules. The distribution of repayment responsibilities over smaller, more frequent, manageable quantities, rather than in lump sum, one-time amounts combine with the inbuilt pressures to ensure repayment; this constitutes innovation at the level of lending technologies. Most microcredit programmes also strengthen the incentives for good repayment behaviour by the promise of continuing access to higher sized loans so that institutional credit access does not remain a one-shot injection (Johnson, 1997). In the case of the self help group model of micro credit, predominant in India, intra-group savings are circulated first as group corpus or “hot money” prior to the entry of external credit or “cold money” sourced either from commercial banks or from the sponsoring NGO/MFI, strengthening further the incentive of members to repay loans on time<sup>2</sup>. Hence microfinance activities typically involve collateral substitutes such as group guarantees or compulsory savings, small loans,



usually for working capital, access to repeat and larger loans, informal appraisal of borrowers and investments, secure savings products and streamlined loan disbursement and monitoring (Ledgerwood, 1999, Sa-Dhan, 2001).

### **I. 3. Differences in the ideological underpinnings of microfinance**

The high repayment performance reported by microcredit projects combined with the relative absence of interest rate subsidies in their programmes have helped microcredit based development interventions win a broad based constituency of admirers including multi-lateral and bi-lateral development organizations, commercial banking institutions and powerful actors among Non Governmental Organizations, enamoured of the potential of microcredit to generate interest incomes that enable the microfinance institution to cover its lending costs to a substantial degree. The “discovery” that not only were the poor bankable, given the adoption of appropriate lending methodologies, but that banking with the poor could be profitable as well, suggested the possibility of a financially-viable, sustainable lending institution, a more promising prospect than the older generation of Rural Financial Institutions, vilified in the microfinance literature as unsustainable, loss making institutions where default arrears eroded sometimes more than half of the institution’s capital (Hulme and Mosley, 1996). Microcredit evangelism has, therefore, found expression in the growing convergence towards the “New Consensus” backed by the most powerful votaries, funders and practitioners of micro credit. The “New Consensus” emphasizes the attainment of the twin prized and complementary goals of “outreach” (extending the coverage of the organization) in order to harvest economies of scale and further reduce operating costs and “financial sustainability” (Johnson, 1997; Morduch, 1999; Tankha, 1999). Johnson (1997) argues that the “New Consensus” is in a sense what demarcates the current obsession with microcredit extension to the poor and adds significant new dimensions to what would otherwise have remained no more than an “old debate with a new gloss”. The microfinance revolution, as Marguerite Robinson (an influential votary of microfinance) puts it, is therefore the “large scale, *profitable* provision of microfinance services – small savings and loans – to economically active poor people by *sustainable* financial institutions (Robinson, 2001, p 10, italics mine).

That the new generation of MFIs is primarily an innovation of the non-governmental sector also explains, in part, the enormous appeal of microfinance programmes in times characterized by the debunking of the state as principal protagonist in the arena of development and the usurpation, of its place, by non-governmental organizations. The dominant discourse around microfinance actively seeks to restrict the role of the developmental state to the creation of an enabling, facilitative policy climate conducive to the smooth functioning and growth of microfinance institutions and to limit the scope of its direct engagement in the execution of microfinance programmes. It would appear therefore that the current aggressive promotion of microcredit is not about the promotion of small credit for development purposes per se but about *the promotion of a particular model and a particular ideological understanding of credit*. This vision emphasizes credit as the most effective weapon against poverty among the array of poverty alleviation instruments

available and consequently advocates the exclusive injection of credit for promoting self employment of the poor, emphasizes non governmental agencies as the most effective channels of delivery of microcredit and advocates an organizational structure for the microfinance institution that prioritizes the optimization of operational efficiency and the attraction of private capital investment so as to eliminate dependence on donor grants and subsidies. As Mayoux (1998) points out, the much-celebrated “win-win” formula of the dominant discourse of microfinance inheres in its presumed ability to alleviate poverty even while generating profits for the lending institution by charging market interest rates.

#### **I. 4. Microfinance and the global poverty agenda**

The early, well-publicized pioneering success of non-state initiatives in credit disbursal to the poor such as the Grameen Bank and the Bangladesh Rural Advancement Committee (BRAC) of Bangladesh established in the 1970s, the ideological shift of aid agencies towards market-oriented development programmes in the 1980s, extensive lobbying by microcredit NGOs and the predominance of financial sustainability compulsions even within development interventions have been identified as having provided the momentum that spurred the meteoric expansion of microcredit programmes in the 1990s (Fernando, 2001). The global consensus around microcredit as a key element of poverty alleviation strategies was evident at the microcredit Summit held in Washington D.C in 1997, which enjoyed the support and patronage of the World Bank, IFAD, private commercial banks and hundreds of leading NGOs across the globe. The resolution of the Microcredit Summit to reach credit assistance to 100 million of the world’s poorest families by the year 2005, especially the women of these families, to enable them to set up income-generating enterprises, most powerfully expresses the micro credit/ micro enterprise as panacea vision for structural problems of poverty and under development (Microcredit Summit, 1997). The establishment of the Consultative Group to Assist the Poorest (CGAP) in 1995 as a multi-donor consortium by nine founding members, including the World Bank, with the mandate of providing financial and technical support to microcredit programmes world wide, is a reflection of the massive global drive behind the microcredit movement. In December 1998, the General Assembly of the United Nations adopted a Resolution declaring 2005 as the International Year of Microcredit, as an important component of the first UN Decade for the Eradication of Poverty (1997-2006). In the Resolution, the UN requested that the observance of the Year be a special occasion for giving impetus to microcredit programmes throughout the world and invited governments, the UN system, NGOs, private actors and the media to highlight the role of microcredit in the eradication of poverty and social development (UN Resolution, 1998)

We note that the growing intensity of concerns about poverty in the wake of the implementation of neo liberal economic reforms and the consequent re-articulation of a ‘New Poverty Agenda’ for the 1990s by important institutional actors such as the World Bank and the UNDP constitute the context within which the phenomenal growth of microcredit programmes as key anti-poverty interventions has been taking place. The public investment reducing effect of Structural Adjustment Programmes (SAPs) in developing

economies, the increase in both absolute and relative poverty in the 1980s in Latin America, Africa and the Caribbean, the worsening access of the poor to quality social services and their falling incomes and employment levels were documented and identified as the anti poor effects of reform policies. The late 1980s witnessed the publication of seminal studies that were critical of the poverty increasing effect of the SAPs, the unbridled market forces they had unleashed and the consequent deterioration of the health and well being of vulnerable sections, UNICEF's "Adjustment with a Human Face" (1987) being the most influential and best known of these. Consequently, debates on the human toll and the social costs of the economic reforms and the decade long decline of several Latin American and African countries forced poverty back on the development agenda of the 1990s (Gershman and Irwin, 2000). Weber (2001) notes the intensification of global efforts in support of international development targets, as exemplified by the OECD's Development Cooperation 2000 Report, which committed the global development community to the goal of reducing the proportion of people living in extreme poverty by half between 1990 and 2015 (Weber, 2001, note 7, p 4).

In a global development climate increasingly sensitive to poverty concerns, Weber (2001) has argued that the "strategic embedding" of microcredit in the global political economy of poverty reduction serves as a political safety net by containing resistance to neo liberal economic restructuring policies through the alleviation of income insecurity and absorption of surplus labour in informal sectors. In 1995 a World Bank report on Privatization and Adjustment in Bangladesh cited microcredit as a strategy to overcome potential resistance to the agenda of privatization in Bangladesh. (Weber 2001, Note 31, P 8). Analysts have pointed to the significant presence of microcredit projects and components in the relief packages, especially the Emergency Social Funds, designed by the World Bank to contain popular agitations in third world countries undergoing structural reform (Weber, 2001; Mayoux, 2002). The Emergency Social Funds, which entail the provision of grants to local groups, in response to locally expressed demand, in a flexible manner are perceived as being different from traditional public welfare programs by virtue of their orientation towards the promotion of private entrepreneurship. The Emergency Social Fund was recommended as a globally applicable strategy and informed the World Bank's Social Funds policy framework, which became a critical component of the poverty reduction strategies of the World Bank. By 1995, 18 Latin American and Caribbean countries had adopted the ESF model. Starting from the earliest instance of Bolivia, minimalist microcredit was integrated as a key component of the ESF strategy. The increasing application of targeted approaches to poverty reduction by the World Bank has increased the appropriation of microcredit programmes (Weber, 2001).

Weber's account of the key presence of microcredit programmes within World Bank relief packages, designed to contain the fallout of the economic reforms, enables an understanding of the global institutional pressures that have ensured the widespread dissemination of these programmes across countries and regions. Mayoux (2002) also notes that microfinance was promoted as the grassroots dimension of the 'human face' of

structural adjustment and economic liberalization in Africa. The promotion of microfinance as the ideal self-help strategy enabling the poor to take loans in order to establish self-employment ventures and pay the increased costs of basic services such as education, health, water and sanitation was undertaken in Africa in the wake of the SAPs which had created widespread unemployment and pushed up the costs of basic amenities (Mayoux, 2002). The Strategy Paper of the Consultative Group to Assist the Poorest (CGAP) for Phase III (2003 – 2008) extols microfinance for its contribution towards the achievement of the millennium development goals that are outlined as including the eradication of extreme poverty and hunger, the attainment of universal education, the reduction of child mortality, improvement of maternal health, the empowerment of women and the combating of disease (CGAP, 2002). When elucidating the means by which microfinance enables poor households to attain these goals, the CGAP document makes it clear that it expects the poor to use their micro loans to purchase essential services such as educational material, health services, nutrition and improved housing which, we note, a national developmental state might have been expected to provide by way of legitimizing its claim to be a welfare state. We note therefore that the dominant vision of microcredit manages to appeal to a diverse constituency of aid organizations and commercially motivated private actors within an overarching framework of neo-liberalism on account of its stipulation that the poor pay their way out of poverty.

Critics of the New Poverty Agenda of the 1990s have argued that it entails soft-pedaling the role of the state in response to the influential neo liberal critique mounted against the state in the previous decade and that it is marked by the conspicuous absence of the agenda of redistribution of economic resources and asset ownership. The World Bank's New Poverty Agenda has been faulted with failing to recognize that skewed asset ownership is as important an impediment to the realization of human development goals as is the lack of access to social services (Gershman and Irwin, 2000). Microcredit programmes do not entail structural redistribution of resources as land reform programmes would for instance and yet constitute an anti-poverty intervention of tremendous public visibility as they mobilize large numbers of the poor seeking access to credit, creating thereby federations of the rural and urban poor. We understand therefore the instrumental and strategic leverage that microcredit programmes offer to powerful global development actors who need to manage economic restructuring-related political and social tensions in developing economies and to respond adequately to studies revealing increasing poverty levels while at the same time maintain a sufficiently enabling environment for the perpetuation of reforming regimes.

To sum up this section, we have shown how microfinance, by definition, refers not only to the provision of small loans for specific purposes to a targeted poor clientele but also to a particular mode of lending that includes, as an integral component, social intermediation or the process by which small, neighbourhood-based peer groups attempt to reduce transaction costs for the lender and the borrower. We have noted that the principal features that differentiate microfinance from an earlier generation of credit for the poor

include crucial aspects of lending methodologies such as group-based lending, market interest rates, repeat loans and effective inbuilt sanctions against defaults which, in turn, have led to a shift in the ideological underpinnings of microfinance. We have argued that the shifting ideological construction of microfinance, premised on the notion of the sustainable and profit-oriented lending institution that addresses poverty concerns even as it covers its own costs, testifies to the overriding dominance of efficiency concerns, inspired by neo-liberal economic policies, within the international development sector. We have also attempted to outline the global institutional pressures that have inserted microfinance into the anti-poverty discourse during a period when the poverty reduction agenda gained political significance on account of the trenchant criticism of the poverty-enhancing effects of the structural adjustment reform packages. In Section II, we will review secondary literature critical of the track record of microcredit programmes effectively meeting the credit and savings related needs of very poor sections of the population.

## **Section II**

### **II. 1. Predominance of the ‘Grameen model’**

At the outset, we note that although research findings relating to the poverty impact of microfinance programmes in other countries that are not modeled on the Grameen are also cited wherever relevant, this section focuses largely on the experience of the Grameen-styled, poverty-targeted Microfinance Institutions of Bangladesh, comprising primarily the Grameen Bank itself, microcredit programmes organized by internationally-acclaimed Bangladeshi NGOs such as the Bangladesh Rural Advancement Committee (BRAC), Association for Social Action (ASA) and Proshika<sup>3</sup> and the Bangladeshi government’s microcredit programmes – the Rural Development Project-12 (RD-12) and the Thana Resource Development and Employment Programme (TRDEP)<sup>4</sup>. We note that some of the largest and best-known MFIs in Bangladesh have modeled the organizational structure of their micro lending programme on the Grameen Bank so that we may speak of a “Grameen system”, as Malcolm Harper (2002) puts it, that is used not only by the three million members of the Grameen, but also by more than a million clients each of Proshika and BRAC. Furthermore, it has been estimated that over 10 million clients in Bangladesh use the Grameen system through 30 MFIs with more than 10,000 clients each and hundreds of other smaller organizations that are following the Grameen model in Bangladesh (Harper, 2002). In their study of BRAC and the government’s Thana Resource Development and Employment Programme (TRDEP), Montgomery et al (1996) note that the leading players in microfinance in Bangladesh have designed programmes that are practically indistinguishable from each other and offer little by way of alternative programme design to clients.

Researchers have pointed to the low levels of institutional innovation within the microfinance sector on account of the propensity to produce clones of the Grameen and have argued that the propagation of the “Grameen model” has assumed hegemonic

dimensions within the microfinance industry, not only within Bangladesh, but globally as well, due to the active promotion of the Grameen, especially by the CGAP, as the ideal model for emulation by microcredit NGOs focusing their services on the rural poor. Prominent global institutions such as the International Fund for Agricultural Development (IFAD) and the Asian Development Bank (ADB) have expressed their willingness to support only those microcredit programmes that are based on the Grameen model (Jain and Moore, 2003). The Grameen Trust, established with the mandate of extending financial and technical assistance to Grameen replicators, was supporting 70 projects in 30 countries in Asia, Africa, Europe and the Americas by the year 2000 (Yunus, 2000). It has been estimated that the Grameen Bank lending model has been replicated in 56 countries including developed nations such as Canada and the US (Rahman, 1999).

A note on the basic organizational structure of microcredit programmes modeled on the Grameen Bank would be in order here given that much of the literature reviewed in the following section involves critical appraisals of Grameen modeled microcredit programmes. The Grameen style groups consist of small borrower groups of about 5 members each at the primary level that are integrated into a “center”/*kendra* consisting of 6-8 such groups at the level of the village. The organizational structure is similar in BRAC wherein “village organizations” of 30-40 members are divided into smaller 5-7 member “solidarity groups” and the government’s RD-12 programme in which “primary cooperatives” of 15-35 members are divided into 4-5 member “solidarity groups”. Group eligibility criteria of poverty-targeted MFIs in Bangladesh entails ownership of less than 50 decimals of land. Groups and centers are constituted separately for men and women. Members deposit their savings (a compulsory amount of about 1-2 taka per week) at regular weekly meetings with the sponsoring NGO/MFI. The MFI onlends subsidized funds to groups sourced from donors organizations, the Central Bank of Bangladesh, microfinance wholesalers such as the Palli Karma Sahayak Foundation (PKSF) and to some degree, borrowers savings. Some of the leading microfinance programmes in Bangladesh including the Grameen, TRDEP and BRAC require members to explicitly state a production related borrowing purpose in order to be eligible for the loan. Repayment is made at the compulsory weekly meetings in 52 installments and is collected by programme staff. Although physical collateral is absent, most programmes deduct a certain percentage of the loan principal as compulsory contribution to a group trust fund or security deposit (Khandker, 1998). The financial resources of the group are usually controlled by the staff of the MFI and members gain little skills by way of savings or loan management. The terms of lending including repayment schedules, interest rates and loan packages are usually standardized for all group members and decided by the sponsoring MFI. Analysts have noted that the peer group, in the Grameen model, exists primarily so as to reduce the transaction costs of the lending institution (Dasgupta, 2001).

## **II. 2. Donor pressures, sustainability imperatives and implications for microcredit practice**

Research on the impact of microfinance on core poor sections enables us to understand

better the limitations of the current generation of MFIs and points to the trade-offs and unintended outcomes that result when programme features aiming to ensuring repayment performance and institutional viability simultaneously discriminate against core poor sections. Donor pressures on the attainment of institutional sustainability have been reflected in policy level decisions to expand manifold the scale of programmes, increase the volume of loans disbursed, locate programmes in better-endowed regions and offer minimalist credit programmes, that sometimes imply an organizational shift away from an earlier engagement with a more integrated, holistic rural development approach to issues of rural poverty. Sustainability pressures have in turn had grassroots level impact on client households of microcredit beneficiaries via changes in loan packages, lending terms, interest rates, salary and incentive of staff and organizational structure of microfinance institutions.

Studies have found that the Bangladeshi NGO Bangladesh Rural Advancement Committee's microcredit programme, that was started in the mid 1980s, and the Grameen Bank, started in the early 1970s, have been moving away from working with core poor sections due to donor imperatives related to the generation of revenues that enable the MFI to cover all costs. Responses by the Grameen Bank to mounting criticism of its reliance on subsidized donor capital took the form of changes in Grameen's loan packages since the mid 1990s. These changes have included introduction of the larger sized seasonal loans and a diversity of loan packages, permission to take 2 or 3 loans at the same time, higher entry point loan size and branch managers' overwhelming obsession with increasing the scale of investment or loan outstanding to the detriment of members' welfare (Matin, 1998; Rahman, 1999; Jain and Moore, 2003). The focus of BRAC, in its phase of expansion from the late 1980s, shifted from efficient poverty targeting at the field level towards repayment performance and from the quality of services to the poorest to the fulfillment of quantitative targets (Montgomery et al, 1996). Micro-level investigation has revealed that the policy of credit deepening (increasing the number of loans per borrower) that Grameen Bank has aggressively pursued since the early 1990s has intensified both the severity and the incidence of inclusion of non-target sections (Matin, 1998), while BRAC's policy of expansion and emphasis on repayment have been likewise reflected in the changing membership profile, with newly-joined members being better off than older members (Montgomery et al, 1996).

The microcredit programme of Association for Social Advancement (ASA) of Bangladesh, that was started as late as the early 1990s in a policy climate influenced by the opinion that minimalist microcredit without donor funding was financially viable, endeavoured from the beginning to reduce dependence on donor funds through larger loan sizes, higher interest rates (when compared to Grameen and Proshika), lower levels of investment in group development or member training and greater emphasis on supervision and repayment control. A study of five credit programmes comprising the Grameen, BRAC, ASA, PROSHIKA of Bangladesh and CARD of the Philippines found that ASA had the largest share of small traders and businesspeople (Jain and Moore, 2003). The Bangladesh government's credit programme RD-12, faced with the prospect of withdrawal of support

by the funding agency CIDA, had introduced new staff incentives to raise the magnitude of loan disbursement and recovery per staff since 1993. Goetz and Sengupta (1996) observe that upscaling strategies may have adverse effects on poor women borrowers of ASA including the pressures to take out larger loans without adequate technical or marketing support leading to the failure of enterprises and pressures to relax membership eligibility criteria so that poorer women may not gain access to loans. In their study of the Diocesan Development Services, a Catholic Mission based NGO operating in Kogi state, Nigeria, McNamara and Morse (1998) argue that the unfortunate coincidence between the pressure applied by a major donor in the late 1980s on the DDS to become financially sustainable within a year or two and the onset of the Structural Adjustment Policies in Nigeria from 1986 led to the DDS being forced to withdraw all the other development programmes that it used to offer and increase lending rates during a period of worsening economic crisis marked by loss of jobs, galloping inflation and delay in the payment of government salaries. While the DDS had prioritized self reliance right from its inception in the early 1970s, the heavy handed donor approach of forcing financial sustainability on the programme and dictating what the DDS should be doing and how it should be done as well, had led to the near-collapse of the programme for a number of years. McNamara and Morse (1998) use the tribulations of the DDS to question the wisdom of pursuing a path of institutional sustainability divorced from the social, political and economic context in which the microfinance organization works.

Gabrielle Athmer (2002) contends that the objective of sustainability, which the Consultative Group to Assist the Poorest has been aggressively promoting, has implied that microfinance clients in countries such as Mozambique tend to be the not-so-poor, urban dwellers and those living in densely populated rural areas. The obvious difficulties in the achievement of institutional viability in a rural environment marked by dispersed population, poor infrastructure, limited monetization, limited small-scale economic activities and seasonality of agricultural production has tended to drive MFIs towards densely-populated settlements with better levels of infrastructure. Studies in Bangladesh also point to the phenomenon of over-crowding of microcredit organizations in certain areas leading to cut-throat recruitment strategies and their relative absence in certain others on account of the higher costs of establishing branches and field offices in relatively under-developed areas (Fernando, 2001; Montgomery et al, 1996). In their study regions, Montgomery et al (1996) found a high degree of territorial overlap amongst microcredit schemes so that in high-density settlements it was common to find one half of the village marked out as BRAC territory and the other as that of Grameen. As larger size translated into greater official and donor support, regional competition among programmes fuelled the speed of territorial expansion. Smaller NGOs were most likely to be adversely affected by this phenomenon as they were captured by either BRAC or Grameen (Montgomery et al; 1996; Ebdon, 1995). Large-scale analysis of secondary data on branch placement in 391 thanas of Bangladesh had attempted to examine whether microcredit NGOs target their programmes to relatively under-developed or better-endowed areas (Sharma and Zeller, 1999). The study assumed that the original poverty mission of NGOs was likely to be



modified by the sustainability requirements of the principal financiers - national and global donors, so that the factors influencing branch placement decisions were the expected demand for credit services, the cost of supplying financial services and the perceived risk of operations in addition to poverty targeting. The researchers argue that the observed lower probability of NGO branch placement in high distress locations (measured by vulnerability to flooding, general wage levels and the availability of irrigation facilities) indicated the inability of even large NGOs to effectively deal with risks. Poverty considerations of the MFIs were not strong enough to compensate for the negative effects of doing financial business in risk prone areas. Overall, the study found that branch placement decisions were sensitive to the availability of transport and communication facilities and branches were more likely to be placed in areas with better infrastructure (Sharma and Zeller, 1999).

Another significant issue uncovered by research on microcredit programmes has to do with the widely reported phenomenon of non-participation of a considerable proportion of eligible target group households despite a dense clustering of microcredit programmes in the area. Hashemi's study of 4 villages with Grameen or BRAC programmes found that 43% of target group households residing in the region, and eligible to join both programmes had not joined either. Close to half of eligible non-member households were worried about going into debt and the inability to repay, while a quarter of women non-members had stated male conservatism of the household head as the prime constraint. 13% reported that other members had refused to let them join (Hashemi, 1997 a). A rigorous and large-scale examination of non-participation of eligible target group members in BRAC found that while more than 76% of rural households in the sample studied did meet the eligibility criteria of BRAC, about 65% of the moderately poor and 60% of the core poor sections were not members of BRAC (Evans et al, 1999). In order to understand the high incidence of non-participation of eligible poor households, the study hypothesized that both programme-related barriers and client-related barriers could have contributed to the non-participation of eligible households in microcredit programmes. The study found that one of the greatest programme-related constraints was the limited availability of microcredit programmes on account of BRAC's strict rule that there be no more than one village organization per village, irrespective of population or local demand for credit. The study also found indirect evidence that peer group expectations and institutional incentives were likely to have also contributed to non-participation of a high section of the poorest perceived as credit liability (Evans et al, 1999). Mounting evidence of the inability of microcredit programmes to successfully attract and retain membership of very poor sections has prompted examination of the mechanisms by which the poor either self-exclude or are excluded through more direct means by group members and programme staff.

In the following section, we will be reviewing ways in which sustainability related pressures on microfinance programmes have led to exclusionary and punitive pressures against the poorest sections through poor-unfriendly programme design and implementation practices.

### **II. 3. Exclusionary and punitive pressures against the poorest**

Studies of poverty-focussed MFIs testify to micro-level evidence of processes by which the poorest are either excluded from membership or are weeded out by their less deprived peer group members. Researchers have pointed out that the design of microcredit programmes and the manner of their implementation may make the arena of the microcredit project a harsh, slippery and unwelcome terrain to negotiate for poorer sections. Rigidities in the financial products offered that do not accommodate the seasonal earnings and income fluctuations of the poor, increasingly punitive strategies deployed by field staff to ensure adherence to repayment schedules, disempowerment of the village organizations vis-à-vis programme staff, exercise of peer pressure at the level of the larger, village level organization rather than at the level of the smaller, primary peer group, intra-group peer dynamics that jeopardize the precarious livelihood sources and asset holdings of the poor and credit escalation related tensions for poorer participants due to MFI policy of credit deepening may be identified as some of the more important research findings that explain the exclusion or expulsion of relatively poorer sections from microcredit programmes. We review these in some detail below.

#### ***a) The rigours of weekly repayment, inflexible loan products and inaccessible savings***

Microcredit programme features that seek to guarantee foolproof repayment behaviour by insisting on weekly repayment of loan installments are further evidence of contradiction between the agenda of ensuring sustainability of the lending organization and that of reaching services to poorer sections. The requirement of most microcredit programmes in Bangladesh that members start repayment from the first week after borrowing ensures that programme clients are not tempted to borrow more than they can repay and that they consequently restrict the loan amount to their capacity to repay from earlier savings. Jain and Moore (2003) emphasize that this provision is however a clear departure from the norms of conventional banking or even those of micro enterprise promotion that expect that borrowers make repayment from the income earned out of the loan financed investment. The logic of the weekly repayment schedule therefore serves as an effective tool of self-exclusion of the poorest, who lacks the accumulated savings stock required in order start repayment. (Jain and Moore, 2003).

Furthermore, it has been pointed out that weekly repayment may not suit the requirements of those maintaining livestock or engaging in occupations where the cash flow generated was not always enough to meet weekly repayment demands (Montgomery et al, 1996). Julie Gifford's review of the operation of five microfinance programmes in Uganda found that the rigid weekly repayment, which was incompatible with fluctuations in the businesses of the women entrepreneurs, forced them to sell their products at a loss in order to meet repayment schedules, restricted programme admission to those working in high turnover businesses, and prevented women from enhancing the productivity of their livelihoods by limiting their choice of activities to those with a high turnover such as petty trade, trade in cooked food and second hand clothes (Gifford, 2002). Inflexible and standardized loan products were also found to have inhibited the income enhancement

effect of programme credit. Since all the Ugandan MFIs in Gifford's study supplied only short-term working capital loans repayable over sixteen weeks with no grace period, women entrepreneurs could not use their programme loans to buy fixed assets, invest in long term investments, or profit from investment opportunities that emerged unexpectedly so as to graduate to higher-return activities (Gifford, 2002).

Easily withdrawable savings, easy-access emergency loans, consumption loans and flexible repayment schedules have been identified as essential ingredients of poor-friendly microfinance practice that protects and cushions the poor from downward mobility pressures which jeopardize their fragile livelihoods and asset holdings (Hulme and Mosley, 1996). A study of 316 clients and a control group of 213 non clients of the Accion Comunitaria del Peru, a microfinance programme focused on micro entrepreneurs in Lima (Peru), found that clients who experienced shock events were more likely to sell assets to cope with them than were non-clients. The greater incidence of asset liquidation among borrowers was attributed to the inflexible repayment pressures and to the consequent lower levels of flexibility in dealing with shocks than among non-borrowers (Snodgrass and Sebstad, 2002). A study of borrowers and savers of the SEWA bank, Ahmedabad attributed the limited role of SEWA's loan programme in helping individuals cope with financial shocks after they occurred to the narrow range of loan products on offer, the inflexible lending terms and the absence of emergency loans (Snodgrass and Sebstad, 2002). It has been argued that the constraints placed by several MFIs (including the prominent Bangladeshi MFIs) on consumption lending - an outcome of the predominance of the micro enterprise promotion agenda within the microcredit sector - has forced clients to camouflage their food, health and medical needs as demands for enterprise loans.

Microcredit research has also been critical of the absence of free access to member savings in Grameen and BRAC and organizations worldwide that follow the Grameen model. Montgomery et al (1996) found that members were deeply unhappy about the rules that restricted member access to their savings by allowing them to withdraw no more than one quarter of their savings after 5 years and one half after 10 years. Owing to BRAC's inflexibility, members perceived both the savings amount and the mandatory 10% deduction from each loan received as contribution to the Group Trust Fund, as additional, albeit disguised, costs of borrowing. Gifford's study of MFIs in Uganda also found that compulsory savings, which were a form of collateral for the loan, could not be accessed until members quit the group, while access to the voluntary savings was conditional upon permission from the loan officer, which took some time to be processed (Gifford, 2002). Hulme (2003) notes that "extreme case" MFIs such as the Kenya Women's Finance Trust and several other East African MFIs have no place for clients who wish to stop taking loans and to only make savings. As savings, unlike loan products, are not designed to cover costs of the lending institution, the propensity of the microfinance industry to force every saver to also be a borrower is identified as part of product design by which MFIs pursue institutional viability (Hulme, 2003).

Jain and Moore's study of 4 of the leading microfinance programmes in Bangladesh (Grameen, BRAC, ASA and Proshika) and one in the Philippines (Centre for Agriculture and Rural Development), described as being part of the "Grameen family" found that the neglect of deposit mobilization, the narrow emphasis on credit disbursal, the limited range of loan sizes, the standardized credit packages and the absence of any choice with regard to repayment schedules were integral components of the strategy of microcredit programmes aiming to make programmes easier to monitor and reduce operational costs and required levels of staff. Arguing that the much-hyped variables of borrower participation in programme design, social collateral generated by the five member, primary-level groups and the absence of subsidy have constituted the popular "myths" of microfinance programme success and have obfuscated the real factors underlying programme success, Jain and Moore (2003) have emphasized that the strategy of maintaining a narrow and standardized operational focus was one of the real reasons for the success of microcredit programmes (Jain and Moore, 2003). Researchers have consequently characterized the current generation of microcredit organizations and programmes as "product-centred" (Dunn, 2002) or a "limited product" industry (Cohen, 2002). While 'product-centred' microcredit programmes, which offered standardized products such as involuntary savings and short term working capital loans, constituted the 'first revolution' in microfinance by facilitating expansion of outreach and reducing transaction costs, they have simultaneously limited the social and financial performance of the microcredit sector by adversely impacting depth of outreach (ability to reach the poorest) and client retention (Dunn, 2002). Product homogeneity has been identified by the microcredit literature as primarily responsible for walk out by borrowers and high rates of client desertion that have plagued several programmes (Dunn, 2002; Cohen, 2002).

***b) Asymmetrical power equations between programme staff and clientele***

The non-participatory nature of programme design, limited member participation in crucial policy and operational decisions, the relative power and authority that programme staff command vis-à-vis clientele and the manner in which these interact with peer group pressures arising from the joint liability contract have been identified as key programme-related factors that limit the scope for manouvre of the poorer clientele of microcredit programmes. Fernando (2001), based on his field study of ASA and Grameen programmes in Bangladesh, notes the popular perception of the MFIs as money lenders whose lending practices were less sympathetic than those of their traditional counterparts. As decisions pertaining to programme goals and the structuring of credit packages were negotiated between donors and the top level NGO management and subsequently standardized and applied nationally, the amount and timing of loan delivery were determined not by the needs of households but by their ability to satisfy the eligibility conditions of NGOs and meet their financial targets. The resultant inflexibility was found to have led to poorer members sometimes paying weekly installments by selling home grown vegetables or giving up the purchase of books for children or medical treatment (Fernando, 2001).

In a study of microcredit programme impact on crises coping strategies of members, Montgomery (1995) found that the resources of the village organizations of BRAC including member savings and the Group Trust Fund were controlled, not by the village organization, but by the field staff, who also controlled the accounting and management of the village organization's financial resources. Jain and Moore's study also points out that borrower attendance at weekly meetings conveyed a semblance of participation but camouflaged the fact that there was in effect no participation of members in either operational or policy decisions of microfinance programmes. The terms of loan, savings, repayment and duration were decided by the organization and the role of members in even sanctioning the recruitment of new members was limited and could be vetoed by staff (Jain and Moore, 2003). Research has also found that the structurally unequal relations between programme staff and clients have worsened even as expansionary pressures and a focus on repayment performance have gained momentum. Observing a shift from a more participatory and egalitarian to an authoritarian and hierarchical pattern of interaction between programme staff and clientele, Montgomery (1995) found that the changing power equations in favour of programme staff circumscribed the capacity of BRAC to address the crisis of members and favoured repayment discipline at the cost of protection of poorer members.

It has also been observed that peer pressure in Grameen styled programmes rarely worked at the level of the primary-level joint liability group of 5 members and operated instead at the level of the larger, secondary-level village organization of 50-55 members (Jain and Moore, 2003; Montgomery, 1995). Jain and Moore (2003) have observed that programme staff, who do not return to the office without the weekly installments, use more influential people within the secondary groups to pressurize defaulters to repay and deploy, in effect, the same strategy as traditional money lenders. Programme staff also presided over informal arrangements by which other secondary group members provided interest free, short term, temporary loans to potential defaulters to enable them to keep up the weekly repayment. Defaulters were subsequently required to repay the informal loans and the programme loans simultaneously. Montgomery's study found that it was customary for field officers to use the threat of starving the entire village organization of future loans unless defaulting members paid up (Montgomery, 1995). The resultant pressures upon the poor were manifested in coercive tactics that involved forced seizure of utensils, small livestock and other property of defaulting members either by other members or by field staff themselves. The exclusionary logic of such pressures have also implied eviction of the poorest members as an act of self protection undertaken by village organizations, which Montgomery (1995) has commented upon as constituting a "notable gap between the rhetoric of BRAC's social objectives and the reality of solidarity group practices which tend to undermine member willingness to extend support to the more vulnerable" (p 14).

*c) Invoking the dark side of peer pressure*

Critics have also contended that microcredit programmes hold punitive implications not only for poorer members but also for individual borrowers facing a cash flow or income

crisis who shift from being “ideal peer” to “bad risk” for their co-members given the dynamic state of poverty and economic well being (Montgomery, 1995). Montgomery’s study found that joint liability groups were much less homogenous than assumed by peer group theory and that the perpetuation of group homogeneity over a period of time was threatened by the contingencies and economic crisis that the poor were always vulnerable to. Based on a study of TRDEP and BRAC in Bangladesh, Montgomery et al (1996) point to the fragile and limited nature of mutual support extended by group members to those in financial difficulty, vulnerable to collapse after the first few weeks under pressure from project officers. A microcredit study in Bangladesh had reported a conversation with a woman BRAC member, who had recalled with pride the experience of pulling down the house of her co-member for defaulting on a housing loan (Khan and Stewart, 1992 in Montgomery et al, 1996). Hulme and Mosley (1996) note that a spate of Grameen member suicides, reported in the Bangladeshi press, had resulted from the incapacity of the unfortunate individuals in question to face their peer group members on account of their inability to honour repayment commitments.

However studies have found that differences among target group members are based, not only on differential experience with repayment pressures, but also on initial levels of asset ownership. In the course of their field study, Montgomery et al (1996) had come upon the case of a large women’s village organization with 65 members, 15 of whom were markedly poorer than the rest and were denied loans by the better off members. Jude Fernando (2001) makes note of the dynamics by which women, belonging to better-off households and married to locally important men, were more likely to be selected by programme staff as group leaders and center chairpersons - an outcome of the NGO’s strategy to ensure local acceptance of the programme. Where group leaders were also moneylenders and suppliers of agricultural inputs, MFI loans were extended to members on the condition that they would purchase inputs only from group leaders. In some cases women were not even aware of the loan amount they had taken from the NGO as the leader herself had bought the cow, goat or chicken. Fernando (2001) observes that peer group pressure could regulate and discipline all consumption activities of households and that members complained of surveillance by co-members of everyday expenditure on food and other essentials and spending on special occasions.

***d) Dangers of cross financing and credit escalation***

Yet another disturbing impact of the policy of credit deepening (increasing the number of loans per borrower) and the weekly repayment schedules pursued by MFIs has been the continuing dependence of client households upon informal moneylender loans so as to enable timely MFI loan repayment. Fernando (2001) found that over 85% of women in his study sample combined borrowing from more than one NGO with loans from informal moneylenders. Women members were anxious to not antagonize their relationship with moneylenders on account of their recognition that they were eligible for no more than one NGO loan a year. Moreover, dealing with NGOs entailed additional costs including compulsory savings, regulation of their consumption pattern and a penalty if the weekly

repayment was not made. Moneylenders' offered a multiplicity of services that were both more flexible and negotiable (Fernando, 2001). Gifford's study of selected Ugandan MFIs found that delay in accessing members savings and the inflexibility of the MFI loan product had led to simultaneous membership of individuals in multiple MFI groups in order to access loans whenever required for business and household needs. The combination of loans from several MFIs and informal financial sources implied high levels of debt that were unsustainable in several cases (Gifford, 2002).

Sanjay Sinha and Imran Matin's comparative analysis of the credit transactions of non-target group (i.e., relatively better off) member households and target group member households of microcredit programmes in a village in North Bangladesh also observed a preference among all MFI members for informal lenders due to their flexible rules and timely loan disbursement (Sinha and Matin, 1998). Target group members, who owned less than 50 decimals of land and were usually engaged in rickshaw pulling, a seasonal and low return occupation, found it hard to keep up with weekly repayments to the MFI and relied primarily on informal sources so as to not renege on their MFI repayment commitments. Female Grameen Bank members had not borrowed from informal sources prior to Grameen membership on account of their lack of creditworthiness in the perception of moneylenders. However, Grameen membership had altered the situation by increasing both their *need* and *ability* to borrow from informal sources. In the absence of other forms of collateral, MFI loans had become the collateral for moneylender loans for women in resource-poor rural households. As the group discussions revealed, women members perceived the real benefits of borrowing from two sources to be increased consumption and nutritional status as many reported that they were able to eat three times a day.

Sinha and Matin (1998) note an important difference in the meaning of cross financing for target group and better-off households. While better off households deployed cross financing as a strategy to meet short term liquidity constraints, target group or poorer members were forced to resort to high levels of cross financing to manage repayment pressures without possessing the actual ability to repay. While cross financing, as Sinha and Matin (1998) note, may have been sustained when loan sizes were small, most MFIs in their study were found to have put borrowers on a treadmill of increasing loan size, which, combined with fixed repayment schedules, could lead to a collapse of the household and the entire credit system. Factors that exacerbated the problem included the lack of concern of the MFI with borrowing purpose, its overriding concern with repayment performance and the absence of an inbuilt mechanism enabling MFIs to differentiate between borrowers who cross financed continuously to meet repayment deadlines and those who did so due to a short term liquidity crisis.

As we have seen above, microcredit programmes offered by MFIs responding to donor-induced sustainability could potentially punish rather than protect poorer clientele and exacerbate exclusionary pressures against the poorest by offering a narrow and standardized package of financial services, provoking coercive repayment strategies in a

context of structural disempowerment of microcredit clientele vis-à-vis programme staff, reinforcing the more dangerous dimensions of intra-group peer dynamics and putting poor households on a treadmill of increasing loan size leading ultimately to collapse. Critical studies have attempted to show therefore that the effect of microfinance programmes upon the economic well-being of client households has had differential implications for different sections of the poor and nowhere is this clearer than in the critical review of the record of microfinance programmes in reaching core poor sections and increasing the incomes of the poor, which we will be examining below.

#### **II. 4. Heterogeneity of the Poor – Lessons from income impact of microfinance programmes**

One of the key insights that we derive from literature on the poverty impact of microcredit programmes is the heterogeneity of the poor and particularly those sections usually lumped together as “below poverty line” sections so that the question of whether microcredit serves the interests of the poor and addresses poverty concerns may be reformulated into one of *which* sections of the poor microcredit is able to reach and effectively serve. David Hulme (2003) argues forcefully that the common assumption that microfinance automatically entails working with the poor needs to be re-examined in the light of the fact that large numbers of MFIs are lending to non-poor sections and even those that claim to be poverty-focussed may be bypassing the poorest. He states unequivocally that MFIs almost never work with the poorest, usually the mentally and physically disabled, the elderly, street children, the destitute and refugees. Furthermore, he notes that several MFIs have high proportions of clients who are non-poor, as demonstrated by the case of a poverty-focussed MFI that he had visited in Nyeri, Kenya, wherein all the members of a 13 member group owned cars. The record of the Consultative Group to Assist the Poorest (CGAP) in reaching microfinancial services to the poorest during its first three years (1995-98) has been inadequate enough to warrant a change of name to the Consultative Group to Assist the Not Very Well-Off (Hulme, 2003).

The commissioned study on microfinance for the World Bank’s World Development Report (2000/1) which reviewed the operation of 7 microfinance programmes in 4 countries (Bangladesh, Uganda, Bolivia and the Philippines) was unequivocal in its finding that microfinance programmes did not reach destitute sections who were firmly outside the reach of most programmes, that the extreme poor sections who did participate were not a majority and that the majority of clients were found to belong to moderate poor and vulnerable non-poor households (Sebstad and Cohen, 2000). The growing body of literature on the functioning of the current microfinance programmes had led to attempts by some NGOs to modify lending strategies and to take up a wider spectrum of development activities that may suit the needs of poorer sections better (Kabeer, 2002). BRAC initiated the Income Generation for Vulnerable Group Development (IGVGD) programme that targeted women from the poorest, landless families and provided them with a monthly wheat ration for two years, during which period they started a savings group, participated in training organized by BRAC in some income generating activity and received credit to



start the activity. The combination of relief, training and credit provided to women from the poorest households was found to have been successful in reaching destitute women, who were usually excluded from NGO activities (Kabeer, 2002). The experience of the IGVGD indicates clearly that core poor sections may need to be pro-actively assisted over a length of time even to qualify for MFI membership.

The urgency of the need to seriously engage with the issue of socio-economic differentials among clientele of MFIs has been reinforced by income impact findings of microfinance programmes, that point to the greater capacity of the “upper” and “middle” poor sections, when compared to the “core poor”, to take advantage of the enterprise possibilities opened up through access to microcredit programmes. David Hulme and Paul Mosley’s study, which critically examined the poverty alleviation impact of 13 selected microcredit programmes worldwide, found that well designed lending programmes could move large numbers of poor people above the official poverty line. However, there was clear evidence to show that the impact of the loan on borrowers’ incomes was related to their existing level of income. As borrowers with higher income levels and higher access to information about market conditions could access a wider range of investment opportunities and cushion themselves better against risks, initial life circumstances was found to be the most important factor accounting for successful entrepreneurship (Hulme and Mosley, 1996). A study of TRDEP and BRAC in Bangladesh (undertaken as part of Hulme and Mosley’s work) by Montgomery et al (1996) found that graduation out of poverty for third time loanees was visible in TRDEP, whereas the evidence on BRAC was less optimistic on account of the relative preponderance of poorer households in BRAC’s overall membership profile. Hence they point out that credit could have different implications for different segments of the poor and could well create additional risks for the very poor.

Differences between the “upper” and “middle” income sections also appear as important as differences between these and “core poor” sections of the population as demonstrated by the Hulme and Mosley (1996) study which found that “upper poor” households may be able to invest in successful income-generating enterprises, whereas the “middle poor”, less-educated and connected than the former, may not be able to profit from enterprise opportunities unless the formal economy experienced considerable growth. Hence, middle poor sections, who are provided with enterprise credit, may require proactive and ongoing assistance from the sponsoring MFI with technical innovation, product development and marketing.

We note that the critical question of differing capacities of different sections of the poor to exploit avenues for income generation through self employment foregrounds a more fundamental limitation of microcredit that transcends issues relating to programme design, poor-unfriendly or otherwise, and points rather to the structural limitations of certain sections of poor households that thwart their capacity to absorb and put to productive use enterprise-linked credit.

## **II. 5. Challenges of enterprise failure, sustained income increases and unfavourable macro economic conditions**

Income impacts of microcredit programmes are further complicated by the observed phenomena of microcredit financed enterprise failures, the inability of microcredit programmes to generate sustained increases in levels of income growth and instability and decline in the larger economy. The Hulme and Mosley (1996) study had found that nearly every programme studied reported cases of borrower bankruptcy after the failure of enterprises. While 10-15% of enterprises of borrowers of Bancosol, Bolivia were reported to go bankrupt, about 20% of the most vulnerable borrowers of the Thana Rural Development and Employment Programme (TRDEP) were observed to have dropped out before they took their third loan. An evaluation of BRAC's group loans for deep tubewells showed that a majority of borrowers, particularly the poorer ones, had lost their assets or suffered income losses on account of their involvement in the programme and that the poor had absorbed the risks of the unviable deep tubewell experiment *initiated by the MFI*. Around 25% of activities funded by the Malawi Mudzi Fund (a Trust fund which is a branch of the central government of Malawi) had failed, especially in the first phase, when managers misunderstood the nature of borrower risks. The operation of the KREP Juhudi programme (an NGO in Kenya) showed unofficial pledging of assets within the group that borrowers were at risk of losing in the event of failure of their enterprises. Hulme and Mosley observe that given the scale of drop out from the selected programmes of their study, there may have been significant under reporting of microcredit-induced crisis. *We note here that given the efficacy of microcredit programmes in reaching sections of the poor hitherto untapped by the mainstream banking sector, the failure of credit-financed enterprises could imply the collapse of livelihoods for these sections, with the costs of collapse being exceptionally high.*

Furthermore, where credit schemes had increased income, Hulme and Mosley (1996) observe that it was largely in the nature of 'one step up' followed by stagnation as reflected in the case of income increases through rice hulling or the purchase of rickshaws. As such activities provided neither the technological nor the entrepreneurial basis for poor borrowers to attain higher levels of sustained income growth, respondents from Bangladesh, Kenya, Malawi and Srilanka were found to have repeatedly expressed a desire for new forms of income generating activities that would facilitate progress beyond present income levels. The study also found no evidence of impact of microfinancial service provision upon structural factors such as an enhanced demand for services or goods produced by the poor or for labour of the poor, at regional or local levels, which could have led to increased wage rates. The study maintains that the above-mentioned structural factors such as changes in the effective demand for the labour or the goods produced by the poor could only have been altered by economy wide changes (Hulme and Mosley, 1996)

Studies have also underscored the need to take cognizance of the prevailing situation in the wider economy and polity, which exercises a pivotal role in determining the fate of the micro enterprises launched by the poor. A study of three microfinance institutions in

Ahmedabad, India (the SEWA bank), Zimbabwe (Zambuko Trust) and Peru (Accion Comunitaria del Peru) argues that the impact of microcredit programmes can be expected to be smaller when the economy stagnates and when opportunities to earn positive returns on investment decline and the pressure to borrow to meet financial obligations increases (Snodgrass and Sebstad, 2002). The study found that structural shifts in the regional economy of Ahmedabad (including the decline of the traditional textile mill sector) had increased competition and crowding in Ahmedabad's urban informal sector, while recession and unreliable economic growth had characterized the study period in Peru. In Zimbabwe, the study years were marked by an economic decline that deteriorated into an economic collapse and by a devastating AIDS pandemic.

The divergent experiences of different sections of the poor with microfinance programmes and especially the findings relating to the disjuncture between enterprise credit and the life circumstances of core poor sections have been manifested in increasing policy interest in and emphasis on "protectional" as opposed to "promotional" credit, as we see in the following section.

## **II. 6. Moving from "Promotional" to "Protectional" Strategies**

A more comprehensive conceptualization of poverty as a dynamic process that is continuously responding to a variety of contingencies exerting downward mobility pressures upon poor households underlies the case forwarded by researchers for strengthening the vulnerability reduction and income-smoothing effects of microfinance programmes. The more multi-dimensional understanding of poverty, which has challenged the conceptualization of households as possessing stable incomes or consumption standards that may be threatened by a sudden shock, holds that incomes of the poor fluctuate all the time in ways that are only partly predictable (Matin and Hulme, 2003). Based on their study of 13 microfinance programmes across the globe, David Hulme and Paul Mosley (1996) argue that microcredit programmes would do well to prioritize protectional strategies (comprising easy access savings, insurance, timely emergency loans and consumption loans as soft loans) or those that prevent the incomes of the poor from falling below a certain threshold level. Protectional strategies work better for core poor sections by smoothing income and consumption fluctuations and strengthening coping strategies in the event of a life cycle (such as the death of an earning member) or a natural disaster related crisis (such as flood or famine that destroys the livestock) (Hulme and Mosley, 1996). It has been argued that risk managing financial services, that constitute an important component of protectional strategies, such as liquid savings that can be drawn down during crises or micro insurance facilities that insure against death, disability, accidents and illness, are not only more appropriate for poorer segments than the traditional micro enterprise loan, but also serve the existing clientele of MFIs better as even successful micro entrepreneurs are vulnerable to economic crises (Churchill, 2002).

Hulme and Mosley (1996) attribute the neglect of protectional strategies within microcredit programmes to the overriding preoccupation with promotional lending for

income enhancement purposes, which has dominated the microfinance sector over the 1980s and 1990s. The consequent focus on rigidly designed enterprise loan schemes has limited the capacity of the microfinance sector to address the fluctuating poverty levels of households through the design of a flexible and wider array of financial services. Promotional strategies, premised on a reductively conceptualized “income-poverty” approach, aim at increasing low incomes of poor households through loan-financed enterprises and derive from an understanding of poverty reduction as a linear, uni-dimensional process of moving households from a stable below poverty line to an above poverty line situation. Hulme and Mosley (1996) maintain that the simplistic understanding, reflected in the “low income, low credit, low investment, more income, more credit, more investment’ model (advocated by prominent microcredit practitioners such as Muhammad Yunus, founder of the Grameen Bank), ignores complicated realities reflected in the differing abilities of the poor to seize entrepreneurial opportunities, their heterogenous economic situations and the situation prevailing in the wider economic environment. By arguing that there is little that promotional strategies can do to protect the poor against downward mobility pressures that increase their vulnerability, they contest the popular assumptions that credit is the primary resource required by *very poor* sections in overcoming poverty and that *microenterprise* loans are invariably effective anti-poverty weapons.

Other impact assessment studies of microcredit programmes have likewise reiterated the protectional role of microfinance upon clients’ incomes and livelihoods and have expressed skepticism about the prospects of promotional lending in the face of hostile macro environments. Snodgrass and Sebstad’s study of three microfinance institutions in India, Peru and Zimbabwe cautions that their findings would disappoint those who expect that microfinance can abolish world poverty since the net movements of households among the three global poverty groups over the two year study period of 1997-1999 were small (Snodgrass and Sebstad, 2002). While programme participation had enabled clients from extremely poor households to meet basic needs better in Zimbabwe, the study found that movement into and out of poverty was associated more with household size and structure than with microfinance access. During the survey period in India (1997-1999), while there was modest net improvement in the poverty status of sample households, many households fell back into poverty or sank from moderate into severe poverty at the same time as many others advanced. Snodgrass and Sebstad (2002) maintain however that their findings firmly establish the protectional role of microfinance, which operated by diversifying sources of household income, increasing savings, expanding credit options and improving household money management.

The evidence on the limited income impact of microfinance, especially upon poorer sections, was also reflected in the theme of the commissioned study for the World Bank’s World Development Report (2000-01) “Attacking Poverty”. The WDR (2000/1) commissioned study on microfinance focused on the impact of microfinance on *non income* dimensions of poverty and specifically on the ways in which people use microfinance services to build assets, mitigate risks and reduce vulnerability (Sebstad and Cohen, 2000). The study found that MFI credit constituted an important part of household money management

strategies and was used as a *protectional risk management strategy* by clients as MFI loans enabled them to build and diversify assets ahead of time that could be drawn upon in times of need. The three key pathways by which borrowers reduced vulnerability through access to microfinance services were identified as being the use of microcredit to smooth income fluctuations through physical (housing), human (investing in the health and education of household members) and social (investing in kin relationships) assets and to empower women (through increasing women's participation in household decision making and their control over household assets). The study also noted that clients preferred to save with informal sources rather than with the MFI in question on account of the absence of good voluntary savings facilities in most programmes. The study outlined the prospective challenge before MFIs as being the need to orchestrate a better fit between microfinance products and client needs by diversifying the hitherto relatively homogenous microfinance product package and by ensuring that loan size, repayment amount and the repayment cycle dovetail better with client needs. (Sebstad and Cohen, 2000).

The emphasis on protectional strategies that are better equipped to address poverty as a dynamic process rather than a static condition has been accompanied by the exhortation to develop a client-responsive, demand-driven and market-driven agenda for microcredit programmes. The growing body of empirical evidence on the adverse effects of homogenous financial products and rigid programme design has caused microcredit researchers to argue the imperative of a shift from a 'product-centred' to a 'client-centred' microcredit sector which understands client needs and preferences, internalizes the basic business principle that "it pays to know the customer" and acquires the characteristics of a demand-driven industry by developing a 'market-driven', 'client-driven' microfinance agenda (Dunn, 2002; Cohen, 2002). Concerns over growing competition within the microcredit sector, client dissatisfaction and high drop out rates from microcredit programmes combined with the recognition that the poor do not want to continuously graduate to higher loan sizes or even borrow all the time have led to MFI interest in understanding the nature of client demand (Cohen, 2002). Restructuring financial products so as to achieve a better fit with client preferences and offering a diversified array of financial services have therefore emerged as priority areas of action for the microfinance sector (Meyer, 2002; Cohen, 2002). It is expected that diversified financial services will not only enhance the developmental impact of microfinance programmes but also address the phenomenon of disgruntled clients 'voting with their feet' by walking out on programmes and thereby address institutional sustainability concerns as well. It is argued therefore that the diversification of financial services could potentially represent a scenario of win-win by reducing client vulnerability as well as improving the financial bottom lines of MFIs (Churchill, 2002). Even as it emphasizes the need to go beyond defining success only in terms of financial ratios calling for the incorporation of client satisfaction measures, the case for a market driven microfinance agenda is made within a framework of long-term institutional sustainability and best practice financial performance (Cohen, 2002).

In Section II, we have seen that pressures generated by the "New Consensus"

emphasizing the twin goals of financial sustainability of the lending institution and expansion of programme outreach have been manifested as increasing pressure on MFIs and NGOs to alter their lending practices so as to ensure the attainment of economies of scale and repayment performance that enable independence from donor subsidized capital. We have reviewed the chequered record of microfinance programmes in enabling poorer sections to overcome poverty and in protecting the poor from plummeting downwards into greater levels of indebtedness and impoverishment on account of enterprise failure or life cycle and other crises. These research findings have caused researchers to argue against the instrumental use of micro loaning to exclusively promote enterprises and to emphasize instead the more useful role that credit could play if its latent protective potential were to be better exploited by microfinance programmes through the design of a wider array of flexible, microfinancial services. We have also seen that socio-economic heterogeneity of the targeted clientele of microcredit raises issues that extend beyond programme design and points to the need to seriously engage with the wider policy environment and the level of preparedness of a household to bear the risks associated with an entrepreneurial venture. Section III attempts to trace the ways in which these insights have found their way into the dominant discourse around microfinance and have forced some of the globally important institutional players in the field of microfinance to take cognizance of the import of research on microfinance.

## **Section III**

### **III.1. Microfinance, Vulnerability reduction and Risk Management**

Research findings that have problematized the “more income, more credit, more investment” model and challenged the exclusive enterprise orientation of microfinance programmes have fed into the microfinance discourse and have effected a shift in the projection of microfinance, best exemplified by the changing references to microfinance between the World Bank’s World Development Report (WDR) of 1990 and the WDR of 2000-2001. The World Development Report “Poverty” published by the World Bank in 1990 along with the UNDP’s annual publication - the Human Development Report have been hailed as the seminal texts signaling the re-articulation of poverty as the prime development concern of the 1990s. Microcredit finds place in chapter 4 of the WDR (1990) titled “Promoting Economic Opportunities for the Poor”, which identifies increasing access to credit as one of the strategies aiming to increase participation of the poor in growth processes along with increasing access to land, infrastructure and technology and improving tenancy. The WDR (1990) argued that the older generation of subsidized credit programmes for the poor had resulted in considerable leakage to the non-poor and non-viability of the lending institution and that very small proportions of the poor had actually enjoyed access to institutional credit in Latin America, Africa and Asia. The report concluded that recent innovations in financial intermediation pioneered by NGOs, donors and governments had led to successful coverage of extremely poor sections, as demonstrated by the case of the Grameen Bank’s clientele, and that micro enterprise lending

was shown to have had considerable impact on the income levels of the poor (World Bank, 1990)

In stark contrast, the WDR (2000-01) emphasized the potential of microfinance programmes to better address concerns of vulnerability and risk management (given appropriate programme design) relative to those of overcoming poverty through income enhancement. As we have already seen, research findings that highlighted the “protectional” as opposed to the “promotional” dimensions of microfinance had influenced the chosen theme of the commissioned study of the WDR (2000/1) on microfinance viz., microfinance impact on *non-income* dimensions of poverty. The World Bank’s framework for attacking poverty, as elucidated in the WDR 2000/1, emphasized action on three inter-related fronts: Empowerment (addressing economic, social and institutional inequalities that prevent the poor from gaining access to influence over policies and interventions that influence their lives), Security (addressing the risk and vulnerability that poor nations are increasingly expected to face in the global economy and that the poor within nations have always experienced) and Opportunity (creating the conditions for human and physical investment and sustainable economic expansion in which the poor participate fully). It is interesting to note that microfinance finds place in the section on “Security” as one of the policy responses for improving risk management alongside health Insurance, old age assistance and pensions, unemployment insurance and assistance, public work programs, social funds and cash transfer to vulnerable sections (World Bank, 2001).

In the WDR (2000-01), risk management and vulnerability reduction emerge as the prime benefits gained through access to microfinance services. It is argued that microfinance helps the poor smooth consumption during periods of shock by averting distress sale of assets and replacing productive assets destroyed during natural disasters and that it helps households reduce vulnerability to income shocks by diversifying income sources and creating the capital needed to expand micro enterprises. As a risk management tool, the WDR (2000-01) reiterates that the key strength of microfinance inheres in the knowledge that loans will be available when needed by client households, who can subsequently move towards more proactive strategies by planning to mitigate risk. In stark contrast to the WDR (1990) which had commended microfinance programmes for their outreach to extremely poor sections, the WDR (2000-01) acknowledges that most programmes are more successful in reaching moderately poor sections or those just above or just below the poverty line rather than the poorest and recommends greater flexibility in loan size and repayment so as to reach poorer sections (World Bank, 2001).

Microfinance impact findings have also influenced the tone of theme papers and documents of the CGAP (the most aggressive propagandist of the sustainability and upscaling paradigm within the microfinance sector) as reflected in the Strategy Paper that sets out the broad directions and priorities that will guide the third phase of the Consultative Group to Assist the Poorest (2003 – 2008) prepared on the basis of discussion between

member donors, the Policy Advisory Group, the CGAP Secretariat and global leaders in the microfinance sector (CGAP, 2002). The Strategy paper asserts that “traditional microfinance”, which used to be understood as a credit methodology that employs effective collateral substitutes to deliver and recover short term working capital loans to micro entrepreneurs, was premised on the perception that the micro enterprises of clients grow, increase their incomes, create employment and lift the poor out of poverty. It notes that the core premises of traditional microfinance have had to contend with the challenges posed by the realization that not all the poor manage growing micro enterprises, given their extreme diversity, and that the poor need financial services that extend beyond working capital loans and encompass services such as savings, insurance and money transfer. The Strategy paper noted that earlier expectations that NGOs offering microfinance programmes would grow, become independent from donors and perhaps even transform into banks for the poor have been belied on account of the considerable challenges that NGOs have faced in terms of cost structures, legal frameworks and governance. It is suggested therefore that institutions with large existing infrastructures such as commercial and state owned banks (“despite their troubled history”), credit union networks, financial cooperatives and even retail chains may provide the answer to the scaling up of financial services for the poor. The “new vision of microfinance”, as elucidated by the Strategy Paper, is therefore about “diverse institutions providing massive and permanent access to a broad range of financial services for a broad range of clients”. This new vision is further reflected in 2 of the 4 strategic priorities that will guide phase III of the CGAP viz., fostering a *diversity* of financial institutions that serve the poor and facilitating the access of the poor to a *wide range* of flexible, convenient financial services (CGAP, 2002, emphasis mine)

An important point to note, at this juncture, is that by tracing the shifting discourse around microfinance as a poverty alleviation strategy, we are not positing that microfinance has been displaced from its former pivotal position within the dominant development discourse as an anti-poverty strategy of great efficacy. As claims regarding the ability of microfinance programmes to lift all poor households above the poverty line have been contested, the current set of expectations of microfinance programmes, propagated by the development orthodoxy, have scaled down the merits of microfinance to a commensurate degree but have not displaced it from its pre-eminent position as a key anti-poverty weapon. We are arguing that even as concerns of vulnerability and risk mitigation have themselves become central to the turn of the century development discourse, and the conceptualization of poverty itself has moved away from an earlier income bias to integrate broader concerns related to well-being, microfinance finds itself upheld as the key route by which poor households may hope to evade downward descent into intensified levels of immiserization. Indeed the valorization of microfinance as a household level risk management strategy has gained importance at the time that “Safety nets”, “Risk Management” and “Vulnerability Reduction” have emerged as the catchwords of the development world concerned over the possibility of - as Naila Kabeer (2003) points out - an increase in the vulnerability of populations across the globe in response to the inception of Structural Adjustment Programmes, economic reforms, globalization processes,



international and regional financial crises, environmental degradation and demographic transition or the phenomenon referred to as “the graying of populations”. Safety nets, already projected as one of the three key anti-poverty strategies espoused by the World Development Report (1990-91) of the World Bank, alongside labour-intensive growth and enhanced investment in human capital, had come to constitute a central plank of the poverty agenda during the 1990s. Safety nets have been propagated as the key mechanism for protecting households and individuals from income shocks (associated with the effects of structural adjustment policies) that threaten their immediate consumption levels or undermine their long term livelihoods (Cook et al, 2003; Vivian, 1995). The conceptualization of poverty as a dynamic process, rather than a static condition and a corresponding concern with unforeseen changes in income flows of poor households have placed vulnerability and risk management at the center of safety net based poverty interventions (Kabeer, 2003). Morduch and Sharma (2001) further note that the emphasis laid on addressing income fluctuations derives from the realization that risk can be a great burden to carry for the poor and that the measures that poor households use to reduce risks can be detrimental and carry significant, long term costs such as withdrawing children from schools, reducing consumption of nutritious food, curtailing investments on business assets, neglecting social obligations, entering patron client relations on disadvantageous terms and selling productive assets. The agenda of reducing vulnerability has therefore ascended to the top of safety net strategies and constitutes the central block of the World Development Report (2000/2001).

### **III. 2. Some questions on the efficacy of microfinance as safety net**

We have seen so far that the poor record of microfinance programmes in reaching the poorest, retaining core poor sections as members, protecting their livelihood strategies and in offering an array of flexible, timely and easy access services that include savings and insurance, and not just a standardized credit package, have forced upon microfinance lobbyists a realization of the yawning chasm between microfinance rhetoric and observed reality. However, it may be argued, that notwithstanding the attempt to detach microfinance from an exclusive focus on micro enterprise lending and to move away from an earlier vision of microfinance as inevitably launching micro entrepreneurs who storm their way out of poverty, by envisioning microfinance as a strategy that protects the incomes, livelihoods and consumption of the poor, the new discourse does remain limited in some important ways.

Responses by the dominant microfinance lobbies to the mounting criticism of microfinance programmes indicate the tremendous resilience of the microfinance discourse and its capacity to reinvent itself, as it were, to suit the changing needs of the situation. Researchers have pointed to the propensity of powerful microfinance lobbies in the development world to deflect the more serious implications of the critical assessments of microfinance programmes and the critical engagement with the practice of microfinance that they warrant either by shifting the terms of reference so that unanticipated outcomes are accounted for or by shifting the nature of claims made about microfinance (Weber,

2001). Mayoux (2002) argues that the poor record of most programmes, where financial sustainability is a key concern, in reaching the poorest sections, rather than provoking a re-examination of the question of whether some level of subsidy may be necessary for microfinance programmes for the very poor, as in the case of other poverty reduction programmes like health and education, has prompted instead a moving away from the focus on credit for these groups to a focus on savings and more recently insurance. This new development may be perceived as being convenient for donors and programmes given that even loan finance for the very poor is not necessary anymore and the latter can be persuaded to forego investment in economic activity and postpone present consumption through the focus on savings, which can then perhaps be used by the MFI as capital to onlend to the less poor and make a profit. Mayoux (2002) sums it up succinctly when she notes that the dominant microfinance discourse appears to be moving away from exhorting people to pull themselves up by the bootstraps (income generation through micro loans), to getting them to pay for the bootstraps (the focus on savings) and more recently towards getting them to bear the risks of the bootstraps snapping (insurance).

We note that the purpose of strengthening the safety net functions of microfinance programmes by incorporating other financial services would be defeated where programme structure continues to be geared towards attaining financial viability. Recently, there has been much discussion on the ways by which the incorporation of micro insurance services into microfinance programmes could contribute immensely towards enhancing the safety net functions of the latter (Churchill, 2002). However, Morduch and Sharma (2001) acknowledge that the tendency of most microinsurance programmes to deny coverage to older clients in order to reduce adverse selection and to avoid selecting clients from the poorest households could end up undermining the safety net function of microfinance. They argue therefore that while micro insurance may help vulnerable households cope with the risks of daily life, it would not be a good substitute for broader public measures that remain indispensable. Research on the poverty impact of microfinance programmes and their treatment of relatively poorer sections that we have reviewed in Section I unambiguously demonstrates that flexible, negotiable and participatory programme design involving multiple financial products is imperative in order to enable microfinance programmes to meet the protectional objective of mitigating risks and reducing vulnerability of poor households to stress events. However, where a narrow and standardized operational focus is an essential programme strategy of cost reduction and easy monitoring (Jain and Moore, 2003; Cohen, 2002), we may well wonder whether the political and institutional configurations that currently sustain the microfinance sector need to radically change in order to enable a sufficiently large number of programmes sensitive to other concerns to emerge. The refusal on the part of the more powerful backers of microfinance to reconsider the issue of forcing sustainability as a necessary objective of the MFI testifies to the intertwining of the global development agenda with neo-liberalism inspired efficiency concerns. Even as the WDR (2000-2001) calls for the redesign of microfinance products so as to reach poorer sections and for more flexible repayment and loan size, it admits

that there is a practical limit to this accommodation as the increasing costs of making such loans will undermine sustainability of the lending institution.

Yet another important limitation has to do with the expectation that microfinance programmes enable the poor to manage risks at a period when the state is withdrawing from its traditional welfare responsibilities, as attested to by studies from several developing countries. The background study of the World Development Report (2000-2001) on microfinance conducted in 4 countries found many clients interviewed across countries and programmes using a part of their loans in order to meet the growing pressures of educational expenses since economic reform policies and decline in public education expenditures had caused unexpected increases in educational expenses (Sebstad and Cohen, 2000). As our perusal of the Strategy Paper for Phase III of the CGAP revealed, the limitations of microfinance programmes in reaching the poorest sections and in enabling the poor to establish viable micro enterprises have only led to an exhortation to broaden the spectrum of financial services offered and to widen the institutional actors involved in the disbursement of financial services to the poor. The most influential actors in the world of microfinance have not seriously interrogated the issue of whether a wider array of financial services, howsoever flexibly delivered, can be effective in mitigating vulnerability and serving protectional purposes in a context of a rolling back of the developmental commitments of the welfare state. We note at this juncture that social policy analysts have been arguing that safety nets need to grow beyond being merely crises coping, transitory and relief-oriented and develop into more sustainable and stable mechanisms of social protection which are integrated within broader economic processes (Cook, 2003). Where macro economic developments appear to suggest the disinclination of the state to continue to fulfill its developmental and welfare responsibilities, it becomes difficult to imagine that the objective policy conditions would facilitate the maturity of microfinance components of safety net strategies into social protection mechanisms integrated within broader economic processes.

In Section III, we have attempted to show how the shifting conceptualization of microfinance as an anti poverty strategy has been reflected in influential policy documents of prominent institutional actors such as the World Bank and the Consultative Group to Assist the Poorest. We have seen also that microfinance continues to enjoy center stage as a critical anti-poverty weapon given that the foregrounding of its potential to enable households to manage risk and reduce vulnerability coincides with the emergence of social protection and safety nets as the prime concerns of the global development community. Finally, we have attempted a critique of the currently celebrated protectional dimensions of microfinance by pointing to the constraining structural conditions within which societies are attempting to use microfinance to meet their social security and poverty related development concerns. In Section IV, we will be attempting to explore the lessons that the critical studies of microfinance and the shifting discourse of microfinance may hold for the Indian microfinance sector.

## Section IV

### **IV. 1. Evolution of the Indian microfinance sector: a differential trajectory**

At the outset, we note that the institutional and policy pressures that have driven the development and the growth of the self help group based microfinance sector in India vary substantially from the global, largely World Bank dictated pressures that we have outlined in Section I. The promotion of self help group based microfinance in India did not come about through dissemination as part of a package of World Bank sponsored social relief programmes aiming to contain the fallout of neo liberal economic reforms as in the case of several other developing countries. A defining feature of the evolving microcredit scenario in India, that several analysts have identified as marking the Indian microfinance landscape as distinctive from that of other countries, has been the significant role that public sector formal lending institutions, especially the nationalized commercial banking structure, has played in the establishment and expansion of financial intermediation through SHGs (Harper, 2002 a). The role of NABARD, the prime institution promoting agricultural lending in the country, in generating widespread policy acceptance for the novel idea of linking NGO-promoted, neighbourhood-based self help groups comprising primarily women from low-income, rural households with commercial banks, has been one of foremost significance. It has been observed that the Indian microcredit experience did not even require considerable conceptual support from external donors as NABARD possessed the requisite professional capabilities to conceptualize the linkage program and select the most appropriate experience for emulation from among the early SHG bank linkage projects in Asia (Kropp and Suran, 2002). NABARD's policy initiatives, supported by the RBI, have been instrumental in the development of the NABARD-MYRADA three year action research project, initiated in 1986-87, into a nation-wide pilot project linking 500 SHGs with nationalized commercial banks in 1992, which eventually culminated in the mainstreaming of SHG banking as a corporate strategy of banks in 1996 (NABARD, 1999; Fernando, 2000) It has since grown into what is often described as the world's largest microfinance programme.<sup>5</sup> NABARD (2002-2003) estimates that over 90% of the self help groups linked to banks under the SHG-bank linkage scheme comprise women's groups.

An account of the evolution of SHG-banking in India describes the NGO MYRADA's struggle against the attempted imposition of the Grameen Bank model in India which would have implied the establishment of a parallel banking structure to cater exclusively to SHGs. Arguing that India has had 196 Grameen Banks (the Regional Rural Banks), older than the Bangladesh model, created in order to provide low-cost, easy-access credit to the poor in a flexible manner and that the nationalized banking infrastructure in India, particularly in the Southern and Western states, was much more widespread than in Bangladesh, Aloysius Fernandez, Executive Director of MYRADA, states the case for strengthening the alternative system of SHG based lending, governed by its own rules and supported by the official banking sector, rather than creating a new structure altogether. Fernandez (2000) notes that some high-ranking Indian officials, enamoured of the Grameen model, had

summarily informed him that the only way was to establish Grameen clones. After the entry of big donors such as the World Bank and the CGAP into the arena of microfinance in the mid 1990s, the agenda of initiating Grameen clones was renewed afresh and a few microfinance organizations in India did adopt the Grameen model so as to become eligible for funding support from the CGAP (Fernandez, 2000)

#### **IV. 2. Peer group based lending in India and Bangladesh: operational differences and their implications**

Where the Indian SHG experience is concerned, we need to note the organizational specificities that distinguish self help group based microfinance in India from Grameen style peer group based lending in Bangladesh and elsewhere. A collective of about 20 members, the self help group, whether sponsored by a government department, commercial bank or NGO, saves a pre-determined amount every month and lends its savings on a monthly basis to group members, whether for consumption or income-generation purposes, usually on terms decided by group consensus. In addition to group savings, repayment installments and interest income from loans that constitute the group's loanable funds, the group may also borrow from outside, either from the commercial bank with which it maintains a group account or from the NGO sponsoring it, in order to supplement the group's loanable funds. Coordinators selected from within the group assume responsibility for maintaining group accounts, liaising with the banks and other government departments. We note the contrast with the Bangladeshi MFI model wherein the group saves with the local branch of the MFI/NGO and borrows loanable funds from the MFI, that the latter, in turn, may be availing from donor sources, whether as grants or as low-interest loans. Borrowing terms are set by the MFI, while paid staff of the MFI manage the group's financial resources.

As SHG members maintain their individual accounts with the SHG (and not with the sponsoring NGO), the village-level primary group or self help group is the retailer in the Indian case and performs most of the transaction functions, unlike in Bangladesh, where the microfinance institution is the retailer. Therefore member-controlled and self-managed SHGs, by virtue of being micro-banks, are posited as being financial organizations in their own right (Harper, 2002 b). Ownership over interest income and group-generated resources is yet another distinguishing feature between SHGs in India and Grameen-styled microcredit programmes in Bangladesh. In the case of Bangladeshi MFIs, interest income paid by clients on MFI loans belongs to the MFI and is perceived as a potential source of income for the MFI. As interest income on group loans is used to augment group corpus funds in the case of self help groups, studies have found that the SHG system, relative to the Grameen system, leaves more money with communities (Harper, 2002 b). The self help group-bank linkage project, pioneered and popularized by NABARD, involves a three-way relationship between the SHG as village-level retailer, the NGO as sponsor or promoter of the group and the commercial bank as financier of the group (Fernandez, 2000). NABARD (2002-2003) estimates that only 8% of the sponsoring NGOs also act as financial intermediaries, that borrow from external sources and onlend to the groups. The predominant model,

accounting for 72% of self help groups linked to banks, comprises SHGs that are promoted by NGOs or government agencies and linked to banks for sourcing institutional credit. In the dominant model, the NGO is only a promoter of groups and does not engage in financial intermediation activities.

#### **IV. 3. Protectional financial strategies – Better realized through SHGs?**

On the basis of the above account, we note that there are clear-cut structural differences in the relationship between the sponsoring agency and the self help groups in India and the MFI and the village level borrower groups in Bangladesh. It is possible that even within a federation of self help groups supported / sponsored by a particular NGO within a geographically contiguous area, the terms of lending on the group's corpus vary from one group to another and are determined by decisions taken at the level of the individual group. This, we note, is quite unlike the negotiation of terms between donors and top-level NGO management and the imposition of a resultant standardized, overly-centralized, top-down and supply-driven mode of microcredit delivery as in the case of the big MFIs of Bangladesh. Therefore a certain degree of flexibility and autonomy of the group from the dictates of the sponsoring agency appear to be built into the structure of self help group based transactions. We hypothesize that self help groups, by virtue of the greater scope for intra-group decision making on the terms of access to group resources and bank funds sourced under the SHG linkage scheme, may be able to more effectively harness the *protective dimensions* of financial services by responding in a timely and sensitive manner to the emergency requirements of individual members. Issues such as immediate access to loans during emergencies, availability of loans to group members at concessional rates during a period of stress, negotiation of repayment schedules and lending terms and withdrawal of savings when necessary (identified as key ingredients of protectional strategies) may be decided by group members on the basis of the perceived authenticity and urgency of co-members' needs.

By speculating that Indian SHGs are relatively free of excessive pressures from powerful and over-bearing NGOs and MFIs driven by donor impulses, we are not suggesting the complete absence of repayment pressures imposed by the sponsoring NGO or bank. We are merely suggesting that there may be more room for maneuver for self help groups not subject to the stranglehold of programme staff and non-negotiable loan packages. The fact that group members' savings, repayment installments and interest income constitute an important source of loanable funds for Indian SHGs could, we propose, have two contradictory implications for the play of intra-group peer dynamics within SHGs. It could imply relative independence from external loans routed through the NGO or sourced from the commercial bank so that groups may feel less pressured to "discipline" defaulters and be able to "protect" them instead, should the group perceive the cause of default as genuinely worthy of assistance. Groups may be able to rely on the strength of their accumulated corpus to bargain for relaxed terms and grace periods, if necessary, for individuals in distress even on external loans sourced through the sponsoring MFI. However, we cannot conclude ipso facto that relative independence from the sponsoring MFI's

pressures would necessarily generate a greater degree of peer sympathy rather than peer pressure in the case of self help groups. The fact that group-generated funds are critical to the total volume of available funds for lending purposes could mean that self help groups are equally prone to disciplinary action in the case of individual defaults. If MFI programme staff in Bangladesh use the threat of cutting off loan access to induce desired forms of group behaviour, the dwindling of loanable resources on account of delayed repayment by members could well bring to bear severe pressures on potential defaulters in the case of SHGs.

Analysis of the willingness of self help groups to accommodate the crises of individual members requires intensive, field-based research on the extent to which group norms enable an individual in distress to access an emergency loan during a period of crisis at concessional rates or to secure a modification in the terms of repayment. In the absence of formal regulations that hold in all cases, a set of informal practices on such matters may have evolved over a period of time. It might be interesting to examine the extent to which these norms apply impartially to all members or whether they are the privilege of some. It may also be the case that willingness to empathize with members in distress may not always translate into effective ability to do so on account of the limited capacity of the group to completely absorb members' crises without considerable damage to its own fragile resource base.

In this context, it may be pertinent to recount two cases of some relevance to the discussion, both of them relating to self help groups belonging to the MALAR network of SHGs of Kanyakumari district<sup>6</sup>. An SHG member who had borrowed a loan of Rs. 1000 from her group, found herself with no means to repay the loan, when her lorry driver husband died in an accident shortly after the loan was taken. Responding to her plight, the group decided to contribute Rs.40 per person to repay the principal and waive interest payment in consideration of the circumstances. We note that the ability to bear the burden of repaying a co-member's loan might not be possible in a more deprived and poorer area (as in several parts of Madurai and Virudunagar) where members' monthly savings do not exceed Rs.20 and group members report having to struggle to pay the monthly savings. In another case in Kanyakumari district, the suicide of a husband following a family dispute, forced a woman to quit the group on the ground that she would not be able to make monthly savings regularly anymore and would feel ashamed in the presence of other members who regularly saved and repaid their loans. While other members did sympathize with her predicament, they accepted her decision to quit the group as the only option available to her. We note that although the woman SHG member in the second case did not have to discharge an outstanding loan, her domestic crises had effectively crippled her capacity to make regular savings, thereby invalidating her claim upon the group's social and financial resources.

The likelihood that peer pressure generated within the self help group is not as subject to donor/lending agency pressures, as in the Grameen-styled programmes, might make it

worthwhile to explore the dynamics of intra-group pressures on defaulters in SHGs by identifying the determinants of such pressures. An analysis of the support and sympathy that individuals in distress can draw upon would warrant consideration of an institutional actor of significance - the commercial bank that the group seeks to link up with. Bank branch officers and managers might insist on checking group repayment records and making direct visits to groups before sanctioning loans under the SHG bank linkage scheme. The extent of their displeasure with the group's tolerance of laxity in repayment could be an important factor influencing the group's course of action in the event of occurrence of default even on group-sourced funds.

Even though we have noted that the self help group can potentially act in greater independence of the position of the sponsoring NGO/MFI on the issue of crises-induced defaults, the attitude of the sponsoring NGO cannot be disregarded entirely. In the case of group-generated funds, the sponsoring NGO might choose to eschew a policy of dictating the appropriate course of action a group should observe in the event of default and leave it entirely to the discretion of the group to be settled on a case-by-case basis. On the other hand, it might indicate through training programmes, interaction with programme coordinators etc that it would prefer to see more stringent / sympathetic action on the part of the groups. It might be important in this context to understanding the social consciousness of the NGO leadership and its ideological orientation viz., whether it perceives itself primarily as an agent enhancing the efficacy of grassroots level financial intermediation processes or whether it visualizes microcredit groups as part of a strategy of social mobilization aiming to build collective action and solidarity among the poor. We conclude this section by emphasizing the need for empirical research on intra-group power dynamics and on the possible determinants of peer group pressures within self help groups, in the absence of donor-induced sustainability imperatives, before we conclude that the greater *potential* for more empathetic group action and for better harnessing of the protectional dimensions of credit based poverty alleviation strategies are necessarily realized through self help group based transactions.

In Section II of the paper we had reviewed the policy implications of the crucial issue of whether all sections of the poor or all those below the officially designated poverty line are equally amenable to the initiation of income generation through loan-financed enterprises, however sensitively the programme is designed. We proceed to examine the implications of findings pertaining to the heterogeneity of the poor in the light of the Indian experience.

#### **IV. 4. Indian debates on the IRDP and lessons for the global microfinance sector**

On the issue of the heterogeneity of the poor, it is important to note that the findings of the Hulme and Mosley (1996) study and others that have reached similar conclusions with regard to the differential income impact of microfinance programmes upon different sections of the poor have been pre-dated and anticipated, as it were, by the earliest critical assessments of the Integrated Rural Development Programme (IRDP) of India - the nationwide, self-employment based, poverty alleviation programme. A perusal of the substantial



scholarship on the critical evaluation of the IRDP would point to the striking similarities between the structural problems encountered by an older generation of individual targeted self employment programmes and the more recent group lending based microfinance programmes. A consistent criticism of the IRDP has been directed at its lack of understanding of the differing resource endowments of the poor and the effect of the Antyodaya principle of pushing the poorest sections – those least able to bear risks and with minimal skills and entrepreneurial support services – into risky self-employment ventures. Pulley (1989) notes that one of the key recommendations of the CRAFTICARD Committee (which provided the conceptual foundation of the IRDP as a national poverty alleviation programme) that the IRDP ignored was the categorizing of poor households into three groups: those who could become viable with just a loan, those who need loan and subsidy and the non-viable poor who need special assistance through social security programmes. Skepticism about the potential of self-employment ventures to lift households in deep poverty population above the poverty line and a critique of planners' perception of the poor as a homogenous, undifferentiated mass constituted key themes in the famous "wage versus self employment" debate that raged among Indian scholars in the mid-1980s. While Nilakantha Rath (1985) had argued that the idea of self employment for the poor was fundamentally flawed and had pointed out that wage employment, an infinitely superior strategy, placed no demands upon the entrepreneurial skills of the poor, created no worry about loan repayment and did not require the demoralizing pursuit of subsidy, Indira Hirway (1985) countered Nilakantha Rath by pointing out that self employment already constituted the major form of employment of the poor in India and could not be ignored by planners. She argued for a distinction between two categories of the poor: those who possessed some skill, education or enterprise and could take up self employment and those who did not and could be considered eligible for wage employment instead. Bagchee (1987) endorsed Hirway's contention but argued for a sub-set within the category of wage employment households comprising those families without an able bodied adult member, that could not make use of wage employment programmes and required access to state sponsored social security schemes on a priority basis.

We argue that the perspectives that have emerged in the context of the wage versus self employment debates in India offer important insights for microfinance programmes in India and elsewhere and for the current microfinance paradigm that aspires to use small peer groups to reach credit effectively to the poor so as to finance income-generating enterprises, thereby alleviating poverty. If the success of employment programmes hinges critically on targeting specific interventions (wage, self employment, social security plus wage employment) towards different sections of the poor and fine tuning these programmes so that they meet the varying needs of the poor, we would need to envision systematic, integrated planning on a nation wide scale in which state planning and implementation bodies must necessarily play the lead role. Such meticulous planning and targeting of specific components of anti-poverty programmes to differently-endowed sections of the poor is not inherently built into the structure of NGO/MFI sponsored self help groups or small borrower groups, in India or elsewhere. In fact attempts to target specific interventions to

different sections of SHG members (as SHGs are not socially or economically homogenous) could carry the danger of being perceived right at the start as an exercise of favouritism or bias by the implementing agency. NGO and government rhetoric that otherwise emphasize “unity” and “solidarity” of the group as a “collective” might militate against any institutionalized attempts to sift through group membership in the interests of matching household circumstances to employment requirements. The point that is being argued here is that the sheer existence and effective functioning of self help groups and other variants of small borrower groups are not by themselves evidence of the operation of decentralized planning or of any kind of planned approach to the employment needs of group members. Therefore, while the involvement of local bodies, forms of local government, community-based development and service organizations would be important when attempting such a mammoth initiative, these can hardly be expected to substitute the role of the state in a task of such complex and vast proportions. It would seem therefore that, in order to succeed, the project of poverty alleviation through micro enterprises financed and supported by microfinance groups would need more of the developmental state rather than less of it - a prospect that runs counter to the dominant microfinance discourse that relegates the state to the peripheral role of creating an enabling environment in which MFIs and microcredit NGOs programmes may flourish unhindered.

#### **IV. 5. Channeling SGSY credit through Indian SHGs: An assertion of promotional dogma?**

If debates among Indian scholars on the comparative efficacy of various forms of poverty alleviation strategies hold important lessons for the global microfinance sector, developments within the microfinance sector, with specific reference to the shifting conceptualization of microfinance as an anti-poverty initiative that we have outlined in Section III, in turn, pose challenging questions to the emerging Indian microfinance experience. If the research perspective critical of the anchoring of microfinance to microenterprise credit delivery constitutes an important insight about the role of microfinance programmes in poverty alleviation, how sound is the Indian government’s strategy of mandating disbursement of enterprise credit under the Swarnjayanti Gram Swarozgar Yojana (SGSY) scheme for the promotion of self-employment through the existing self help groups? The SGSY, successor to the IRDP and DWCRA, was introduced as a nationwide, self-employment based, poverty alleviation programme in April 1999 and substituted the IRDP, DWCRA, TRYSEM, SUME, Million Wells Scheme, SITRA and Girijan Kalyan Yojana. The SGSY, which seeks to use self help groups as channels of delivery of credit-cum-subsidy assistance to below-poverty-line sections, aims to bring every assisted family above the poverty line in three years by creating a monthly income of at least Rs.2,000 from the activity undertaken, after repayment of the bank loan. The SGSY, as enunciated in its guidelines issued by the Ministry of Rural Development, declares as a fundamental article of faith, its belief in the latent entrepreneurial capacities of the rural poor, expressed in its statement that with the right support, the poor would emerge as successful producers of goods and services (GOI, 1999). The SGSY in its conceptualization is, therefore, primarily about injecting credit for promotional purposes and is premised on the expectation

that households can use the credit-financed enterprises to make a linear, uni-dimensional movement from below poverty to above poverty line status.

The SGSY, which attempts to capitalize on the group lending process that had been initiated by NABARD through the launch of the SHG-bank linkage pilot project in 1991, contrasts in many ways with the SHG-bank linkage program. The SGSY is striking for the range of institutional actors that have been involved in the selection, planning and monitoring process, including banks, the District Rural Development Authority, Panchayat institutions, block development officials, district line department officials, NGOs and of course, the SHGs. The SHG-bank linkage scheme involves only the bank, the self help group and the sponsoring NGO or voluntary organization. Even while exhorting banks to prioritize the SHG-bank linkage program within its lending portfolio, NABARD and RBI circulars had emphasized that the linkage scheme was to be perceived as a credit innovation and not a targeted intervention. The SGSY, in marked contrast, is a targeted intervention (like its predecessor, the IRDP) and is charged with the mission of covering 30% of BPL families in a block within a period of 5 years (GOI, 1999). Premised on the understanding that the constituency of SHGs was generally the rural poor, who were most attracted by the low amounts of repeat loans for consumption purposes, the SHG-bank linkage scheme had not specified BPL status for loan recipients, unlike the SGSY. The SHG-bank linkage program, which had reiterated that minimal documentation be gathered from the groups, in a relatively de-bureaucratized manner, had marked a change in bank policy towards weaker section lending by legitimizing non-collateralized loans for consumption purposes (NABARD, 1992). In contrast, the SGSY, intended as a self-employment program, ties SGSY loan use to individual or collective enterprises and treats any consumption spending as diversion from permitted purpose.

We note, therefore, that certain structural features of the SGSY could potentially threaten the flexibility of SHG-based savings and credit transactions and consequently also the protectional dimension of SHGs. By mandating that bank officials ensure distribution of their annual “quota” of SGSY-related loan finance through self help groups, bank staff could be forcing larger amounts of loans tied to the end use of enterprise promotion upon women who are neither willing, nor able, to engage in loan-financed income generation. This could, in turn, imply the establishment of unviable enterprises by women members of SHGs forced to invest in income earning activities, or subversion of the programme’s objectives by SHG members, camouflaging their consumption needs as self-employment needs. The probability that only those who genuinely need to invest in income-generation activities are borrowing for these purposes appears to be higher in the case of the SHG-bank linkage scheme, as consumption related expenditure is permitted here. The SGSY also appears to be re-defining the terms of relationship between the commercial bank and the group in more authoritarian and coercive ways as reflected in field reports that indicate that bank officials have tended to make access to the SGSY, for the group as an entity, contingent upon *individual* members’ repayment of balances on older schemes such as the IRDP that their family members may have taken. Group pressures on individual members

fuelled by bankers' efforts to secure older defaults through the SGSY scheme contain the potential to provoke exclusionary pressures attempting to discipline co-members, also defaulters of earlier schemes. We have reviewed the repercussions of such pressures upon the dynamic of intra-group peer transactions in terms of the willingness and capacity of the group to extend support to poorer members, or those in situations of distress, in Section I. Yet another feature of the SGSY with disquieting implications for the protectional dimensions of SHG-based microfinance has to do with the target-orientation of the programme and the consequent primacy accorded to quantitative assessments such as the number and volume of financial assistance disbursed and number of beneficiaries reached. Field reports<sup>7</sup> indicate that some SHGs have been created with the sole agenda of absorbing the SGSY loan funds, under the aegis of block and district level administration, through the expansionary impulse of the target-driven SGSY, and these appear to be short-lived and unsustainable, oftentimes dissolving after the loan has been disbursed, in the absence of sufficient time for, and facilitation of, intra-group cohesion. This would in turn appear to jeopardize the social mobilization or the 'empowerment' processes, also expected of SHG-based collectivization of rural women. At this juncture, we note that the SGSY has provoked the ire of existing microfinance players who have critiqued the programme for its capacity to sabotage the network of self help groups through the introduction of subsidies, the non-linkage between group generated savings and the external loan amount, the infusion of large amounts of loan finance into the group in a relatively short period after group formation and the threat of hijack of NGO sponsored groups by block and district bureaucracy (Sinha, 2000; Harper, 2002; Malhotra, 2000).

Policy response to trenchant criticism by Indian researchers of the unsuitability of the poorest for the risks of loan financed enterprises has taken the form of jettisoning the Antyodaya principle or the priority selection of the poorest within the BPL sections in the SGSY. However, the SGSY continues to be ill-equipped to meet the challenges of the agenda of gauging the suitability of differently placed poor households for various forms of employment programmes depending on their initial asset position or possession of prior entrepreneurial experience, training or skills. Another area of concern relating to the SGSY is the promotion of micro enterprise lending through SHGs without adequate support to the agenda of ensuring access to protected markets for SHG women. The SGSY's requirement that at least 50% of the SHGs reached in a block be women's groups and the Central government's decision to route the SGSY scheme through self help groups in a context where there is a massive policy support behind the creation of women's self help groups may be perceived as important means of reaching higher volumes of institutional credit to women in order to finance their enterprises. When we consider, however, that critical studies of the IRDP have revealed the variety of mechanisms by which the process of selecting enterprises and providing support services were even more inadequate in the case of women beneficiaries (World Bank, 1991; Kabeer and Murthy, 1996), it is disturbing that the official guidelines of the SGSY take no note of the additional forms of support that first time women entrepreneurs may need in order to be able to successfully access markets, manage their enterprise independently and generate sufficient incomes from their

chosen activities. Especially on the issue of market access, this is what the guidelines of the SGSY have to say: “It is possible that this might appear to be a formidable proposition and that the field functionaries might feel that they are unequal to the task. Happily, this is not so. While to most of us, market mechanism may appear unintelligible and a complex task, in reality it means checking out what sells and what does not. Goods and services are traded every day in all parts of the country. What is needed is to see what sells in the local markets” (GOI, 1999). Such breezy confidence on the critical issue of marketing belies research on the IRDP, which has painstakingly documented the many ways by which successful market access had evaded the grasp of IRDP clients. Although the guidelines envisage an elaborate process of planning at block and district levels by block and district committees of the SGSY prior to the choice of enterprises with regard to availability of infrastructure, markets, technology and the capacities of Swarozgaris, early assessments of the SGSY indicate that the notion of comprehensive, holistic planning at the block and district levels remains as much of a fantasy in the SGSY as it did with the IRDP (Ghosh, 2001; Nair and Mathew, 2000; Reddy, 2000).

The prospects for the financial viability of the income-generating activities of the poor, on an economy wide scale, appear even more remote when we factor in analyses that demonstrate the marginalization of wage employment generation programmes. An examination of the pattern of intra sectoral allocation within the sector of “rural development” programmes in central government expenditure found that rural wage employment programmes (both the JRY and the EAS), which were the most important components within the rural development sector (claiming a share of more than 70% in 1994-95) showed a declining trend in the second half of the 1990s and fell dramatically to 23.7% in 2001 (Mooij and Dev, 2002). In the light of the dwindling resource allocation for wage employment generation in central government expenditures in the late 1990s, we recall Nilakantha Rath’s argument that the economic feasibility of enterprises of the poor depend critically upon wage employment programmes that generate the large-scale markets for the goods produced by them (Rath, 1985).

While it is well beyond the scope of this paper to attempt to provide a complete assessment of the implications of the SGSY for the protectional dimensions of SHG based savings and credit transactions, we do note that Indian policy makers appear to have not sufficiently factored in findings related to the structural limitations of promotional lending strategies, that have emerged both from the global microfinance experience and from the older IRDP experience closer home.

#### **IV. 6. Microfinance initiatives and rural credit scenario**

Research on the impact of financial liberalization and banking reforms policies upon the rural and agricultural sector point to the emerging neglect of the needs of weaker section and priority sector lending. This is reflected in the declining share of rural branches in total commercial bank branches, the falling percentage of rural to total bank credit, an adverse movement of the credit-deposit ratio, the drastic reduction of the exclusive weaker

section lending focus of Regional Rural Banks to no more than 10% of their total lending and the gross levels of under- utilization of resources earmarked for the agricultural sector through the Rural Infrastructural Development Fund (RIDF) constituted at NABARD in 1995. The latter has been critiqued as having become a safe parking place for funds deposited by commercial banks so as to make good deficiencies in their priority sector lending targets (EPW, 2000; Majumdar, 1999; Nair, 2000). While the share of agriculture, within the priority sector, has not attained the mandated norm of 18% of total advances since 1995-96, the share of direct lending to agriculture (within the category of agricultural lending) had declined sharply between 1995-96 and 1999-2000. On the other hand, indirect lending to agriculture, including the purchase of vehicles and land for housing purposes, had doubled over the same period (EPW, 2000). Analysts also note the redefinition of the “priority sector” by the RBI during 1997-98 and 1998-99 and caution that increases in priority sector lending towards the late 1990s might be reaching the newer sub-sectors that were not part of the priority sector in 1991. (Ramachandran and Swaminathan, 2003; Shahjahan, 1999). It has been argued that the idea of harnessing the potential of the credit system to help weaker sections, the underlying rationale of the social banking era, came under assault when the Narasimham Committee (1991) advocated that fiscal instruments be used instead (Narayana, 2000).

It may therefore well be the case that the greater access of women members of self help groups belonging to poor, rural households to institutional credit is taking place during a period marked by an overall scaling down of institutional finance for the rural sector. In order to obtain a perspective on the magnitude of institutional credit extended to poor women through SHGs, we note that disbursements under the SHG-bank linkage programme in the year 2000-2001 constituted less than half of 1% of the total amount that was disbursed for agriculture and allied activities by the banking system during that year, while disbursements under the SGSY scheme, targeted at officially-designated BPL families, constituted more than two and a half times the advances under the SHG-bank linkage (Tankha, 2002). This divergence between micro initiatives such as microfinance and macro policies relating to the rural credit sector raises the question of how MFIs and NGOs can possibly hope to fill the gap created by a reversal of state commitment to financing the production and consumption needs of the rural poor and therefore whether the current policy thrust accorded to the agenda of expansion of self help groups can amount to much more than rhetorical tribute to concerns of poverty alleviation.

In Section IV, we have attempted to show that the Indian microfinance experience, based primarily on self help groups of rural poor women, represents an experience, that differs quite significantly, at the levels of policy support, institutional ramifications and organizational specificities, from the dominant Bangladesh MFI model that we have reviewed extensively in the preceding sections. We saw that the more autonomous and self-managed mode of operation of SHGs could imply freedom from excessive dependence on the MFI and therefore greater maneuverability so as to respond better to the needs and special circumstances of poorer individuals within groups. We also noted that global debates on

the differential income impact of microcredit programmes acquire resonance in the Indian context, in the light of our older experience with self-employment initiatives for the poor and that the rich legacy of Indian scholarship on this question may hold significant lessons that unsettle established microfinance orthodoxies. We suggested further that the conversion of SHGs into channels for the delivery of SGSY credit could imply a loss of the earlier flexibility of the SHG-bank linkage programme, under attack from the exclusive enterprise focus of the SGSY. We also questioned whether the diminishing volume of institutional credit to the designated weaker sections within priority sector lending and the greater profit orientation of the commercial banking structure, since the inception of the banking sector reforms, bode well for the agenda of expanding the access of the poor to institutional credit despite the mounting statistics on the numbers of SHGs linked to banks with every passing year.

### **Conclusion**

By way of conclusion, we note that further evaluation of the efficacy of self help group based savings and credit transactions, either in promoting the incomes of poor households through investment in income-generating activities or in protecting households from damaging their precarious economic resources during periods of crises warrants field studies that can perhaps make an important contribution by undertaking a mapping of the heterogenous poor who currently constitute the clientele of self help groups in India. Studying the differential loan histories of different individuals within groups may offer a clue to understanding which sections of the poor within SHGs are graduating over to time to income-generation and which are resorting to more distress-related borrowing. We can perhaps seek to further complicate the picture by situating the SHGs being researched in different contextual settings: areas / regions marked by accountable public institutions relating to the delivery of health, education and the PDS vis-a-vis more deprived pockets of the country marked by a complete absence or near breakdown of government provisioning of essential services. It may even be worthwhile to probe the question of whether research on the borrowing and saving patterns of differently placed SHG members can be used to provide a micro view of the failures of the welfare state.

## End Notes

1. Adverse selection or hidden information refers to the inability of the lender to distinguish a good borrower from a bad one at reasonable cost. Moral hazard or hidden action refers to the inability of the lender to ascertain whether a poor harvest and loan default were due to bad weather or poor effort without incurring high costs of monitoring labour input. See Bell, 1990.
2. Von Pischke, Hartmut Schneider and Rauno Zander (1997) argue that credit project beneficiaries tend to differentiate between funds based on the source. Funds based on member savings are treated as “warm” money that is alive and vibrant and deserving of effective management whereas funds sourced from distant donor organizations are perceived as “cold” money, alien and aloof, which does not warrant equally responsible repayment behaviour.
3. The Grameen bank developed from an experimental project launched in 1976 by Muhammad Yunus (an Economics professor) to target credit to the poor organized into joint liability groups without demanding physical collateral. Having received critical support from the central bank of Bangladesh in its early years, the Grameen project was established as a bank to work exclusively with the poor with its own charter in 1983, with the government holding 90% of the shares in paid up capital. By 1995, individual borrowers held 85% of the paid up capital of the Grameen Bank.

Bangladesh Rural Advancement Committee (BRAC) was established by F.H.Abed in 1972 as a charitable organization to help resettle displaced households during the 1971 war and expanded its operations from relief to integrated community development including infrastructure building and provision of various services to targeted poor households. Described as the world’s largest indigenous development NGO, BRAC runs 35,000 non-formal education schools, reaches over 12 million members through its health and education programmes and employs more than 23,000 staff and 33,000 part time teachers in its non-formal primary schools. BRAC’s microcredit programme, that was modeled on the Grameen Bank, was started in the mid 1980s, and has been influenced by its belief that the poor need assistance with marketing and technical skills, in addition to credit access. Hence it has attempted to combine lending with organizational inputs and social development including skills promotion, training, consciousness raising and business support services. Microcredit is currently BRAC’s single largest programme and is estimated to have reached over 2 million households by 1999.

Association for Social Advancement, which was started in the early 1980s with the agenda of social transformation and mobilization of the landless, decided to focus its activities on economic empowerment and since the early 1990s, it has chosen microcredit, modeled on the Grameen, as its core activity. ASA’s growth in microcredit has been meteoric as reflected in a ten-fold expansion of its borrower base over a six year period (1992-98).

Proshika, which was created with the mandate of organizing the poor through self-sufficient local organizations, began to provide revolving fund to its group in mid 1980s to supplement group capital. Its microcredit programme began to grow in an organized fashion from 1994. Unlike the Grameen model, lending is not done directly to members through the staff of Proshika, but is undertaken by local group leaders. The role of the primary groups in sourcing funds from Proshika and recovering loans from borrowers is greater than is customary in other NGOs modeled on the Grameen. It has been noted that although Proshika appears to differ in some fundamental ways, it has been recently converging towards the Grameen approach.



4. The Rural Development Project-12 or the RD-12, funded by the Canadian International Development Agency (CIDA), is one component of the Rural Poor Programme, the government's largest credit based rural development programme targeting the landless. It is part of the Bangladesh Rural Development Board (BRDB) that grew out of the famous pilot projects in the Comilla region of Bangladesh in the 1960s, which promoted new agricultural technology through the provision of subsidized credit.

The Thana Resource Development and Employment Programme (TRDEP), a project overseen by the Bangladesh government's Ministry of Youth and Sports, was initiated by the government in 1987 in order to reproduce the principles of the Grameen Bank. Initiated through four branches in two thanas in 1987, it had received assistance from the Asian Development Bank to expand to around 60 branches in 25 – 30 thanas in the 1990s. References for notes 3 and 4: Jain and Moore, 2003; Khandkher, 1998, Hashemi, 1997 b; Goetz, 2001, Montgomery et al, 1996.

5. As of March 2003, under the SHG bank linkage programme, 11.6 million poor households in 523 districts covering all the states and Union Territories in India had received microcredit through the intermediation of 7,17,360 self help groups credit linked to banks (including RRBs and cooperative banks) in what has become the world's largest microfinance programme in terms of outreach. A total number of 2,800 Self Help Promotion Institutions including 48 commercial banks, 192 RRBs and 264 cooperatives, NGOs and other formal agencies have participated in the programme (NABARD, 2002-03)
6. The field reports refer to the previous work experiences of the current research scholar as an activist with a non governmental organization - Tamilnadu Science Forum - that has been attempting to mobilize women using SHGs in several parts of Tamilnadu. The Tamilnadu Science Forum, has been active for over two decades in the state of Tamilnadu in popular science communication, community health and literacy campaigns. The references to self help groups in Kanyakumari are drawn from a self help group network of over 1,500 self help groups spanning Kanyakumari district. The Mahalir Association for Literacy, Awareness and Rights (MALAR) network of SHGs was initiated by the district committee of the Tamilnadu Science Forum, Kanyakumari district and developed as an off-shoot of the Arivoli (total literacy) campaign in the district. The current researcher worked as district coordinator for the MALAR network between October 1997 and December 1998.
7. NGOs in Tamilnadu engaging in microcredit have had to contend with the phenomenon of DRDA-formed self help groups that were organized in haste so as to acquire eligibility for the SGSY loan and were often disbanded after the loan was disbursed. More recent reports indicate that the DRDAs in Tamilnadu have given up the agenda of direct formation and sponsoring of groups. The government agency entrusted with the responsibility of SHG promotion is the Tamilnadu Women's Development Corporation which operates through partner NGOs under the Magalir Thittam scheme.

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