Role of SHGs in Socio-Economic Development

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Abstract

This research is undertaken to identify the role of microfinance in the economic welfare of beneficiaries like individuals and self-help groups. The outcome of the analysis shows that demographics ages, gender, income, are dependent in determining the role of microfinance. The study has been undertaken in areas of Jaipur (Mansarover, Jhalanadungri, Sanganer). The primary data is collected of 60 data points. Analysis has been done on the basis of Correlation methodology & various simple quantitative methodologies. The finding of the research favors the impact of microfinance in economic growth and sustenance of individuals and groups.

Keywords: Microfinance, microcredit, self help groups.

Introduction

Microfinance is defined as any activity that includes the provision of financial services such as credit, savings, and insurance to low income individuals which fall just above the nationally defined poverty line, and poor individuals which fall below that poverty line, with the goal of creating social value. The creation of social value includes poverty alleviation and the broader impact of improving livelihood opportunities through the provision of capital for micro enterprise, and insurance and savings for risk mitigation and consumption smoothing. A large variety of actors provide microfinance in India, using a range of microfinance delivery methods. Since the ICICI Bank in India, various actors have endeavored to provide access to financial services to the poor in creative ways. Governments also have piloted national programs, NGOs have undertaken the activity of raising donor funds for on-lending, and some banks have partnered with public organizations or made small inroads themselves in providing such services. This has resulted in a rather broad definition of microfinance as any activity that targets poor and low-income individuals for the provision of financial services. The range of activities undertaken in microfinance include group lending, individual lending, the provision of savings and insurance, capacity building, and agricultural business development services. Whatever the form of activity however, the overarching goal that unifies all actors in the provision of microfinance is the creation of social value. Microfinance started with the recognition that poor people had the capability to lift themselves out of poverty if they had access to affordable loans. High repayment rates in the industry have changed the perception that the poor are not credit worthy. With the right opportunities, the poor have proved themselves to be productive and capable of borrowing, saving and repaying, even without collateral.

According to International Labor Organization (ILO), "*Microfinance is an economic development approach that involves providing financial services through institutions to low income clients*".

In India, Microfinance has been defined by "The National Microfinance Taskforce, 1999" as "*provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi-urban or urban areas for enabling them to raise their income levels and improve living standards*".

"The poor stay poor, not because they are lazy but because they have no access to capital."

Traditionally micro finance was focused on providing a very standardized credit product. The poor, just like anyone else, need a diverse range of financial instruments to be able to build assets, stabilize consumption and protect themselves against risks. Thus, we see a broadening of the concept of micro finance, our current challenge is to find efficient and reliable ways of providing a richer menu of micro finance products. Micro finance is not merely extending credit but extending credit to those who require most for them and family survival. How credit availed is used to survive and grow with limited means.

The typical micro finance clients are low-income persons that do not have access to formal financial institutions. Micro finance clients are typically self-employed, often household-based entrepreneurs. In rural areas, they are usually small farmers and others who are engaged in small income-generating activities such as food processing and petty trade. In urban areas, micro finance activities are more diverse and include shopkeepers, service providers, artisans, street vendors, etc. Micro finance clients are poor and vulnerable non-poor who have a relatively unstable source of income.

Access to conventional formal financial institutions, for many reasons, is inversely related to income: the poorer you are the less likely that you have access. On the other hand, the chances are that, the poorer you are, the more expensive or onerous informal financial arrangements. Moreover, informal arrangements may not suitably meet certain financial service needs or may exclude you anyway. Individuals in this excluded and under-served market segment are the clients of micro finance.

As we broaden the notion of the types of services micro finance encompasses, the potential market of micro finance clients also expands. It depends on local conditions and political climate, activeness of cooperatives, SHG & NGOs and support mechanism. For instance, micro credit might have a far more limited market scope than say a more diversified range of financial services, which includes various types of savings products, payment and remittance services, and various insurance products. For example, many very poor farmers may not really wish to borrow, but rather, would like a safer place to save the proceeds from their harvest as these are consumed over several months by the requirements of daily living. Central government in India has established a strong & extensive link between NABARD (National Bank for Agriculture & Rural Development), State Cooperative Bank, District Cooperative Banks, Primary Agriculture & Marketing Societies at national, state, district and village level.

Due to the sheer size of the population living in poverty, India is strategically significant in the global efforts to alleviate poverty and to achieve the Millennium Development Goal of halving the world’s poverty by 2015. Microfinance has been present in India in one form or another since the 1970s and is now widely accepted as an effective poverty alleviation strategy. Over the last five years, the microfinance industry has achieved significant growth in part due to the participation of commercial banks. Despite this growth, the poverty situation in India continues to be challenging.

Some principles that summarize a century and a half of development practice were encapsulated in 2004 by Consultative Group to Assist the Poor (CGAP) and endorsed by the Group of Eight leaders at the G8 Summit on June 10, 2004:

- Poor people need not just loans but also savings, insurance and money transfer services.

- Microfinance must be useful to poor households: helping them raise income, build up assets and/or cushion themselves against external shocks.
- "Microfinance can pay for itself." Subsidies from donors and government are scarce and uncertain, and so to reach large numbers of poor people, microfinance must pay for itself.
- Microfinance means building permanent local institutions.
- Microfinance also means integrating the financial needs of poor people into a country's mainstream financial system.
- "The job of government is to enable financial services, not to provide them."
- "Donor funds should complement private capital, not compete with it."
- "The key bottleneck is the shortage of strong institutions and managers." Donors should focus on capacity building.
- Interest rate ceilings hurt poor people by preventing microfinance institutions from covering their costs, which chokes off the supply of credit.
- Microfinance institutions should measure and disclose their performance – both financially and socially.

Microfinance can also be distinguished from charity. It is better to provide grants to families who are destitute, or so poor they are unlikely to be able to generate the cash flow required to repay a loan. This situation can occur for example, in a war zone or after a natural disaster.

Review of Literature

In developing economies and particularly in the rural areas, many activities that would be classified in the developed world as financial are not monetized: that is, money is not used to carry them out. Almost by definition, poor people have very little money. But circumstances often arise in their lives in which they need money or the things money can buy.

In Stuart Rutherford's recent book *The Poor and Their Money*, he cites several types of needs:

- *Lifecycle Needs*: such as weddings, funerals, childbirth, education, homebuilding, widowhood, old age.
- *Personal Emergencies*: such as sickness, injury, unemployment, theft, harassment or death.
- *Disasters*: such as fires, floods, cyclones and man-made events like war or bulldozing of dwellings.
- *Investment Opportunities*: expanding a business, buying land or equipment, improving housing, securing a job (which often requires paying a large bribe), etc.

Poor people find creative and often collaborative ways to meet these needs, primarily through creating and exchanging different forms of non-cash value. Common substitutes for cash vary from country to country but typically include livestock, grains, jewellery and precious metals.

As Marguerite Robinson describes in The Microfinance Revolution, the 1980s demonstrated that “microfinance could provide large-scale outreach profitably,” and in the 1990s, “microfinance began to develop as an industry”. In the 2000s, the microfinance industry’s objective is to satisfy the unmet demand on a much larger scale, and to play a role in reducing poverty. While much progress has been made in developing a viable, commercial microfinance sector in the last few decades, several issues remain that need to be addressed before the industry will be able to satisfy massive worldwide demand.

The obstacles or challenges to building a sound commercial microfinance industry include:

- Inappropriate donor subsidies
- Poor regulation and supervision of deposit-taking MFIs
- Few MFIs that mobilize savings
- Limited management capacity in MFIs
- Institutional inefficiencies
- Need for more dissemination and adoption of rural, agricultural microfinance methodologies

The micro credit of microfinance program was first initiated in the year 1976 in Bangladesh with promise of providing credit to the poor without collateral, alleviating poverty and unleashing human creativity and endeavor of the poor people. Microfinance impact studies have demonstrated that

- Microfinance helps poor households meet basic needs and protects them against risks.
- The use of financial services by low-income households leads to improvements in household economic welfare and enterprise stability and growth.
- By supporting women economic participation, microfinance empowers women, thereby promoting gender-equity and improving household well being.
- The level of impact relates to the length of time clients have had access to financial services.

Although neither of the terms microcredit or microfinance were used in the academic literature nor by development aid practitioners before the 1980s or 1990s, respectively, the concept of providing financial services to low income people is much older.

While the emergence of informal financial institutions in Nigeria dates back to the 15^{th} century, they were first established in Europe during the 18th century as a response to the enormous increase in poverty since the end of the extended European wars (1618 – 1648). In 1720 the first loan fund targeting poor people was founded in Ireland by the author Jonathan Swift. After a special law was passed in 1823, which allowed charity institutions to become formal financial intermediaries a loan fund board was established in 1836 and a big boom was initiated. Their outreach peaked just before the government introduced a cap on interest rates in 1843. At this time, they provided financial services to almost 20% of Irish households. The credit cooperatives created in Germany in 1847 by Friedrich Wilhelm Raiffeisen served 1.4 million people by 1910. He stated that the main objectives of these cooperatives “should be to control the use made of money for economic improvements, and to improve the moral and physical values of people and also, their will to act by themselves.”

In the 1880s the British controlled government of Madras in South India, tried to use the German experience to address poverty which resulted in more than nine million poor Indians belonging to credit cooperatives by 1946. During this same time the Dutch colonial administrators constructed a cooperative rural banking system in Indonesia based on the Raiffeisen model which eventually became Bank Rakyat Indonesia (BRI), now known as the largest MFI in the world.

Micro financing institutions significantly contributed to gender equality and women's empowerment as well as poor development and civil society strengthening. Contribution to women's ability to earn an income led to their economic empowerment, increased well being of women and their families and wider social and political empowerment.

Microfinance programs targeting women became a major plank of poverty alleviation and gender strategies in the 1990s. Increasing evidence of the centrality of gender equality to poverty reduction and women's higher credit repayment rates led to a general consensus on the desirability of targeting women.

Self Help Groups (SHGs)

Self- help groups (SHGs) play today a major role in poverty alleviation in rural India. A growing number of poor people (mostly women) in various parts of India are members of SHGs and actively engage in savings and credit (S/C), as well as in other activities (income generation, natural resources management, literacy, child care and nutrition, etc.). The S/C focus in the SHG is the most prominent element and offers a chance to create some control over capital, albeit in very small amounts. The SHG system has proven to be very relevant and effective in offering women the possibility to break gradually away from exploitation and isolation.

How self-help groups work

NABARD (1997) defines SHGs as "small, economically homogenous affinity groups of rural poor, voluntarily formed to save and mutually contribute to a common fund to be lent to its members as per the group members' decision".

Most SHGs in India have 10 to 25 members, who can be either only men, or only women, or only youth, or a mix of these. As women's SHGs or sangha have been promoted by a wide range of government and non- governmental agencies, they now make up 90% of all SHGs.

The rules and regulations of SHGs vary according to the preferences of the members and those facilitating their formation. A common characteristic of the groups is that they meet regularly (typically once per week or once per fortnight) to collect the savings from members, decide to which member to give a loan, discuss joint activities (such as training, running of a communal business, etc.), and to mitigate any conflicts that might arise. Most SHGs have an elected chairperson, a deputy, a treasurer, and sometimes other office holders.

Most SHGs start without any external financial capital by saving regular contributions by the members. These contributions can be very small (e.g. 10 Rs per week). After a period of consistent savings (e.g. 6 months to one year) the SHGs start to give loans from savings in the form of small internal loans for micro enterprise activities and consumption. Only those SHGs that have utilized their own funds well are assisted with external funds through linkages with banks and other financial intermediaries.

However, it is generally accepted that SHGs often do not include the poorest of the poor, for reasons such as:

(a) Social factors (the poorest are often those who are socially marginalized because of caste affiliation and those who are most skeptical of the potential benefits of collective action).

(b) Economic factors (the poorest often do not have the financial resources to contribute to the savings and pay membership fees; they are often the ones who migrate during the lean season, thus making group membership difficult).

(c) Intrinsic biases of the implementing organizations (as the poorest of the poor are the most difficult to reach and motivate, implementing agencies tend to leave them out, preferring to focus on the next wealth category).

Sources of capital and links between SHGs and Banks

SHGs can only fulfill a role in the rural economy if group members have access to financial capital and markets for their products and services. While the groups initially generate their own savings through thrift (whereby thrift implies savings created by postponing almost necessary consumption, while savings imply the existence of surplus wealth), their aim is often to link up with financial institutions in order to obtain further loans for investments in rural enterprises. NGOs and banks are giving loans to SHGs either as "matching loans" (whereas the loan amount is proportionate to the group's savings) or as fixed amounts, depending on the group's record of repayment, recommendations by group facilitators, collaterals provided, etc.

How SHGs save

Self-help groups mobilize savings from their members, and may then on-lend these funds to one another, usually at apparently high rates of interest which reflect the members’ understanding of the high returns they can earn on the small sums invested in their micro-enterprises, and the even higher cost of funds from money lenders. If they do not wish to use the money, they may deposit it in a bank. If the members’ need for funds exceeds the group’s accumulated savings, they may borrow from a bank or other organization, such as a micro-finance non-government organization, to augment their own fund.

The system is very flexible. The group aggregates the small individual saving and borrowing requirements of its members, and the bank needs only to maintain one account for the group as a single entity. The banker must assess the competence and integrity of the group as a micro-bank, but once he has done this he need not concern himself with the individual loans made by the group to its members, or the uses to which these loans are put. He can treat the group as a single customer, whose total business and transactions are probably similar in amount to the average for his normal customers, because they represent the combined banking business of some twenty ‘micro-customers’. Any bank branch can have a small or a large number of such accounts, without having to change its methods of operation.

Comparative Analysis of Micro-finance Services offered to the poor

Parameter	Money Lender	Commercial Banks	Govt. Sponsored Programs	Financial products of MFIs
Ease of Access	High	Low	Low	High
Transaction cost of Access	Low	Very High	Very High	Low – Medium
Lead time for Loans	Very Short	Extremely Long	Extremely long	Short
Repayment Terms	Fixed and Rigid	Fixed and Easy	Fixed and Easy	Flexible
Interest Rates	Exorbitantly High	Low and very Affordable	Low, Affordable and Subsidised	Reasonable and Affordable
Incentives	None	None	None	Repeat and larger loans, Interest Rebates
Repeat Borrowing	Possible	Possible but not likely	Possible but not likely	Stream of credit is assured
Loan Access Procedures	Very Quick	Extremely Time Consuming and complicated	Extremely Time Consuming and complicated	Simple and Quick
Loan Application Procedures	Informal but exploitative	Exhaustive and Complex	Exhaustive and Complex	Simple and Informal
Collateral and Demand Promissory Note	Mandatory	Required but hypothecation of asset may suffice	Not required although a charge on the asset becomes automatic	Not required – social collateral is used for physical collateral

Source: R. Arunachalam - Alternative Technologies in the Indian Micro- finance Industry.

Research Methodology

This chapter describes the research design used in this study. This study is a based on Correlation analysis & qualitative analysis conducted to understand the Micro finance industry, how it has worked towards self sufficiency of the less resourceful people.

Hypothesis

H1: the current year income rose from previous year after taking loan from microfinance.
Test – Correlation

Sample size – 60 data heads would be collected from 3 different companies.

Company Names – SKS microfinance, Basix, Bandhan.

The study was conducted with the view to attain the given objectives:

1. To understand the theoretical framework of Micro Finance Industries.
2. To understand the need patterns of the people applying for the Micro finance.
3. To understand the development of social aspect among the poor people.
4. To see the Financial changes occur with the inception of MFI.

For obtaining the first objective, study material on MFI advisory module, various books and literature based on Microfinance were studied. Practical and real view of the objectives was attained through the observation of the company and through interaction with various types of people who have taken the Micro Loans. For doing research on second, third and fourth objectives a questionnaire based survey was being conducted in various areas of Jaipur (Mansarover, Jhalanadungri, Sanganer).

RESEARCH DESIGN

The technique used to perform the research is called the research design. In the above mentioned research, correlation type of research design has been used.

CORRELATION RESEARCH

Correlation research is used when very little is known about a given area and one has to identify reasons or facts to find solution to the given problem. Here major emphasis is given determining the general nature of the problem and the variable related to it.

Exploratory research is generally carried out by tapping two sources of information i.e.;

1. Study of secondary Sources.

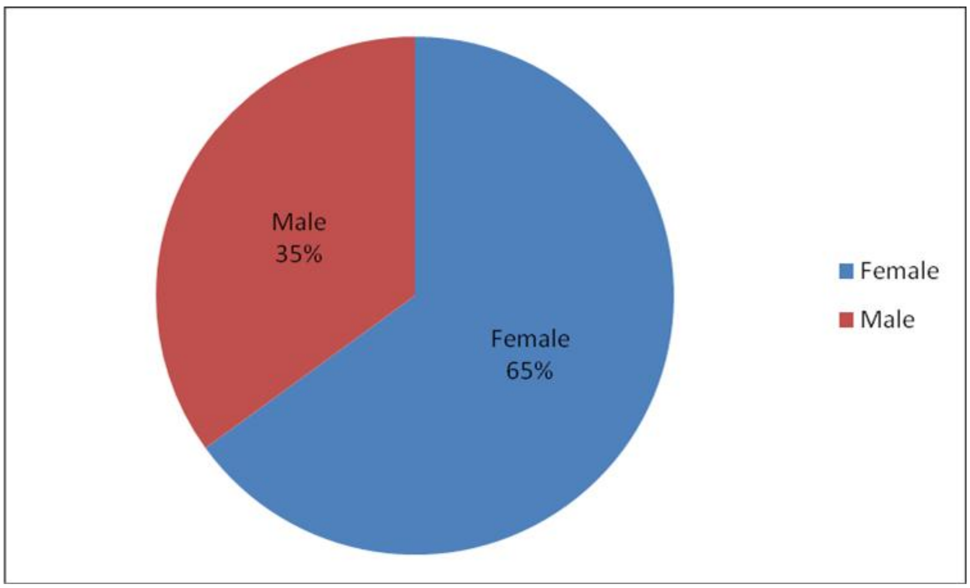
2. Discussion with individuals from Primary Sources.

DATA SOURCES

For the purpose of data collection both primary and secondary data were collected, as these two modes are necessary to give a right form of data required for the research to be done.

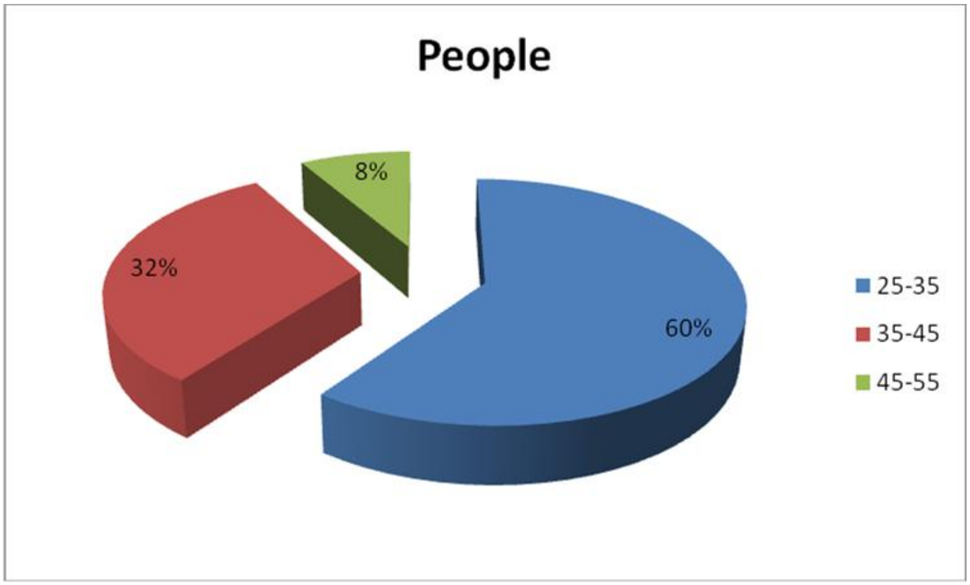
Findings

Ratio of Male & Female Applicants



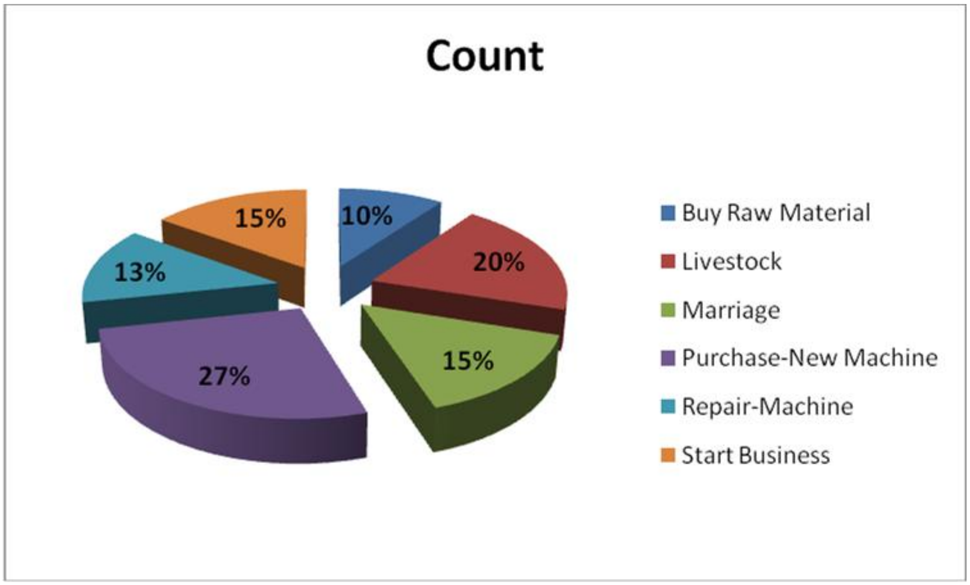
It is evident from the above pie chart that majority of the respondents 65% were Female applicants for Micro Finance Loans and the Male applicants were 35%.

Age of People Applying for Microfinance loans:-



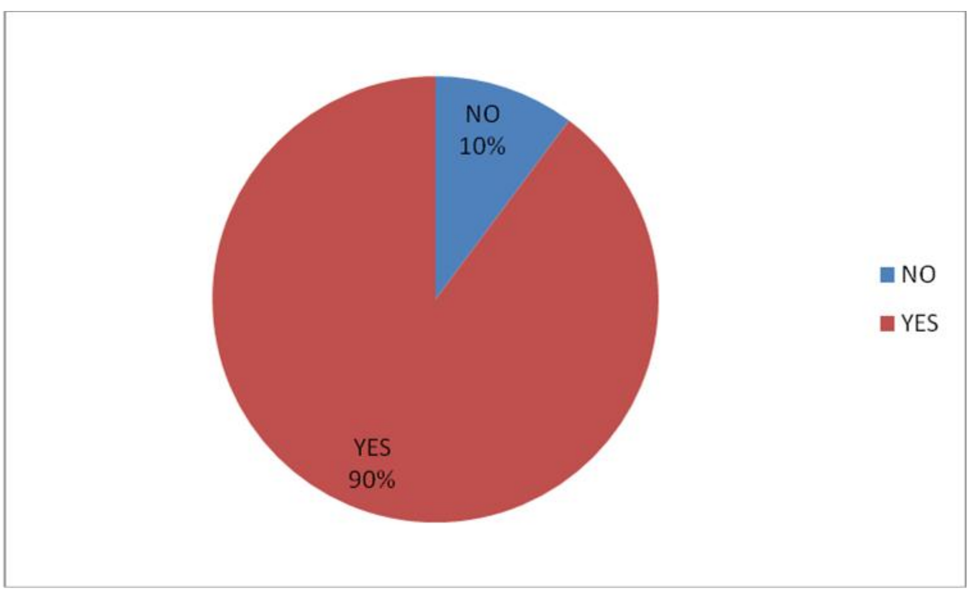
From the above Pie chart it is reflected that major percentage of the population 60% is in the age group of 25-35 yrs, and percentage of people applying for Microfinance loans in the age groups 35-45 & 45-55 remains 32%, and 8% respectively.

Major Purpose of the Micro finance Loans



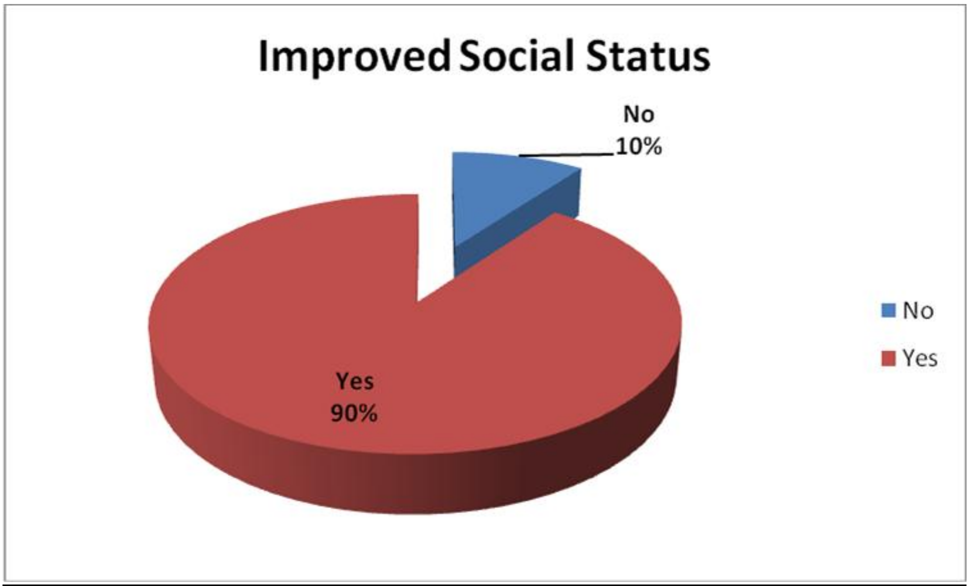
From the above mentioned pie chart the 27% of the people use Microfinance for purchase-new machine, 20 % of the people use it as a source to purchase livestock, 15% for start the Business & for marriage, 13% for the repairing of machines & 10% to buy raw material.

Payment Vs Default %



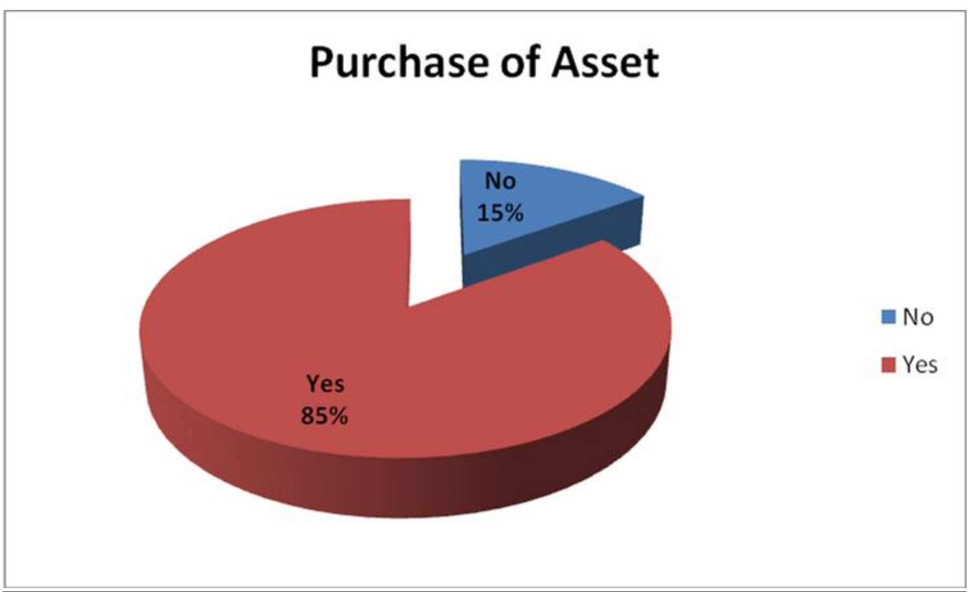
From the pie chart it has been depicted that the small creditors have a good paying capacity with just 10% defaulters and remaining 90% people pays their loan amounts on time.

Improved Social Status



From the pie chart it has been depicted that the social status for people using microfinance has risen significantly & 90% of users have improved their social status as well.

Purchase of Assets



From the pie chart above it is been shown that 85% of the users have purchased new assets for their business use or either their personal use, which shows good & improved life style.

Average Income Increase in the Population

Average	59%
STD	0.3087537

From the population sample that has been taken from the 2 different areas but from the people have the same earning limits it has been found out during the study that there has been a Significant Increase of 59% in the Earning capacity of the people as compare to the last year's data where they didn't took the loan, with the microfinance loan they have expanded their business unit and thus find a increase in their earnings.

After analyzing via correlation these two things have significant relation – Current year income(after using microfinance) v/s previous year income.

H1 : the current year income rose from previous year after taking loan from microfinance.

Correlations			
		Annual Income Current Year	Annual Income Previous Year
Annual Income Current Year	Pearson Correlation	1	0.864464884
	Sig. (2-tailed)		0.02
	N	61	61

The hypothesis is accepted and the current year income has increased significantly.

Conclusion

The analysis made in this study with the help of primary data has brought out many salient features about the changes in the social and economic aspects of the sample respondents who are the members in SHG. It is clear that the SHG plays a pivotal role in enhancing the both social and economic lives of the members, bring them more respect both domestically and socially. The sample respondents who were either unemployed or engaged in petty activities during their pre-member period, have become very active by becoming full employed in varied activities and thereby earning more. This has been proved even scientifically with the help of analysis. Hence, it can be concluded that the self help groups contribute substantially in pushing the conditions of the female population up and through that chip in poverty eradication as well.

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