

Microfinance Outreach
Comparing Banks and MFI (Bandhan)
in Cooch Behar District

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Executive Summary

Objectives

The faster growth of mFIs in the last few years raises the following questions:

- Are mFIs supplementing the role of banks by reaching the unreached?
- Are they providing better products and services to the existing customers of banks?

Answers to these questions can help in fine-tuning the microfinance strategy of both banks and MFIs for increasing their outreach in a coordinated way. It was, therefore, decided to take up a comparative study of the operation of a fast growing mFI (Bandhan) to compare the performance of banks in its area of operation in Coochbehar District of West Bengal.

Observations

Important observations of the study are as follows.

- ❖ 43% of the Bandhan clients were already members of some Self Help Group formed under NABARD's SHG-Bank Linkage Programme or under the Swarna jayanti Gram Swarozgar Yojana (SGSY).
- ❖ Most of them (57%) indicated non availability of adequate credit from SHGs as the reason for taking loan from Bandhan. The second most common reason for joining Bandhan programme by SHG members was non availability of loans from SHGs (34%). The remaining 9% indicated that they did not get the second loan from SHG as the bank did not give second loan to their SHGs.
- ❖ One of the important reasons that came out of discussions with the Bandhan groups and the Credit Officers of Bandhan was that the women who had joined SHGs were more aware and empowered than others. These women, therefore, were quick to understand the Bandhan approach, they were more articulate and quick to join the micro loan programme of Bandhan to fulfill their unmet credit needs
- ❖ The issue, therefore, is not the delivery model but rather inadequacies in the delivery **process**. While Bandhan has been able to maintain the sanctity of

the delivery process, banks, for various reasons – some of them beyond their control – have not been able to maintain the sanctity of the delivery process leading to poor performance in terms of access and outreach.

- ❖ What is interesting, though, is the awareness among most of the clients/SHG members surveyed that banks are charging lesser interest than Bandhan. Most of them, however, are not aware of exact loan terms of banks. But, they have ‘heard’ from friends and relatives and ‘believed’ that it was cheaper to borrow from banks than from Bandhan
- ❖ The most important reason which they indicated in group discussions was that banks were not as accessible as Bandhan. One had to go to the bank branch for everything while Bandhan officials visited their groups every week.

Conclusion

The comparison of Bandhan with the operations of Banks in terms of the outreach and customer preference has brought out the following issues:

- ❖ Is multiple membership of poor borrowers a matter of choice or a reflection of their desperation?
- ❖ While Bandhan takes its job of microfinance seriously, banks still continue to treat it as social responsibility.
- ❖ Given a chance, most Bandhan clients express their eagerness to deal with banks provided banks were as accessible as Bandhan

In short, the poor still have more faith in the banks; if only banks could respond.

And, for banks to respond, it is suggested that they may take up microfinance as a business by adopting a low cost model of satellite microfinance branches based on the Bandhan Model.

Introduction

1.1 Microfinance in India has been growing both in terms of outreach and loans outstanding. In India, unlike in other countries, the sector is characterized by a strong participation of banks through the Self Help Groups (SHG)-Bank Linkage programme. As of March 2007, total number of 28,94,505 SHGs were having outstanding bank loans of Rs 12,366.49 Crore (NABARD, 2008). In addition, the client outreach of MFIs has exceeded 10.5 million clients and their gross loan portfolio (loans outstanding) has crossed Rs. 3,987 crores from a meagre Rs 5.4 Crore as on March 2002 (Sa-Dhan,2007a). An interesting aspect in Indian microfinance is the financial assistance being provided by the mainstream banks to the mFIs for on lending to their clients. As on 31 March 2007, 27 banks (12 Public Sector Commercial Banks, 12 private Sector Commercial Banks, 4 Regional Rural banks and 1 Cooperative Bank) have outstanding loans of Rs 1422.55 Crore to MFIs which is more than 10% of the total loans outstanding of banking sector under microfinance (NABARD, 2008). MFIs are increasingly being seen as having potential to play a significant role in facilitating financial inclusion because of some of their inherent strengths like operational flexibility, limited geographical area of operation, greater acceptability amongst the poor and better understanding of the issues specific to the poor (Committee on Financial Inclusion, 2008).

1.2 The growth of microfinance in India has been uneven in different regions and, the skewed geographical distribution of microfinance intervention has been an area of concern. In March, 2001, 71% of the linked SHGs were from Southern Region consisting of Andhra Pradesh, Karnataka, Kerala and Tamil Nadu. The share of Southern Region has come down progressively over the years but it is still at 44%. The spread of SHG-Bank Linkage Programme in different regions has been uneven on account of various factors like pro-active role of State Governments, presence of well performing NGOs, socio-cultural factors, better performance of SHGs etc (Committee on Financial Inclusion, 2008). Initially most of the MFIs had also been concentrated in the four south Indian states – with 8 of the top 10 MFIs operating in the South Indian states (CFM-IFMR, 2006). It is observed that most of the MFI

activity has been concentrated in the areas endowed with better infrastructure - both banking and general infrastructure (Sriram and Kumar, 2006). Of late, a conscious effort by all stakeholders has ensured that microfinance has started moving to all regions. Recent years have seen the share of eastern and North Eastern parts of the country going up in annual loan disbursement to SHGs through banks and similar trend is observed in the growth of outreach and loans outstanding of MFIs (Sa-Dhan, 2007a). Simultaneous increase in the number of clients supported by banks under SHG-Bank Linkage Programme and those supported by MFIs is a positive development which can go a long way in achieving financial inclusion provided the client overlap is minimal and the genuine credit needs of the borrowers are fulfilled by both the channels in comparable manner. While the issue of multiple borrowings from different MFIs arising out of competition is already drawing the attention towards the need of a transparent financial reporting by MFIs and information sharing among them (Sa-Dhan, 2007b), the issue of overlapping of SHG-Bank Linkage and MFI clients has not received the desired attention except immediately after the so called 'Andhra Pradesh Crisis' in March 2006 when the Government of Andhra Pradesh ordered all MFIs functioning in Krishna district to stop their operations as there were complaints of very high rates of interest being charged by the MFIs and abusive methods of collection of recovery adopted by their staff. In the aftermath of the crisis, Sa-Dhan hurriedly adopted a voluntary code of conduct on 20 March 2006 which, among other things, prescribed that –

1. MFIs will ensure that they complement the credit provided to poor households under the SHG-Bank Linkage Programme, and specially extend services to those not served adequately by banks
2. MFIs will avoid over-financing of the same household by different MFIs, by informal information sharing on operations among themselves and with banks doing SHG lending.

1.3 Various causes for the AP crisis have been advanced by different commentators. To some, it was a fall out of the competition between a politically attractive and high visibility programme being implemented by the State and the microfinance programmes of various MFIs (Ghate, 2007); to others, the poaching of SHGs was a natural outcome of excessive competition and absence of coordination among lending agencies (Shylendra, 2006). The fact remains that Andhra Pradesh has witnessed the maximum outreach of microfinance both through SHG-Bank Linkage Programme and MFI lending. By March 2005, 92% of the poor households were already reported to have been covered under SHG-Bank Linkage under the Velugu

project (Government of AP, 2005). Any MFI would, therefore, necessarily face the challenge of reaching out to the same poor households which were already members of SHGs. One of the important lessons of the crisis is the realization that MFI model has to develop a harmonious relationship with SHG-Bank Linkage Programme because both the models have been expanding in their outreach and, in the long run, geographical separation is not possible (Ghate, 2007).

1.4 Such a harmonious relationship is all the more important when microfinance is breaking new grounds in the east and the north east. And, unlike Andhra Pradesh, these new areas do not have a strong and successful state supported intervention like Velugu (now renamed as Indira Kranthi Patham). Above all, the increasing lending by banks to MFIs for on lending has added a new dimension to the competition between SHG-Bank Linkage and MFI Model – banks are now into wholesale and retail lending both. This calls for a closer interaction between MFIs and bank branches at the field level in ensuring that there is no unhealthy competition between the two. At the same time, the faster pace of growth of some of the MFIs in some states like West Bengal as compared to the growth of SHG-Bank Linkage Programme also warrants a closer look at the operational efficiencies of the two models to afford cross learning and a synergistic growth of microfinance leading to greater financial inclusion.

Objectives of Study

1.5 The faster growth of mFIs in the last few years raises the following questions:

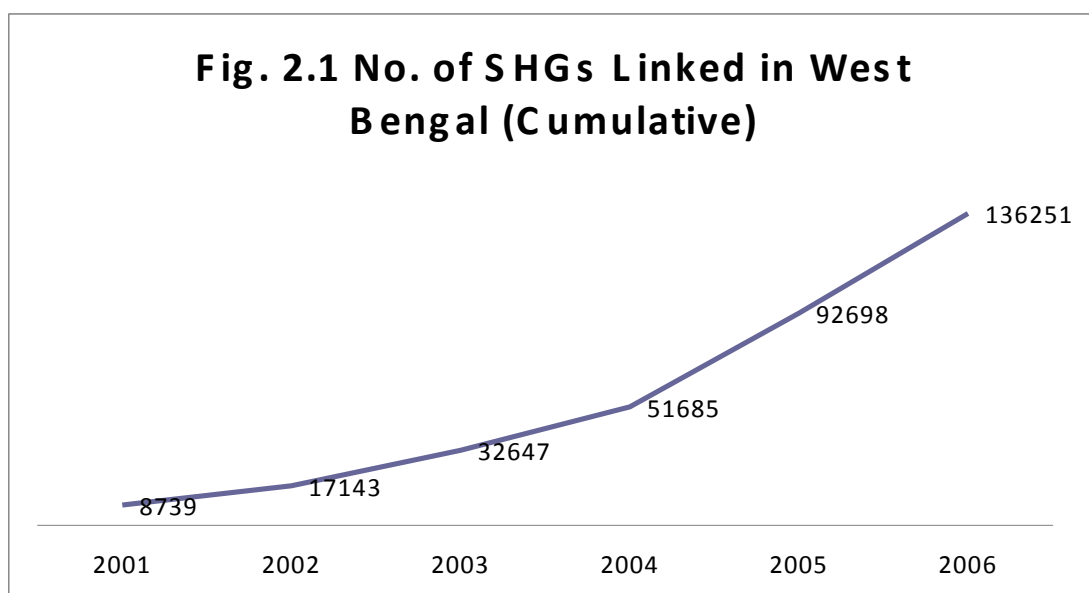
- Are mFIs supplementing the role of banks by reaching the unreached?
- Are they providing better products and services to the existing customers of banks?

Answers to these questions can help in fine-tuning the microfinance strategy of both banks and MFIs for increasing their outreach in a coordinated way. It was, therefore, decided to take up a comparative study of the operation of an mFI to compare the performance of banks in its area of operation.

Methodology & Study Design

Selection of State

2.1 West Bengal is one of the thirteen priority states which have been identified by NABARD for giving focused attention for increasing the microfinance outreach. This has resulted in an impressive growth in the number of SHGs linked with banks from 8739 SHGs in 2001 to more than 1 lakh SHGs by the year 2006 (Fig 2.1)

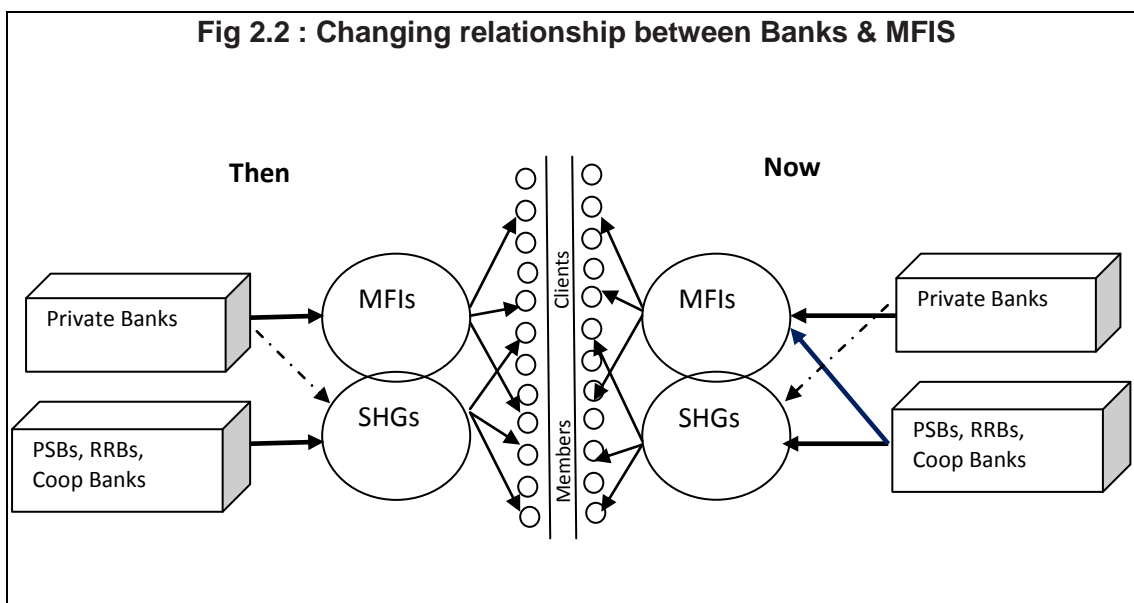


Source : NABARD, 2006

In the absence of a database of MFIs in the country, it is not possible to compare this growth in SHG-Bank Linkage with the growth in financing of MF client by MFIs. However, the Sa-Dhan member MFIs have shown an impressive growth in the eastern India, particularly in West Bengal.

2.2 West Bengal, therefore, presents an interesting microfinance scenario where both the prominent models of microfinance – Bank Linkage and MFI model – are increasing their outreach simultaneously. Unlike in the south where SHG Bank Linkage had already reached a sizeable scale by the time MFIs entered in a big way with the support of a few new-generation private sector banks. Another, important development is the role of public sector banks in providing financial support to MFIs

in the state. In the past few years, there has also been an increased awareness among banks and government about the role of MFIs in supplementing the efforts of banks in reaching out to micro clients.



Selection of District

2.3 Coochbehar district is selected for the purpose of the study because it is one of the less developed districts of West Bengal and compares unfavourably with the state averages in respect of most of the important parameters. The district is predominantly rural with the share of rural population in the total population of the district being 91% as against the state average of 72%. The share of SC population is 50.11% which is very high compared to the state average of 23%. The district also shows a high incidence of poverty with 41% of families below the poverty line (BPL Survey, 2002) as against 36.38% of the families below the poverty line at the State level. While the average daily wage rate of male field labourers in West Bengal increased to Rs 66.67 in 2006-07 (July 2006 to June 2007) from Rs 62.86 in 2005-06, it has marginally declined in Coochbehar from Rs 63.52 to Rs 62.98 (Economic Review, GoWB, 2007-08). The district falls in the lower bracket in respect of major district wise developmental indices of the state of West Bengal (Table 2.1). The state has 19 districts.

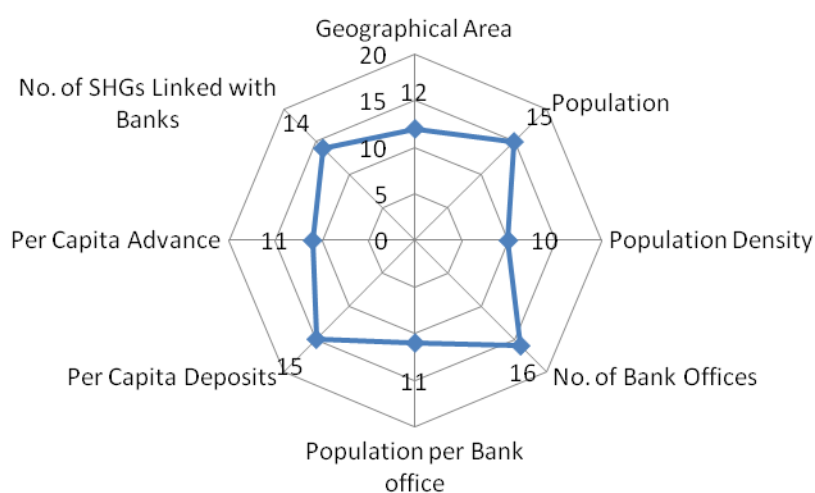
Table 2.1 : Major Developmental Indices

Index	Value	Rank among 19 Districts
Human Development Index	0.52	11
Gender Development Index	0.45	12
Education Index	0.65	10
Health Index	0.50	16
Income Index	0.41	9

Banking Infrastructure

2.4 The district has 112 branches of Scheduled Commercial Banks (including RRBs) with average population per bank office at 24000 being higher than the State average of 19000 (RBI, 2007). The district ranks 11th in the average population per bank office. Although the district has a CD Ratio of 57.23%, it ranks 16th in total advances outstanding at Rs 570 Crore as at the end of June 2007.

Fig 2.3 : Rank of Koch Behar in West Bengal



With a cumulative total of 4746 SHGs linked with banks upto March 2006, the district ranked 14th among 19 districts of West Bengal. The average disbursement of Rs

16721 was also less than the state average of Rs 17795 disbursed per SHG (NABARD, 2006). The district does not have significant NGO activity. While 68 NGOs in different districts of West Bengal have been provided grant support by NABARD as on 31 March 2007 for promotion and linkage of SHGs, not a single NGO from Coochbehar has received such a grant support till that date presumably because of the absence of good quality NGOs coming forward to take up SHG promotion and linkage. Under SGSY, of course, a few NGOs are active. Koch Behar, therefore, is a district which is relatively underserved by microfinance and it is interesting to compare the functioning of MFI and banks in this district. 95% of adults have not taken any bank loans. This becomes all the more interesting because the district ranks fourth in the number of groups supported by Bandhan as also in Bandhan's loans outstanding against its microfinance clients. **This is an apt example where MFI has not followed a strong bank linkage programme.**

Selection of MFI

2.5 Although no authentic database is available regarding MFI operations in the state or the districts, it is known that Bandhan has emerged as one of the fastest growing MFIs in the Eastern parts of the country and has been ranked first in India and second in the world on the Forbes list of 50 microfinance institutions in the year 2008. Bandhan, registered as a society, started its microcredit programme in the 2002. By March 2008, it has been operating in 7 states in 31 districts which include all the 19 districts of West Bengal. Bandhan is operating through 16 Divisional Offices, 80 Regional Offices and 502 Branches covering 13104 villages. The growth of loan portfolio of Bandhan has been very impressive (Fig 2.4). From a very modest figure of Rs 1.2 Crore in the year 2003-04, the loans outstanding have increased to Rs 330.96 Crore in the year 2007-08.

2.6 It is interesting to note that total loans outstanding to micro clients by Bandhan as on 31 March 2007 is more than the loans outstanding to SHGs by all the three RRBs operating in the state of West Bengal taken together. Similarly, in Coochbehar district also, the outstanding portfolio of Bandhan is higher than the SHG linkage portfolio of all banks taken together. This is in spite of the fact that Bandhan has started its operations in Coochbehar district only in the year 2005. The district provides an opportunity to understand why an MFI is able to increase its outreach and depth while the formal financial institutions are not able to reach out to the poor in a comparable manner.

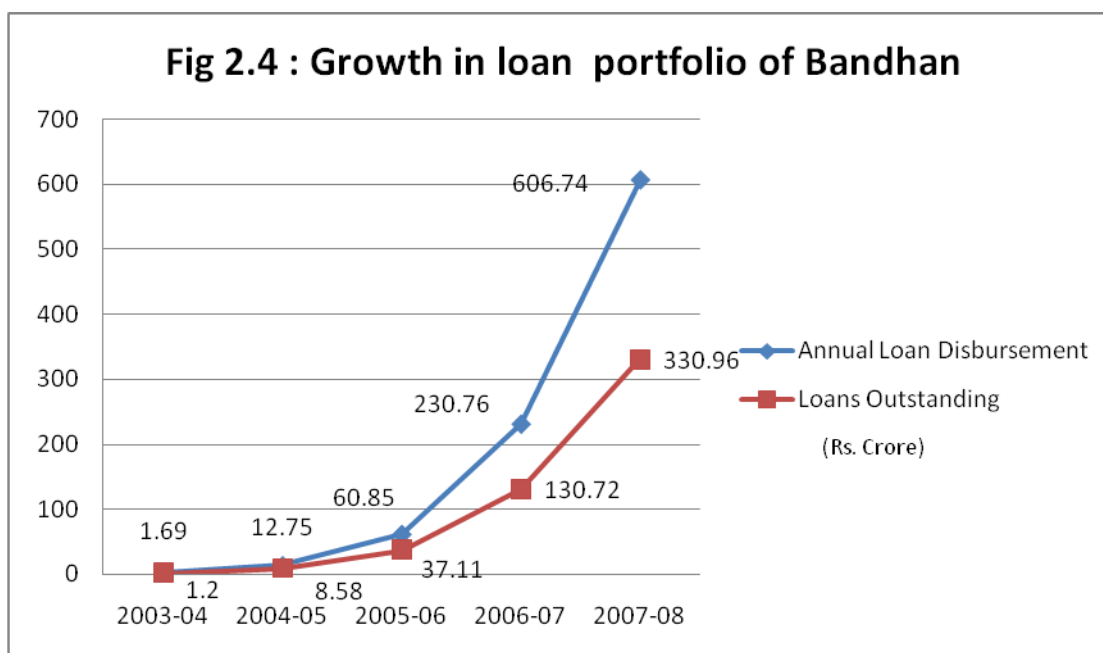


Table 2.2 : Microfinance in West Bengal – RRBs and Bandhan

Name of RRB/MFI	No. of SHGs/Groups	Loans Outstanding (March 2007)
		Rs lakh
Paschim Banga GB	4796	1583.99
Bangiya GB	59194	7576.70
Uttar Banga KGB	8940	1265.20
Sub Total (All RRBs)*	72930	10425.89
Bandhan (MFI)**	21891	12219.70

Source: *NABARD, 2007; **Bandhan Annual Report, 2007

Microfinance products of Bandhan

2.7 Bandhan currently offers three loan products to its clients. It has also tied up with Life insurance Corporation (LIC) to provide insurance cover for the entire loan

amount availed by the clients in case of death. A brief description of its loan products is given below.

1. Micro Loans

2.8 Bandhan gives micro loans to its clients for a uniform tenure of one year. It follows a group based individual lending approach adapted from ASA, Bangladesh. A group of 10-25 women is formed who are expected to meet regularly every week. A member becomes eligible for her first loan from Bandhan after she has attended two successive group meetings. Loans are disbursed individually and directly to the borrowers. The group has an important role in recovery of installments from the members every week. The target group of Bandhan for its micro loan programme comprises poor women from rural and urban areas.

The terms of loans are as follows:

- The first loan is between Rs 1000 and Rs 7000 for the rural clients and between Rs 1000 and Rs 10000 for urban clients.
- Subsequent loan is Rs 1000 to Rs 5000 more than the previous loan
- The loan is to be repaid through 45 equal weekly installments within 52 weeks (one year). There is a grace period of 7 weeks.
- Interest rate is 12.50% per annum calculated on flat rate basis
- A Security Fund equal to 10% of the principal amount is collected from the borrowers at the time of sanctioning the loan. No interest is offered by Bandhan on this security fund. However, if the spouse of the borrowers expires during the currency of loan, Bandhan gives her a grant of Rs 3000. The Security Fund is returned to the borrower on the day she pays the last loan installment.
- In addition a Risk Fund equal to 1% of the principal amount is collected from the borrower to provide insurance cover to the outstanding portfolio of the client in the event of her death. This insurance cover is provided by Bandhan through LIC.

2. Micro Enterprise Programme

2.9 The microenterprise programme has been started by Bandhan in January 2006. The microenterprise programme aims at providing individual loans for undertaking microenterprises to the clients who after taking one cycle of micro loan have reached a stage where they need high amounts of microenterprise loans. Under this programme 80% of the borrowers are those micro loan clients who have graduated to taking up microenterprises. Loans are required to be invested in existing enterprise. The client should directly be involved in running the enterprise. It is also stipulated while sanctioning the loan that the client should generate employments opportunity for at least one poor person in her vicinity.

Important product features are as follows:

- The first loan ranges from Rs 20,000 to Rs 50,000 with an increase of Rs 5000 for every subsequent cycle.
- Disbursement and repayment in cash.
- Repayment in 1 year by 45 equal weekly installments.
- Grace period of 7 weeks – 3 weeks on medical grounds and 4 weeks for important religious/social events.
- Rate of interest is 12.50% per annum calculated on flat rate basis.

3. Micro Health Loans

2.10 Realising that many clients used the micro loans given by Bandhan for meeting unforeseen medical expenses instead of using them for income generating activities, Bandhan launched micro health loan product in February 2007 to enable its clients to meet the emergency needs of clients and their families (husbands and children only). To be eligible for a micro health loan, the client should have completed two cycles of micro loan and has exhibited good repayment behavior.

Important features of micro health loans are as follows:

- The micro health loan size ranges from Rs 1000 to Rs 5000 depending upon the requirements of the client.
- The repayment period of micro health loans is also one year like the other two products.
- However, repayment structure is flexible. The clients are given a choice to repay either in weekly or monthly installments depending on their convenience. The repayment schedule is fixed in consultation with the clients

- Repayment starts two weeks after the date of disbursement.

2.11 The micro loans continue to be the main portion of Bandhan's loan portfolio (Table 2.3) reaching out to more than 10 lakh clients in 7 states. The product development reflects the ability of the institution to learn from the field and its commitment to meet the genuine credit needs of the poor.

**Table 2.3 – Microfinance operations of Bandhan at a glance
(As on 31 March 2008)**

Particulars	Micro Loans	Micro Enterprise Programme	Micro Health Loans
Year of Commencement	July 2002	January 2006	February 2007
No. of groups	43,472	-	-
No. of members	1,017,925	5,424	186
Cumulative loan disbursed (Rs million)	749.12	22.37	0.17
Loans Outstanding (Rs million)	3,205.62	103.57	0.46
Repayment Rate (On time)	99.99%	99.99%	100%

Source: Bandhan Annual Report, 2008

2.12 In addition to these three products, the Institution is also experimenting with a product specifically aimed at the hardcore poor – the destitute. The product has been designed after realizing that the poorest of the poor are not able to join the micro loan programme because they are too poor to use and manage the loan for income generation activities. The programme recipients are identified through PRA process and are provided grant support to acquire an income generating asset. This helps them graduate to the Micro Loan programme and they are expected to become normal micro loan clients. The programme, known as Targeting the Hardcore Poor (THP) is currently being implemented in three districts of West Bengal, viz., Murshidabad, Malda and 24-Parganas(South).

Table 2.4 : Bandhan's Outreach in Coochbehar District

Sr No.	Particulars	Number/Amount
1	Branches	42 (5)
2	Villages covered	1110 (8)
3	Total Staff	230 (3)
4	Credit Officers	188 (3)
5	Groups	3712 (4)

6	Loans Outstanding (Rs lakh)	2982.83 (4)
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Source : *Bandhan* (Figures in bracket indicate the rank among all districts of West Bengal)

In Coochbehar district, Bandhan has more than doubled its loans outstanding from Rs1124.21 lakh as on 31 March 2007 to Rs 2982.83 lakh as on 31 March 2008 which is the fourth highest in any district of West Bengal. The highest being in 24 Parganas-N (Rs 4090.89 lakh) followed closely by 24 Paragnas-S (Rs 3156.11 lakh) and Nadia (Rs 3158.83 lakh).

Methodology & Data Collection

2.13 Since the study aims at comparing the outreach of MFI with banks, it was decided to select a few branches of the MFI which already had started the second cycle of loan. The loan clients of following branches of Bandhan were visited:

Dinhata, Putimari, Bhetaguri, Suktabari, Chegrabandha, Pundibari, Ghughumari, Tufanganj

Similarly, SHG members of the SHGs having accounts in the following bank branches were visited:

CBI, Dinhata, UBKGB, Kashiabari, UBKGB, Maruganj, Allahabad Bank, Panisala, CBI, Dewanhat, CBI, Chandimari, UBKGB, Kuchlibari .

While there is no one to one correspondence of the areas of operations of Bandhan branches and banks branches, these bank branches are more or less overlapping the operational areas of the Bandhan branches. A randomized sample of 300 clients of the Bandhan and 250 SHG members of all branches put together were selected to assess the perceived impact and their perception of the quality of services.

Limitations

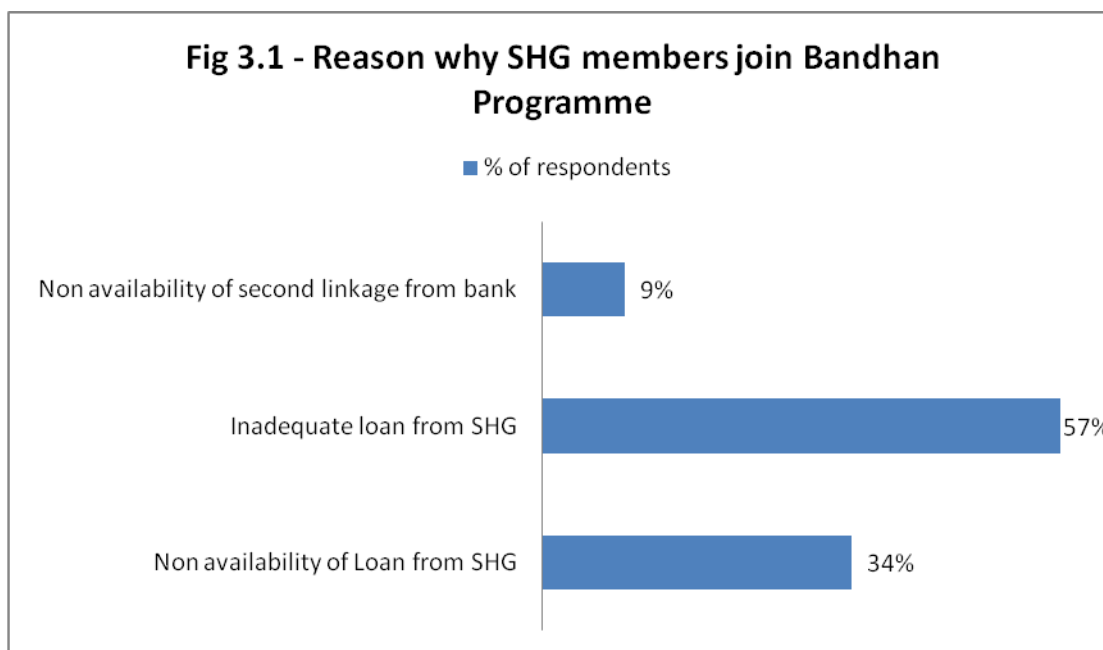
2.14 The study has been taken up in a specific context and its observations may not be representative of the entire state or country. But, issues raised and suggestion offered may be useful in similar contexts.

Observations

Multiple Memberships

3.1 In an area where SHG-Bank Linkage has not reached a scale where all rural households have become members of SHG linked with bank credit, it would be safe to surmise that any MFI entering the area would have a potential market comprising a large number of poor who do not have any access to bank credit. This could safely be presumed then that the MFI would naturally tend to involve only such unreached clients. Bandhan, on its part, takes care to identify only the genuinely poor women for its micro loan products. The small amount of the loan (Rs 1000 to Rs7000) in the first instance also act as a disincentive for the non-poor to join Bandhan's microfinance programme. However, at the field level the possibility of multiple membership cannot be avoided altogether. In the case of the sample selected in Koch Behar, 43% of the Bandhan clients were already members of some Self Help Group formed under NABARD's SHG-Bank Linkage Programme or under the Swarna jayanti Gram Swarozgar Yojana (SGSY).

3.2 It must be clarified at the outset that none of the Bandhan groups studied consisted of members drawn from a single SHG. The multiple memberships did not appear to be a result of conscious effort by the Credit Officers of Bandhan but it appeared to be resulting from the decision of the poor women to use the opportunity they had in the form of an alternative credit delivery mechanism available at their doorstep in the form of Bandhan. An attempt was made to understand why these women who were already members of some SHGs had decided to join Bandhan's micro loan programme (Fig 3.1). Most of them (57%) indicated non availability of adequate credit from SHGs as the reason for taking loan from Bandhan. The second most common reason for joining Bandhan programme by SHG members was non availability of loans from SHGs (34%). The remaining 9% indicated that they did not get the second loan from SHG as the bank did not give second loan to their SHGs.



Source : Field survey

3.3 One of the important reasons that came out of discussions with the Bandhan groups and the Credit Officers of Bandhan was that the women who had joined SHGs were more aware and empowered than others. These women, therefore, were quick to understand the Bandhan approach, they were more articulate and quick to join the micro loan programme of Bandhan to fulfill their unmet credit needs.

Dakhin Balari Schoolpara Mahila kalyan Samiti is a Self Help Group with 12 members in Dakhin nawabganj Balari village. It was formed on 26 June 2001 and opened a savings bank account with UBKGB, Saheberhat. But it could not get its first loan in the form of a cash credit limit of Rs 20000 under SGSY only on 27 Jan 2005, after almost three and a half years. It had to wait further for three years to get a term loan of Rs 2.5 lakh. While the term loan was distributed among members equally, the loan out of its own saving was taken mostly by the office bearers who had not changed since inception. Out of twelve members this SHG had, seven have taken loans from MFIs – 5 from Bandhan and 2 from a small local NGO - Dibakar. When asked why they had to take loan from Bandhan, the immediate response was that Bandhan was more flexible than bank in giving individual loan.

Sahiberhat Mahila Kalyan Samiti is a Self Help group of 10 women formed on 10 Dec 2002 by Coochbehar Aashar Aalo, an NGO working in the area. It was given a term loan of Rs 6000 on 10 Sep 2003 by UBKGB, Sahiberhat. The loan has been repaid but the group has not received further loan from the bank. Coochbehar Aashar Aalo which till two years back was working only as a Self help Promoting institution has

now decided to become a full fledged MFI. It has given a loan of Rs 2500 to each member of the group. All the group members are aware that Coochbehar Aashar Aalo is charging an interest rate that is higher than the rate charged by the bank but bank does not give the loan when it is needed the most, say most of the members.

Access to Credit

3.4 One of the major difference between the members of SHGs and Bandhan clients was the greater and more frequent access to credit enjoyed by the Bandhan clients. Almost all Bandhan clients received their first loan within 2 months of joining the group. More than 80% of the Bandhan clients reported to have received the third loan. On the other hand, only 37% of SHG members reported to have received loan from the bank loans taken by their SHGs. It appeared that the major share of the bank loan went to the office bearers. Is it because the design defects in SHGs? Or, is it an issue related to institutional inadequacy? In the district itself, some of the SHGs have been functioning very well. SHGs formed and nurtured by Dinhat Nari Kalyan Pariseva Mulak Samvay Samiti, an NGO are a case in point. The NGO has formed 250 SHGs out of which 90 SHGs have linked with credit through a loan of Rs 43 lakh from West Bengal State Cooperative Bank. Many of these SHGs have taken up income generating activities. **The issue, therefore, is not the delivery model but rather inadequacies in the delivery process.** While Bandhan has been able to maintain the sanctity of the delivery process, banks, for various reasons – some of them beyond their control – have not been able to maintain the sanctity of the delivery process leading to poor performance in terms of access and outreach.

Cost of Credit

3.5 The demand for microcredit is normally considered to be inelastic in relation to the cost of credit (Ledgerwood, 1999). There is also a case often made out in favour of higher rates of interest charged by the MFIs in view of the higher transaction cost for smaller loans. Such an argument may hold good in countries where formal financial institutions do not engage in microfinance. In a country like India, where formal financial institutions have been the largest player in the microfinance, it is not pertinent to ask why MFIs are charging rates of interest higher than the banks. Rather, the more pertinent question to ask is why poor women continue to borrow from MFIs at a higher rate of interest when cheaper loans are available from banks. Are the poor borrowers unaware of the comparative rate of interest being charged by

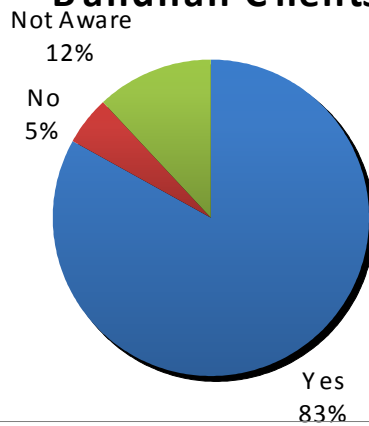
banks and MFIs. If so, who is at fault? MFIs who, out of their compulsions or design, charge higher rate of interest or banks who are not able to position and sell their products. But, this leads to the further question – are banks selling microfinance product or they are just completing ‘targets’ to fulfill their ‘social responsibility’. Are the banks as serious about microfinance as MFIs. Apparently, at the corporate level all banks appear to be serious about microfinance and that is reflected by their assertions in their annual reports and other publications. But, at the field level this seriousness does not seem to be percolating. Most branch managers see microfinance either as a government sponsored programme (SGSY) or NABARD programme (SHG-Bank Linkage Programme) and the SHGs under these programme being referred to BPL Groups (SHGs comprising members who are below the poverty line) and APL Groups (SHG comprising members who are above the poverty line as per the official list of families below the poverty line). This gets reflected in the poor outreach of banks.

3.6 The rate of interest charged by Bandhan is 12.5% p.a on flat rate basis. The effective rate on declining balance works out to about 24% which is almost more than double the rate of interest charged by banks. In addition, Bandhan also collects a security fund from the clients @ 10% of the principal amount. The security fund is refunded to the client at the time of the payment of the last installment by the client. Bandhan does not pay any interest on this security fund. **This fund, however, is used by it to pay an ex gratia amount of Rs 3000 to the client in case her husband dies.**

What is interesting, though, is the awareness among most of the clients/SHG members surveyed that banks are charging lesser interest than Bandhan. Most of them, however, are not aware of exact loan terms of banks. But, they have ‘heard’ from friends and relatives and ‘believed’ that it was cheaper to borrow from banks (Fig 3.2) than from Bandhan.

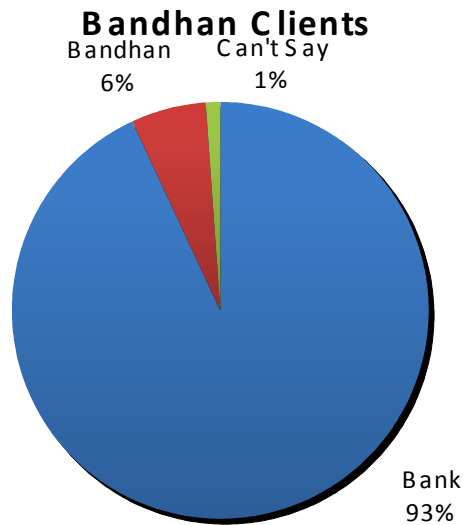
3.7 Why, then, are they still with Bandhan? Why are they not accessing loans from banks? Almost half of Bandhan clients (57%) have not got any loan from banks and the other half (43%) of the clients who are also SHG members have their reasons which are already explained in Fig 3.1. The most important reason which they indicated in group discussions was that banks were not as accessible as Bandhan. One had to go to the bank branch for everything while Bandhan officials visited their groups every week.

Fig 3.2 : Is Bandhan Charging Higher Rate of Interest than Banks? - Response of Bandhan Clients



Source : Field Survey

Fig 3.3 : If Bank gives loans as easily as Bandhan whom will you prefer? - Response of Bandhan Clients



Source : Field Survey

3.8 But, most of the Bandhan clients were very vocal in saying that if banks became as accessible as Bandhan they would prefer banks rather than Bandhan. The most important reason they gave was the lower rate of interest charged by banks and, of course, possibility of loan waivers which could never be thought of in the case of Bandhan.

Institutional Arrangements – Comparison between Banks & MFIs

3.9 The reason why MFIs were increasing their outreach in the district are not far to seek. They are taking their business seriously and they specialize in this. Banks, on the other hand, view microfinance as a small part of their portfolio and the staff does not specialize in it. The commercial banks have an added problem of limited tenure of rural posting of branch managers. By the time a branch manager acquires the skills to deal with the poor he/she starts expecting a change. To understand the difference in the institutional arrangements of banks and MFIs the following questions were posed to SHG members/Bandhan clients:

- How many times the branch managers/other branch officials participate in the meeting SHGs?
- How many times Bandhan officials participate in Group meetings?
- Do the SHG members/loan clients know the loan terms like rate of interest, total interest amount to be paid, repayment period and schedule etc.?
- Are the loan terms indicated on the loan passbook?

3.10 One of the most important aspects of microfinance operations is customer relations. Whether in SHG model or in group based individual lending model, the bank or MFI has to have a sound relationship with group. And, this relationship has to be cultivated from the first day of formation of the SHG/Group for helping the group to develop along the desired lines so as to develop the credit management capacity of its members help it develop it into a sustainable entity which can take up many of the activities of bank/mFI in due course. However, an on-going relationship between the financing bank/MFI and the SHG/Group is a sine qua non. **During the course of the study we did not come across a single SHG whose members could recall participation of branch officials in their periodical meeting.** There have been sporadic visits by branch officers. Some of the SHGs recalled meeting branch officials in training programmes organized by DRDA/NABARD. The Branch Officials of most of the banks, on their part, expressed their inability to attend meetings of SHGs because of other official preoccupation. On the other hand, all the Bandhan group meetings are invariably attended by the Credit Officers. The Branch Managers, Regional Managers and Divisional Managers of Bandhan also regularly attend the meetings of their group periodically. This keeps them in touch with the groups and helps develop a bond and mutual understanding. Bandhan has been able to design new products because of the need assessment done by its officials in such meetings.

3.11 The Second important aspect of a sustainable and mutually useful relationship is clarity of terms and conditions of the contract. This is true in case of all relations. More so, when one has to deal with poor illiterate SHG members of MFI clients. All Bandhan clients know that on a loan of Rs 1000 they have to repay Rs 1125 in 45 weekly installments. They also know that for a loan of Rs 1000, a client has to deposit Rs 100 with Bandhan as Security Fund which is refunded after the repayment of the last installments. They also know that for a loan of Rs 1000 a client has to repay Rs 25 every week for 45 weeks. This “financial literacy” is acquired by the group members in the weekly meetings which are attended invariably by the Credit Officers of Bandhan and quite often by other senior officials. However, in case of banks, most of the SHG members are not aware of the loan terms as clearly as Bandhan clients. Only 22% of SHG members are aware of the exact rate of interest charged by the bank. Most of them are also not aware of exact amount of reayment schedule and repayment period fixed by the bank – this is across all the banks.

3.12 While in case of Bandhan, the loan passbooks contain all details of principal, rate of interest, amount and periodicity of repayment installments, total interest a client has to pay. These passbooks are updated by the Credit Officers every week during the group meetings. In case of SHGs, the bank pass books do not indicate all the loan terms as clearly as in case of Bandhan. Secondly, in most of the cases these passbooks are in English making it difficult for the SHG members to read and understand the terms. In some cases, the banks do not issue the loan pass books. Wherever issued, the passbooks are also not updated in time.

3.13 Lastly, the monitoring and supervision mechanism of banks is very weak as compared to Bandhan. Except one branch, other branches visited could not provide on demand a list of SHGs linked and those that were eligible for linkage. Even where such details were present, the branches were not maintaining any MIS to monitor the health of SHGs so that appropriate actions could be initiated in case of weaknesses in the SHGs. In short, there did not appear any effort at the level of branches either to track the maturity of SHGs formed for credit linkage or to review the linked SHGs for further linkages and to prevent delinquencies. This clearly indicate an unprofessional approach towards the microfinance portfolio of the branch. Every Bandhan branch on the other hand maintains elaborate MIS on each and every group and the clients. This helps them not only to increase the portfolio but also to maintain its quality by regular monitoring and supervision.

Suggestions & Conclusion

4.1 The most important observation of the study is multiple memberships of poor women who join both SHGs and Bandhan groups. The single most important reason that these multiple members gave was inadequate loan from banks. Looking at the per SHG loan disbursement of Rs21000 and just 24% of SHGs getting second linkage, the credit needs of all the SHG members are not fulfilled and they are drawn towards Bandhan programme on the first opportunity. Secondly, by being the members of SHGs women develop confidence and articulation that help them pass the appraisal test of Bandhan. In fact, it is the better service being provided by MFIs like Bandhan that weighs heavily on the side of the poor women to join them. The better services are in terms of door step collection of recovery, having to deal with the institution in a structured way every week etc. On the face of it, there is nothing wrong in a poor woman accessing two sources of credit. However, from planners' perspective it is an avoidable duplication. When banks and MFIs are striving to achieve the same goals and magnitude of goal is huge, it would be appropriate to have a synergy in the efforts of banks and MFIs. This is all the more significant now that banks have also entered into financing MFIs.

4.2 Another interesting aspect is that most banks did not see Bandhan or other MFIs in the district (SKS Microfin has started its operation in the district) as their competitors. They were rather unaware of the magnitude of Bandhan's presence. Some of them had a vague idea that it was doing money lending. Not knowing that Bandhan had 44 branches in the district with a Divisional Managers, four regional Managers, 44 Branch Managers and more than 200 Credit Officers who deliver loans to their Group members in a very professional and systematic way adopted from ASA, Bangladesh. Most of the bankers see competition coming from new generation private banks but seem to be unaware of this competition in their backyard. The growth of Bandhan in terms of its outreach and outstanding portfolio are the two most important indicators of their ability to provide microfinance in sustainable manner – the Operating Self Sufficiency of Bandhan is 149%.

4.3 The outreach of both the institutions – Banks and MFIs has to still increase if all the BPL households are to be covered. With 46.01% of families in the district identified as BPL, more than 2 lakh households have to be provided access to credit. Both the banks and MFIs put together the outreach is just around 50%. But, in SHGs linked by banks the real access to credit is only to about 31% of members; the effective access is therefore only about 30%. Thus essentially, Banks and MFIs have to work together to ensure that all poor are able to access credit.

Based on the observations and interaction with various stakeholders, the following suggestions are being made to increase the outreach and efficacy of microfinance programme.

Suggestion Related to Banks

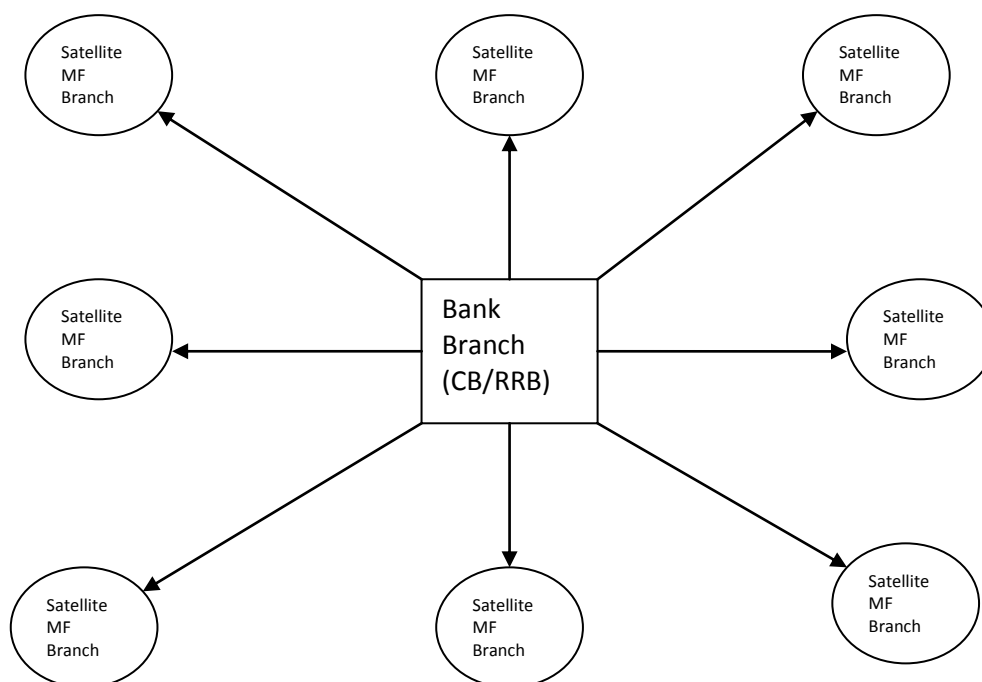
4.4 The fast growth of Bandhan can be ascribed to the professional approach adopted by it based on ASA, Bangladesh with cost effective human resource management and a branch structure which helps it monitor the clients regularly. A typical branch of Bandhan has one Branch Manager and five Credit officers who manage 2500 clients (about 100 groups). Once the number of clients crosses 2500, a new branch is opened. Such an arrangement helps them do effective monitoring and follow up for loan recovery as also for meeting the credit needs of these 2500 clients after the first cycle of loan. Banks on the other hand take up microfinance to SHGs as one of the many activities and there are no exclusive staff in any branch to deal with SHGs. This is the reasons that SHGs do not recall participation of any bank official in their group meetings. While some bank officers out of their personal motivation have been involved even in formation of SHGs - and many such bank officials are remembered fondly by members of SHGs. But, their transfers unsettle all the work done by them in case the successor is not so motivated and interested in promoting and nurturing SHGs. For taking SHG movement forward, specially in areas like Coochbehar with low presence of good SHPI-NGOs, banks will have to own the linkage programme. Currently, NGOs are expected to provided hand holding support to SHGs for six months after credit linkage with banks. Most SHGs are left to fend for themselves after this period and in the absence of a continuous relationship with NGO or bank they seem to show signs of disintegration. Members of such groups are quick to join other microcredit programmes, if there is a possibility.

4.5 The following two approaches are suggested for increasing the outreach of banks:

a) Exclusive Microfinance Satellite Branches : It is established beyond doubt that micro credit requires efficient supervision and follow up. Bandhan's case reinforces this. The predominant SHG-Bank Linkage model which has NGO as SHPI and bank as microcredit provider is good enough for the first linkage. For the second and subsequent linkages there has to be a dedicated staff appraising the credit needs of SHGs or their individual members as also for supervision of the credit. The World bank assisted Velugu/Indira Kranthi Patham programme implemented by the Govt of AP is a case in point where a dedicated staff structure at block and village level has provided continuous support to the SHGs and helped them evolve and stabilise the village/block level federations. For replication of 'Andhra Model' the primary requirement is political support which the SHG programme has received form two successive Chief Ministers. Such support can not be guaranteed in all other states.

It is, therefore, suggested that on the lines of the 'Microfinance Window' of the Rural Banks in the Philippines, the rural branches of commercial banks and RRBs can have exclusive microfinance branches in a hub and spoke model. These microfinance branches have to be low cost branches based on 'Bandhan Model' with exclusive 'Microfinance Staff' recruited for these branches.

Fig 4.1 : Satellite Microfinance Branches



4.6 Each satellite branch should be able to promote and link 200 SHGs covering on an average 2500 members. Each branch can be manned by a 5 Facilitators and One Team Leader. In the changed scenario, banks can effectively manage to keep these Microfinance Branches low cost branches by local recruitment and less personnel costs. The costs can be further reduced by using smart card and mobile technology for disbursements and collections. Such an arrangement will have following advantages:

- ◆ SHG-Bank Linkage will be seen by banks as a business rather than a social responsibilities
- ◆ The dedicated satellite branch network with dedicated staff will be able to increase the outreach as also the depth of microfinance services.
- ◆ Various savings and insurance products can be channelised through these satellite branches
- ◆ Such an arrangement will help in the growth of microfinance market.

b) Bank Branches as Wholesalers: Currently many banks are financing MFIs. This is being done at the corporate office level of Banks. many of the branch/district level staff are not even aware that an MFI has been financed by their bank. Since bank branches are not able to nurture and monitor SHGs because of various constraints and NGOs, in may cases, stop nurturing SHGs beyond a point, it is suggested that bank branches may finance local NGO who can then on lend to SHGs. Such an arrangement is already permission under RBI/NABARD guidelines but has not been adopted by most NGOs because of their inability to bear credit risk.

Suggestion Related to MFIs

4.7 The biggest criticism of MFIs is the high rate of interest being charged by them. While most of them try to defend it by comparing it with the rates of interest being charged by informal moneylenders, the crucial issue remains that poor clients flock to MFIs because they find their services more friendly than banks. In plain word it is availability versus cost. In order to achieve financial inclusion in true sense a two pronged strategy will have to be adopted by policy makers and organisations like NABARD. On the one hand, Banks have to be motivated and supported to take up microfinance as a business as suggested in the previous paragraphs. Simultaneously, the MFIs which have been functioning well and are carrying out their operations in a transparent manner and are willing to supervision by organisations

like NABARD/SIDBI should be provided loan funds at lower rate, preferable at the rates of refinance, so that they are able to reduce their financial costs.

Conclusion

4.8 The comparison of Bandhan with the operations of Banks in terms of the outreach and customer preference has brought out the following issues:

- ◆ Is multiple membership of poor borrowers a matter of choice or a reflection of their desperation?
- ◆ While Bandhan takes its job of microfinance seriously, banks still continue to treat it as social responsibility.
- ◆ Given a chance, most Bandhan clients express their eagerness to deal with banks provided banks were as accessible as Bandhan

In short, the poor still have more faith in the banks; if only banks could respond.

And, for banks to respond, it is suggested that they may take up microfinance as a business by adopting a low cost model of satellite microfinance branches based on the Bandhan Model.

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