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"WHY SANGHAMITHTRA IS DIFFERENT"

by

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The observations made in this article apply only to the Rural Programme of Sanghamithra – not to the Urban. They also apply to the Indian context – and to areas in India where the tradition of banking and banking infrastructure is comparatively well-developed. The author is aware that there are certain 'atypical' areas where networks and facilities are weak, or even threatened by a breakdown of law-and-order. Such areas merit separate processes and institutional arrangements. Universal solutions that work under all conditions are rare, if they exist at all. ***While writing this paper, the author had two options – produce a regular paper on Sanghamithra's performance or explain why it is different; he chose the latter.***

"SANGHAMITHRA – A MFI WITH A DIFFERENCE" is the title of a book published in July 2004 by this author. The reasons for this "difference" will form the major content of this article. These reasons may also serve another purpose, namely - they may help to throw some light, as a first step, on the several queries and criticisms related to micro credit/finance ranging from whether NGOs should be involved in MF to its impact on poverty. It is also hoped that this effort to explain the differences will help to set the framework for further detailed studies to test the assumptions behind the claims to be different and the reasons for these choices. The queries and criticisms are many, but the following will be addressed, however inadequately, given the limitations of this article: (A brief response to these issues, is also given in the first few paragraphs so that the position of Myrada/Sanghamithra is clear at the start; these responses are further elaborated later in the article for those who have the time to go further.)

1. Why did Myrada, an NGO, which has been involved in promoting self help affinity groups (SAGs) [2] since 1984-1985 and the SAG Bank Linkage programme since 1992,

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[1] My colleagues contributions to this paper are acknowledged with thanks. Ms.Vidya Ramachandran, clarified several points and edited the paper; Ms.Chandra Singh, Mr.William D'Souza and Mr.S.M.Adiga contributed data.

[2] When MYRADA started working in 1984-85 with affinity groups, which emerged when the cooperative Societies broke up, they were called Credit Management Groups. When NABARD provided MYRADA with a grant in 1986-87, the name was changed to Self Help Groups (SHGs). When in early 2000, MYRADA discovered that SHGs were being formed on the basis of external criteria, provided with credit just after formation with little or no institutional capacity building, it changed the name of its groups to SAGs (or Self-help Affinity Groups) in order to stress the "**affinity**" which binds the members together.

decide in 1993 to set up a **separate MFI** (Micro Finance Institution) – Sanghamithra – instead of lending money itself?

Briefly the answer rests on Myrada's assessment that there is a difference in culture of the staff and in the supporting and monitoring systems required by the two types of institutions (the NGO and the MFI). There are other reasons also, that are explained later.

2. Several studies have articulated that the priority of the poor is often to have **a safe place to save** even more than a place that they can borrow from, and that many NGO-MFIs are unable to fulfil this requirement. Given this shortcoming, they question the ability of NGO-MFIs to provide the full range of financial services. The counter-question that Myrada has attempted to address is: should the NGO-MFI necessarily be the only institution to fulfil this requirement? Can there be other institutions which people find more accessible, where their savings are more in their control than if they were with the MFI? Are such MFIs that can collect savings for safekeeping necessarily the preferred option of the people if they were not under compulsion to save in the MFI as a pre-condition to get loans? Can it not be inferred, even if it is left unsaid, that NGO-MFIs retain savings to establish a degree of control over borrowers?

The brief answer (which is expanded later) based on Myrada's experience of over 20 years is that the MFI need not be the only savings institution. Myrada does recognise the fact that people need a place to save that is safe, convenient and easily accessible. The SAGs - which started by mobilising savings *and lending them to members before any outside finance was provided - have proved that they are capable of performing this savings function in a way that the poor find more appropriate. In the initial two or three years, it may be their only place to save; gradually, they diversify to make individual savings in the bank and/or post office. It is quite common to hear people grumble that the bank which willingly keeps their savings is not so forthcoming when it comes to advancing loans; it is rare to hear them grumble that the MFI that gives them loans is not collecting savings.*

3. The corpus of literature on Micro Finance is growing by the minute - just as the number of international MFIs setting up base in India, often with the assumption that little has been done before their arrival. Alongside this growth there are also several articles that take a critical look at the MF sector, especially the homegrown SAG approach, which they find does not fit in neatly with the models promoted in other countries. This article attempts to query the issues they raise by asking the following questions: **a) Is the criticism valid that NGO-led micro finance tends to adopt a minimalist approach** – that credit suffices for the borrower to take off on the growth path? Credit only or credit first? (Are the NGO-MFIs, the only operators who are vulnerable to the minimalist tag?) – And as a partial consequence. **b) Is the criticism valid that NGO-led MFIs can at best achieve consumption smoothing and not true enterprise development**? The contention is that they focus on the symptoms of poverty and not on the cause which can be removed only if the NGO-MFI promotes enterprise (business) development. This they do not or are unable to do, either because on the one hand as NGOs, they do not have the resources to build a supporting environment and the skills to promote genuine businesses, or because they think that enterprise/business development will take them away from focusing on the poor, while on the other hand as MFIs the pressure to **grow rapidly and become financially sustainable** pushes them to promote a portfolio of loans that are small and fast moving, which are largely loans for consumption or at best small trading which, according to the opinions of some, are not truly business enterprises. This in a way takes the discourse back to the first issue – whether the NGO's programme should be separated from that of the MFI. Doing so would enable the former to retain its poverty focus while providing the latter with the space to grow in response to the demands of business enterprises which may require larger loans, several tranches and which generally tend to gravitate to those above the poverty line who are able to take the risk and establish the linkages required to sustain a business enterprise. **c) But it does carry this concern/issue a step further – whether the two (the NGO and the MFI) – working as separate legal entities – can be closely meshed so that a balance can be maintained between on the one hand promoting social concerns and a supporting environment while on the other promoting a loan portfolio which includes activities that increase income through productivity, scale and a genuine business initiative**. *This article attempts to describe Sanghamithra's and Myrada's efforts to keep their identities so that their respective missions are not compromised, but at the same time, to share a common vision. It describes briefly the strategy adopted to* ***embed credit in a broader supportive framework of service providers and investment*** *that has the potential to lift the poor above the poverty line and keep them there. Myrada attempted to create this balance when it promoted Sanghamithra and has continued to do so. Whether it has succeeded or not will require further and more in-depth studies; this article's intention is to state what Myrada and Sanghamithra are attempting to do because this is one of the reasons why Sanghamithra is different. The criticism that micro credit does not support micro enterprises raises several issues which are discussed later.*

The present scenario in the MF Sector (driven to a large extent by sources which are from or have their roots abroad) can be described by the following analogy: The MFI is a steam driven train, pushed to go faster and faster (growth). New carriages are attached (credit, savings, insurance, etc.). There are ticket inspectors (rating experts) who walk through the train, concerned only about whether the ticket is correct; they have no time or interest to look outside the window. The train driver is someone who has seen a lot of trains pass by and always felt that given a chance, (s) he would make a much better driver – in most cases (s)he was running a popular hotel on the platform (an NGO in close touch with people and their needs) - and so (s)he knows how many people to expect on the train, how much of food and drink is required. In some cases (s)he is the Station Master who has experienced the power of stopping trains and letting them go even if (s)he has never driven one (Government Officers with authority but little experience in the financial sector who are put in charge of micro finance companies). But once in the driver's seat they have no clue about what the signals (the ratios that indicate the health of an MFI) mean as they flash past. The Manual of Instructions, supporting the corporate objective demands an increase in the speed of the train. After all, it has to make many trips back and forth – to earn enough to be a viable (sustainable MFI) route. But once again the train drivers cannot read the curves in the line and they do not know when and how much to slow down and when to accelerate. Some wagons – the lower class ones – get derailed (the MFI's too rapid grow results in increasing NPAs and opening of branches without adequate support). There is little maintenance and no upgrading of the track (Capacity building of MFI staff and the constant upgradation of supporting systems are usually given last priority); yet faster speeds are encouraged - Station to Station (MFI growth YoY, QoQ,); there is little or no attention to or concern for the impact this has on the passengers – who are thrown around and often fall off, especially those in the general/unreserved and lower class compartments (the poor) where the supporting system of protective railings and "hand hold" straps are missing (in the credit alone-minimalist approach).

To elaborate further on each of the three questions/issues raised above:

1. Why did Myrada promote a separate institution – the MFI called Sanghamithra – to manage micro finance? And how does this make Sanghamithra different?

Sanghamithra [3] is not an NGO-MFI. It is a separate MFI promoted by Myrada. Myrada pioneered the SAG movement and continues to promote the SHG-Bank Linkage Programme. Though Sanghamithra was deliberately set up by Myrada as a separate institution, it shares the vision of Myrada – promoting self-governed institutions of the poor – though its Mission is more restricted – to provide credit to SAGs. The Chairperson and several of the Board members of Sanghamithra are from Myrada. The intention of promoting Sanghamithra was that it would provide credit to SAGs (where the banks left gaps) formed by Myrada in the first phase and then to SAGs promoted by other institutions, provided they met the performance criteria set by Myrada/Sanghamithra. While, therefore, Sanghamithra functions independently with senior staff who have banking experience, Myrada continues to guide it so that it continues to share and promote a common Vision. Apart from lending to SAGs, Sanghamithra is also now lending to Watershed Management Associations (Area Groups comprising all stakeholders in a micro watershed) formed by Myrada and other NGOs.

With the credibility of SHGs gaining ground in the mid-nineties – due to the good performance in disbursement and repayment through the NABARD-sponsored SHG Bank Linkage Programme – Myrada was offered loans by several Banks and by one Government sponsored Micro Finance Institution to on-lend to self help groups. The reasons for this offer from Banks were related to their priority sector lending requirements, to image building and to the need to reduce transaction costs involved in lending to SHGs directly; an easy solution was to lend in bulk to NGOs. This also provided the Banks with a degree of security since they held (often implicitly) the NGO responsible for repayments. NABARD supported this approach of the banks to use NGOs as intermediaries since it helped to achieve the ambitious targets set by Government for the SHG-Bank Linkage Programme.

Myrada at that time (and even today) was strongly promoting the SHG-Bank Linkage Programme which took at least four years to take off after it was launched by NABARD in

[3] Sanghamithra has two programmes: Rural and Urban. The **Rural Programme** Head Office is in Mysore. It started lending in February 2000. Cumulative disbursements as on September 30, 2005 stood at Rs.43.7 crores. Outstanding client SAG Accounts is 4116. One credit officer serves 187 SAGs; outstandings per credit officer is Rs.82.25 lakhs. Net Operational surplus (after depreciation and prudential provisioning) is Rs.38.36 lakhs. Operation Sustainability Ratio is 239%, Financial Sustainability Ratio is 142%, Financial Sustainability (including imputed cost of net owned funds at 6%) is 120%. Interest on loans to SAGs is 12% **The Urban Programme** started lending in October 2000. Cumulative disbursements as on September 30, 2005 stood at Rs.15 crores, Outstanding SAG accounts number 2946. One credit officer serves 120 SAGs. Outstandings per credit officer are Rs 68.60 lakhs. Operational Sustainability Ratio is 106% and Financial Sustainability Ratio 92%. Interest on loans to SAGs is 24%.

1992. While NABARD spared no efforts to persuade senior banking staff to promote the programme, Myrada was a major player at field levels, relentlessly lobbying with Branch Managers and trying hard to remove hurdles which impeded the progress of the programme; it also undertook to train about 3,000 bankers (a large number of them with NABARD support) in the art of relating to and assessing SHGs.

But at times this effort was frustrating. Some Branch Mangers were just too comfortable in their "box"; some "cooperative" Managers were transferred and succeeded by totally "non-cooperative" persons. Some major banks were responsive and even proactive; others woke up to the SHG-Bank Linkage Programme as late as 2000. As a result, even in the so-called successful

South (of India), there were and still are large gaps in SHG Bank Linkage. Myrada decided that an alternative arrangement/institution was required, mainly to fill these gaps, to provide some degree of continuity in an area but also to introduce an element of competition between the "alternate institution" and the Banks. Myrada's position was that even if this alternate institution was promoted, Myrada would continue to promote the Bank Linkage Programme. The assumption on Myrada's part was that competition was required; it would serve to keep both the Banks and the proposed institution (i.e. Sanghamithra) on their toes. Subsequent experiences between 2000 and 2003 proved this assumption to be correct. [4]

To fill in the gaps left by the Banks, Myrada had three management options: (1) to borrow money and lend **through** its existing extension staff and organisational structure using the same financial systems (which were computerised and inter-connected at this time); in fact, most NGOs in India who decided to receive funds in bulk and on-lend adopted this approach. (2) To borrow money and to lend under the name of Myrada but to set up a parallel department **within** the organisation which would **function separately** from the programme department; the need to collaborate would be present, but the pattern and dynamics would be worked out in the field. There were a few examples of this approach, the most notable one being BRAC of Bangladesh. (3) to set up a **separate** financial institution, with staff having experience in banking and finance, while ensuring an organisational structure that would enable Myrada to ensure that the institution shared Myrada's vision and sought to promote this vision in its operations. Myrada decided in 1993, after considerable thought and discussion, on the third option for the following reasons:

The first option was rejected because while the financial systems in Myrada were good and suited its needs of programme management, they did not suit the needs of an MF Institution. For example, Myrada's systems were not generated or programmed to throw up the critical ratios that a professional MFI management requires to monitor performance. Besides, the culture of Myrada staff differed from what an MFI would feel comfortable with. For example, when Sanghamithra required two post dated cheques from the SAGs as an insurance against possible repayment delays, the Myrada field staff thought that this requirement questioned the integrity of the SAGs, even if this was not the intention. Thirdly the general opinion was that Myrada's image as an NGO would be compromised if it entered the business of lending money on interest. The current practice of NGO-MFIs both in other countries and increasingly in India was to lend at real rates ranging from 20 to 35% which was far above the "acceptable" rates expected from an institution like an NGO. While some of these NGOs-MFIs are complimented by donors for achieving financial and operational

[4] Impact Assessment Report by Ms. Girija Srinivasan, September 2003.

sustainability and observing internationally accepted standards and norms governing credit delivery, they tend to lose the credibility required to support social and economic change; in many cases, supporting these changes could be seen as undermining the interests to which an MFI gave priority.

The second option did not find favour since, even though the departments would be different, cross subsidisation in terms of services could not be avoided and this would not help to capture a correct financial picture of the micro-finance initiative. Further, several in Myrada suspected that the micro finance department would very soon take priority and overshadow the concerns and priorities of the social/development programmes both in the field (where the agenda and time of groups would begin to be dominated by financial issues to the detriment of social ones) and within the organisation. The micro finance department would require regular and precise reporting and feedback mainly related to financial matters which would, in turn, condition the meetings and priorities of the organisation and of the SAGs. It was suspected that the SAG meetings which hitherto devoted considerable time to socio/political/gender issues (apart from credit matters) would tend towards devoting most of their time and energy to credit/financial matters related to disbursements and repayment since they would be under pressure to report monthly on the progress in these areas which are critical to the health of a credit programme.

Studies and visits also indicated that several NGOs that went into micro finance continued to manage their micro finance initiative within their existing organisation, staff and systems; this created a scenario where cross subsidisation went unnoticed, where staff who were not equipped with the necessary skills were given charge of managing micro finance and where the warning lights regarding the health of the credit programme were disregarded or their messages not recognised. The results of such overlap of functions are disturbing and have given rise to several developments, which the critics of micro finance have spotted and rightly criticised.

This left the third option, i.e. that of starting a separate micro financial institution. This had to face several hurdles as official policy at that time (between 1993 and 1996) did not favour or support such initiatives. These matters took 3-4 years to resolve. The book referred to above: "Sanghamithra - a MFI with a Difference" records in detail the long process that eventually resulted in Sanghamithra being able to start lending operations in 2000. But the process, though long and tedious, did serve to prove that even the official financial system – the RBI and the Income Tax Authorities – can and will support an initiative if they understand its value to support the poor and are convinced that the promoters have no other agenda.

In hindsight, it now appears that while the policy of lending to NGOs and asking them to on-lend did help the official financial institutions to reach the target of lending to SHGs which was set by the Central Government, it surely did not help to professionalise the credit strategy. A similar criticism can be made of several programmes supported by Multilateral/Bilateral Agencies including DFID and the World Bank, which include a component of credit which a village association is expected to manage. The more recent initiatives to help these NGO-MFIs to morph into professionally managed MFIs and to even provide them with a transformation loan/grant (SIDBI is an example) to facilitate the process is an effort to correct this aberration.

Therefore, the decision was taken to vest the development programme and micro finance functions in legally separate institutions (Myrada and Sanghamithra). This was a considered step that has enabled each to remain focused on its priorities, and yet the close collaboration between the two has served until now to manage some of the dilemmas outlined above.

2. Even if the position of several critics and experts that the priority of the poor is to have a safe place to save rather than to borrow is universally valid, should the NGO-MFI necessarily be the only institution to fulfil this requirement? Can there be other institutions which people find more accessible, where their savings are more in their control than if they were with the MFI, which often prefers to retain their savings to establish a degree of control over borrowers – which is often left unsaid?

Critics of NGO-initiated micro-finance programmes, while pointing out that micro-credit alone is not enough, list a number of issues that also need to be addressed in order to make a dent on poverty, development and economic growth: one of these issues relates to savings. They point out that many (majority) of the poor value a place to save just as much (or even more than) access to credit. For good reasons, many NGO-MFIs cannot fulfil this need. The key sub-components include that the savings are safe, liquid, interest-bearing and that the savings facility is convenient. They conclude that assisting the poor in ***protecting*** *and* ***growing*** *their savings is a clear route to financial independence and thus, "highly developmental".* ***Myrada could not agree more****. When Myrada started identifying and promoting self-help affinity groups and building their institutional capacities, the first activity promoted was regular savings. The habit of savings/thrift (regularly, mainly weekly) was projected as even more important than just periodical savings. Loans were promoted only after 6 months of savings and institutional capacity training. As of June 30, 2005, Myrada has 9,304 SAGs in its projects. They have a total capital Rs.103 crores of which* ***Rs.45 crores is savings*** *and Rs.23 crores interest earned from giving loans to members.*

The evidence that Myrada's experience over 20 years provides does confirm that poor households (which have either the husband or wife who wants to get out of poverty and is willing to take decisions - sometimes hard ones - that reduce unnecessary consumption like liquor) want to save in cash provided the savings are in their control (so that they are readily accessible) and safe. They are not inclined to invest their savings initially in banks even if they earn interest. The transaction costs to the poor in dealing with banks just to deposit small amounts of regular savings – which is the only pattern of savings suitable to their lifestyle – are considered to be too high, and the "pigmy collection" system of house-to-house collection of daily savings introduced by the Banks of Dakshina Karnataka in the early 20th century is no longer such a ubiquitous service.

Myrada's position is that even if the assumption that the transaction costs of savings in an MFI are lower than the cost of savings in banks is valid, why should the poor person be expected – or compelled – to invest in the MFI only? Is it to reduce transaction costs to the saver that MFIs wish to accept savings? Or is it because the MFI sees this as a significant means to augment loanable funds? Is it to enhance the credibility of the MFI as a professional and full-range service provider? Is it because the MFI makes savings with it a condition for lending? Is it because the MFI feels that it helps to establish a degree of control over borrowers? Is this the MFI's strategy to build in risk coverage? These may be valid reasons and Myrada has enough experience to know that most MFIs which support a policy that requires the poor to save with them are motivated by one or more of these reasons. True, cheap and ready capital may be an important factor, but this is questionable since many MFIs obtain grants from donors. On the other hand, the group members can often obtain better returns from investing in other financial institutions than in the MFI, so why should they invest in the MFI unless under some degree of compulsion to do so as mentioned above? Besides, given the current spate of Finance Companies defaulting on deposits, the perception of risk of the member investing in an MFI is significantly high.

Sanghamithra does not have the licence to accept public deposits but even if it did have this licence, would people freely invest their savings in it when they have banks which surely generate more confidence than a new MFI? This is doubtful, unless of course Sanghamithra applies pressure and conditionalities related to loans. On the other hand, over the last twenty years, the SAGs have proved that they are capable of performing this savings function in a way that the poor find more appropriate at least in the first two to three years of the SAG's existence. Later, Myrada's, studies show that they diversify their financial savings, keeping a part in the common fund of the SAG and another part in the local bank. Sanghamithra in turn builds on the strength of the members and the SAGs – namely the willingness and ability of the members to save and their confidence that the SAGs function in a manner that helps them to manage their savings according to their priorities that change from season to season (not just from year to year). For Sanghamithra, the SAGs' performance in management of savings is an important criterion to extend a loan.

For Myrada/Sanghamithra the priority concern is for the poor to have an institution in which they have confidence so that they willingly deposit their savings over which they have control so that their access to and management of their savings is governed by their own decisions and not by an outside agency like an MFI (which will always have a greater influence on the management of savings than the people's group). In Myrada's strategic approach, this institution is the SAG. Sanghamithra, on its part, lends only to SAGs, and since in its assessment of the SAGs, their performance in the regularity and management of savings are important indicators, it is obvious that Sanghamithra promotes not only savings but also the management of savings by the SAG.

Myrada's strategy has been to build on the strengths of people. One of their major strengths is their relation of affinity that exists between a set of households; this affinity is based on relationships of trust and mutual support including the acceptance of sanctions for deviant behaviour once the rules governing behaviour and credit transactions have been agreed to. These relations in turn help the group to balance the common good with individual benefit and at times – particularly in the initial stages – to place the common good above individual benefit. This common good is the common fund of the SAG into which each member contributes regular savings. Each member realises that his/her contribution to support the common good has its returns to the individual - up to a certain point. Myrada's experience indicates therefore, that the MFI need not be the only institution that offers a savings instrument for the poor; the SAG could be and has emerged as another instrument and a more appropriate one.

A study of the SAGs in Myrada projects shows that the SAG members are able to decide on how much to save and invest in the common fund of the group from which they extend loans. They decide whether to reduce or increase the amount of weekly savings depending on seasonal cash flows. Each member is free to decide to save independently in the bank after the group's obligations are met – and most start saving independently after 3-5 years of being a member. Many SAGs offer interest to their members on the savings in the common fund. Several SAGs after functioning for 10 years have decide to distribute all or part of their common fund and to start over again, sometimes with several new members.

Does this mean that the MFIs will have to depend on donor funds to meet their capital requirements? Yes and no. Sanghamithra for instance started with donor funds but thereafter has borrowed from NABARD, Canara Bank, Indian Bank and currently has no problem to meet its capital requirements through bank loans. Does donor funding reduce the professionalism demanded by the MFI sector? The initial infusion of grants surely helped Sanghamithra to break even quicker than if it had to depend on loans from the start. However, there is no evidence that the initial dependence on grants weakened or undermined Sanghamithra's commitment to manage credit/finance in a professional manner with qualified staff paid competitive remuneration and supported by the most appropriate systems. Professionalism in micro finance is not determined by the acceptance or non-acceptance of grants; there are other factors related to the management of this finance that serve as more valid indicators to measure professionalism.

3. Let us take up the points mentioned in the third set of issues separately

A. The Minimalist Approach: Is the criticism valid that NGO-led micro-finance adopts a minimalist approach – that credit suffices for the borrower to take off on the growth path? Are NGO-MFIs the only operators who are vulnerable to the minimalist tag? Is the strategy of minimalism adopted because the MFI needs to grow rapidly to achieve self-reliance?

There is evidence that some NGO-MFIs believe that credit is the critical and only trigger necessary for growth in the informal sector where the poor operate; therefore, once it is provided, the borrower is capable of finding opportunities to invest and grow in a sustainable manner. Critics say that this is not a valid assumption since their studies show that micro credit can provide only consumption smoothing and at best small activities which do not add value or increase productivity and generate employment; they say that micro credit may increase scale to some extent, but the activities are usually seasonal and not viable; this is not adequate to lay the basis for eradicating poverty in a sustained manner, and for increasing the GDP.

The reasons why the impact of NGO-led MFIs is limited, however, are not clearly spelt out by many vocal critics: Is it that other supporting services are required for credit to blossom into productive investment (which NGO-MFIs in particular cannot provide if they are to achieve financial sustainability), or is it that the pressures to achieve financial sustainability and growth pushes MFIs into a portfolio that gives priority to small loans with a quick turnover – growth is thus based on new small loans ("firm births and not firm growth") rather than on larger loans over a longer period which, critics say, have the potential to increase productivity, income, employment and sustainable growth? Is there a difference in the loan portfolio of MFIs which stand alone (in other words MFIs which started out and remain as financial institutions without linking with organisations that promote all round development in the areas where the MFI provides credit) and those MFIs which work within a broader development context?

Myrada and Sanghamithra's position is that credit is necessary but not enough; supporting services are required (this is elaborated later). However, these supporting services need not be provided by the MFI; they can be provided by an NGO or come from the all-round growth in the area where the MFI operates. This is one of the reasons why Sanghamithra, even though it provides credit directly to SAGs, nevertheless enters into formal partnership agreements with NGOs promoting the SAGs as part of a broader development strategy. There is some reassurance in knowing that while credit flows to the SAGs from Sanghamithra other capacity building and back stopping services needed for the SAG members to improve their livelihood prospects are provided by the NGO partners. In the case of Myrada for example, SAGs are formed in the context of livelihood support programmes such as watershed development, skills training, linkages with technical and marketing support services and animal husbandry, agriculture, horticulture and non-farm enterprise extension services. Since the risk mitigation measures and improved investment opportunities are created under the programme, credit linkages with banks or Sanghamithra enable greater livelihood security and enterprise development. Once it breaks even and earns a surplus, the MFI can provide funds to invest in certain of these support services (including management and skills training, market linkages and infrastructure development). In fact, it can even raise separate grants for this purpose provided there is clarity on end-use and separate tracking of such funds. This is exactly what Sanghamithra has started to do after three years of functioning. FWWB (Friends of Women's World Banking) is another micro-credit provider that has demonstrated a similar partnership approach that engages with its partners to create a supportive environment through capacity building, leadership development and linkage establishment where credit has a greater chance to be productively deployed and build sustainable livelihoods. *(However, the deployment of surplus income for capacity building and provision of other support services is valid only for MFIs which are not-for-profit and which do not distribute dividends.)* In areas bordering small towns and cities which experience all round growth due to investment from private and public sources, there are often adequate opportunities and support services including linkages and market information without the need for NGO intervention in these areas.

The priority given by some MFIs to small loans to individuals with a quick turnover in order to reduce risk and increase the number of loans in the rush towards sustainability is another noticeable trend. It is also driven by the model where the MFI controls the size and purpose of loans. In the Myrada/Sanghamithra model, the MFI (Sanghamithra) does not control the size and purpose of loans to members. The SAG is in control of both. The SAG also negotiates the size of the loan from Sanghamithra. Studies indicate that in the first year or two the loan size from Sanghamithra to the SAG is small (Rs 10,000 to Rs 50,000), but it increases from the third loan where loans of Rs 2 to 3 lakhs are becoming common. Where SAGs do not divide the MFI loan equally between all members (as no well functioning SAG will do – equal division in fact is a sign of a weak SAG which should not have been eligible for a loan in the first place), the average loan size to individual members [5] is increasing year on year. **A survey in 2005 of the size of loans taken by individual members in 238 SAGs (in Myrada Projects) shows that 83.6% of loans to individual members are over Rs 10,000 [6] and 8.3% between Rs. 5,001 and Rs 10,000 [7]** . There is adequate anecdotal evidence that this amount provides the borrower with a financial base which he/she can then invest in small enterprises or businesses which earn an adequate income to keep the family above the poverty line. Case studies to provide further insights into this process and on the impact will be undertaken by Myrada/Sanghamithra.

A major feature in the minimalist approach adopted by some MFIs is the trend to lend to individuals. There is evidence that this trend is accompanied by the rapid shift in the borrower profile from those below the poverty line to those above, who have basic assets/resources and can acquire the skills and linkages required to negotiate for a loan and to utilise the credit productively. This trend to raise the profile of borrowers is also evident where MFIs engage intermediaries on commission or incentive basis who in turn try to cut their risks and transaction costs and increase their profits by pushing larger loans to borrowers who can provide proof that they possess adequate resources and productive assets, which are (implicitly or explicitly) offered as guarantee. Myrada/Sanghamithra has no quarrel with this trend to lend to borrowers who are above the poverty line since they also do not have access to credit from official institutions which is adequate to start or expand small business enterprises. **However to include such initiatives under the label "Micro Finance Institutions" does not exactly reflect the origin of micro credit which began with a clear focus on poverty.**

The problem arises in remote and neglected areas where MFIs enter with credit provision only and where there is no NGO promoting growth through an all round development programme, and neither is there adequate growth in the area due to public or private investment. Our understanding of Growth here includes investment to increase productivity and to reduce risk of existing livelihood activities, undertaking new ones, investment in health, basic education, infrastructure and linkages and above all in the building of people's institutions appropriate to the resource to be managed (examples being SAGs to manage savings and credit, Micro Watershed Management Associations, Milk Societies, Village Water and Sanitation Committees, functioning Gram Sabhas and Gram Panchayats, etc). In such areas, which are remote and neglected, the evidence indicates that the provision of micro credit/finance alone is insufficient to raise people and keep them above the poverty line. Besides being insufficient, the Non-Performing Assets also increase rapidly which makes it difficult to sustain the MFI.

Sanghamithra also differs from other MFIs in its approach to "growth". Unlike the train described above, Sanghamithra does not seek to grow faster and faster; it slows down at the curves, and gathers speed required by the external situation rather than by the internal organisational demands. What does this mean on the ground? Sanghamithra has a clear policy

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[5]Average number of members in an SAG in Myrada is 18.

[6] In fact, a large number of these loans are for amounts ranging from Rs.20,000 to Rs.30,000 but since Myrada's current software stops distinguishing after Rs.10,000 we cannot break this down further.

[7]In fact, a large number of loans are over Rs.15,000 but the software was not developed to capture this.

that it will enter an area where Myrada and other NGOs have functioned for some years; it will lend to SAGs only if the local banks are not responsive. In Dharmapuri District for instance Myrada alone had over 1,000 SAGs eligible for bank linkages, but very few were linked. Sanghamithra opened a branch there. Within six months, the bank managers who were aware of the success of Sanghamithra's activities since all transactions passed through the banks came forward to lend. The Chairman of the Bank visited Sanghamithra's Chairman and offered full cooperation in extending credit to SAGs. Sanghamithra therefore scaled down its involvement. A similar situation was encountered in Chitradurga District, where a very dynamic Bank Chairman increased the bank linkage programme by over 100% enabling Sanghamithra to withdraw from SAGs and to look for other people's groups which were functioning well, like the Watershed Management Associations. However, if the bank's performance falls, as has happened in the service areas of some branches when the managers were transferred, Sanghamithra enters the area once again. Sanghamithra's corporate policy is not to grow rapidly or to grow into a mammoth institution. It plans to target an outstanding portfolio of around Rs.30-35 crores and is planning its staff and supporting systems to manage this portfolio effectively and efficiently. Myrada plans to start other Sanghamithras in other areas. These Sanghamithras will be supported and regulated by a Fund Management Company which, it is hoped, will introduce and implement a regulatory mechanism that is both institutionalised and distinct from Myrada and Sanghamithra.

Both Myrada and Sanghamithra recognise that credit is important but not a sufficient condition; other support services are necessary; they also recognise that even credit is inadequate if it is not available is repeated and timely tranches and in a adequate size/amount. But they also recognise that it is not necessary for the MFI to provide all these support services in the first phase especially when its energies are focused on finance management (mobilising, lending, repayments and building up the infrastructure and staff to support its operations) and when it has still to break even. As far as Sanghamithra is concerned, after it achieved financial/ operational sufficiency, it has invested in institutional capacity building both of SAGs and NGOs, which with

Myrada's support it has the capacity to implement. However Myrada and Sanghamithra still believe that services like insurance, for example should be left to other institutions more capable than the MFI to provide these services.

To conclude the discussion on the 'Minimalist Approach', if minimalism refers to credit provision alone, without attempting to foster an enabling environment in which this credit has the opportunity to convert to flourishing enterprise, is it borne out by fact that this tag can be applied only to NGO-MFIs? How many non-NGO Financial Institutions – including large banks – can claim to be doing more than credit provision? Their loan sizes and transaction volumes may be larger than NGO-MFIs but it still amounts to giving loans and doing no more than that. Several recent entrants into the Micro Finance Sector – many of them with previous experience in major banks – tend to view MF institutions in the same frame that they view Banks and other Financial Institutions which are driven by growth and profit and which largely restrict their services to finance provision and to enable transactions to be carried out quickly, at any time and in any place. The major concern of these stand alone, as against NGO-backed, financial institutions, is growth and sustainability (after all they have to keep their shareholders happy). In the final analysis, the MFI comes first – and often last; the impact of the loan may be relevant from a development point of view but it is not a critical indicator of success provided repayments are made on time. This group too is open to the minimalist tag.

B. Is the criticism valid that NGO-led MFIs can at best achieve consumption smoothing and not true enterprise/business development?

There is a great deal of variation in the understanding of the terms "livelihoods", "micro- enterprises" and "micro businesses". This is from where some of the confusion arises.

Livelihood activities are understood by experts [8] as those which involve only one individual or family. They are small, do not employ others, are not driven by sound business norms, are low skill, operate out of home or are mobile, with low margins and low growth rates and do not bring the household out of poverty – at least not in a sustained manner; they do not contribute to growth of employment and GDP. These livelihood activities serve to address the symptoms of poverty rather than to eradicate it. An analysis of the purposes of loans given by SAGs in Myrada's Projects indicates that, a large number of loans fall in this pattern. They are managed by one family, require low/traditional skills, do not employ others and have low margins and growth rates. (However, it must be noted that "low" margins relate to expectations) Examples of loans falling in this category in SAGs promoted by Myrada are (a) agriculture, (b) animal husbandry, (c) cottage industries, (d) trading/hiring. But is the assumption valid that these livelihood activities address only the symptoms of poverty? Myrada's experience indicates that they go further.

Enterprises are distinguished by these experts from livelihood activities. In the early 1980s, enterprises were described as businesses from which the expected outcomes are increased productivity, jobs and purchasing power adequate to lift a poor family out of poverty permanently and to contribute to overall growth, employment and GDP. However by the late 1980s the term micro enterprise, they claim, entered the development discourse and came to be associated with the informal sector and with the poor. A summary of micro enterprise characteristics drawn from the literature on the informal sector during the nineties shows that micro-enterprises are similar to livelihood activities described above. Hence, Thomas Dichter concludes "*Many micro enterprises (including livelihood activities) are thus hedges, not ways to build sustainable growing business. Few are dynamic firms. In the majority of developing countries only a minority of informal firms with four workers or less experience growth of any sort. Indeed informal sector growth comes not from firm growth, but from net gains in firm "births" (pg 16 op cit).* This understanding of micro enterprises appears to be the common one in India. For example a recent flier (November 2005) from IRMA announcing a programme called "Development and Management of Micro enterprises" defines micro enterprises as *"tiny businesses employing one or two or a few family members and lying in the informal sector …they show marked heterogeneity in size, investment outputs, viability and survival. With the governments paying little attention to them, they need to be supported by voluntary agencies and donors, at least in their initial stage, and helped to graduate to small viable units*". This removes the distinction between livelihood activities and enterprises and both are considered to be non-viable by themselves.

[8]According to Thomas **Dichter "Case Studies in Micro finance: Discussion/Technical Paper – NGOs in Micro finance: Past, Present and Future – An Essay 1999".**

What does viable mean? The dictionary meaning is "capable of working successfully or surviving". For poor people an activity is viable if they feel that they get an income from the activity which they think is worthwhile – or worth the effort put into it either in comparison to some other income generating activity or (more commonly in the rural area) in comparison to doing nothing that brings tangible benefit. Some of these activities by their very nature are seasonal; therefore "survival" has to be interpreted differently. They survive for a short period every year. Dryland Agriculture is a good example. Further, Myrada's data indicates that the activity for which micro loans are taken is one of several income generating activities that households juggle with to meet their daily needs throughout the year. Given the scarce resources, poor infrastructure and inability to take risks due to lack of supporting systems, poor people tend to opt for a bundle of livelihood activities just as they practice multi-cropping due to the uncertainty of rain. Does this lower the value of a micro enterprise and make it just a non-viable activity or a consumption smoothing one? The critics of micro credit assume that a genuine enterprise should be a business large enough to provide full employment throughout the year to the family, and even to employ others. Such an enterprise, however, has to be the only income generating activity since it demands the full time and attention of the household. Why should the poor be put into this straitjacket of "one major enterprise" throughout the year? Are they not the ones to choose what they find most suitable and "viable"? Getting involved in one major enterprise throughout the year may be considered by them as too large a risk which the household is not capable of handling. In this they are not different from large business houses that also do not put "all their eggs in one basket". And finally, why should an activity be downgraded if it does not provide employment to others? [9]

To go back to the analysis of 238 SAGs related to the purpose and size of loans, which Myrada undertook recently (2005 September). It indicates that **83%** of the loans taken by individual members were over **Rs 10,000**. The purposes for which members took these loans were for: agriculture/horticulture/sericulture inputs (33%); household expenses like purchase of jewellery, vehicles, health, food, clothing socio-religious functions (35%); non-farm activities like cottage industries, small businesses, trading, hiring equipment (18%); animal husbandry/ poultry/ fisheries, insurance (8%); high cost debt release- from personal bondage, mortgaged lands & assets (2.7%); housing related – biogas/cylinders, toilets/bathrooms (1.75%); new opportunities, like training in skills, education, land purchase (1.5 %).

Some of these activities are seasonal (agriculture related and some non-farm activities), others continue throughout the year, others are one time purchases partially as savings or for better living conditions (jewellery, vehicles, land purchase, release from bondage and land mortgage which makes productive assets available and provides opportunities to people to work for themselves or to be educated). We venture to assume that an investment of over Rs.10,000 in these activities - in the context of an overall development programme in the area managed by an NGO or Government/private enterprise - has the potential to provide an increase by 75% to 100% in family income. Besides, the households have in most cases also

[9] Under the IRDP programme one viable activity projected was a sheep unit of 20 (female) plus 1 (male). A poor woman who got this unit had to give up all other livelihoods in order to maintain this sheep unit. How was she to survive? She solved her problem by selling one sheep every month until she felt her flock was of a manageable size that she could juggle with her other livelihood activities. The “viable unit” concept did not survive!

taken other loans from the groups at other times for other income generating activities. Further data on the impact of these loans is being collected and case studies are planned to assess whether this assumption is generally valid or not. However, at first sight, it does not appear that these loans are only for consumption smoothing or for “non-viable” activities.

Thus, Myrada’s experience indicates that the criticisms related to “consumption smoothing loans” raised by critics cannot be applied to all SAGs or NGO-MFIs. Much depends on the opportunities provided in the area due to investments from NGOs, the private sector and government and if the borrowers are also resource owners (like landowners) which they can improve or utilise more productively by borrowing from micro credit institutions for inputs like assured irrigation. In such cases or in such situations, there is ample evidence to indicate that group members (SAGs, Joint Liability Groups) have borrowed for investments that may not have created additional employment but have surely increased their incomes in a sustainable manner through increases in scale and productivity. In the case of loans taken for trading and cottage industries there is also ample evidence that members of groups around cities and towns where there is over-all economic growth have increased their incomes substantially, some by increasing the scale of their enterprise, others through productivity increases (and for the poor person income is important, more than how it is achieved). These households have risen above the poverty line and remained there. It is true that not all the members of the groups have progressed in this manner. But then the ability and willingness to take risks also differs from person to person not just with the poor but also with all of us involved in development.

C. While preserving their separate identities can the two (NGO and MFI) be closely meshed so that a balance can be maintained between, on the one hand promoting a supporting environment for poverty eradication and on the other a loan portfolio which includes activities that increase income through genuine business initiatives?

This meshing is what Myrada and Sanghamithra have attempted to accomplish. Can Myrada preserve its primary objective to assist the poor in building their institutions and necessary linkages so that they have an institution to manage credit/finance as well as a power base to influence change in society and at home while at the same time can Sanghamithra achieve financial sustainability while providing credit in a manner which supports the efforts of the poor to rise above poverty? What is common to both institutions (Myrada and Sanghamithra) is the vision; both believe in “building poor peoples institutions” and to work with institutions of the poor appropriate to manage finance, namely the Self help Affinity Groups. [10] Myrada’s mission is to assist in building the SAGs to manage their affairs including finance (this requires investment which SAGs cannot provide and therefore comes from elsewhere, usually as a grant) while Sanghamithra’s mission is to provide these institutions with credit – it does not lend to individuals, neither does it lend to individuals in groups (the Joint Liability Model), it lends to the SAGs. Over the past 5 years during which

[10] Myrada also helps to build other types of institutions like the Watershed management Associations, Gram Sabhas, School Management Committees, water and Sanitation Committees, etc. Sanghamithra also lends to Watershed Management Associations

Sanghamithra has been functioning, there is ample evidence that these two institutions have been able to work to support one another, while maintaining their identities. [11]

Maintaining this balance is not easy. Myrada attempted to create this balance when it promoted Sanghamithra, and continues to do so. In substantial part it has been made possible by the fact that several of Myrada’s senior staff are on Sanghamithra’s Board; and there is a regular exchange and sharing of reports and assessments. It also requires that Sanghamithra shares the vision of Myrada while maintaining an independent mission. This again is not easy to achieve. Sanghamithra is under various pressures - both from external sources – (originating from the prevalent culture in the Micro Finance Sector and the various appraisals that it is subject to by rating agencies and individuals prior to being accepted as eligible for a loan from a financial institution) as well as from internal sources, since the staff tend to slip into the “growth/sustainability box” as the only or dominant organisational objective. These pressures can cause it to drift away from its original objectives. Maintaining this balance requires constant monitoring of Sanghamithra’s operations. Whether it has succeeded or not will require further and more in-depth studies; this article’s intention is to state what Myrada and Sanghamithra are attempting to do. Meanwhile, in order to maintain this balance the following signposts guide the decisions of Myrada and Sanghamithra:

- *Credit is critical but can be absorbed productively only within a larger development context*: While Myrada does not promote micro finance, neither does Sanghamithra open branches except within a context of over-all development investment and growth which is undertaken by the NGOs who implement an integrated development programme within which formation and training of SAGs is a critical component. Most of this investment is a grant. People's investment in cash is mobilised and their participation in planning, managing budgeting and implementing these activities and maintaining assets is critical. Within this context, Sanghamithra (or the Banks) are brought in to extend loans.

- *Credit alone is not enough but this does not mean that the Sanghamithra has to become the single-source agency for all financial services*. Savings, insurance, marketing, capacity building, linkages are equally important components necessary to sustain livelihoods. Since Sanghamithra's focus is only to provide credit, can this be called a minimalist approach? Is it necessary for Sanghamithra to take on all functions? Myrada/Sanghamithra's view is that it is not necessary. Other institutions must be brought in. Myrada/NGOs provide the infrastructure, linkages and training as described above, but not all the other services. For example, when Birla Sun Life came up with a good insurance product that appealed to SAG members, it was decided that this service could well be performed by them. The Company relates directly with the Projects where Sanghamithra is lending. The administration required to support the insurance policies is carried out by the Community Managed Resource Centres (which earn a commission) and not by Myrada or Sanghamithra. Similarly several insurance agencies have been brought in to cover animal insurance. Health insurance is now being explored. And savings, as already mentioned, is a service managed by the SAGs themselves.

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[11] For more on this refer to "Putting Institutions First – Even In Micro Finance" by this author…

- *Growth in size of loan portfolio is not the major driving force or measuring stick*. True, Sanghamithra had to achieve a certain size in order to achieve operational and financial self-sufficiency, which took it 3 years from the date it advanced its first loan. Now that this stage is reached, it can resume focus on its original goal to be "not the sole one and not the biggest but the best". It would like to contribute to setting standards in good practices. A portfolio of Rs.30-35 crores outstanding – which is what it intends to remain at for the moment – may not make it a 'big' organisation but it can still prove itself to be an effective organisation. There is no doubt that this came about solely because it was born as, and continues to be a 'Sister Concern' of Myrada. However, this influence extends only to providing the parameters for lending and growth; it does not compromise on the other banking practices needed to make it a self-sufficient organisation as long as it chooses to remain in the sector.

- *Not competing but creating competitive conditions*. Myrada has endeavoured to push the SAG-Bank Linkage Programme, while at the same time promoting Sanghamithra. Myrada thus fosters competition in the sector because it believes that competition plays a critical role in ensuring the best service to the members of the SAGs. Consequently, Sanghamithra has been under pressure to keep its service charges (including interest rates) comparable to the banks and to provide better service – at the doorstep. The results of this competitive environment during the past five years are evident. Banks in rural areas filled in the gaps they had left when they found that Sanghamithra's loans were being repaid on time, they also increased the size of loans to match with Sanghamithra. Bank Managers went to the SAGs and even to the houses of the SAG representatives requesting them to take loans (a totally new experience). Some of them also set up facilities and funds for SAG training. Sanghamithra on its part has had to keep its transaction costs down and to ensure that its services were friendly and at the doorstep in order to remain competitive. True, it has had to mobilise grants in the initial phase so that it could keep the cost of credit low, but this was clearly stated up front by the founders of Sanghamithra and incorporated into the strategic business plan. Whether this pressure from Bankers to link with SAGs will continue in future given the increasing focus on profit and in view of the amalgamations of several Regional Rural Banks, is a major concern at this time.

To conclude, Myrada's experience indicates that the pebble of micro finance causes larger ripples than its size leads one to presume.

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