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# Access to Finance in Andhra Pradesh

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## Glossary

Term	Meaning
<b>AIDIS</b>	All India Debt and Investment Survey, a decennial survey conducted by the National Sample Survey Organization to gather quantitative data on debt, assets and expenditures of households throughout India.
<b>Chit Fund</b>	A revolving credit fund in which members contribute a predetermined amount at specified intervals and auction the pool regularly.
<b>DCCB</b>	District Central Co-operative Bank, one level of the short term cooperative credit structure
<b>DWCRA</b>	Development of Women and Children in Rural Areas Program, a program launched in 1982 to promote the wellbeing of women through income-generating activities. A key feature of DWCRA was the formation of groups, through which members would receive a stipend and revolving fund to undertake group economic activities.
<b>JLG</b>	Joint Liability Group, JLGs are generally promoted by private MFIs and consist of fewer members than SHGs (usually 4-5). Members are responsible for repayments of their peers in case of default.
<b>KYC</b>	Know Your Customer norms, due diligence guidelines which must be followed by banks to identify account holders.
<b>MFI</b>	Microfinance Institution, any private organization that provides microfinance loans. MFIs can take many legal forms, including non-profit societies and for-profit NBFCs.
<b>NABARD</b>	National Bank for Agriculture and Rural Development, the apex development bank responsible for regulating credit flow and promoting integrated development in rural areas. Since 1992, NABARD has promoted India's largest microfinance program, the SHG Bank Linkage Programme.
<b>NBFC</b>	Non-Banking Financial Company, a type of for-profit company which may offer financial products to customers and which is regulated by the RBI. Most of India's largest MFIs are registered as NBFCs.

<b>No-frills account</b>	A basic savings account that the RBI encouraged banks to provide to unbanked customers with 0 or minimal balance as part of its financial inclusion drive.
<b>NREGA</b>	National Rural Employment Guarantee Act, a centrally-sponsored government scheme enacted in 2005 that ensures a minimum of 100 days of unskilled, minimum-wage employment to all rural households.
<b>PPI</b>	Progress Out of Poverty Index, a simple proxy measure of the likelihood that a household is beneath a given poverty line. See Appendix E for a detailed explanation.
<b>RBI</b>	Reserve Bank of India, the central bank of India that controls monetary policy.
<b>RRB</b>	Regional Rural Bank. RRBs were established in 1972 to provide credit to weaker sections of society of rural areas, such as small and marginal farmers, artisans, and agricultural labourers. RRBs are regulated by NABARD.
<b>SBLP</b>	SHG-Bank Linkage Programme, a program sponsored by NABARD to promote and provide credit to SHGs nationally. Through SBLP, banks provide SHGs with credit after an initial period of saving and internal lending.
<b>SHG</b>	Self Help Group, one of the two major microfinance models in India. SHGs generally consist of 10-20 members that save regularly and extend internal loans through group savings. Groups may also be sanctioned external loans from banks, federations, or NGOs.
<b>SGSY</b>	Swaranjayanti Gram Swarojgar Yojana, a centrally-sponsored program launched in 1999 to support poor families through the provision of subsidies and bank credit distributed via SHGs.

## Executive Summary

In this report, we present results from the first ever household survey on access to finance in India which includes information on microfinance, is representative of an entire state's (Andhra Pradesh) rural population, and for which the data is publicly available". The key findings from the survey and analysis are as follows:

1. The proportion of households with a savings account is much higher than previously estimated. According to the A2F survey conducted by the authors, 78.6% of rural AP households have access to a savings account. A previous survey conducted by the World Bank and NCAER in 2003 found that in both AP and UP the proportion of households with a savings account was only 41%.
2. Only a small proportion of savings accounts (14.3%) were opened for the purpose of savings. Many accounts were instead opened for the purpose of receiving government benefits or to help in receiving a loan.
3. Perhaps because they were not opened for the purpose of savings, a large share of savings accounts (approximately 41%) appear to be completely dormant or used only to receive government benefits. Yet even after excluding those accounts which appear to be dormant, the proportion of households with a savings account remains relatively high at 60.6%.
4. The proportion of rural households with a loan from any source is much higher than previously estimated. According to the A2F survey, 93.1% of rural AP households have a loan outstanding. The All India Debt and Investment Survey, conducted in 2003 by the NSSO, found that only 33.2% of rural AP households had a loan outstanding.
5. Despite concerns of over-borrowing from MFIs, only a small share of rural households (11%) had a loan outstanding from an MFI.
6. Roughly three quarters (72%) of rural households had a member who belonged to an SHG. Roughly half (53.5%) of rural households have a loan outstanding to an SHG.

7. Indebtedness to moneylenders remains relatively high. (An estimated 17% of rural households have a loan outstanding from a moneylender.) Yet interest rates charged by moneylenders were, in most cases, only slightly higher than those charged by MFIs.
8. Multiple borrowing is very common. (An estimated 83.7% of rural households had more than one loan outstanding.) Yet very few households had more than one loan from an MFI.

## Introduction

Access to finance allows the poor to make investments to increase their income, better smooth consumption, and protect against shocks such as bad weather or illness.<sup>1</sup> The importance of access to finance for reducing poverty and allowing the poor to lead more fulfilling lives has long been recognized by policymakers in India. Indeed, many of the country's key banking policies since independence – from the creation of the cooperative banking sector to the nationalization of private sector banks in 1969 and 1980– were initiated, among others, with the aim of increasing access to appropriate financial products. Recently, the government and central bank have set upon the task of increasing financial inclusion with renewed zeal. The central government has formed two high level committees (the Committee for Financial Inclusion and the Committee for Financial Sector Reforms) with mandates to investigate what can be done to increase financial inclusion<sup>2</sup>; and the RBI has pushed banks to make basic “no frills” accounts available to low income households<sup>3</sup>, allowed banks to reach out to customers through agents (or “business correspondents”)<sup>4</sup>, and relaxed restrictions on placement of new ATMs. In addition, with the rise of microfinance, a large number of non-bank organizations now seek to increase the poor's access to financial services.

Yet despite (and in part because of) this focus on financial inclusion<sup>5</sup>, many questions remain unanswered when it comes to the state of

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<sup>1</sup> For a general discussion on the importance of access to finance see Armendáriz and Morduch (2005) and Beck and Demirgüç-Kunt (2008). For an insightful investigation into the specific financial needs of the poor see Collins et al (2009).

<sup>2</sup> The reports of these committees are now publicly available. See references section for links to the reports.

<sup>3</sup> For more information on the RBI's push to make “no frills” accounts available to low income households see Ramji (2009) and Thyagarajan and Venkateshan (2008).

<sup>4</sup> For more information on the RBI's business correspondent model see Kobishyn et al (2009).

<sup>5</sup> We use the term “financial inclusion” to mean convenient and affordable access to those financial products needed by a household. As this report seeks only to describe

financial inclusion in the country. While several excellent surveys have been conducted in the past<sup>6</sup>, increases in financial access and a profusion of new types of financial service providers have rendered much of the information gathered by these surveys out of date. Currently, we do not have accurate estimates of the number of people reached by several types of financial service providers (in particular, microfinance institutions (MFIs)). We do not know how the demographic and economic characteristics of the clients of different types of financial service providers (and those not reached by any formal financial service provider at all) differ. Nor do we know the reasons for or the extent of multiple borrowing. This lack of knowledge of the current state of financial inclusion hampers efforts to craft appropriate policies to further increase financial inclusion, makes it more difficult for financial institutions to choose appropriate expansion locations, and creates the risk that we are ignoring significant distress-induced multiple borrowing.

In this report, we present preliminary findings from a detailed survey of access to finance conducted in rural areas of Andhra Pradesh, the state in which microfinance has achieved its greatest success to date in India. The survey on which the results contained in this report are based is, to the authors' knowledge, the first survey which includes detailed information on microfinance, which is representative of an entire state's rural population, and for which the data is publicly available<sup>7</sup>.

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the current situation with regard to access to finance rather than to make statements as to what should be the situation with regard to access to finance, a more precise definition of the term is not necessary.

<sup>6</sup> The National Sample Survey Organisation conducts a nationwide survey of access to several types of financial services (the All India Debt and Investment Survey or AIDIS) on a decadal basis which is available for a nominal fee. The AIDIS was last conducted in 2003 and does not contain information related to microfinance borrowings though. A private company, IIMS Dataworks, conducted a nationwide survey of access to several financial services in 2007. The survey, while excellent, does not contain detailed questions related to microfinance.

<sup>7</sup> Due to difficulties in surveying in one area of Andhra Pradesh, the survey results are representative of the entire rural population excluding Krishna district in which surveying proved impossible. See appendix A for more details on the sampling methodology and the reasons for this exclusion.

This report is organized as follows. We first provide some context for the results by describing the history of microfinance in Andhra Pradesh and the current landscape of providers of financial services to the poor. The subsequent sections contain the main findings from the survey. In the appendices, we provide an overview the methodology used to conduct the survey and describe how to access and use the data.

## **Microfinance in Andhra Pradesh**

Andhra Pradesh has been labeled the “Mecca of microfinance” in India and with good reason. According to the best estimates available, penetration rates of microfinance in Andhra Pradesh are far higher than in any other state in India;<sup>8</sup> several of India’s largest MFIs including SKS, Spandana, BASIX and Share, are based in Andhra Pradesh and began operations in the state; and the state is home to India’s largest state-led microfinance initiative – the Velugu program.

The origins of microfinance in Andhra Pradesh can be traced back to government led attempts to form “Self Help Groups (SHGs),” or groups of 12 to 20 (mostly) women which collect regular savings from members and make loans internally to members. The first such attempt to form SHGs was through the Development of Women and Children in Rural Areas (DWCRA) program (a sub-component of the centrally-sponsored Integrated Rural Development Program) in 1982. Nationally, 2.73 lakh groups were formed under the program until its absorption into the larger Swarnajayanti Gram Swarojgar Yojana (SGSY) program in 1999.<sup>9</sup> Formation of SHGs at a large scale did not take off until the creation of the SHG-Bank Linkage Program (SBLP) in 1992 though. Under the program, NABARD (India’s apex agricultural development bank) provided

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<sup>8</sup> Making comparisons of microfinance penetration between areas is difficult due to the lack of comprehensive information on the outreach of private MFIs. Yet based on outreach figures from the largest MFIs and official statistics on SHGs, microfinance penetration in AP is far higher than in other parts of the country. (See the Centre for Micro Finance’s Map of Microfinance, located at <http://ifmr.ac.in/map>, for more information.)

<sup>9</sup> Department of Rural Employment and Poverty Alleviation. “Annual Report: 1998-1999.” Ministry of Rural Development, New Delhi: 1999.

a set of incentives for banks to lend to SHGs which adhere to certain guidelines, such as collecting regular savings from group members.<sup>10</sup>

In 2000, SHG promotion in AP was massively expanded with the launch of the 5-year Andhra Pradesh District Poverty Initiatives Project (APDPIP). The program, known locally as Velugu, meaning “light” in Telugu, and modeled after an earlier program led by UNDP<sup>11</sup>, marked a watershed for microfinance in the state. Formation of SHGs increased immensely with the program. As a result, close to half of all bank-linked SHGs were originally located in Andhra Pradesh (see graphs below).

As the SHG movement was being scaled up in the late 1990s, private MFIs also began entering the state. In 1996, Vijay Mahajan created the MFI BASIX, with funding from the Ford Foundation, the Swiss Agency for Development and Cooperation and the Sri Ratan Tata Trust.<sup>12</sup> BASIX's for profit model and reliance on loans and equity rather than grants for financing marked a first not just for AP, but for India as well.<sup>13</sup> SHARE, which had been operating as a non-profit society since 1989 in Guntur and Kurnool districts, followed in BASIX's footsteps, registering as an NBFC in 2000. Spandana, which had begun in 1998 as a non-profit offering microfinance under the SHG model in Guntur district of AP, incorporated itself as an NBFC in 2003,<sup>14</sup> while SKS waited until 2005 to go private.

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<sup>10</sup> Fernandez, Aloysius P. “History and Spread of the Self-Help Affinity Movement in India: the Role Played by IFAD.” Occasional Paper Series, IFAD, July 2007.  
< <http://www.ifad.org/operations/projects/regions/pi/paper/3.pdf>>

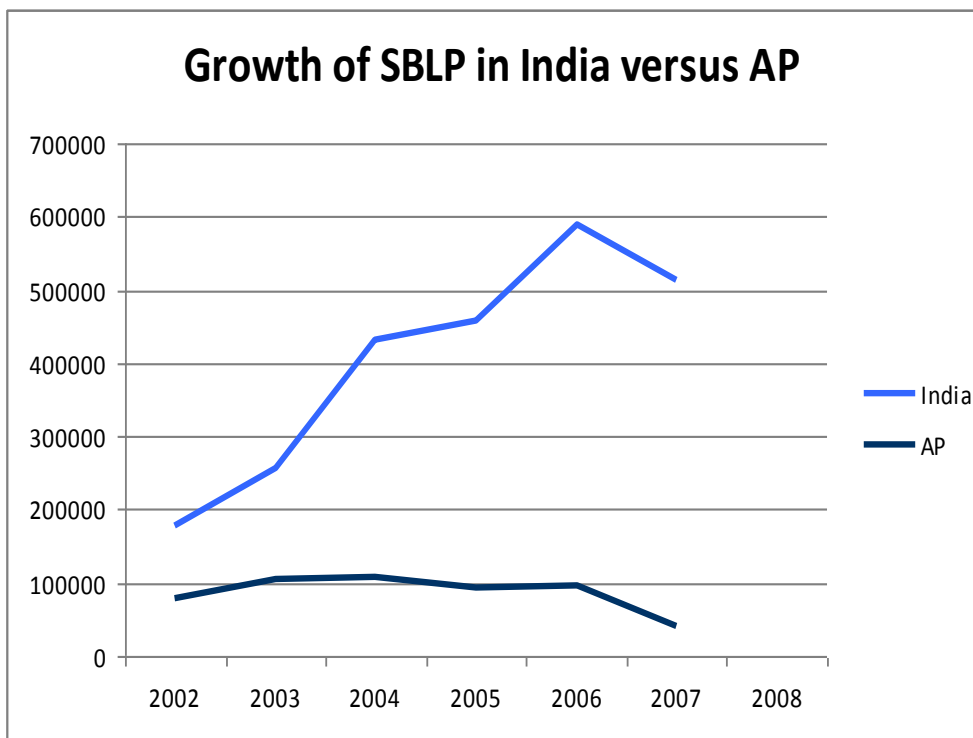
<sup>11</sup> Deininger, Klaus and Yanyan Liu. “Economic and Social Impacts of Self-Help Groups in India.” Policy Research Working Paper 4884, World Bank, March 2009.

<sup>12</sup> Sriram, MS. “Commercialisation of Microfinance in India: A Discussion on the Emperor’s Apparel.” Working Paper No 2010-03-04, Indian Institute of Management, Ahmedabad, March 2010.

<sup>13</sup> Interview with Vijay Mahajan, Access Development Services, Contribution to the Sector Award, 2009.  
<[http://www.microfinanceindia.org/download\\_reports/awards\\_brochure\\_2009\\_mahajan.pdf](http://www.microfinanceindia.org/download_reports/awards_brochure_2009_mahajan.pdf)>

<sup>14</sup> Sriram, MS. “Expanding Financial Services Access for the Poor: The Transformation of SPANDANA.” Indian Institute of Management, Ahmedabad, April 2005.  
< <http://www.iimahd.ernet.in/~mssriram/spandana-wp.pdf>>

**Figure 1: Growth of SBLP in India versus AP**



**Source: NABARD**

Note: The India numbers exclude groups linked in AP. In addition, these numbers only reflect new group linkages provided by banks refinanced by NABARD—in reality, the number of SHGs in India and AP will be much higher, including SHGs that have instead received funding from NGOs, banks that did not require refinancing, SHGs and SHG federations that extended loans directly, and groups that have received repeat linkages.

Since 2000, outreach of private MFIs in AP has grown at a frenetic pace, with total numbers of borrowers more than doubling each year. In 2005, several of the fastest growing MFIs in the world were based in Andhra Pradesh.<sup>15</sup> This explosive growth has at times led to tension between MFIs, those they serve, and government officials. In 2006, Andhra Pradesh was the site of the first large-scale confrontation between microfinance borrowers and MFIs in the country. Borrowers in two districts of Eastern Andhra Pradesh (Krishna and Guntur) protested against what they claimed were exorbitant interest rates and unfair

<sup>15</sup> [www.themix.org](http://www.themix.org)

business practices. Local bureaucrats quickly intervened, shuttering several offices of the MFIs and publicly stating that borrowers need not repay loans. While the crisis was eventually resolved and an agreement was reached by the MFIs and local government officials, the MFIs in the area suffered a huge write-off as a result of the crisis.<sup>16</sup> Yet despite the crisis, the microfinance sector in Andhra Pradesh continues to grow at a rapid pace.

## **Catalogue of Financial Services Providers**

The poor in India access financial services from a variety of different providers. We briefly describe the most important of the entities currently providing financial services to the poor in India below – how they are regulated (if at all), the types of products they offer, and their overall size and market penetration. We have loosely categorized these entities into the groups “formal”, “semi-formal”, and “informal” below based on whether the entities are (typically) regulated by the RBI, regulated by some other agency, or not regulated at all. In many cases though, the distinction between these categories is blurred. (For example, a few microfinance institutions such as SEWA Bank and BASIX are registered banks. Some chit funds and even a few moneylenders are registered as formal institutions. And the cooperative banking sector and regional rural banks are directly supervised by the National Bank for Agricultural and Rural Development (NABARD) rather than the RBI.)

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<sup>16</sup> The AP crisis is often portrayed as either the natural outcome of the immoral behavior of overly profit-seeking MFIs or, alternatively, as the product of bureaucrat’s jealousy over MFIs’ success compared to the state-led SHG program. The reality is much more subtle and complex. For an excellent account of the crisis, see Prabhu Ghate’s analysis in the Microfinance India State of the Sector Report, 2006. < [http://www.microfinanceindia.org/download\\_reports/state\\_of\\_the\\_sector\\_06.pdf](http://www.microfinanceindia.org/download_reports/state_of_the_sector_06.pdf)>

**Table 1: Formal Financial Service Providers in India**

<b>Entity</b>	<b>Description</b>	<b>Examples of Products Offered</b>	<b>Examples</b>	<b>Penetration<sup>17</sup></b>
Public sector commercial banks	Commercial banks in which the government owns a majority stake.	Various	- State Bank of India - State Bank of Hyderabad - State Bank of India	- 27 banks - 55,921 total branches
Private sector commercial banks	Commercial banks in which the government does not have a majority stake.	Various	- ICICI - Axis Bank - HDFC	- 22 banks - 8,965 total branches
Regional Rural Banks (RRBs)	Special type of commercial bank with an explicit mandate to focus on rural operations. All RRBs are owned in part by the central government, in part by the government of the state in which they operate, and in part by a single commercial bank. RRBs may only conduct operations in a single state and are supervised by NABARD.	Various, with focus on loans for agricultural purposes	- Andhra Pradesh Grameena Vikas Bank - Andhra Pragathi Grameena Bank	- 86 banks - 15,144 total branches
District Central Cooperative Banks (DCCBs)	Second tier in the rural cooperative banking structure.  In addition to serving as a source of financing for	DCCBs' only product directly offered to customers		-371 banks (March 2008)

<sup>17</sup> All statistics taken from the Reserve Bank of India's "Report on Trend and Progress of Banking in India 2008-2009" unless otherwise specified.

Entity	Description	Examples of Products Offered	Examples	Penetration <sup>17</sup>
	PACs (see below) by borrowing from State Cooperative Banks and on-lending to PACs, DCCBs also directly offer one product, Kisan Credit Cards, to farmers. DCCBs are supervised by NABARD.	is the <b>Kisan Credit Card</b> , a line of credit which allows farmers to purchase agricultural inputs, such as seeds and fertilizers, in a timely manner.		
Primary Agricultural Cooperative Societies (PACs)	Bottommost tier of the rural cooperative banking system. They primarily provide. PACs focus primarily on providing credit for agricultural purposes and are regulated by NABARD.	<b>- Crop loans</b>		<ul style="list-style-type: none"> <li>- 94,942 total (end March 2008)</li> <li>- Average of 7 villages covered by each PAC</li> <li>- 131 billion members (79 billion borrowers)</li> </ul>
Post office <sup>18</sup>	In addition to delivering mail, India Post offers a variety of financial services such as money transfers and recurring deposit accounts. India Post is regulated and supervised by the	<b>-Small Savings schemes</b> - basic, recurring, time deposit, monthly		<ul style="list-style-type: none"> <li>- 154,000 branches</li> <li>- 174 million savings accounts</li> <li>- Rs. 5.64 trillion outstanding</li> <li>- 21 million</li> </ul>

<sup>18</sup> India Post Annual Report, 2008-2009

Entity	Description	Examples of Products Offered	Examples	Penetration <sup>17</sup>
	Ministry of Finance rather than the RBI.	income, national savings certificate, etc. - <b>NREGA</b> wage disbursal - <b>Old-age pension</b> disbursal - <b>Money Transfer</b>		NREGA accounts (Dec 2008)
Insurance companies	Public and private insurance companies offer a variety of insurance products. Insurance companies are regulated and supervised by the Insurance Regulatory and Development Authority (IRDA).	- <b>Various insurance products</b> - health, life, accident, home, motor, travel - <b>Pension plans</b>	-Life Insurance Corporation of India -ICICI Prudential	
Central and state governments	In some instances, central and state government directly provide financial services to citizens.	- <b>Health insurance</b>	- <b>Rajiv Gandhi Aarogyasri Community Health Insurance</b> for BPL card holders	-As of January 2010, 27 lakh screenings have been conducted and 5 lakh treatments have been provided under the Rajiv Gandhi Aarogyasri health insurance program

Entity	Description	Examples of Products Offered	Examples	Penetration <sup>17</sup>
Deposit taking Non-Bank Finance Companies	In addition to formal banks and the post office, non-banking finance companies which satisfy certain regulatory requirements such as maintaining a 200 lakh net owned fund may accept deposits from the public.	- <b>Fixed deposits</b> minimum 12 months at a max interest rate of 12.5% - <b>Recurring deposits</b>	- Sahara - Peerless	- 314 such institutions as of January 2010 <sup>19</sup> - Of these, 8 are registered in AP

**Table 2: Semi-Formal Financial Service Providers in India<sup>20</sup>**

Entity	Description	Examples of Products Offered	Examples	Penetration
Microfinance Institutions (MFIs)	Private providers of microfinance loans. May take a variety of institutional forms, but the largest MFIs are typically registered as NBFCs and as such are regulated by the RBI.	- <b>Joint liability group loans</b> – Group loans in which all members of a group (typically 5 members in size) are jointly responsible for all group members' repayments. Tenure of loan is typically one year and repayments are most often weekly	- SKS - Spandana - Share	- Approximately 250 MFIs - 20 million clients in India (25%, or nearly 5 million in AP) - Rs. 117 million outstanding (2009) - Rs. 5200 average per capita outstanding

<sup>19</sup> Reserve Bank of India, "List of Deposit Taking Companies Cat 'A'"

<sup>20</sup> Statistics taken from "Microfinance India State of the Sector Report 2009" unless otherwise cited

Self Help Groups (SHGs)	Groups of 10-15 which borrow from (typically) a bank or (less commonly) other lender and lend internally to members. The SHG model of microfinance differs from the MFI model in that SHGs typically borrow from banks and lending decisions are made internally by the group itself. NABARD provides financial incentives to banks to support SHG lending.	- Various types of loans	NA	-2.8 million SHGs -Rs. 241.9 million outstanding (as of March 2009) -54.3 million clients in India (29%, or 1.58 billion in AP)
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**Table 3: Informal Financial Service Providers in India**

	Description	Examples of Products Offered	Examples	Penetration
Money-lenders	Any informal lender. There are a variety of types of moneylenders active in India – shopkeepers who lend in kind, crop traders who lend against purchase of harvest, landowners who lend to tenants, and jewelry merchants who lend against jewelry as collateral are just a few of the better known types of moneylenders	- Traditional cash loans - Agricultural input loans (direct provision of seeds, fertilizers, etc.)		
Chit funds	A type of revolving credit fund in which members contribute a pre-determined amount at	- Chit loan	- Shriram Chits	-As of November 2009, 100 chit funds are registered under

	Description	Examples of Products Offered	Examples	Penetration
	specified intervals and auction the entire amount each meeting to one member. <sup>21</sup> Large chit funds are typically formally registered while smaller chit funds often operate without any formal registration.			the Madras Chit Funds Act and another 70 under the 1982 Chit Funds Act <sup>22</sup>

## Saving

### **A large proportion of households hold a formal savings account.**

Over the past five years, the regulator and banks have engaged in several initiatives to increase access to savings accounts throughout the country. In 2005 the RBI instructed banks to make available basic “no frills” accounts with low or minimal balance requirements and usage fees. The RBI also relaxed the Know Your Customer (KYC) requirements on these accounts to make it easier for potential customers without formal documents to open an account.<sup>23</sup>

Yet despite mandating the availability of no frills accounts, many poor households continued to lack access to a formal savings account. To further drive take up of formal savings accounts, in 2006 the RBI launched a “100% financial inclusion drive” in which at least one district in

<sup>21</sup> An example may serve to make the concept clearer: 20 members join a “chittie” and agree to pool Rs. 200 monthly. Each month, an auction is held in which members bid for the pool. The highest bid will translate to a percentage deduction from the entire amount (example a bid of 20%). The winner will receive the pool minus the deduction amount (Rs. 8000), while the remaining members will receive an equal percentage of the deduction amount (Rs. 2000). This would continue for 20 months, and the final member would receive the entire pool without penalty of deduction.

<sup>22</sup> Department of Chit Funds. (2009). “List of Chit Fund Companies Working Under the Chit Funds Act, 1982.”

<sup>23</sup> Speech delivered by Smt. Usha Thorat, Deputy Governor, Reserve Bank of India at the HMT-DFID Financial Inclusion Conference 2007 on June 19, 2007. Transcript available at <http://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/78680.pdf>

each state was targeted for 100% financial inclusion.<sup>24</sup> Under the drive, banks were assigned responsibility for opening at least one basic account for each financially excluded household in a given area in each district selected for inclusion in the drive. Civil society and the media were engaged to create awareness of the program and to highlight the benefits of having a bank account to the poor.<sup>25</sup>

The state government has also played a major role in increasing access to formal savings accounts in Andhra Pradesh in recent years. Over the past three years, the state government has made a concerted effort to deliver all wages to participants in NREGA (a national workfare program) through a formal savings account (typically a post office account).<sup>26</sup> While the primary motivation for using formal savings accounts to deliver NREGA wages was to reduce corruption, the policy also had a substantial impact on access to savings accounts as many NREGA participants lacked a formal savings account prior to the policy.

Results from the survey show that the cumulative effect of these policies has been a large increase in the share of rural households with a formal savings account. Table 4 shows the penetration rate of formal savings accounts by bank type. Overall, a staggering 78% of rural households now have access to a formal savings account. While earlier estimates of the share of rural households in AP having access to a formal savings account are not available, a similar study by the World Bank and NCAER in 2003 found that only 41% of rural households in both AP and Uttar Pradesh had access to a savings account. (Basu and Srivastava, 2005) Further, this same study found that access to savings accounts was concentrated in the hands of the relatively well off: 70% of marginal farmers and landless labourers in rural AP and UP did not have a formal

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<sup>24</sup> While initially only one district in each state, selected by the State Level Bankers' Committees, was to be included in 100% financial inclusion drive later the drive was expanding to include many more districts. See Thyagarajan, S and Jayaram Venkatesan (2009).

<sup>25</sup> The following districts in AP have claimed to have achieved 100% financial inclusion under the drive: Srikakulam, Nizamabad, Rangareddy, Chittoor, Warangal, Kadapa, Nellore, Prakasam, Kurnool and Ananthapur. Out of these districts, three (Nizamabad, Kadapa and Prakasam) were included in this survey.

<sup>26</sup> The Ministry of Rural Development, the agency overseeing NREGA, mandated in 2008 that all NREGA wages be paid through a formal account. The extent to which states have adhered to this mandate has varied greatly though.

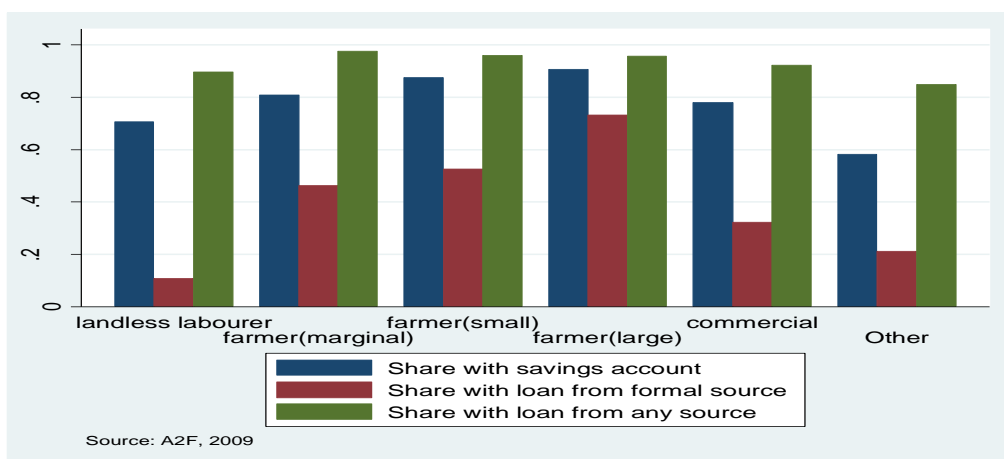
savings account. Our survey finds that in rural AP at the time of the survey over 70% of landless labourers and marginal farmers *did* have access to a savings account.<sup>27</sup>

**Table 4: Share of Rural AP Households with a Savings Account by Bank Type**

	Share of HHs with Savings Account	Share of HHs with Savings Account (excluding 0 and Rs 50 balance accts)*
Private Sector Bank	1.3%	1.0%
Public Sector Bank	40.9%	36.0%
Regional Rural Bank	14.1%	13.1%
Cooperative Bank	13.6%	11.7%
Post Office	42.1%	11.4%
<i>Any of the above</i>	<i>78.6%</i>	<i>60.6%</i>

\*Source: A2F, 2009

**Figure 2: Financial Inclusion by Occupational Category**

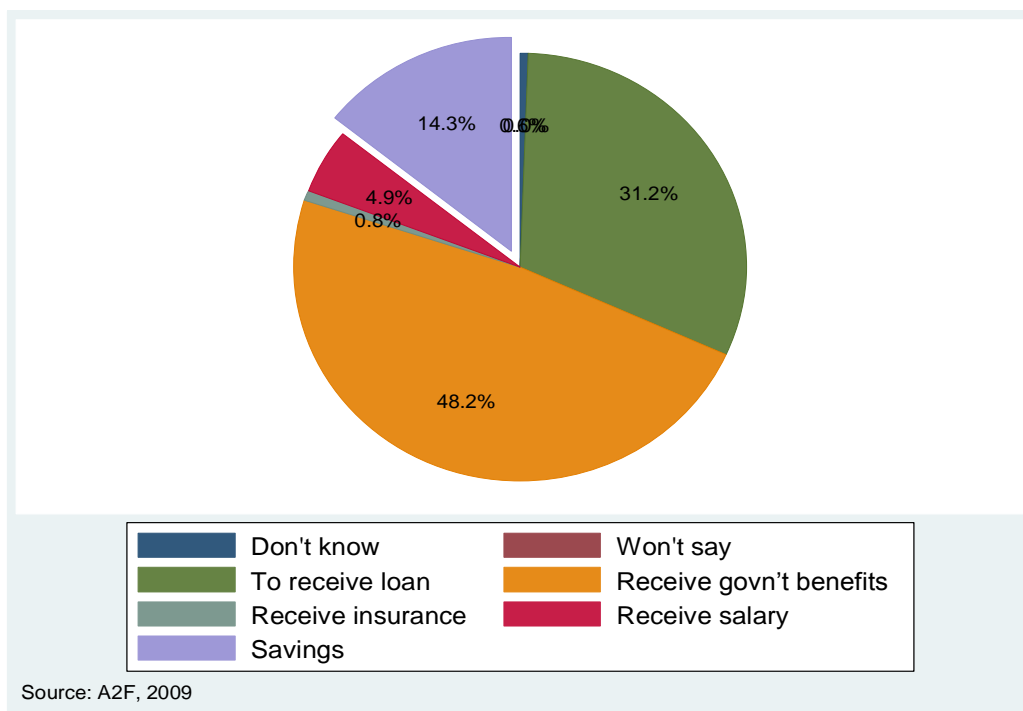


<sup>27</sup> An explanation of how households were assigned occupational categories may be found in Appendix C. Please note that the methodology for assigning occupational categories used in this report differs slightly from that used by Basu and Srivastava (2005).

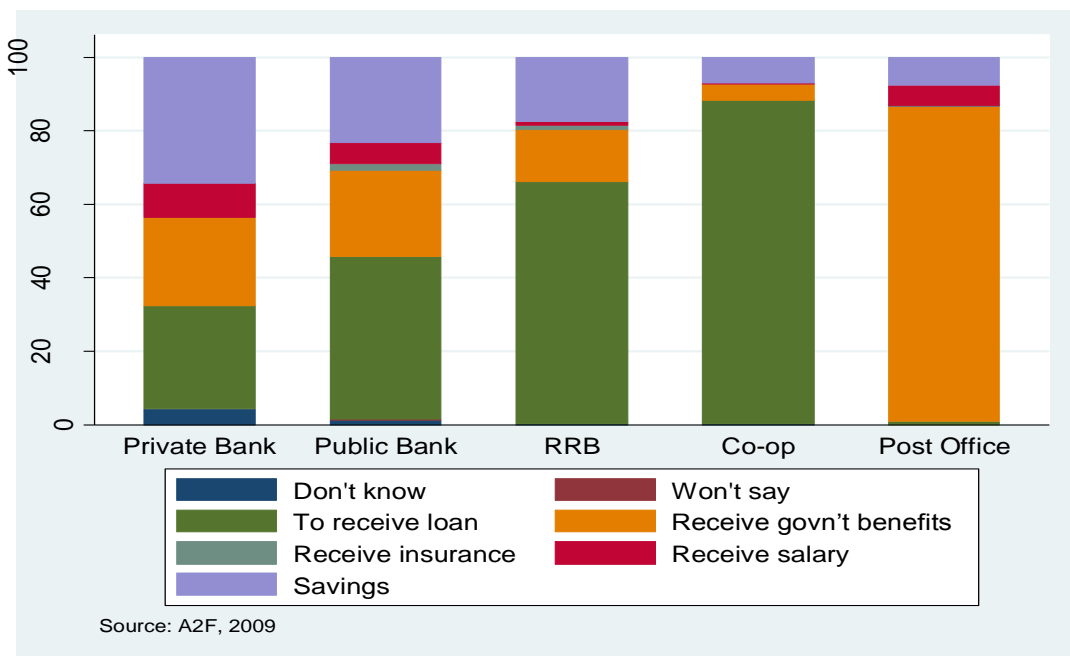
**...yet a large portion of savings accounts are not used for saving.**

While the share of rural households with access to a savings account is high, only a small minority of these accounts (14.3%) were opened for the purpose of savings. The vast majority of accounts (79.4%) were opened either to receive government benefits or to increase chances of receiving a loan. This is especially so in the case of post office savings accounts, the vast majority of which were opened for the purpose of receiving government benefits, and savings accounts at co-operative banks, the vast majority of which were opened for the purpose of obtaining a loan.

**Figure 3: Stated Reasons for Opening Savings Account**



**Figure 4: Stated Reasons for Opening Savings Account by Bank Type**



In light of the policy initiatives described above, this is hardly surprising. Most post office savings accounts were likely opened for the express purpose of receiving NREGA wages while many of the bank accounts were likely opened as part of the 100% financial inclusion drive and not due to a customer directly requesting an account. Nor do these findings necessarily imply that the holders of these accounts do not use the accounts for savings. An account opened for a purpose other than savings may still be used for saving at a later date. Indeed, instilling savings behaviour in beneficiaries is a much cited reason for delivering government benefits through formal savings accounts.<sup>28</sup>

Yet a closer look at savings account balances reveals that a large share of the savings accounts held by rural households were dormant: 13.1%

<sup>28</sup> See, for example, comments made by PC Jaffer, former district program coordinator for NREGA in Gulbarga District of Karnataka, available at <http://www.solutionexchange-un.net.in/NREGA/documents/NREGA-Gulbarg.pdf>

have 0 balance and 28.9% have Rs. 50 balance.<sup>29</sup> Column 3 of table 4 shows the share of households which hold a savings account with a balance not equal to 0 or Rs. 50 from each type of bank, the post office, and overall. While the overall rate of access to a formal savings account, at 60.6%, is still very high when these dormant accounts are excluded, it is significantly lower than the unadjusted figure which includes dormant accounts.

**Cooperative banks perform relatively well in reaching out to marginal farmers while public banks and the post office perform well in reaching out to landless labourers.**

Figures 5 and 6 display the proportion of clients from each broad occupational category by bank type.<sup>30</sup> Figures 7 and 8 display the average score on the progress out of poverty index of clients of each bank type.<sup>31</sup>

The graphs reveal that cooperative banks, true to their mandate, have a disproportionately large share of marginal farmers among their clients compared to other types of banks. Likewise, public sector banks and the post office count a relatively large share of landless labourers among account holders. This finding does not change when zero balance accounts are excluded from the analysis indicating that the policy of opening post office accounts for NREGA workers is not the primary driver of these results.

Unsurprisingly, unbanked households tend to be poorer than those with accounts and clients of private banks tend to be richer than clients of other banks regardless of whether zero balance accounts are included.

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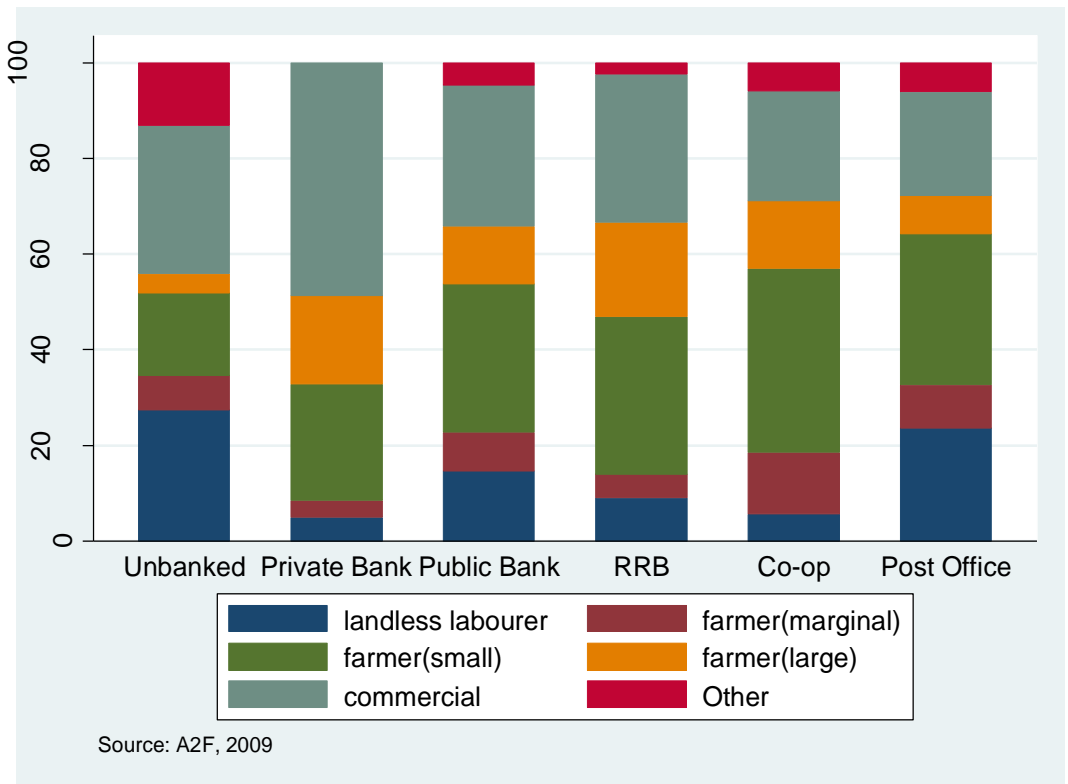
<sup>29</sup> “No frills” accounts commonly have either zero balance or a Rs. 50 minimum balance requirement.

<sup>30</sup> For an explanation of how occupational categories of households are determined please see Appendix C.

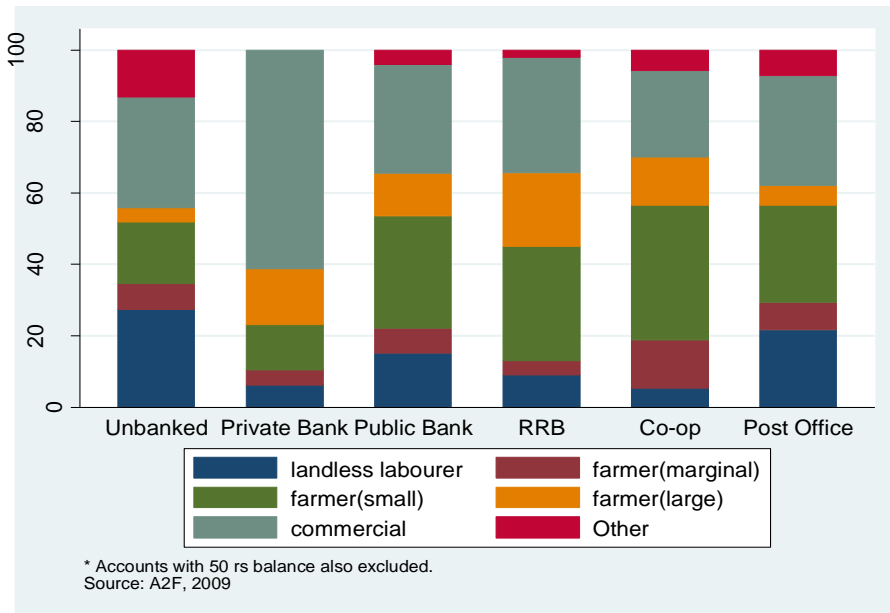
<sup>31</sup> The progress out of poverty index (PPI) is a simple poverty scorecard developed by the Grameen Foundation. A household’s score on the PPI may be used to determine the likelihood that the household falls below various poverty lines with lower scores corresponding to a higher likelihood that the household falls below a poverty line. PPI scores may be averaged across households to arrive at a poverty rate for the entire group. For more information on the progress out of poverty index see [www.progressoutofpoverty.org](http://www.progressoutofpoverty.org).

(This is demonstrated visually from the box plots below. In addition, the mean PPI of unbanked households and the mean PPI of banked households are statistically significantly different at the 1% level regardless of whether zero balance accounts are included based on a two way t-test. The mean PPI of households with an account at a private bank and the mean PPI of households without an account at a private bank are statistically significantly different at the 5% level regardless of whether zero balance accounts are included based on a two-way t-test.)

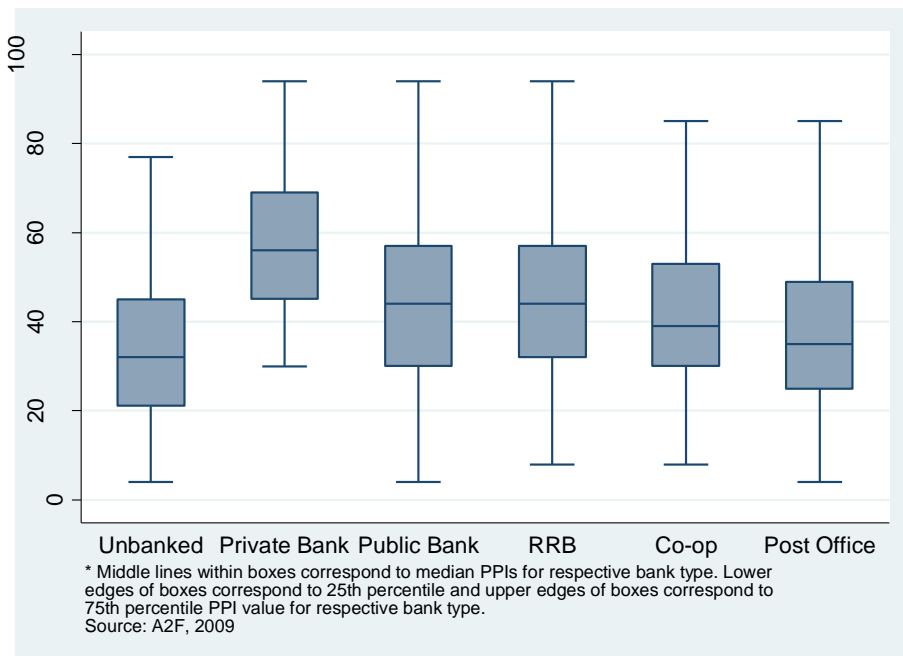
**Figure 5: Client Profile by Bank Type**



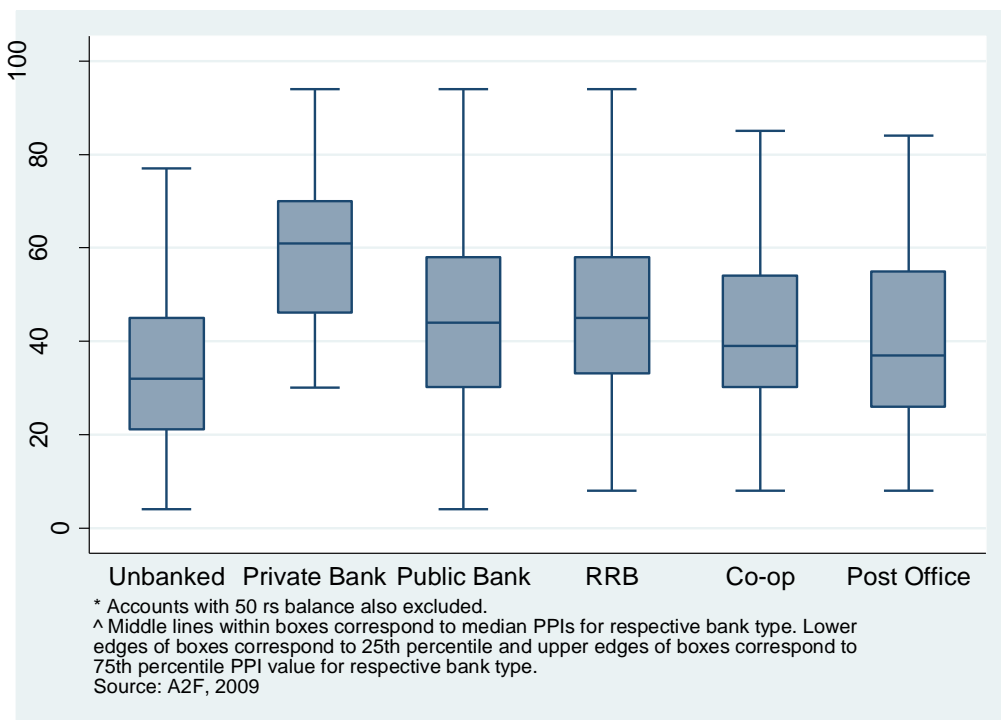
**Figure 6: Client Profile by Bank Type (excluding 0 balance accounts)\***



**Figure 7: PPI of Account Holders by Bank Type\***



**Figure 8: PPI of Account Holders by Bank Type (excluding 0 balance accounts)\*^**



**Households without a savings account cite insufficient savings, lack of awareness of savings products, and lack of need as the primary reasons for not opening an account.**

When asked why they did not have a savings account, the most common reasons given by unbanked households was that they did not have enough savings for an account, didn't understand savings products, didn't need a savings account, or didn't have the proper documentation to open a savings account. Surprisingly, very few unbanked households cited distance to the bank branch, trustworthiness of the bank, or the attitude of bank employees as reasons for not opening an account.

**Table 5: Stated Reasons for Not Availing Savings Account among Financially Excluded**

<b>Reason</b>	<b>Share Households Citing Reason</b>
No or not enough savings for bank account	37.9%
Have no idea about banks or bank products	27.3%
Don't want/need	24.1%
Don't have proper documentation	14.3%
Fees/expenses	4.7%
Applied but rejected	3.1%
Procedures/application too difficult to understand	2.0%
Save through other means	1.5%
Not enough land	1.3%
Takes too much time	1.0%
Banks not trustworthy	1.0%
Branch officials not friendly/courteous	0.6%
Lack of guarantor	0.6%
Moving	0.5%
Branch too far	0.3%
Will apply	0.2%
Loan repaid already	0.2%

Source: A2F, 2009

### **Many unbanked household own mobile phones**

Over half (51.1%) of rural households have mobile phones. In addition, 36.2% of households with no savings account own at least one mobile phone. (If 0 and Rs. 50 balance accounts are excluded, this figure rises to 36.4%.) This suggests that mobile banking may be an effective method of providing the unbanked with financial services.

## Borrowing

**Table 6: Percentage of Rural AP Households Indebted by Source**

Major Source	Sub-source	Estimated Share of households with loan from source based on A2F	Estimated Share of households with loan from source based on AIDIS 2003	Estimated Share of households with loan from source based on AIDIS 1991
<b>Formal</b>				
	Private	0.5%	Not Available	Not Available
	Public	19.6%	Not Available	Not Available
	RRB	8.6%	Not Available	Not Available
	Coop	9.6%	Not Available	Not Available
	Government Program	0.1%	Not Available	Not Available
	All formal sources	37.5%	11.1%	10.6%
<b>SHG</b>		53.5%	Not Available	Not Available
<b>JLG</b>		11.4%	Not Available	Not Available
<b>Informal</b>				
	Moneylender	17.2%	20.9%	Not Available
	friends (with interest)	57.3%	Not Available	Not Available
	friends (no interest)	9.3%	1.7%	3.7%
	Employer	3.4%	Not Available	Not Available
	Landlord	20.6%	0.6%	4.4%

<b>Major Source</b>	<b>Sub-source</b>	<b>Estimated Share of households with loan from source based on A2F</b>	<b>Estimated Share of households with loan from source based on AIDIS 2003</b>	<b>Estimated Share of households with loan from source based on AIDIS 1991</b>
	unknown sub-source	1.4%	Not Available	Not Available
	All informal sources	82.4%	24.8%	28.4%
<b>Any loan source</b>		93.1%	33.2%	34.7%

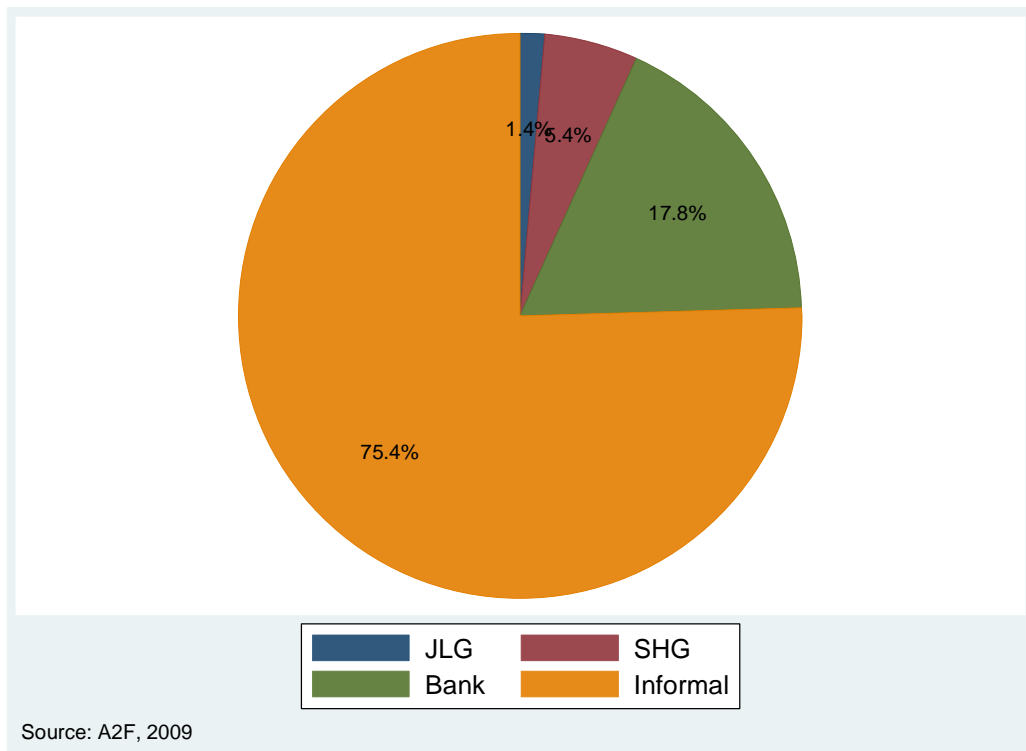
Source: A2F, 2009, NSSO All India Debt and Investment Survey Rounds 1991 and 2003

**Table 7: Percentage of Rural AP Households Indebted, other sources**

<b>Major Source</b>	<b>Sub-source</b>	<b>Share of households with loan from source</b>
<b>Credit card</b>		0.5%
<b>Overdraft</b>		0.1%
<b>In kind ag input loan</b>		12.3%
	without commitment	5.6%
	with commitment (e.g. - portion of harvest must be sold at fixed price to lender)	6.7%
<b>Routinely purchases from shop on credit</b>		36.5%
<b>Member of chit fund</b>		7.5%

Source: A2F, 2009

**Figure 9: Share of Total Borrowing by Source**



**Overall rate of indebtedness is extremely high**

Our survey reveals that overall rates of indebtedness, from virtually all sources, are much higher than previously estimated. According to the 2003 round of the All India Debt and Investment Survey (AIDIS) conducted by the National Sample Survey Organization, 33.19% of rural households in AP had a loan outstanding from any source, 11.06% had a loan from a formal source, and 24.8% had a loan from an informal source at the time of the survey (2003). Data from our more recent survey shows that the current overall rate of indebtedness in rural AP to any source is over 93%, 37% of households have a loan from a formal source, 82% have a loan from an informal source, and over half have a loan from either a MFI or an SHG – a loan category that was so negligible at the time of the AIDIS that it was not even included in the survey.

It is unclear how much of the discrepancy between our estimates and that of the NSSO are due to differences in survey methodology and how much are due to actual changes in rates of indebtedness between the survey periods.<sup>32</sup> Nevertheless, our data indicate that actual rates of indebtedness are much higher than previously estimated.

The average and median amounts of principal borrowed from all sources (formal, semi-formal, and informal) and loans currently outstanding were also incredibly high. Table 8 displays these amounts, broken down by household occupational profile as well as for SC, ST, and Muslim households. Large farmers, in particular, borrowed an average of well over 1 lakh.

**Table 8: Mean Outstanding per Household by Occupational Category**

Total Loans (All sources)					
Household Profile	% with outstanding loan	Mean Principal (INR)	Mean Outstanding (INR)	Median Principal (INR)	Median Outstanding (INR)
Other	84.93%	53,395	48,412	33,750	29,500
Landless Laborer	89.42%	40,198	36,933	25,000	21,600
Commercial	90.06%	63,103	57,948	40,000	33,680
Farmer - Marginal	96.84%	57,747	54,446	43,000	37,450
Farmer - Small	95.81%	83,432	77,728	60,000	53,000
Farmer - Large	95.43%	115,869	110,534	91,500	82,000
SC	93.56%	55,842	49,861	38,000	31,220
ST	90.48%	67,995	65,026	33,000	30,100
Muslim	84.21%	62,938	55,794	45,500	140,200

Source: A2F, 2009

<sup>32</sup> Despite significant effort by the authors to identify substantive differences in the methodologies of the two surveys (e.g. – a definition of what constitutes a loan), we were unable to uncover any differences significant enough to account for these discrepancies.

**Over half of rural households borrow from SHGs, but only around 11% borrow from MFIs.<sup>33</sup>**

Since the crisis in Krishna and Guntur in 2006, many in the microfinance community have expressed concern that several areas in Southern India, and in particular AP, have become over-saturated with microfinance and that borrowers are taking on more debt than they can handle. (See, for example, Rozas and Sinha (2009)) While data from this survey does not permit us to assess the truth of this statement as we are unable to determine absolute borrowing capacity, it does allow us to compare rates of indebtedness to microfinance lenders versus other types of lenders.

Data from the survey show that indebtedness to SHGs is indeed extraordinarily high at 53%. Indebtedness to MFIs, at 11%, is significant but not nearly as high as indebtedness to SHGs and both figures pale when compared with the rate of indebtedness to informal sources.

**Indebtedness to moneylenders remains high, but, in most cases, interest rates charged by moneylenders are only slightly higher than those charged by MFIs.**

The one category of borrowing which did not rise significantly, and even declined somewhat, was loans from moneylenders.<sup>33</sup> While borrowing from moneylenders remains relatively high at 17%, the interest rates on

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<sup>33</sup> In the Access to Finance survey and in this report, microfinance lending is divided into two primary categories: Self Help Groups (SHGs) and Microfinance Institutions (MFIs). Given the sometimes subtle distinction between these two forms of microfinance, surveyors were given extensive training on how to distinguish between MFI groups and SHGs. If the categorization was not immediately clear from the name and description of the group and organizing entity (which sometimes respondents did not know), surveyors probed further to understand the number of members of the group, management of any group savings, and process for managing and distributing credit. It should also be noted that this distinction between MFIs and SHGs slightly oversimplifies the ground reality of microfinance in India in that MFIs also occasionally lend to SHGs. In case where a household was a member of an SHG that was created and lent to by an MFI we have classified the loan as an SHG loan. Also, any loan that is received through an SHG is categorized as “SHG” and not as “Bank”, although SHG loans themselves frequently originate from banks through the SHG Bank-Linkage Programme.

Care should be taken in inferring from this that borrowing from moneylenders has declined. Our data show a very high incidence of borrowing from friends with interest—a type of borrowing that was classified as moneylender lending by the NSSO survey.

loans from moneylenders were, in most cases, much lower than the exorbitant rates often attributed to moneylenders by the press. Of those loans from moneylenders for which the interest rate was provided by the respondent, 57.0% had an interest rate 2% per month or lower, a rate comparable to loans from mainstream MFIs. An additional 39.1% of loans had an interest rate between 2% and 3% per month. A further 3.8% of loans had an interest rate between 3 and 10% per month. And only a handful of loans had interest rates greater than 10% per month.

**Non-routine expenditures are common and are typically due to need for medical treatment or festivals. Non-routine expenditures are overwhelmingly financed through own savings or informal sources.**

A majority (64.3%) of rural households were forced to make a non-routine expenditure of some sort during the six months prior to survey. By far the largest portion of these non-routine expenditures were incurred to pay for medical treatment.<sup>34</sup> Table 10 shows that when it comes to non-routine expenditures, perhaps due to a reluctance on the part of formal lenders to lend for unproductive purposes or alternatively to an increased speed or flexibility on the part of informal lenders, households relied almost exclusively on informal sources to finance these expenses.

**Table 9: Top 5 Non-routine Expenditures and Share of Households that Incurred Them in 6 Months prior to Survey**

<b>Non-routine Expenditure</b>	<b>Share of Households which Incurred Major Expenditure on Item in prior 6 Months</b>
Health	36.0%
Festival or special event aside from marriage	11.3%
Marriage	10.8%
Buy agricultural machinery or inputs	10.0%
Home improvement/repair/construction	6.4%
<i>Any non-routine expenditure</i>	<i>64.3%</i>

**Source: A2F, 2009**

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<sup>34</sup> This result is especially salient in light of the state government’s generous health insurance program which allows any BPL household to receive treatment for a variety of ailments for free at a wide range of both public and private hospitals. See the section on the Arogyasri Health Insurance Scheme below for more details.

**Table 10: Top 5 Sources of Financing for Non-routine Expenditures incurred in prior 6 Months**

Source	Share of Non-routine Expenditures Financed through This Source
Loan from friends/relatives	42.7%
Own income or savings	29.4%
Loan from moneylender	13.0%
Loan from landlord	10.5%
Loan from JLG/SHG	5.7%

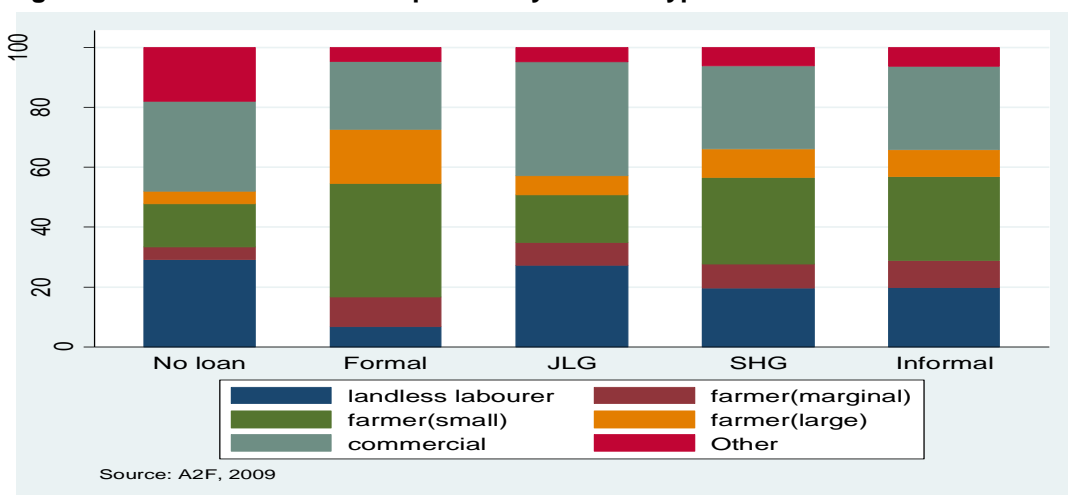
Source: A2F, 2009

### What Type of Clients Do Different Lenders Reach?

**MFIs reach relatively more landless labourers and fewer farmers than other lenders.**

Microfinance lenders, especially JLGs, reach significantly fewer farming households and significantly more landless labourer households than formal lenders. Figure 10 presents the breakup of borrowing households into occupational category by lender type. The graph shows that the share of farming households of all types (marginal, small, and large) among JLG and SHG borrowing households is significantly lower than the share of farming households among those households which borrow from a formal source.

**Figure 10: Profile of Client Occupations by Lender Type**



### **Average poverty levels of clients reached by different types of lenders are relatively similar**

Microfinance institutions are widely perceived to reach out to poorer households than banks or other formal lending sources. (Morduch, 1999) Yet surprisingly, we find almost no difference in the mean PPIs of the set of households borrowing from different lender types. While the mean PPI of households with no loan from any source is statistically significantly lower than the mean PPI of households with a loan, there is no statistically significant difference between the PPIs of the set of households borrowing from different lender types.

Due to the limitations of the data it is based on, the PPI index is not as accurate an indicator of poverty as those measures based on detailed consumption surveys. Further, a simple test of means may hide interesting differences in the distribution of the poverty scores of households which borrow from different sources. Nevertheless, this result shows that the poverty profile of borrowers of different lender types may not be as large as many believe.

### **Households abstain from borrowing for a variety of different reasons.**

Appendix D lists the top five reasons cited for not availing a loan from a source. In the case of banks, many of the reasons cited were external such as lack of land, lack of guarantor, application rejected and lack of documents suggesting that there is a high pent up demand for loans from formal sources.<sup>35</sup> A large majority of those households with no loans from JLGs cited the inability to make regular payments or to save regularly as a key reason for not availing a JLG loan. Many of those who abstained from joining SHGs also cited an inability to save regularly as a barrier, though far less frequently than those who abstained from JLG loans. Several households with no loan from an SHG also cited potential for group conflict and an inability to find a group willing to accept them. (Interestingly, these reasons are nearly absent from the list of reasons for not joining JLGs.)

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<sup>35</sup> Lack of documents was the sixth most common reason for not taking a loan from a bank. An estimated 9.7% of rural households without a loan from a bank, did not take a bank loan for this reason.

That an inability to make regular payments is an often cited reason for not availing a microfinance loan is hardly surprising. Microfinance loans, especially JLG loans, often have extremely rigid and frequent repayment schedules. More surprising is that households without a loan from an informal source also cited an inability make regular repayments as a prime reason for not availing such a loan nearly as frequently as those without loans from JLGs and even more frequently than those without loans from SHGs. This suggests that, at least in the case of SHGs, we should be cautious in inferring from these results that inflexibility of repayment schedules is a major hurdle to households joining SHGs.

Lastly, a similar pattern emerges in the responses to those who did not participate in a chit fund. Interestingly, the issue of trustworthiness of chit fund operators, much cited in the press, was not cited as a major factor among those who did not participate in chit funds.

### How Do Borrowers Use Their Loan Money?

**Table 11: Usage of Loan Money by Lender Type**

	<b>Bank</b>	<b>JLG</b>	<b>SHG</b>	<b>Informal</b>
Start New Business	2.0%	2.5%	1.9%	1.1%
Buy ag inputs	57.5%	13.2%	19.3%	19.9%
Purchase stock	3.0%	9.9%	4.2%	2.7%
Repay old debt	14.6%	25.4%	20.4%	7.0%
Health	11.4%	10.9%	18.6%	25.3%
Marriage	4.3%	4.8%	2.2%	12.2%
Funeral	0.1%	0.2%	0.5%	1.7%
Other festival	0.6%	3.5%	3.6%	4.8%
Home improvement	9.7%	22.1%	13.0%	14.2%
Unemployment	0.0%	0.0%	0.1%	0.8%
Purchase land	0.8%	0.9%	0.7%	0.6%
Education	4.1%	4.4%	5.7%	5.3%
Purchase jewelry	0.5%	0.6%	1.6%	0.4%
Consumption	26.5%	31.6%	49.9%	24.9%
Buy livestock	2.7%	6.0%	5.6%	1.7%

Source: A2F, 2009

**Note:** Totals may be greater than 100% as loans may be used for more than one purpose

### **Loans from different sources are used for different purposes.**

Data on loan usage reveals that loans from different sources are used differently. Bank loans are used to finance the purchase of agricultural inputs to a much greater extent than loans from other sources. Loans from informal sources are used for health and marriage related expenses much more than loans from other sources. And SHG loans are disproportionately used to finance consumption.

The data also reveals that a large share of loans are used to repay old debt. While this finding may appear worrying at face value as it suggests that households are entering a vicious debt cycle, it may also be the case that households are simply using new loans with lower interest rates or better terms to pay off older loans. (Unfortunately, the survey did not include a question on why the new loan was used to repay the old and thus we are unable to distinguish between these two cases.)

### **Multiple Borrowing**

In January 2009, microfinance operations in Karnataka erupted in a frenzy when the Muslim clergy in Kolar district called for a halt in microfinance repayments.<sup>36</sup> The resulting Kolar crisis sent the microfinance community—in India and abroad—abuzz with talk of debt fatigue and over borrowing. A *Wall Street Journal* article declared India to be facing an imminent “credit crisis,” implying that the sector was approaching bubble conditions. (Ghokale, 2009) The Kolar crisis was highly reminiscent of the AP crisis detailed above and both raise serious questions about whether microfinance clients are taking on more debt than they can handle and, in particular, about the extent of multiple borrowing.

Unfortunately, prior to the survey whose results are reported here, there existed very little data on the prevalence of multiple borrowing for any sizeable area. In the absence of reliable data on multiple borrowing, researchers have been forced to rely on indirect methods of estimating multiple borrowing (see, for example, Krishnaswamy, 2007) or on surveys conducted in small areas with a known high incidence of multiple borrowing (see, for example, Kamath, Mukherji, and Ramanathan, 2008, or APMAS, 2006). While such studies may provide a general range for

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<sup>36</sup> For a detailed account, please refer to the “India Microfinance State of the Sector Report, 2009.”

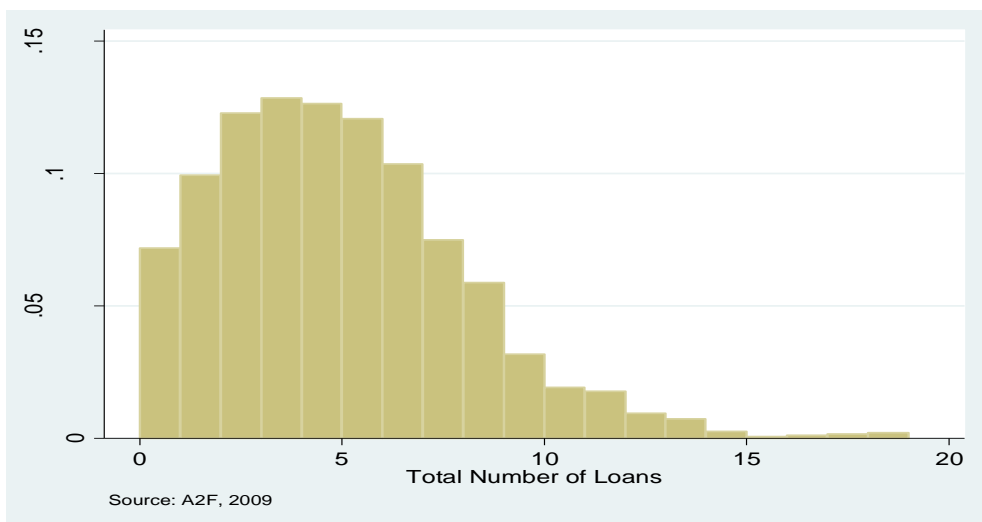
the extent of multiple borrowing overall, or more precise estimates for certain specific areas, they do not answer the much larger question of how prevalent multiple borrowing is overall.

The lack of hard data on multiple borrowing has led to wildly divergent claims on multiple borrowing and whether it should be a source of concern for the microfinance sector. In one camp, there are those who claim that it is widespread and may even be the cause of a whole-scale crisis of the sector. Some have even gone so far as to compare the state of the microfinance sector in Southern India with that of the sub-prime mortgage market in the US prior to the recent financial crisis. (Rozas, 2009) Those in the second camp assert that reports of multiple borrowing are exaggerated and, to the extent it exists, multiple borrowing is caused mainly by borrowers' inability to fulfil their complete credit needs from a single source. Below we attempt to bring hard data to this debate.

### Multiple borrowing is extremely common...

Multiple borrowing was found to be extremely common, with an estimated 83.7% of households having two or more loans from any source. (One household even reported having 19 loans outstanding!). Surveyed households reported a median of four loans outstanding from all sources. Figure 11 shows the distribution of total loans per household from all sources.

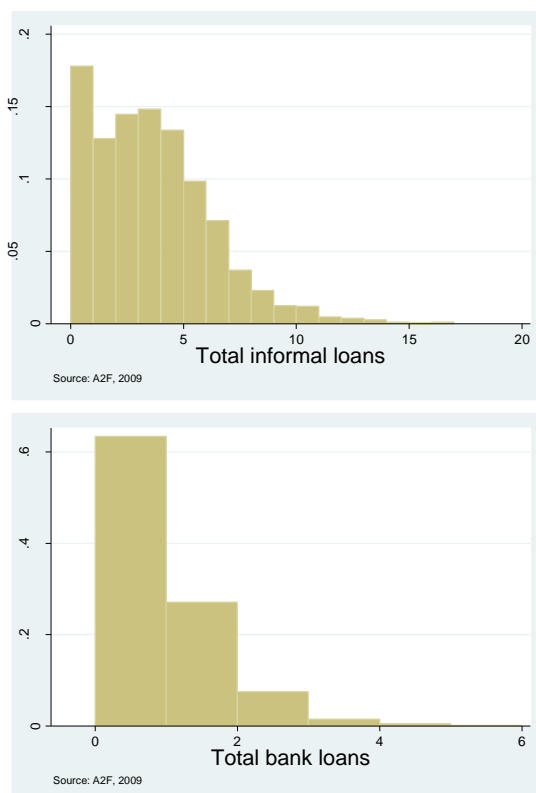
Figure 11: Histogram of Total Loans per Household

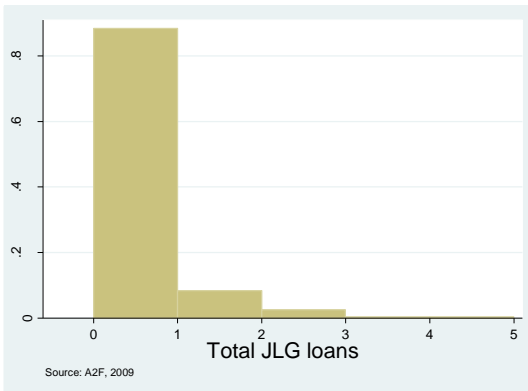
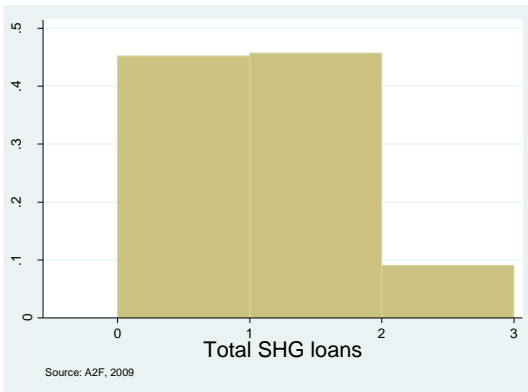


**...but is mainly due to multiple loans from informal sources.**

Yet when the source of loans is taken into consideration, the situation related to multiple borrowing does not appear nearly so dire. Much of the recent debate regarding multiple borrowing has been over the extent to which microfinance clients, and in particular clients of MFIs, are borrowing from multiple microfinance lenders at the same time. Figure 12 plots histograms of total loans per household from informal sources, banks, SHGs, and JLGs. As the figure shows, while many households in the sample have numerous loans from informal sources, very few have multiple loans from banks and even fewer have multiple loans from SHGs or MFIs.

**Figure 12: Distribution of Total Loans per Household by Source**





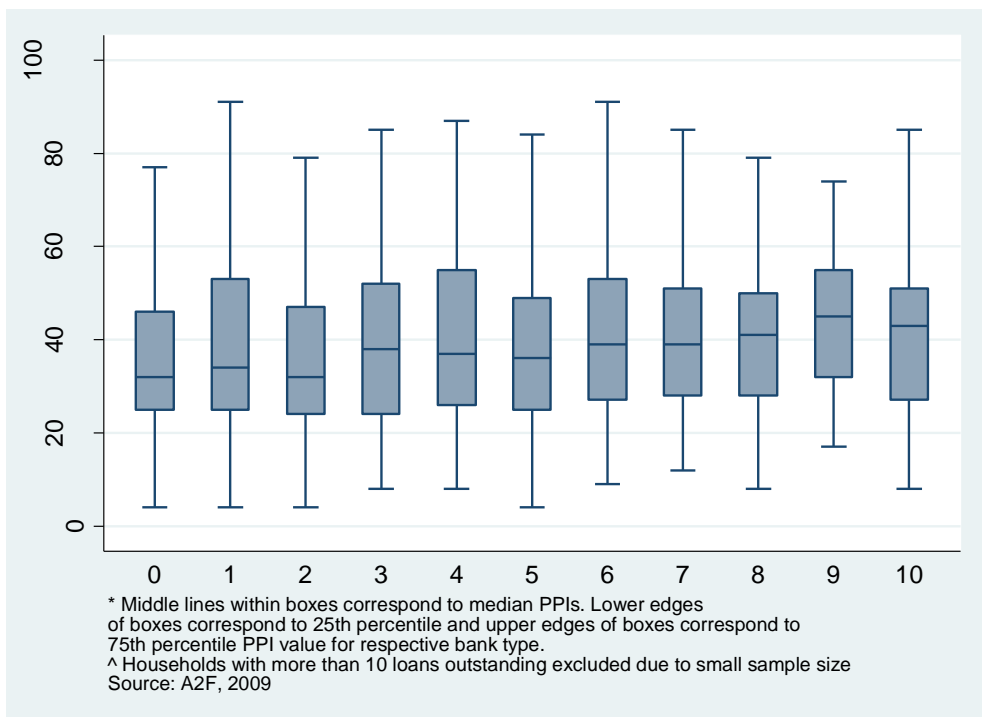
These histograms may hide multiple borrowing across sources though. Yet the share of households borrowing from both at least one JLG and at least one SHG was only 7.4% indicating only a slight correlation in the propensity to borrow from these two sources. (If SHG and JLG borrowing was not correlated at all roughly 6% of households would have loans from both an SHG and JLG.)

**Multiple borrowing appears to be more common among the better off.**

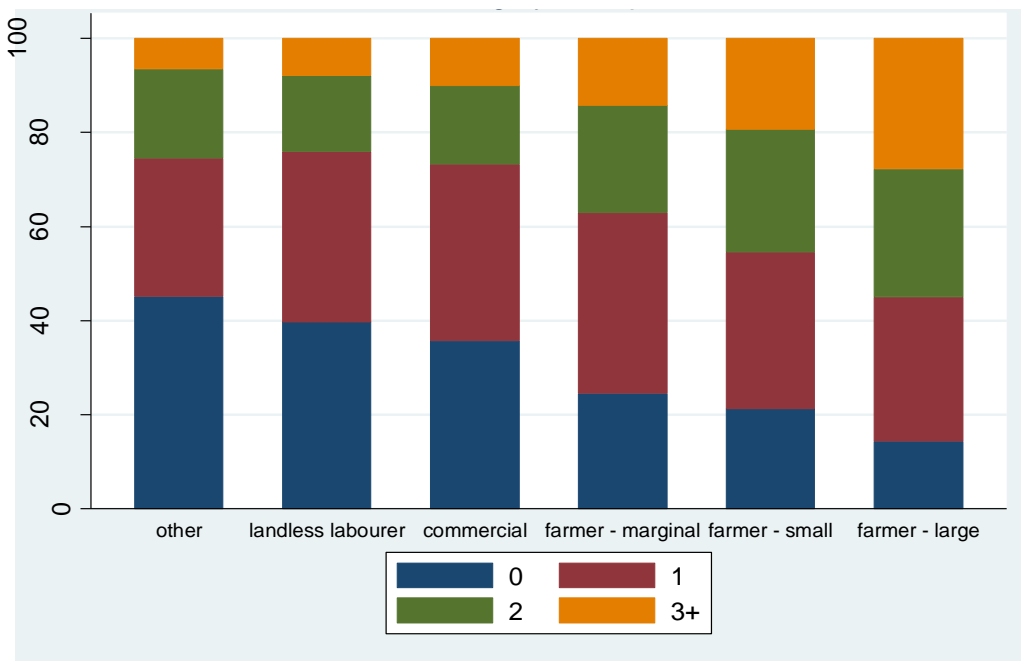
Households with more loans outstanding appear to be better off than those with fewer loans outstanding on average. Figure 13 displays PPI scores of households according to the number of loans outstanding the household has. The graph exhibits a clear upward trend indicating that a household's PPI score is strongly correlated with the number of loans outstanding the household has. Figure 14 displays loans outstanding by

occupational category. Households in the relatively well off categories of “large farmer” and “small farmer” have a far greater propensity for multiple borrowing than those households in the relatively worse off categories of “landless labourer” and “marginal farmer”.

**Figure 13: Progress out of Poverty Score by Number Loans Outstanding\*^**



**Figure 14: Distribution of the Number of Outstanding Loans from Formal Sources by Occupation**



Source: A2F, 2009

**Many cases of multiple borrowing appear to be driven by an inability to obtain sufficient credit from a single source.**

Whether multiple borrowing should be a cause for concern or not depends greatly on the underlying reason for which the borrower has availed multiple loans. If it is because the borrower cannot make repayments on a loan, then the multiple borrowing is indeed a cause for concern. If, on the other hand, it is because he or she is unable to obtain sufficient credit from a single lender, then the borrowing is much less distressing.

While it is difficult to ascertain the true reasons for multiple borrowing based on a relatively short survey, based on the timing and purpose of loans it appears that many households in our sample borrowed from multiple sources for the latter reason – that is because they could not obtain sufficient credit from a single source. A large share of those households with more than one loan outstanding has two or more loans

which were disbursed in the same month for the same purpose. Households with at least two informal loans had an average of just over one such instance.

The average total amount borrowed in these cases was Rs. 45,279.86. The main loan usages for such borrowings mirror the overall usage of informal borrowings:

**Table 12: Usage of Loans Taken Out in the Same Month**

<b>Loan usage</b>	<b>Share</b>
Health	20.13 %
Buy agricultural inputs	18.36 %
Home improvement/construction	18.05 %
Marriage	17.44 %
Household consumption	16.95 %

Source: A2F, 2009

### **In Depth Look at SHGs**

#### **Indebtedness to SHGs in rural AP is quite high but not as high as some previous estimates**

Estimates of microfinance penetration<sup>37</sup> of the target population (those households just below the poverty line) in Andhra Pradesh have recently been as high as 224%, implying that each household below the poverty line belongs to at least 2 groups, if not more. (Rozas and Sinha, 2010)

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<sup>37</sup> These figures include both major models of Indian microfinance, SHGs and JLGs.

Andhra Pradesh has even been deemed the most saturated microfinance market in the world, surpassing even Bangladesh.<sup>38</sup>

Our study found penetration to be significantly lower. Of all rural households, membership in at least one SHG came to just under 72%. We believe that this discrepancy comes 1) from looking only at households with SHG membership, and 2) from the fact that the previous estimates are based on cumulative bank linkages in India since the inception of the SHG Bank-Linkage Programme in 1992. Our estimate should reflect a more accurate level of current membership levels, given the dissolution of older groups. See the SHG/JLG portion of the multiple borrowing section for data on levels of borrowing from both of these sources.

**Principal loan amounts received by SHG members increased significantly with membership years.**

The median principal loan amount received by members was Rs. 6,800, while the average came to Rs. 9,416.82. These amounts are comparable with industry estimates of an average loan size of Rs. 7,344 in Andhra Pradesh, compared to an all-India average of Rs. 5,544.<sup>39</sup>

These amounts differed significantly with duration of group membership:

**Table 13: SHG Members’ Principal Outstanding by Age of Group**

<b>Membership Years</b>	<b>Avg Principal</b>	<b>Median Principal</b>
<b>0-5 years</b>	INR 7,965	INR 5,000
<b>6-9 years</b>	INR 10,855	INR 9,000
<b>10+ years</b>	INR 13,211	INR 10,000

Source: A2F, 2009

<sup>38</sup> Rozas and Sinha (2010) estimated microfinance penetration in AP to be 17.2% as opposed to 16.4% in Bangladesh. These numbers include both SHG and MFI membership.

<sup>39</sup> Estimates based on state-wise SHG average savings and loan amounts, taken from the Microfinance India State of the Sector Report 2009.

The average age of groups was 5.2 years, while average membership was 4.8 years. 36.6% of groups were formed in the last 2 years, while 31.5% were older than 8 years.

**The majority of SHG members had an outstanding loan at the time of survey.**

Of all SHG members, 72% had an outstanding loan, and only 16.9% of members belonged to groups that had never received a bank loan. Of these, 35% were formed in 2007 or earlier, implying that there has been a slight delay in receiving their first loan. Generally, groups will save for 6 months to 1 year and undergo rating by a bank before being sanctioned a bank loan.

Of groups that had received at least one bank loan, 89.4% of groups currently have a group loan outstanding. Within these groups, 96% of members had individual loans outstanding, a significant proportion. For those groups that did not have loans outstanding, just over half of the previous loans were completed during the previous two years. Only 10% of these groups had not been issued a new bank loan in the past five years, as shown in Table 14 below.

**Table 14: Year of Most Recent Loan among SHGs with No Loans Outstanding**

<b>Last Loan Year</b>	<b>Percentage</b>
2008	25.66%
2007	25.25%
2006	14.63%
2005	7.85%
2004 or earlier	9.43%

**Source: A2F, 2009**

**Regular savings, the defining aspect of self-help groups, was overwhelmingly strong...**

The primary component of self help groups is regular savings—from these savings, groups generate a common pool through which they can extend emergency loans and avail bank loans. 99% of groups reported

regular savings. 95.5% save monthly at Rs. 50 per month, while 3.7% of groups save weekly at an average of Rs. 16.5 per week (Rs. 66 monthly).

**...as were regular group meetings, despite many groups not having received a follow-up loan.**

87.3 percent of groups reported meeting monthly, and 7% meet weekly. Only 1.5% of members reported that their groups no longer meet--it's likely that these groups have become defunct. It's likely that groups continue to meet and avail of common group savings to extend loans for members in need, even if they have not received fresh bank loans in recent years.

Meeting times averaged at 80 minutes while traveling to and from meetings rounded out at 20 minutes total. A member typically spent 192 minutes traveling to (and waiting at) a bank to deposit or withdraw savings. From this, we can gather that the member in charge of bank transactions (usually the president or treasurer) typically spends an average 5 hours monthly, or nearly an entire working day, on SHG business.

**Reports of dropouts and defaults were limited.**

Nearly 74% of groups had no dropout members, while 11.5% reported only 1 such member. The mean age of groups with no dropouts was 4.4 years, while the age of those with 1 or more dropout was 7.9 years. The top reasons for dropping out were repayment problems and members moving to new locations.

**Table 15: Stated Reasons for Leaving SHG among Drop-outs**

<b>Reason</b>	<b>Percent</b>
<b>Repayment Problem</b>	33.55%
<b>Moved</b>	32.00%
<b>Old Age</b>	23.15%
<b>Group Conflict</b>	8.90%

Source: A2F, 2009

88% of groups reported having had no default members. Still, 2.4% of these reported having at least one dropout as a result of repayment problems.

**And multiple SHG/JLG memberships by individual SHG members seems to be driven by credit need.**

As we saw in the multiple borrowing section, only 8.6% of households had 2 or more SHG loans.

Looking specifically at multiple membership by individual members, we found 13% of SHG members and 67% of JLG members belonged to at least one SHG and one JLG simultaneously. 23% of these individuals had no outstanding SHG loans, and half of these had never received a loan from their SHGs at the time of survey. Dual membership, therefore, may be driven by the need for more immediate loan sanctions, which JLGs often provide.

Only 66% of all SHG members reported having 0 multiple borrowers in their groups, while another 18% claimed to have no idea of whether multiple borrowing was taking place. 12 and 17% of SHG members with dual SHG/JLG membership reported 0 multiple borrowers or having no idea about such borrowings in their groups, respectively.

Only 2.5% of SHG members belonged to more than one SHG.

**Although groups were overwhelmingly government-formed, most members did not receive SGSY subsidies.**

95% of SHG groups were government formed—it can be assumed that they were formed under the DWCRA or Velugu programs. Of these, only 2% received SGSY subsidies. The average individual subsidy received came to Rs. 12,739. Only 7% of rural members reported politicians approaching their groups for political support.

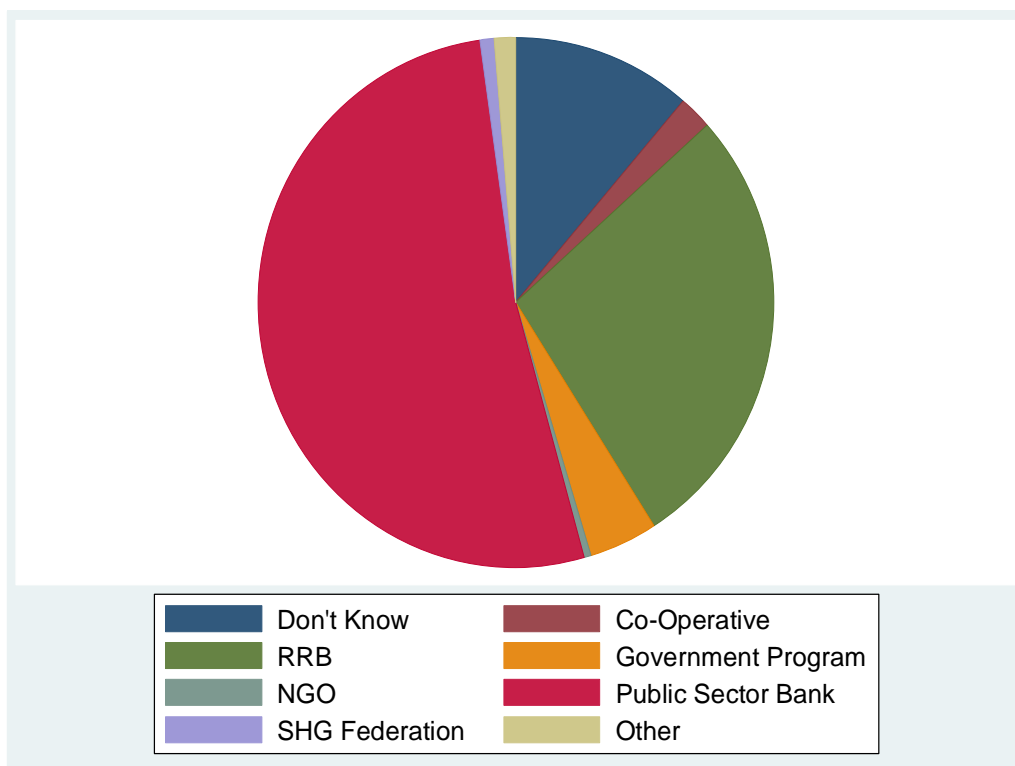
**Group credit was overwhelmingly extended by public sector banks.**

Over 50% of group loans were issued by public sector banks, followed by Regional Rural Banks, as illustrated in figure 15 below. These numbers align with industry calculations of 2009 national bank linkages in which commercial banks issued 55% of credit and RRBs 26.5%.<sup>40</sup>

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<sup>40</sup> See Microfinance India State of the Sector Report, 2009.

**Figure 15: Break up of Lending to SHGs**



Source: A2F, 2009

**Capture by elites was not evident, either in terms of leadership or household profile.**

The average principal amounts borrowed by leaders was only slightly higher than that of members, at Rs. 9804.61 versus Rs. 9371.26.

In addition, average and median loan amounts borrowed remained largely identical across occupational profile as well as for SC, ST and Muslim households, with the exception of those that fell into the Other category.<sup>41</sup>

<sup>41</sup> This could be explained by the fact that many households in the “Other” category were retired and, thus, probably had a lower credit requirement.

**Table 16: Borrowing Rate and Principal Outstanding of SHG Members broken up by Various Categories**

<b>SHG Loans</b>			
<b>Household Profile</b>	<b>% with o/s loan</b>	<b>Avg Principal</b>	<b>Median Principal</b>
Other	46.58%	INR 12,677	INR 6,733
Landless Laborer	52.16%	INR 11,029	INR 9,500
Commercial	51.42%	INR 13,014	INR 10,000
Farmer - Marginal	56.32%	INR 12,078	INR 8,800
Farmer - Small	58.45%	INR 11,182	INR 8,800
Farmer - Large	53.81%	INR 10,920	INR 8,700
SC	58.42%	INR 11,462	INR 9,750
ST	55.10%	INR 11,825	INR 9,000
Muslim	57.89%	INR 11,744	INR 8,575

Source: A2F, 2009

## **JLG Borrowing**

### **Borrowing from MFIs was much lower than anticipated for rural Andhra Pradesh...**

Only 12% of rural households belonged to a JLG formed by a private microfinance institution, and 95% of members had MFI loans outstanding at the time of interview.

### **...and average years of membership was surprisingly low.**

The average duration of membership in JLGs was only 1.6 years, and nearly 64% of members had been in their groups for 1 year or less as shown in Table 17 below. This could be due to the inability of households to repay loans consistently over a longer period of time, compared to SHGs in which members borrow only according to credit need. Alternatively, this could also reflect the continued rapid expansion of MFIs in the state.

**Table 17: Distribution of Years of Membership in JLG**

<b>Years of membership with JLGs</b>	<b>%</b>
0	36.67%
1	27.12%
2	10.77%
3	11.76%
4	4.44%
5	4.15%
6	2.57%
7	0.64%
8	1.07%
9	0.18%
10	0.62%

Source: A2F, 2009

**Loan sizes, unsurprisingly, increased with membership more rapidly than in SHGs.**

Average loan amounts received during the first year started at close to Rs. 10,000 and gradually increased to just over Rs. 13,000 after 5 years of membership, half the time it would take to receive a comparable amount in an SHG.

**Table 18: Principal Outstanding by Age of JLG**

<b>Membership Years</b>	<b>Avg Principal</b>	<b>Median Principal</b>
0-1 years	INR 9,541	INR 10,000
1-2 years	INR 10,361	INR 10,000
2-3 years	INR 10,511	INR 10,000
3-4 years	INR 11,711	INR 10,000
4-5 years	INR 12,787	INR 12,000
5 years	INR 13,083	INR 10,000

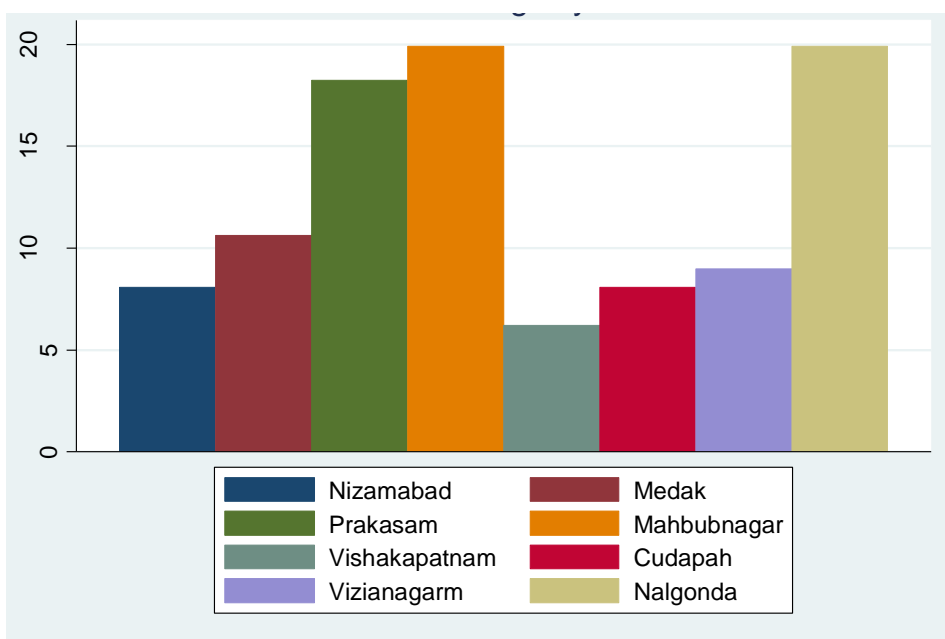
Source: A2F, 2009

Average loan sizes in rural AP also came out significantly higher than the national average outstanding amount of Rs. 5,200.<sup>42</sup>

**Borrowings were greatest in districts with proximity to Hyderabad.**

Nalgonda and Mahbubnagar, both bordering the capital of Hyderabad, led in terms of number of JLG memberships. Prakasam, which borders the saturated Guntur district, followed closely behind. Unsurprisingly, Vishakapatnam and Vizianagarm districts, both with large populations of Scheduled Tribe and Scheduled Caste populations, had the lowest outreach.

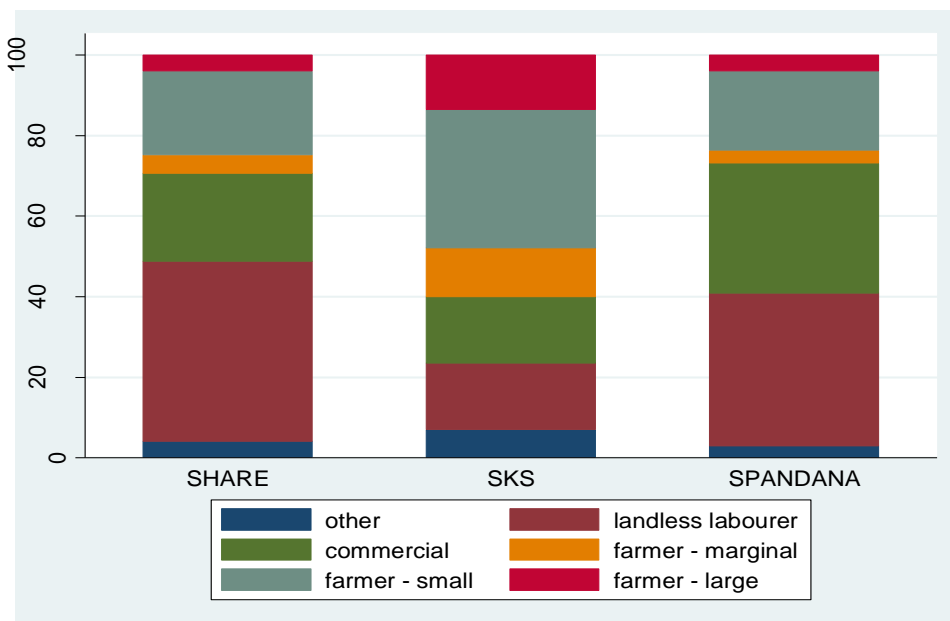
**Figure 16: Incidence of JLG Borrowing by District**



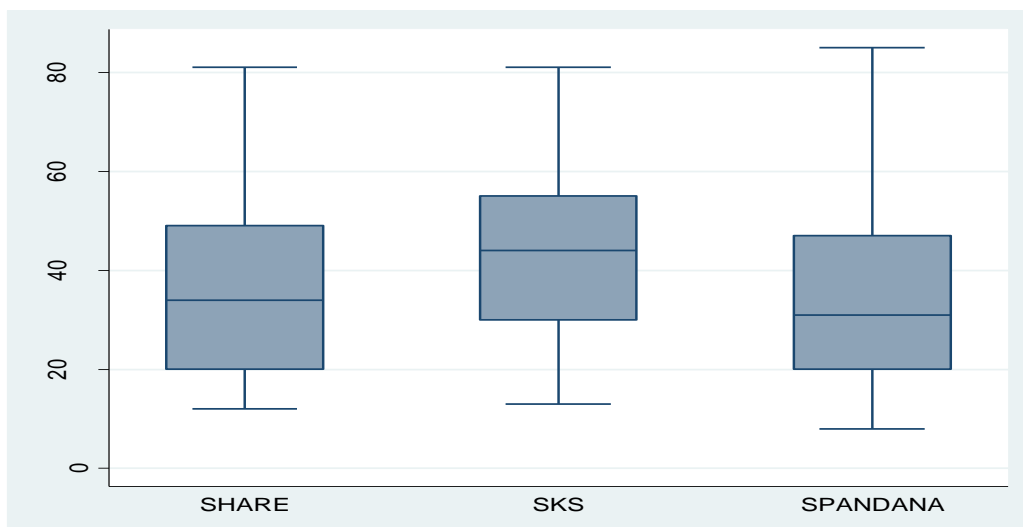
SHARE and Spandana tended to target more landless labourers, while the majority of SKS clients were small farmers.

<sup>42</sup> Microfinance India State of the Sector Report 2009

**Figure 17: Client Profiles of Three Major MFIs**



**Figure 18: Client PPIs of Three Major MFIs**



Note: Due to the small number of observations of households having membership with other MFIs, we include household profiles and PPI scores only for borrowers from the following 3 MFIs.

## Other Financial Products

### Chit Funds

**Membership in chit funds remained limited to a small portion of the population.**

Only 7.6% of households reported having membership in a chit fund. Proportion of borrowers by household occupation was as follows:

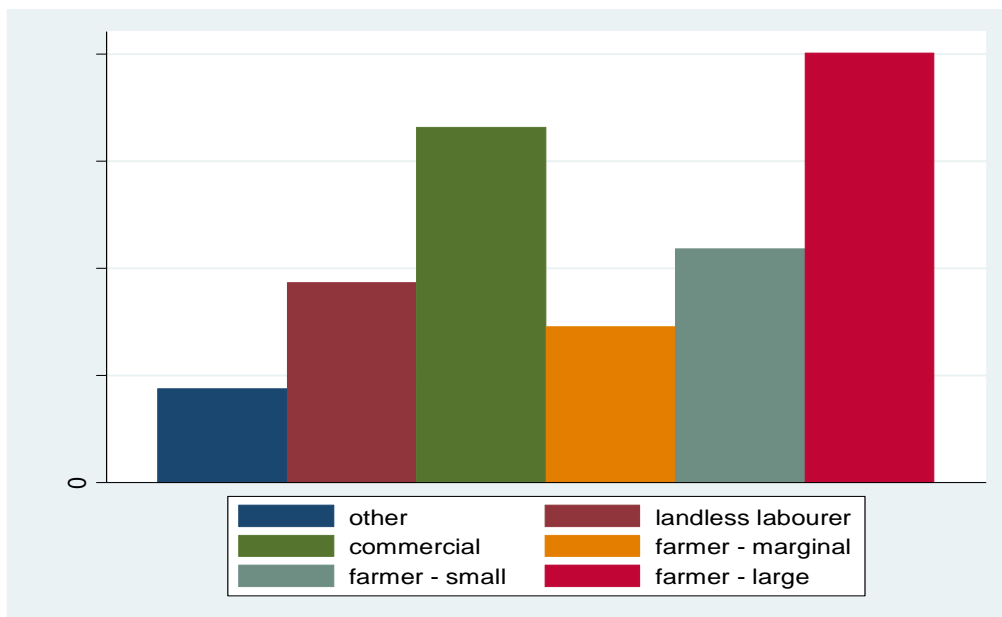
Only 5% of groups had to provide documentation to join their chit group—we can assume that the remaining groups are unregistered.

**And initial payments varied widely according to household profile.**

The average amount of initial payment was Rs. 2363. This rose to Rs. 6653 for registered groups. The range of initial payments varied from as little as Rs. 50 to Rs. 32,000.

The mean chit pool (average total amount which was auctioned at regular meetings) came to Rs. 53,553. Broken down by household profile, the averages varied considerably:

**Figure 19: Average Chit Pool Size by Occupation of Member**



Source: A2F, 2009

## **Remittances**

### **Very few households receive remittances.**

Only 3.68% of rural households receive money from a household member living outside the household. Out of these households who received remittances, bank transfers and cash were used as methods of delivering funds more frequently than cheques or postal money orders.

### **Arogyasri Health Insurance Scheme**

In 2007, the government of Andhra Pradesh launched a comprehensive health insurance scheme for poor households – the Rajiv Arogyasri Health Insurance Scheme. The scheme provides BPL card holders with up to Rs. 1.5 lakh in coverage for major health procedures such as surgeries or cancer treatments. Treatment is cashless and beneficiaries may receive treatment at any hospital, public or private, participating in the scheme.

### **A significant portion of non-BPL households have Arogyasri cards.**

Despite the fact that only BPL households are eligible for the Arogyasri, a small but significant portion of rural households without BPL ration cards (3.0%) also have the Arogyasri card.

### **Many households received treatment under Arogyasri but a significant portion were forced to pay out of pocket expenses.**

A significant portion (4.7%) of rural households had received medical treatment under the Arogyasri program since the launch of the program. Yet, despite the fact that the program is intended to be cashless for patients, a large portion (35.5%) of patients who had received treatment under Arogyasri reported having to pay out of pocket fees.

## **Other Insurance Products**

### **Many households have life insurance but few have any other insurance product.**

Nearly half (43.8%) of rural households have life insurance but, not including the Arogyasri health insurance scheme, few have any other form of insurance.

**Table 19: Take up of Various Insurance Products**

<b>Insurance Product</b>	<b>Share of Households with Product</b>
Life	43.8%
Health (not including Arogyasri)	1.7%
Crop or weather	0.5%
Accident	0.4%
Cattle	0.3%

**Source: A2F, 2009**

## **Conclusion**

The results contained in this report, derived from a first of its kind survey of access to finance, reveal that the actual levels of financial inclusion of rural AP households is far different from what we previously believed. A far greater share of rural households have access to a formal savings account than did only ten years ago, though many of these accounts are not actively used for savings. Similarly, a much larger proportion of households are indebted, many of them from multiple sources, than were ten years ago.

The results from this report amply illustrate that recent government initiatives as well as the burgeoning microfinance sector have had an enormous impact on financial inclusion of rural households in recent years. More effort is required to understand the changing landscape of financial inclusion in other states across the country.

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## Appendix A – Sampling Methodology

The survey employed a three stage sampling design in which first districts, then villages, and then households were randomly selected. Details of the method of selection at each stage are provided below.

**Table 20: Overview of Sampling Strategy**

Stage	Selection Strategy
District	<p>Districts were selected using stratified random sampling. The 22 districts of Andhra Pradesh containing at least one rural area (one district in the state, Hyderabad, contains only urban areas) were divided into four strata based on the following two variables:</p> <ul style="list-style-type: none"> <li>• The estimated share of rural households falling under the official poverty line obtained from Chaudhuri and Gupta (2009)</li> <li>• The estimated share of adult women belonging to a microfinance group based on data collected from MFIs by the Centre for Microfinance.</li> </ul> <p>Within each stratum, two districts were selected with simple random sampling without replacement.</p>
Village	<p>Within each district, villages were selected using stratified random sampling. In all districts except for Ranga Reddy, villages were divided into four strata based on the distance to the nearest bank branch according to the village directory data of the 2001 census. In Ranga Reddy district, where a bank branch is present in all villages, villages were divided into four strata based on the distance to the nearest town.</p> <p>Within each stratum, two villages were selected with probability proportional to size (based on number of households) without replacement.</p>
Households	<p>Within each village, households were selected with simple random sampling without replacement. A village mapping exercise was conducted to enumerate all households living in the village.</p>

In the course of surveying, the surveying team encountered significant difficulty in conducting surveys in one of the districts selected, Krishna district. In the weeks before the surveyors arrived there had been a spate of robberies perpetrated by thieves fraudulently posing as surveyors. After several encounters with angry villagers, the survey team decided to abandon all attempts to survey in Krishna district and instead randomly selected another district from the same district strata to conduct surveys in.

Due to the omission of surveying in Krishna district, the data collected as a result of the survey is not representative of the rural areas of the entire state but rather the rural areas of the entire state *excluding Krishna district*. Often in this report, the authors use the phrase “rural households in Andhra Pradesh” in place of the more accurate but less concise “rural households in Andhra Pradesh excluding Krishna district.” Readers should note that all estimates presented here in this report are strictly valid for rural households in Andhra Pradesh excluding Krishna.

Rigorous quality checks were undertaken throughout the survey, both in the design of the field team structure and through supervision by CMF staff. Prior to surveying, staff received intensive training, both in a classroom setting and in the field, to ensure accurate data collection. In addition to thorough scrutiny of each survey by all levels of the team (surveyor, supervisors, and monitors), supervisors and monitors accompanied surveyors or conducted backchecks on at least 50% of surveys collected daily. Further surprise backchecks and accompaniments were undertaken by both the CMF Research Associate and Regional Field Coordinator throughout the length of the field work. In case of any doubts, either the Research Associate or Project Assistant conducted re-visits before completing data collection in a district. The rate of non-response was extremely low, and in such cases, replacement households were randomly selected.

## **Appendix B – How to Access and Use the Data**

The questionnaire and all data used in this report are available for download at: [http://www.birdindia.org.in/study\\_reports.htm](http://www.birdindia.org.in/study_reports.htm) A detailed description of the contents of the various data files is also.

## **Appendix C – Determination of Occupational Categories**

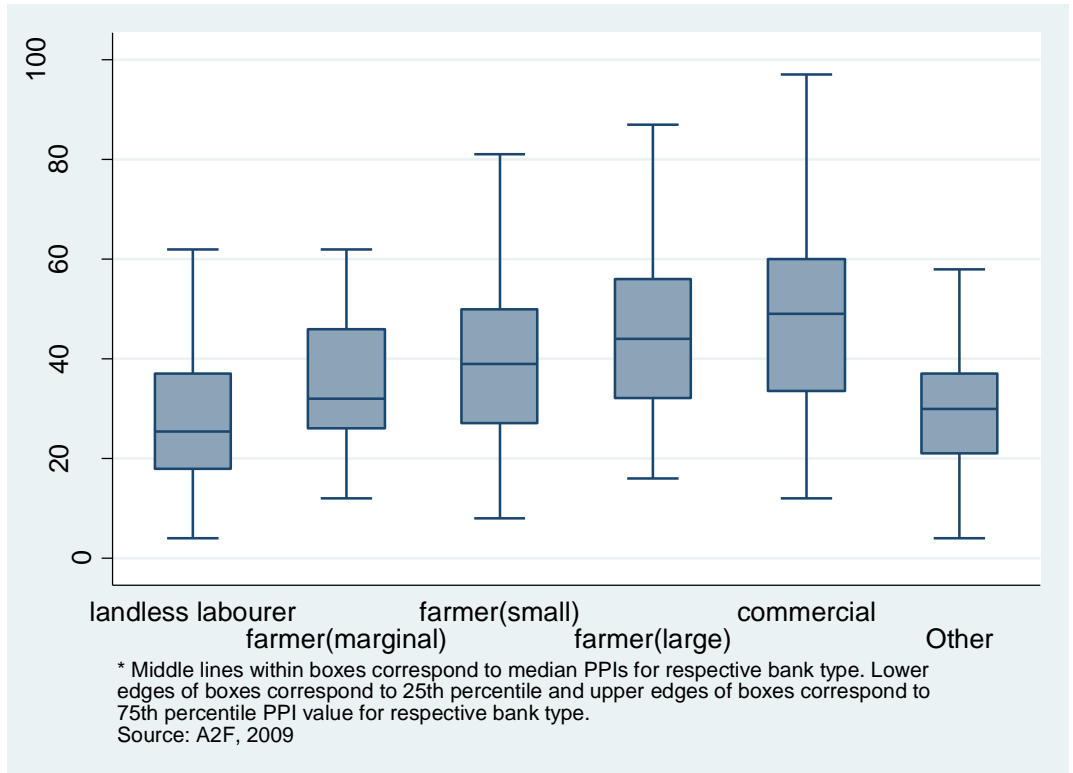
Households were assigned to one of five occupational categories and the residual category “other” based on the rules described below. Please note that the definitions used to determine occupational categories, especially the distinction between marginal, small, and large farmers, varies by context and that the definitions used here may not match those used by other researchers or government agencies. (In particular, the definitions used here do not match the definitions used to determine eligibility for the recent loan waiver.)

### **Rules for how occupational categories were assigned**

- If agriculture on land owned by the household was one of the household’s two main sources of income the household was classified as a farming household.
- Farming households owning less than one acre of land were classified as marginal farmers. Farming households owning between one and four acres of land were classified as small farmers. Farming households owning more than four acres of land were classified as large farmers.
- Non-farming households which relied on salaried employment or an own business as one of the household’s two main sources of income were classified as commercial.
- Non-farming, non-commercial households which relied on wage labour (either via agriculture, as a coolie, or in NREGA) as one of the household’s two main sources of income were classified as landless labourers.

- All households not falling into any of the categories above were classified as other.

**Figure 21: Progress out of Poverty Scores by Occupational Category**



## Appendix D – Five Most Frequently Cited Reasons for Not Availing a Loan by Lender Type

**Table 21: Top 5 Reasons for Not Availing a Loan from a Formal Source**

<b>Reason</b>	<b>Share</b>
Have no idea about these sources or their products	19.4%
Lack of land	12.7%
Already had or could get loan from another source	12.2%
Lack of guarantor	10.8%
Application rejected	10.6%

Source: A2F, 2009

**Table 22: Top 5 Reasons for Not Availing a Loan from a JLG**

<b>Reason</b>	<b>Share</b>
Irregular income flows or repayment capacity	60.0%
No JLGs are close enough to join	24.3%
Have no idea about JLGs or how they function	18.5%
Can't save regularly	11.7%
Don't know any JLGs or members	6.3%

Source: A2F, 2009

**Table 23: Top 5 Reasons for Not Availing a Loan from a SHG**

<b>Reason</b>	<b>Share</b>
Irregular income flows or repayment capacity	28.5%
Can't save regularly	10.4%
Tried but was unable to join	9.2%
Don't want group conflict	8.5%
Have no idea about SHGs or how they function	5.1%

Source: A2F, 2009

**Table 24: Top 5 Reasons for Not Availing a Loan from an Informal Source**

<b>Reason</b>	<b>Share</b>
Irregular Income Flows/ Repayment capacity	44.6%
No need	15.2%
Already had or could get a loan with other source	12.9%
Interest rates are too high	6.7%
After cultivation	6.6%

Source: A2F, 2009

**Table 25: Top 5 Reasons for Not Availing a Loan from a Chit Fund**

<b>Reason</b>	<b>Share</b>
Irregular income or repayment capacity	71.2%
Can't save regularly	15.9%
No chit funds close enough to join	13.9%
No idea about what chit funds are or how they work	9.2%
Not trustworthy	2.8%

Source: A2F, 2009

## **Appendix E – Interpreting Progress Out of Poverty Index Scores**

PPI scores were calculated using the India Poverty Scorecard designed by Mark Schreiner. The Poverty Scorecard is a proxy survey which estimates the likelihood of a household's being under a given poverty line (in our case, we use India's National Poverty Line). The scorecard was created using data from Round 62 data of the National Sample Survey Organization's (NSSO) India Socio-Economic Survey. The table below lists the likelihood of being under the poverty line for the specified PPI ranking.

**Table 26: PPI Ranges and Corresponding Likelihood of Falling below Poverty Line**

<b>PPI</b>	<b>Likelihood of Being below National Poverty Line</b>
0-4	77.0%
5-9	58.5%
10-14	51.2%
15-19	35.5%
20-24	28.7%
25-29	21.3%
30-34	18.9%
35-39	14.9%
40-44	10.0%
45-49	4.5%
50-54	5.1%
55-59	5.7%
60-64	6.1%
65-69	3.7%
70-74	1.5%
75-79	1.6%
80-84	0.7%
85-89	1.2%
90-94	0.0%
95-100	0.0%

Source: [www.progressoutofpoverty.org](http://www.progressoutofpoverty.org)