

# **GRAMEEN BANK GROUPS AND SELF-HELP GROUPS; WHAT ARE THE DIFFERENCES?**

Malcolm Harper

## **1. INTRODUCTION**

Most micro-finance institutions (MFI) use some sort of group system to distribute their services to their clients. There are some exceptions, including the Village Unit system of BRI in Indonesia, the world's biggest and most profitable MFI, but groups seem generally to predominate. Many otherwise well informed observers and even some senior bankers in India and elsewhere, appear to believe that the group system pioneered in 1976 by the Grameen Bank in Bangladesh is the predominant or even the only such system. One purpose of this paper is to show that this is not the case. Both systems have their advantages and disadvantages, and practitioners need to be aware of the options that are available. We shall attempt in what follows to describe and explain each system, and to compare their sustainability, their outreach and impact on the poor and their institutional feasibility. Our arguments are briefly summarised in the table which follows the text.

There are two very different ways of using groups for financial intermediation. One is the Bangladesh Grameen Bank method, which we shall for convenience refer to as the Grameen system, and the other is the so-called Self Help Group, or SHG, system. There are many variants of each system, and they are often referred to as the 'solidarity group', and the 'village banking' systems. We shall, however, use the terms 'Grameen' and 'SHG', since these are more familiar in the South Asian context.

Both systems are dominated by female clients, but they differ in many other fundamental respects, which have important implications for their clients and for the institutions which offer them. The systems are also implemented in many different ways, depending on local circumstances. The fundamental characteristics of each system, and the critical differences between them, are briefly described below. Further more detailed accounts of each system can be obtained from a number of sources, including Fugelsang and Chandler, Wahid, Holcombe and Harper 1998.

### **1.1 The Grameen system**

Potential clients are asked by the MFI to organise themselves into 'Groups' of five members which are in turn organised into 'Centres' of around five to seven such Groups. The members make regular savings with the MFI, according to a fixed compulsory schedule, and they also take regular loans. They each have individual savings and loan accounts with the MFI, and the main function of the Groups and Centres are to facilitate the financial intermediation process, through performing tasks such as:

- holding regular and usually weekly meetings which are supervised by a MFI worker who maintains the records, where savings and repayments are collected and handed over to the MFI worker,
- organising contributions to one or a number of group savings funds, which can be used by the group for a number of purposes, usually only with the agreement of the MFI which maintains the group fund accounts,
- guaranteeing loans to their individual members, by accepting joint and several liability, by raising group emergency funds and by accepting that no members of a Group will be able to take a new loan if any members are in arrears,
- arising from the above, appraising fellow-members' loan applications, and ensuring that their fellow-members maintain their regular savings contributions and loan repayments.

## **1.2 The SHG system**

The members form a group of around twenty members. The group formation process may be facilitated by an NGO or by the MFI or bank itself, or it may evolve from a traditional rotating savings and credit group (ROSCA) or other locally initiated grouping. The process of formal 'linkage' to an MFI or bank usually goes through the following stages, which may be spread over many years or which may take place within a few months.

- The SHG members decide to make regular savings contributions. These may be kept by their elected head, in cash, or in kind, or they may be banked.
- The members start to borrow individually from the SHG, for purposes, on terms and at interest rates decided by the group themselves.
- The SHG opens a savings account, in the group's name, with the bank or MFI, for such funds as may not be needed by members, or in order to qualify for a loan from the bank.
- The bank or MFI makes a loan to the SHG, in the name of the Group, which is then used by the Group to supplement its own funds for on-lending to its members.

The SHG need never go through all these stages; it may satisfy its members' needs quite effectively if it only goes to the second or even to the first stage, saving money and possibly not even withdrawing it (Harper M 2000, pp. 39-42).

The SHG carries out all the same functions as those required by the Grameen system, but they do this on their own behalf, since the SHG is effectively a micro-bank, carrying out all the familiar intermediation tasks of savings mobilisation and lending. The MFI or bank may assist the SHG in record keeping, and they may also demand to know who are the members and impose certain conditions as to the uses of the loan which they make to the SHG, but the SHG is an autonomous financial institution in its own right.

The members have their accounts with the SHG, not with the MFI or bank, and the MFI or bank does not have any direct dealings with the members.

## **2. WHERE, BY WHOM AND WHY ARE THE TWO SYSTEMS USED?**

### **2.1 The Grameen System**

The Grameen system dominates the market in Bangladesh, where it has been widely imitated by a number of large and small MFI. The system was pioneered by Professor Yunus in 1976, and has grown very rapidly since.

In addition to the originator, the Grameen Bank, with 2.2 million members, two other major users of the system, BRAC and Proshika, each have over a million clients, and there were in 1998 some thirty other MFIs with over 10,000 members, and many hundreds of other smaller organisations (CDF 1998). It has been estimated that some ten million people in Bangladesh receive financial services through this system. It has also been widely replicated by MFIs elsewhere, including a small number in India and in more than twenty other countries in Asia, in Africa, Latin America and also in disadvantaged rural and urban areas in North America and Europe. The Grameen Trust supports 'replicators' with funding and technical assistance; at the end of 1999, these replicators had 420,000 clients, including about 42,000 in India (Grameen Trust, *passim*)

Low or no-cost foreign donations represent the largest source of on-lending funds for the large MFI which use the Grameen system in Bangladesh, but members' savings and the accumulated surplus from operations each contribute some 20% of the necessary funds. The interest rates vary, and it is difficult to estimate the actual rates because there are a number of fees, forced savings requirements and other charges, and the methods of calculation also differ from one institution to another. Broadly speaking, the cost to the final borrowers amounts to at least 2% per month, and often substantially more.

The Grameen system requires a dedicated special purpose organisation. The success of the weekly or occasionally fortnightly or monthly meeting routine depends on tight discipline and adherence to a regular schedule, and it is difficult for a commercial bank which also has other financial products to integrate the Grameen system into its own operations. One of the few institutions which have done this is the Islami Bank of Bangladesh. By 1998 45 of its more than 100 branches had financed over 12,000 people through groups and centres, more or less following the Grameen system (Alamgir, pp. 72-75). One important difference, however, is that this is an Islamic Bank; most of its credit is disbursed in kind, and the Bank is far more intimately involved in its clients' use of their finance than Western style banks. Although loans under the group system amounted to only about a quarter of one per cent of its total portfolio in 1998, the Islami Bank intended massively to expand this approach.

### **2.2. The SHG System**

The SHG system is mainly found in India, where it is used by both MFIs and banks. There also some important users in Indonesia, parts of South East Asia, Africa and elsewhere. The SHG system in India was initiated by NGOs, and is used for financial intermediation both by commercial banks and by MFIs. By April 2001 some 285,000

SHGs had taken loans from 41 Indian commercial banks, 166 regional rural banks and 111 co-operative banks. The average loan per group was about Rs 18,000 and the average loan per member was Rs 1,100, or just under twenty five dollars. During the year 2000/2001 171,000 SHGs took loans, of which 149,000 were first time borrowers. (NABARD, Micro-credit Innovations Department, personal communication).

The average membership is around seventeen people per SHG, so these figures mean that about four and a half million people in India have access to formal savings facilities and loans through their SHG membership. In just one year, the number of new members was in excess of two and a half million people, or well over the total membership of even the largest institutions in Bangladesh.

The formation of SHGs for savings and credit, and their linkage to commercial banks, was initiated in India by MYRADA in the mid-1980s (Fernandez 1998). NABARD management had around the same time had some exposure to similar experiences in Thailand and Indonesia, and they responded favourably to MYRADA's suggestion that this could be a useful way to bring formal financial services to the rural poor.

Since that time, SHG linkage has been vigorously promoted by NABARD and other institutions. It generally involves two institutions. Most NGOs do not play any financial role. They promote and train the groups, and assist them through the qualifying process of saving and internal lending. The groups are introduced to a bank to open a savings account, and later to take a loan. The NGO may remain heavily involved, assisting the members to manage their affairs, and possibly promoting higher level clusters and federations of SHGs, or it may withdraw and work with other groups.

Other NGOs also act as financial intermediaries by borrowing from NABARD or elsewhere and on-lending to SHGs, either because they aim to become MFIs, or because this is often the only way by which the groups could access finance, because many bankers refused to lend to SHGs directly, or even to open savings accounts for them. The financial margin on this business is however insufficient to cover more than a small part of the transaction costs. Over a third of the 'linked' SHGs borrowed from MFIs rather than from banks in 1998, but this proportion dropped to a quarter in 1999 and is rapidly decreasing further as banks become more aware of the business opportunity represented by SHGs (NABARD, 1998, 1999).

In addition to paying the cost of training the bankers and the staff of the NGOs, NABARD also encourages the banks to lend to SHGs by refinancing the loans at the subsidised rate of six and a half per cent. This subsidised refinance was used to finance 83% of the loans made to SHGs in the year 2000/2001. (NABARD, MCID, *ibid.*) Loans to SHGs are excluded from the maximum interest ceiling of 12% which still applies to other loans under Rs. 20,000 (RBI 2000), but the banks have generally not taken advantage of this freedom, and most still lend to SHGs at about 12%. The resulting 5.5% spread is felt to be enough to cover the transaction costs so long as the SHG promotion, training and development task has been carried out by an NGO, at no cost to the bank.

The on-time repayment rates on SHG loans are usually well over 95%. This is so much higher than the normal performance of loans granted under government 'schemes' to poorer people that the banks are generally satisfied with this form of intermediation, even if the spread is less than that which they usually obtain. The SHG members are free to charge themselves whatever rates of interest they chose; the annual rates can range from 12% to 60% per year (Harper et al, 1998, p.76).

There is also a large and increasing number of MFIs in India, most of which use the SHG method. A small number of these MFIs use the Grameen system, but the portfolio of the approximately thirty-five larger MFIs which use the SHG system, and are doing business with the recently established SIDBI Foundation for Micro-credit (SFMC), amounts to almost around 85 crores of rupees or thirteen million dollars. These MFIs were said in early 2001 to be serving about 200,000 eventual clients, of whom 94% are women. (SFMC, personal communication). By contrast, the total number of people in India served by the eighteen institutions using the Grameen system at the end of 1999 was approximately fifty thousand. (Grameen Trust, 2000, pp. 72-78).

NABARD forecast in early 2001 that by 2008 about one million SHGs would be taking loans from banks, with a total membership of around seventeen million people. This estimate was based on a forecast of 50,000 SHGs taking loans in 2001-2002, rising to a rate of 110,000 per year from 2005 onwards. In the event, 149,000 new SHGs took loans in the financial year ending 31.3.2001, so that these forecasts may be well below what is actually achieved. In terms of membership numbers, using the same average of 17 members per group, this amounts to an addition in just one year of almost three million clients, or well over the total membership of any of the Bangladesh institutions. This has been achieved by effective collaboration between the banks, NGOs, MFIs and NABARD, with the necessary recognition and authority from the Reserve Bank. There are as yet no 'giant' institutions on the Bangladesh model, nor perhaps will there ever be; the SHG system reflects the scale, and the institutional diversity, of the Indian financial system.

SFMC for their part anticipate that by 2009 their partner MFIs will be serving 1.3 million clients. SHARE of Andhra Pradesh, the largest user of the Grameen system in India, projects that it will be reaching over 1.7 million women by early 2006.

If these figures are even remotely realistic, and actual performance suggests that they may be under-estimated, micro-finance in India has finally reached 'take-off'. Estimates of the numbers of people below the poverty line vary quite widely, but the figure of 40% of the population is quite commonly accepted. This amounts to 400 million people, or some 80 million households. It is unusual at the present time for more than one member of a household to be an SHG member. If the NABARD and SFMC forecasts are fulfilled, and if the present growth in the numbers of poor people does not accelerate, over a quarter of the poorer Indian households will by 2009 have access to formal financial services. The vast majority, however, even if SHARE's forecasts are achieved, will still be using the SHG system.

### 2.3 Why Grameen in Bangladesh and SHGs in India?

The rural poor in India are not so different from their counterparts in Bangladesh, and the differences between Northern and Southern India, for instance, are certainly more pronounced than those between poor rural communities in West Bengal, or UP, Bihar and Orissa, from their neighbours in Bangladesh. It seems *prima facie* to be odd, therefore, that two such different systems have evolved, and that there are, as yet at any rate, so few examples of the SHG system in Bangladesh or of the Grameen system in India.

There are a number of possible explanations. None of them is probably sufficient on its own, but they may together account for the present situation.

Bangladesh has less experience of any form of democracy than India; its people are used to military governments, and may for that or other reasons be more disciplined and less individualist. The Grameen system is often criticised for being over-disciplined, or even militarist, with its tradition of saluting, of meetings with imposed seating systems and the necessity for strict adherence to pre-set schedules, by staff and members alike. It may, for that reason, be more acceptable in Bangladesh. In India, on the other hand, many NGOs see credit as an entry point for wider goals. Fernandez (2001, p. 6-7), for instance, mentions credit only as the third aspect of MYRADA's involvement in SHG promotion; the identification and strengthening of traditional, social and institutional capital are given greater emphasis.

Early experiments with formal micro-finance began in the late 1970s in both countries, without any initial donor assistance. Micro-finance has however been largely a donor-driven phenomenon, everywhere, and the Grameen system was and indeed still is lavishly supported by donors in Bangladesh. It was and indeed still is an ideal channel for donor assistance, since it is relatively standardised and transferable, it is dominated by a few large institutions, it depends mainly on subsidised funds and is more or less totally independent of existing local banks. Development aid to India was \$1.90 per head of the population in 1985, and was at the same level in 1997. The equivalent figures for Bangladesh were \$11.40 and \$9.00 (World Development Reports, 1987 and 1999). This difference may in itself account in part for the predominance of the Grameen system in Bangladesh.

Bangladeshi village communities are generally more socially and economically homogeneous and less divided by caste, than their Hindu equivalents in India. It may therefore be easier in Bangladesh to persuade people to join together in groups and centres which follow a standardised system. The freer and more flexible SHG system may be more appropriate for the Indian situation. However, neither of the two main exponents of the Grameen system in India, SHARE in Andhra Pradesh and neighbouring states, and the much newer Cashpor in Eastern UP, have reported any particular difficulty in introducing the system in India. Generalisations are dangerous, since India is more diverse than many continents and the differences between or even within States are often greater than between other neighbouring countries.

Bank workers in the Grameen system visit every group, every week. Experiments with less frequent meetings have generally not been successful. The banker or NGO field worker may visit the SHG members even more frequently during the initial group promotion stage, but the aim is to help the group keep their own records and run their own meetings. Once this has been achieved, there is no further need for weekly or even monthly visits. Clearly, the Grameen system is better suited for more densely populated areas. There are parts of India which are as densely populated as Bangladesh, and some of the Northern hill tracts, and some part of the Sundarbans, are fairly thinly populated. The population density in India is about 300 per square kilometer, whereas there are about 850 people per square kilometre in Bangladesh. It is unlikely that the Grameen system could have spread all over India as it has in Bangladesh.

The Indian banks have over 70,000 branches in rural areas, and there is a long if expensive and not particularly successful history of government-sponsored poverty alleviation programmes which have been delivered through the banking system. The Indian banks are also compelled to direct a substantial proportion of their credit to the so-called 'priority sectors' and 'weaker sections'. The SHG linkage system is ideal for banks; any branch can do business with one or a number of SHGs, without making significant changes to its operating procedures.

The SHG itself must of course be developed, but there is an increasing range of possible ways in which this can be done. If no NGO is active in the area of a given branch, the banks' staff themselves may perform this role. The Prathama Regional Rural Bank in Moradabad in UP has mobilised local farmers' clubs to form over 1100 SHG (Prathama Bank, 2000), government agencies are active in some states, and financial institutions such as Basix Finance and the Jamuna Gramina Bank are experimenting with low cost methods of promoting and training groups. As the scale of the SHG 'movement' grows, groups, or their federations, such as those promoted by Dhan Foundation or MYRADA, are themselves spreading the message, and many people observe, learn from and copy their neighbours, without any institutional intervention.

It would have been difficult, if not impossible, to introduce the SHG system in Bangladesh, where the branch coverage is much less and banking management are in general less eager and under less compulsion to identify with new ways of reaching the poor. By the same token, it can be argued, it is unnecessary to introduce the Grameen system in India, since the banking network already exists. What is needed is a system for reaching the poor which demands the minimum of institutional change, and the SHG system is just that.

More immediately, the two major apex financing institutions have also played an important part in determining which system predominates in each country. NABARD is vigorously and successfully marketing the SHG linkage system, through subsidised refinance, extensive training for bankers and for NGOs, and through exhortation. During the financial year 2000/2001, for example, NABARD organised 3200 training courses on SHG linkage, with 166,000 participants (NABARD MCID, *ibid.*). This single-product approach inevitably imposes some uniformity, and there has also been some question as

to whether institutions which use the Grameen system are eligible for NABARD refinance at all.

In Bangladesh, the PKSF wholesale fund, which provides almost 20% of the on-lending finance to the country's MFI (CDF, p. iv) has set criteria for its partner institutions which effectively debar institutions which do not follow some variant of what we have called the Grameen system (Alamgir p.90). Institutional inflexibility may in both countries have played some part in determining which systems are used.

### **3. "SUSTAINABILITY"**

One of the main reasons for the popularity of micro-finance as a poverty alleviation tool is that it is believed that MFI can eventually become 'sustainable'. This term has many meanings, ranging from continuing ability to find and retain donors, to ability to cover all costs including the cost of finance, the reduction in fund value caused by inflation and even a return on the investors' equity.

Donors appear willing to continue to extend large sums of money to cover the costs, and the funding needs, of micro-finance, even when this actually inhibits the development of unsubsidised financial institutions serving the poor. Nevertheless, financial services for the poor must eventually cease to depend on subsidy. Only then will it be possible for all the people who need such services to receive them, and to continue to do so for as long as is required. We must therefore attempt to compare the 'sustainability' of the two systems.

The recent M-Cril Report contains information for 10 MFIs which use the Grameen system, three of which operate in India, and 31 using the SHG system, all of which are Indian. Much of the data is unfortunately not comparable, because the Grameen users are on average much older, and much larger. The differences in their scale and maturity conceal many of those that might arise from distinctions between the two systems. The figures do show, however, the critical difference between the charges levied under each system. The average yield on the Grameen portfolio is 23.7%, whereas the comparable figure for the SHG MFI is only 8.9% (M-Cril, annex table 3).

Much of this difference arises because the younger SHG institutions have large sums of un-lent funds on deposit, and because they are wholesaling funds to the SHGs which perform the retail function. Nevertheless, the figures do show that the Grameen system has to take a much larger proportion of the money out of the hands of its clients, to cover its higher staff costs. The SHG system does leave more money with the communities, but, like any retailer, they do have to perform more of the transaction functions in return.

Two writers in the Microbanking Bulletin's issue on efficiency (pages 19 and 41) concluded that efficiency does not depend on the methodology employed. Christen, however, suggests that the 'efficiency drivers' are the average wage paid to staff, the average balance per loan and the number of clients per staff member. These variables are themselves to an extent dependent on the methodology.

The Grameen method tends to be able to use lower paid staff, since the system is rigidly structured and uniform within and even between institutions. The SHG system is more flexible; the financial institution usually has less frequent contact with the groups, once they have reached the stage of taking loans, but the assessment and guidance of an autonomous micro-bank requires a higher level of skill than is needed in the Grameen system. It needs fewer, more highly paid, staff.

The loan balances to SHGs are much higher than those to Grameen group members, because the SHG is a retailer; the amounts and balances of the loans it makes to its individual members, and also of any savings it mobilises from them, need not and usually cannot be recorded by the lending institution. Similarly, the Grameen system requires more staff per client, because the lending institution is acting as a retailer.

On the whole, therefore, the SHG system appears more likely to be associated with the two 'drivers' of high average loan balances and high numbers of clients per staff member, while the Grameen system requires less qualified and thus lower paid staff. If two drivers count for more than one, the SHG system may tend to be more 'efficient' than the Grameen system.

Ideally, we should compare the costs of two institutions serving the same numbers of clients, one of which works with SHGs and the other with the Grameen system. This is not easy; the SHG system is mainly operated by banks for which it is only one of a number of products, and it is difficult to separate out the costs of this one product. Also, and more importantly, the promotion of the groups themselves has at least until recently been usually undertaken by an NGO whose costs are not borne by the bank. Many of the bankers who have themselves developed SHGs have done this on their own initiative outside office hours, so that the costs are not recorded. In the Grameen system however, the bank itself carries out the whole operation.

The financial performance of the institutions which use the Grameen system is well documented. The Grameen Bank itself made a profit of just over one hundred million taka in 1998, before taxes and after providing some 750 million taka against bad debts (Grameen Bank, 1999). This contrasted with a figure of only 14 million taka the previous year, and it represents a low return on the total capital employed of over nineteen thousand million taka. Over half this capital was provided from concessional sources, the majority at interest rates as low as two per cent.

SHARE in India is a much younger institution, and it does not aim to reach 'financial self-sufficiency', which is microfinance language for real profitability, until 2006, long after it has become a very substantial organisation. We can only conclude that the Grameen system has not as yet proved itself to be the basis of a genuinely profitable business, which can raise capital and loan funds on a commercial basis.

The Rudrapur branch of the Oriental Bank of Commerce, near Dehra Dun, is unusual if not unique in that its only customers are SHGs; it therefore enables us to assess the

profitability of this type of customer. The SHGs have been promoted and developed by staff of the branch; no NGO has been involved so the branch's costs cover all aspects of the operation.

In March 2000 this branch had outstanding loans of about one crore (ten million) rupees, over 80% of which was funded by customers' deposits. The branch would have made a loss of just over five lakhs rupees without any subsidy, but the Bank was able to claim subsidised NABARD refinance against the loans at the rate of five and half per cent. This subsidy meant that the branch approximately broke even. The members of the SHGs agreed that their groups would have been willing and able to pay well over the 12% interest rate required by NABARD, had this been necessary. On this basis the branch would have broken even without subsidy.

It is more usual for SHGs to make up only a small proportion of a branch's business, and for the group promotion task to be undertaken by an NGO. The cost of initially developing and assessing an SHG has been variously estimated to range between about \$30 (Rs 1350) and \$355 (Rs 16,000) (Harper et al, 1998, p. 73, Fernandez 2001, pp.35-36), but experiments with dedicated SHG development agents by Basix Finance and others seem likely significantly to reduce this towards the lower end of the range. One Indian banker (Harper et al, p. 64) stated that it was actually easier and thus less expensive to appraise an SHG loan application than an ordinary loan of a similar size.

It is also possible to compare the operational costs of the two systems, by reference to the Rudrapur branch of OBC and SHARE. The costs and overheads of the Rudrapur branch amounted to seven rupees per hundred rupees lent, while the equivalent figure for SHARE in September 2000 was ten rupees. This over-simplified comparison takes no account of the level of development of the respective organisations, but it does confirm the general impression that it costs less to do business through an SHG than through the Grameen system. Additionally, and very importantly, the SHG system requires less investment in institutional development. Any existing bank branch can service an SHG and its members.

'Sustainability' is not only a matter of cost, but also of the price that is charged. SHARE and Cashpor, two of the main users of the Grameen system in India, charge their clients an effective annual rate of about 50% per year, while most institutions in Bangladesh charge closer to twenty per cent. These figures are not directly comparable with the rate of 12% that is charged to SHGs by most banks in India, since the SHG is a retailer.

The members of SHGs themselves pay their groups a wide range of different rates of interest. Although the individual member has to bear the cost, she is also a part owner of the SHG; she therefore benefits from the surplus it generates, whereas all the charges paid to institutions using the Grameen system accrue to the institution itself.

SHGs may be a less expensive distribution channel than Grameen groups, but they may also themselves be less durable. This has implications not only for their members, but also for the financial institution which must incur the investment of replacing them if they

fail to survive. SHGs, like the ROSCAs from which many of them originate, will only last as long as the members continue to gain from them. They are fragile social entities; it is difficult for them to absorb the shocks of changes in membership, and they can easily be destroyed by minor disputes or disagreements.

Because SHGs are genuinely autonomous independent entities, they have little protection against 'hi-jacking', either from within, or from outside, apart from their own internal solidarity or from whatever collective strength they can mobilise through coming together in clusters and federations. The government, at the state and national level, has already identified the potential of SHGs as a channel for the delivery of subsidy. The new SGSY initiative, which is designed to replace the massive but largely ineffective IRDP and other poverty alleviation programmes, is based on groups. Government development staff have already started to nominate existing SHGs for the receipt of support under this programme, and many bankers are alarmed at the possible effects this will have on their SHG clients which have thus far remained 'unpolluted' by subsidy.

Well over half the SHGs which were financed in 2000/2001 were in the single state of Andhra Pradesh, where the state government has for some years been using SHGs as subsidy distribution channels. Some groups have turned down such offers, because their members are well aware of their destructive effects, and very strong groups can take advantage of subsidies without being damaged. Less mature groups can easily be destroyed by grants, however, and this has already happened in some cases (Harper 1996, pp.88-89).

Membership in a Grameen Bank group demands more time but less management. SHG members are running a bank, albeit on a very small scale; the members who are not officers must at least understand issues such as interest rates and risk. A Grameen member has to attend weekly meetings, and to maintain her regular saving and repayment schedule. The group and centre heads have only to ensure that the payments will be available on time; they are not bankers in any sense. If the members of an SHG are lucky enough to identify and retain skilled officers, or if they can continue to enjoy the support of an NGO, the issue of management may not limit the life of their group; otherwise, it may collapse. Their bankers have many other customers, and cannot be expected to devote a great deal of time to sustaining their client SHGs. Grameen groups, on the other hand, are very much 'driven' by the bank staff; they are the *raison d'être* of the bank, and staff are judged by their success in opening up new groups and preserving old ones.

SHGs may also switch to a different financial institution for their savings or loan requirements, and their new supplier may be able to offer a better deal partly because he has not had to incur the initial customer development cost. Grameen groups, on the other hand, are tied to and kept alive by the institution which created them. Members can and do switch to different suppliers, and groups do sometimes collapse, but they are on the whole more durable and longer-lasting than SHGs.

In summary, therefore, we can tentatively conclude that at least in India the SHG system is more economical, and thus more financially 'sustainable', in the short to medium term

at any rate, in spite of the fact that SHG members usually pay a lower price for their loans than members of Grameen groups. There is as yet, however, no proven method whereby new SHGs can be developed at a cost which is low enough to make them into immediately profitable clients. This customer creation investment has to be undertaken by NGOs which benefit from external subsidy, or by the efforts of unusually committed bank staff. The key to successful micro-finance, however, is access rather than price, and we must therefore enquire which system is most effective at reaching poorer people.

#### **4. OUTREACH TO AND IMPACT ON THE POOREST**

The prime aim of micro-finance is not to maximise profits, nor even to cover all its costs. It is intended to alleviate poverty, and if some element of subsidy is needed to enable it to do this effectively, most would agree that such subsidy should be provided. We must therefore ask which of the two group systems reaches and benefits the poorest people most effectively.

There is little direct evidence as to whether the SHG or the Grameen system is more effective at reaching the poorest people. It is now generally acknowledged that micro-finance in general does not reach the 'poorest of the poor', and that the poorer people whom it does reach benefit less from micro-finance than those who are better off. This applies to the SHG as well as to the Grameen system (Clar de Jesus, p.21, Wright, pp.56, 262, Hulme and Mosley p. 115).

The poor are excluded not only by other better off members, but they also exclude themselves. They are afraid that they will not be able to save regularly, their poverty means that they lack profitable investment opportunities, and they may also not be able to attend meetings regularly. Their exclusion may be in their own interest; poorer people benefit less than others from micro-finance, and many poorer micro-finance clients have suffered great hardship, and have even been driven to suicide, as a result of their 'micro-debt' (Hulme, p.26).

The Grameen system is older and better documented, and there is little published material on the 'downside' of the SHG system. One study however (Harper et al, pp.27 and 41) found that the poorest people are also excluded from SHGs, and that many SHG members had suffered as a result of their membership. Fernandez, on the other hand (2001 chapters 10 and 11), reports that poorer people are included in the groups promoted by MYRADA. They take smaller loans than those who are better off, for consumption rather than investment, but they do enjoy as much access to the loans as their better-off fellow members.

MYRADA attempts to promote as many groups as possible in each village, in order to include every socio-economic level, and they have found that over half of the poorest families are represented in SHGs after two or three years. It may be significant that MYRADA is also one of the highest cost SHG promoters (Fernandez 2001, p. 35). Social inclusion has a high cost.

There is only one case known to the writer where both systems are operating in the same area. Basix Finance is working through SHGs in Eastern Andhra Pradesh, and SHARE is also working in the same part of the State through the Grameen system. Neither organisation can claim to have fully covered the market, but there have thus far been no instances where they have reached the same clients. No systematic attempt has been made to compare the wealth of their respective clients, but in brief meetings with both types of groups the SHG members appeared to be somewhat better off than the members of the Grameen-type groups.

The members of both types of groups are initially self-selected, as is necessary if they are to be willing to guarantee each others' loans. The staff of Grameen system institutions, however, make a point of assessing the poverty level of the prospective members by visiting every member's home before their groups have been formally accepted (Fugelsang and Chandler, p. 110). ASA, which serves 12,000 women using a modified Grameen system, requires potential members have less than half an acre of irrigated land, or one and a half acres of dry land, and household income of less than Rs 18,000 per annum.

Additionally, their field staff check poverty levels with a sixteen point housing quality index and a participatory wealth ranking exercise (Hishigsuren pp. 29-30). ASA also ensure that the first groups in any village only include Dalits. There is some evidence, however (Matin p. 50), that poorer people are gradually excluded from Grameen groups over time, as the bank workers have less influence over the recruitment of new members than they do when the groups are first formed.

Bankers, and NGO staff who promote SHGs, are more likely to accept the members without question. Many SHGs are formed from pre-existing groups (Harper et al. p. 19), and neither NGO workers nor bankers are likely to demand that certain members leave because they are not poor enough, or that others are admitted on the basis of their poverty. Grameen groups, on the other hand, are effectively formed or at least quite rigorously screened by the bank staff before acceptance. The basic unit of the Grameen system is in theory the five member group, and it would appear *prima facie* to be easier for the institution to influence the membership and the operations of such a small group than that of an SHG with twenty or more members.

In practice, however, it is suggested that the real unit of operations is the 'Centre', with thirty or more members (Matin, p.266). This is similar to an SHG, and suggests that the apparent benefits of the smaller group may be illusory. A larger group is more likely to be influenced by existing social and economic structures within a community, rather than by the poverty alleviation agenda of the financial institution. This influence can be benign, but is perhaps more likely to be oppressive (Harper A 1998, Harper A, 2000 p 25).

The operations of Grameen groups are very much under the control of the institution, through the weekly meetings, whereas SHGs are much more free to manage their affairs

as they wish. NGO or bank staff may attend their meetings, but as observers rather than managers, and the usual intention is to phase out regular attendance of this sort. This regular supervision can serve to protect weaker members from exploitation by those who are stronger, and in particular to ensure that all members have equitable access to loans. It is also possible, however, as some experience in Bangladesh has shown, that pressure for high recoveries can lead the bank workers to act even more oppressively than fellow-members. Regular institutional supervision can be a two-edged sword.

It is clear, however, that the SHG system requires its members to demonstrate a much higher level of management skill and initiative than the Grameen system. They have in effect to manage their own bank, financed by their own savings, by accumulated interest earnings and by institutional finance, and with a range of loans of different maturities and often at different interest rates. Grameen clients, on the other hand, are bound and protected by a rigid and highly disciplined system. They have regular weekly contact with bank staff, and they have little discretion as to the amounts or terms of loans, or even as to who receives them. In effect, they have merely to do what they are told.

Poorer people may be more likely to accept these rigid conditions and to need the protection they imply, and less likely to be able to cope with SHG membership, than those who are better off. This may in itself tend to exclude the poorest from SHGs.

There are, however, some exceptions which suggest that the opposite may be the case. Ashrai is one of the few institutions in Bangladesh which effectively operates with the SHG system (Alamgir, pp. 79-81). They work with over 1000 groups of tribal people, who are from what are said to be the very poorest people in the country.

In summary, the evidence seems on balance to suggest that SHGs are probably rather less likely to include poorer people than Grameen groups; neither system reaches the very poorest. Given the very rapid growth of the SHG system in India, more work is urgently needed to ascertain whether SHGs have the same damaging effects on their poorer members as Grameen groups, and, if they do, how to minimise these effects.

## **5. 'EMPOWERMENT'**

Much is made of the way in which access to appropriate financial services has a non-economic empowering effect on poor and marginalised people, particularly women. 'Empowerment', like 'sustainability', can be variously defined, but there is little question that micro-finance has enabled large numbers of poor people to improve their social and even their political status. This effect is also closely related to the group-based methods of intermediation which are used. An individual woman may not be able to make much difference to her social position, even within her own family, if she improves her financial position, but if she has the support of her fellow group members she can do much more. Which of the two group-based systems which we are considering is more likely to have this non-economic effect?

The members of an SHG are effectively the owners and managers of a small bank. This may place a heavy burden on their time and ability, but if they are successful it would seem to be obvious that this will enhance their status more than the fact of being a client of a bank, which is what the members of Grameen groups are. The bank of which they are clients has at least until recently been far from customer-friendly; although competition is forcing Grameen institutions to be more flexible, they still have rigid loan rotas and repayment schedules, and freely withdrawable savings are still the exception rather than the rule. The sustainable livelihoods framework of analysis is increasing our understanding of the complexities of poor people's financial needs, and it is clear that the original rigid Grameen approach only satisfies a small part of those needs.

SHG members can themselves decide who gets loans, when, and at what interest cost. They are indirectly remunerated for their management time and effort, in that the spread between their costs of funds and the interest they decide to charge themselves is retained by the micro-bank of which they are the owners. They build their own equity, whereas the high interest rates which Grameen clients must pay goes to pay the wages of the large numbers of staff which the system demands. It could indeed be claimed that the Grameen system is yet another way by which the relatively elite, bank employees, sequester the hard-earned incomes of the poor.

SHGs are more vulnerable to 'hijacking' by vested interests, and to inequitable distribution of the benefits, because they are less closely supervised by the financial institution where they deposit their savings and from which they may take loans. There have in India been many cases where SHGs have been used as channels for government grants and other poverty alleviation programmes. These programmes can be very beneficial to the members, and strong groups in particular can use such assistance to strengthen their own position. Assistance of this sort often comes at a price, however; political interests use them as a form of patronage to demand votes or other support; grants can also erode the sense of ownership and responsibility which are necessary for effective groups, and can even destroy the groups altogether.

Both systems appear to empower their members in the literal sense of giving them the confidence to put themselves forward for membership of local government bodies, such as Panchayati Raj institutions. Fernandez (2001, p. 91) reports that some 200 or about 2.5% of the total of 77,495 members of SHGs sponsored by MYRADA, were elected to their Gram Panchayats in 2000. In 1999, thirty members, almost exactly the same percentage, of the 12,000 members of ASA's Grameen-type groups in Tamil Nadu were similarly elected (ASA, p. 91).

Some Indian SHG promotion institutions, such as Dhan Foundation, CDF and MYRADA, encourage and assist 'their' SHGs to come together in clusters and federations. These bodies may or may not themselves be involved in financial intermediation, and some of them have become large and powerful institutions in their own right.

Grameen groups have less need to come together in this way, since the members do not themselves perform the banking management tasks demanded of SHG members. Some Grameen replicators, however, such as ASA in Trichy (ASA pp. 27-28) also encourage their members to form similar apex groupings, for a variety of non-financial functions. In Bangladesh many Grameen type groups have also switched their business from one bank to another, in search of better services; this is good evidence of their independence and empowerment.

Grameen groups are much better protected against internal or external threats; their members are less vulnerable, but also less empowered, since empowerment is freedom and this must also include freedom to face and if possible to overcome threats.

SHG membership is thus more empowering, but at the same time more vulnerable. This serves to confirm our earlier tentative conclusion that Grameen groups are more suitable for poorer, more vulnerable groups. K-Rep in Kenya found that some Grameen or 'Juhudi' groups evolve into SHGs, and they also found that it was less expensive to service SHGs than to use the more labour intensive Grameen method (Harper et al., p.107). SHGs are a more empowering instrument than Grameen groups, but they also demand more of their members, and expose them to greater risks. Freedom does not come without a cost.

## **6. INSTITUTIONAL FEASIBILITY**

There is a great need and demand for microfinance services, throughout the world. Large sums of money are also available, whether from the savings of poor people themselves or from government and foreign sources.

The main constraint is the lack of institutional capacity to deliver the services to those who need them. Institutional capacity building takes time and costs money. A system which requires less institutional development must therefore be attractive, even if it is not obviously less expensive to operate.

SHGs can evolve quite easily from existing ROSCAs or other traditional financial or non-financial groups, and any bank can do business with them, so long as its management are prepared to deal with this unfamiliar but potentially highly profitable market segment. If there are many pre-existing groups, and if there is a wide network of bank branches, which need new business opportunities, the environment would seem to be ideal for the SHG system.

It takes time to change management attitudes, and regulations may make it difficult to lend without collateral, or to do business with informal groups which have no legal status. In the early years of the SHG movement in India many bankers showed that it is not impossible to overcome these constraints, and the regulatory environment has now changed so that there are no legal barriers to which a conservative banker can appeal as a reason for hesitation. It took some seven years for Indian bankers to appreciate the

potential of SHGs as customers, but the recent rapid expansion in the numbers of SHGs which have borrowed from banks shows that their not unreasonable scepticism is now being overcome.

Those few institutions which work with the Grameen method in India are also expanding very fast, and it is to be hoped that there will in the future be many occasions when people can make their own choice from two or more competing institutions. Then and only then will it be possible to determine which system is actually most suitable for which types of customer, so long of course as customer choice is not distorted by excessive or misplaced subsidy.

Until that time, we can tentatively conclude that the Grameen system is more expensive but may nevertheless be more suitable for poorer communities, particularly in places where there are few NGOs to develop the groups, and few bank branches whose staff are willing to serve them. Elsewhere, the SHG system is probably 'better' for Indian conditions, as the present and projected numbers seem to suggest.

## **7. CONCLUSIONS**

Bangladesh is a relatively homogeneous, very poor, and to the casual observer at least there seems to be little opportunity for progress. It may be an appropriate location for a rigid, institutionally autonomous, readily transferable and dependence-creating system which can alleviate poverty for large numbers.

India is fiercely diverse as a nation, and most communities are also diverse in caste, opinion and religion. Indians are also known for their sense of personal independence, which is often translated into indiscipline, whether on the roads, in political assemblies or elsewhere. The SHG system reflects this independence and diversity. It allows people to save and borrow according to their own timetable, not as the bank requires, and SHGs can also play a part in a whole range of social, commercial or other activities. They can be vehicles for social and political action as well as for financial intermediation.

This flexibility and freedom also has its price. Politicians are driven by their need for popularity and power, and bureaucrats by their need to achieve numerical targets. SHGs can provide both with a ready-made vehicle. If their members can identify and resist the disadvantages of being 'used' by outsiders, and can exploit them rather than be exploited, the movement may in time play an important role in the reduction or even the elimination of India's main claim to fame, its leadership in world poverty. If not, however, they will become no more than another milestone in the nation's long list of failures.

## SUMMARY OF PROS AND CONS OF THE SHG AND THE GRAMEEN SYSTEM

	<b>SHGs</b>	<b>Grameen Bank groups</b>
Plusses for clients	<ul style="list-style-type: none"> <li>• Flexible</li> <li>• No need for bank at all</li> <li>• Highly empowering</li> <li>• Members can save and borrow as needed</li> <li>• Free to chose suppliers</li> <li>• No enforced loan ladder</li> <li>• Can evolve from existing groups, chit funds, credit unions etc.</li> <li>• Can access the full range of bank services</li> <li>• Can evolve into Federations, and Co-operatives</li> </ul>	<ul style="list-style-type: none"> <li>• No need for literacy</li> <li>• No need for members' initiative</li> <li>• Protected from internal and external exploiters</li> <li>• Poorer people are included</li> <li>• Belong to and are supported by the bank</li> <li>• Bank can offer a range of additional tailor-made services</li> </ul>
Minuses for clients	<ul style="list-style-type: none"> <li>• Need management skills and time</li> <li>• Depend on good accounts</li> <li>• Can be hijacked internally or externally</li> <li>• Cash may not be secure</li> </ul>	<ul style="list-style-type: none"> <li>• Must meet frequently</li> <li>• Little freedom or flexibility</li> <li>• Group composition not wholly under member's control</li> <li>• Pressure to borrow</li> <li>• Interest rates inflexible</li> </ul>
Plusses for Banks	<ul style="list-style-type: none"> <li>• Lower transaction costs</li> <li>• Can fit into any branch</li> <li>• Graduation easier</li> <li>• Can build on existing groups</li> <li>• Savings mobilisation easier</li> <li>• Groups can absorb odium of expelling members</li> </ul>	<ul style="list-style-type: none"> <li>• Can resist subsidised 'schemes'</li> <li>• Tighter control</li> <li>• Standardised MIS</li> <li>• Standardised procedures</li> <li>• Easier to forecast need for funds</li> <li>• Can use lower-grade staff</li> </ul>
Minuses for Banks	<ul style="list-style-type: none"> <li>• Hard to monitor</li> <li>• May be tempted by other banks or by politicians</li> <li>• Slow to develop</li> <li>• May form own federations</li> <li>• MIS more complex</li> <li>• Need NGOs or highly committed staff to develop groups</li> </ul>	<ul style="list-style-type: none"> <li>• Higher transaction costs</li> <li>• Need continuous guidance and presence</li> <li>• Need dedicated system</li> <li>• Hard to evolve and change</li> </ul>
Suitable conditions	<ul style="list-style-type: none"> <li>• Existing bank network in rural and poor areas.</li> <li>• Diffused communities, castes, wealth levels</li> <li>• Tradition of informal financial services</li> <li>• Wide variety of scale and nature of investment opportunities</li> <li>• Some local leadership</li> <li>• NGOs and/or committed bank staff</li> </ul>	<ul style="list-style-type: none"> <li>• Very poor, homogeneous communities</li> <li>• Marginalised people, with little hope and initiative</li> <li>• Few traditional informal financial mechanisms.</li> <li>• Lack of financial institutions</li> <li>• Resource poor, little hope of graduation</li> <li>• Large numbers of small business opportunities</li> <li>• Few NGOs</li> </ul>

## **BIBLIOGRAPHY**

Alamgir Dewan AH, Microfinancial Services in Bangladesh, Review of Innovations and Trends, Dhaka, CDF, Dhaka, 1999.

Clar De Jesus RB, Assessment of six linkage banking projects in Asia: synthesis report (draft), APRACA/GTZ, 1997.

Credit and Development Forum, CDF Statistics, Microfinance statistics of NGOs and other MFIs, CDF, Dhaka, 1998.

Fernandez A P, Putting institutions first, even in micro-finance, MYRADA, Bangalore, 2001.

Fernandez, A P, The MYRADA experience, Alternative Management systems for savings and credit of the rural poor, second edition, MYRADA, Bangalore, 1998.

Fugelsang A and Chandler D, Participation as Process: what we can learn from the Grameen Bank, NORAD, Oslo, 1986.

Fugelsang A, Chandler D, Participation as Process, NORAD, Oslo, 1986.

Grameen Bank, Annual Report 1998, Dhaka, 1999.

Grameen Trust, Annual Report 1999, Dhaka, 2000.

Harper A, Group-based management of savings and credit - the case of AKRSP, Pakistan, Small Enterprise Development, Vol. 9, no. 2, June 1998.

Harper A, Microfinance peer lending groups: Empowering the poor or Perpetuating Inequality? Unpublished MSc thesis, SOAS 2000.

Harper M, Empowerment through Enterprise, New Delhi, Oxford and IBH Publishers, London, IT Publications, 1996.

Harper M, Esipisu E, Mohanty AK and Rao DSK, The new middlewomen: profitable banking through self-help groups, New Delhi, Oxford and IBH Publishers, London, IT Publications, 1998.

Harper M, Profit for the Poor, Cases in micro-finance, New Delhi, Oxford and IBH Publishers, London, IT Publications, 1998.

Harper M, Co-operative Success, what makes group enterprise succeed? New Delhi, Oxford and IBH Publishers, London, ITDG Publications, 2000.

Hishigsuren G, Holistic Approach to Development, ASA, Tiruchirpalli, 2000.

Holcombe S, Managing to Empower, The Grameen Bank's experience of poverty alleviation, Dhaka, University Press Limited, London, Zed Books, 1998.

Hulme D, "Is micro-debt good for poor people?", Small Enterprise Development, Vol. 11, no. 1, March 2000.

Hulme D and Mosley P, Finance against Poverty, Routledge, London, 1996.

M-Cril, The M-Cril Report, 2000, Micro-credit Ratings and Guarantees India Limited, Delhi, 2001.

Matin I , Grameen and Shakti Groups, Unpacking joint liability credit contract, PRPA Working paper series, number 6, Grameen Trust, Dhaka, 1997.

Matin I, "The negotiation of joint liability; notes from Madhupur", in Wood GD and

Sharif IA, Who needs credit, Poverty and Finance in Bangladesh, Dhaka, The University Press, 1997.

Microbanking Bulletin, Issue no. 4, February 1999.

NABARD, SHG Bank linkage programme, status as on March 31 1998, NABARD, Mumbai, 1998.

NABARD, SHG Bank linkage programme, status as on March 31 1999, NABARD, Mumbai, 1999.

VVV, SHG and Prathama Bank, unpublished mimeo, Prathama Bank, Moradabad, 2000.

Reserve Bank of India, Circular RPCD NO.PL.BC. 62/04.09.01/99-2000, Mumbai, February 2000.

SHARE Microfin Limited, 1999-2000 annual report and accompanying brochure, Hyderabad, 2000.

Wahid ANM, The Grameen Bank, Poverty Relief in Bangladesh, Boulder, Westview Press, 1995.

Wright GAN, Microfinance systems, The University Press Limited, Dhaka, 2000.