Chapter 7

Self-help groups and Grameen Bank groups: What are the differences?

by Malcolm Harper

Introduction

Most micro-finance organisations (MFOs) use a group system to distribute their services to their clients. There are some exceptions, including the village unit system of Bank Rakyat Indonesia (BRI), the world's biggest and most profitable provider of micro-financial services, but groups generally predominate.[1]

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 chapter is to show that this is not the case.

Group systems for micro-financial services evolved in particular in Bangladesh (the Grameen Bank method) and in Latin America (solidarity groups and village banking), as well as in India (self-help groups or SHGs). While there are thus many variants, there are broadly two very different ways of using groups for financial intermediation. For convenience I term these two systems the Grameen system and the SHG system, using the terms that are familiar within the South Asian context.

Both systems have their advantages and disadvantages, and practitioners need to be aware of the options that are available. In this chapter I describe and explain each system, and compare their sustainability, their outreach and impact on the poor, including their empowerment impact, and their feasibility within their respective environments. My arguments are briefly summarised in Table 7.1 in the conclusion to this chapter.

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 organisations which use 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 next. Further more detailed accounts of each system can be obtained from a number of sources, including Fugelsang and Chandler (1986), Harper M (1998), Holcombe (1998) and Wahid (1995).

The Grameen system

Potential clients are asked by the MFO 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 MFO, according to a fixed compulsory schedule, and they also take regular loans. They each have individual savings and loan accounts with the MFO, 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 an MFO worker, where savings and repayments are collected and handed over to the MFO worker who maintains the records;
- 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 MFO 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 member 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.

The SHG system
The members form a group of up to 20 members. The group formation process may be facilitated by a non-governmental organisation (NGO) or by the MFO 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 MFO 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 MFO or bank, for funds that are not needed by members, or in order to qualify for a loan from the bank.
- The MFO or bank 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 it 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: 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 members have their accounts with the SHG, not with the MFO or bank, and the MFO or bank does not have any direct dealings with the members. The MFO or bank may assist the SHG in record-keeping; they may also demand to know who the members are and impose certain conditions on the uses of the loan which they make to the SHG.

However, the SHG is an autonomous financial organisation in its own right (see Chapter 5).

Where, by whom and why are the two systems used?

The Grameen system

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

In addition to the originator, the Grameen Bank, with three million members, two other major users of the system, BRAC and Proshika, each have over a million clients. In 1998 there were some 30 other MFOs with over 10,000 members, and many hundreds of smaller organisations using the system (Credit and Development Forum, 1998). It has been estimated that some 10 million people in Bangladesh receive financial services through this system.

The system has also been widely replicated by MFOs elsewhere, including a small number in India and in more than 20 other countries in Asia, Africa and Latin America, as well as 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, 2000).

Low or no-cost foreign donations represent the largest source of on-lending funds for the large MFOs that use the Grameen system in Bangladesh, while members' savings and the accumulated surplus from operations each contribute some 20 percent 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. The methods of calculation also differ from one MFO to another. Broadly speaking, the cost to the final borrowers amounts to at least 2 percent 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. It is difficult for a commercial bank which also has other financial products to integrate such a Grameen system into its own operations.

One of the few banks 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, 1999: 72-5). 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 1 percent of its total portfolio in 1998, the Islami Bank intended massively to expand this approach.

The SHG system

The SHG system is mainly found in India. There are 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 by MFOs and by commercial banks. 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 1100, or just under US$25. During the year 2000-1, 171,000 SHGs took loans, of which 149,000 were first time borrowers (National Bank for Agriculture and Rural Development or NABARD, personal communication).

The average membership is around 17 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. While the vast majority of these members are saving regularly, not all of them will have taken a loan.

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). Around the same time the management of NABARD had 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, the linkage of SHGs to banks has been vigorously promoted by NABARD and other organisations. NGOs often play an important role in the linkage process, and have promoted some 80 percent of SHGs linked to banks (Sa-Dhan, 2001: 15). However, NGOs usually do not play a 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 (see Chapters 5, 8 and 9 for detailed examples).

Other NGOs also act as financial intermediaries by borrowing from NABARD or elsewhere and on-lending to SHGs, either because they aim to become MFOs, or because this is the only way some groups can access finance, because many bankers still refuse 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 incurred by these NGOs.

Over a third of the linked SHGs borrowed from MFOs 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, 1999a).

In addition to paying the cost of training bankers as well as staff of NGOs, NABARD also encourages the banks to lend to SHGs by refinancing the loans they make to SHGs at a subsidised rate (currently 6.5 percent). This subsidised finance was used to refinance 83 percent of the loans made to SHGs in the year 2000-1 (NABARD, personal communication).

Loans to SHGs are excluded from the maximum interest ceiling of 12 percent that still applies to other loans under Rs 20,000 (Reserve Bank of India, 2000), but the banks have generally not taken advantage of this freedom, and most still lend to SHGs at about 12 percent. They feel the resulting 5.5 percent spread is enough to cover their transaction costs so long as the task of promoting, training and developing SHGs is carried out by an NGO, at no cost to the bank.

The on-time repayment rates on SHG loans are usually well over 95 percent. 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 choose; the annual rates can range from 12 to 60 percent a year (Harper M *et al*, 1998: 76).

There is also a large and increasing number of MFOs in India, most of which use the SHG method. The portfolio of the approximately 35 larger MFOs which use the SHG system, and are doing business with the recently established SIDBI Foundation for Micro-credit (SFMC), amounts to almost Rs 850 million or US$13 million. These MFOs were said in early 2001 to be serving about 200,000 eventual clients, of whom 94 percent are women (SFMC, personal communication). SFMC anticipate that by 2009 their partner MFOs will be serving 1.3 million clients.

NABARD forecast in early 2001 that by 2008 about one million SHGs would be taking loans from banks, with a total membership of around 17 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 new groups a year taking loans from 2005 onwards.

In the event 149,000 new SHGs took loans in the financial year ending in March 2001, so that these forecasts may be well below what is actually achieved. In terms of membership, using the same average of 17 members per group, this amounts to an addition in just one year of two and half million clients, almost equivalent to the total current membership of the Grameen Bank. This has been achieved by effective collaboration between the banks, NGOs, MFOs and NABARD, with the necessary recognition and authority from the Reserve Bank of India.

There are as yet no giant organisations comparable to the MFOs in Bangladesh, nor perhaps will there ever be; the SHG system reflects the scale, and the organisational diversity, of the Indian financial system.

A small number of Indian MFOs use the Grameen system. The total number of people in India served by the 18 MFOs using the Grameen system at the end of 1999 was approximately 50,000 (Grameen Trust, 2000: 72-78). SHARE in the state 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 the figures for the growth of SHGs 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[2], but the figure of 40 percent of the population is quite commonly used. 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 poorer Indian households will by 2009 have access to formal financial services. The vast majority, even if SHARE's forecasts are achieved, will be using the SHG system.

Why Grameen in Bangladesh and SHGs in India?
The rural poor in India are not so different from their counterparts in Bangladesh. Indeed, the differences between northern and southern India are certainly more pronounced than those between poor rural communities in the Indian states of West Bengal, Uttar Pradesh, Bihar or Orissa and 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. I start with political and social factors.

Bangladesh has less experience 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, and there is strong emphasis on democratic organisation and decentralisation (see Chapter 5). Fernandez (2001: 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.

It is not surprising therefore that bank workers in the Grameen system visit every group, every week. Experiments with less frequent meetings have generally not been successful. In contrast, as illustrated in Chapter 9, the NGO field-worker or banker may visit an SHG 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, while some parts of the Sundarbans in Bangladesh are fairly thinly populated. The population density in India is about 300 per square kilometre, 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.

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 Uttar Pradesh, has reported any particular difficulty in introducing the Grameen system in India. Generalisations are therefore dangerous, since India is more diverse than many continents, and the differences between or within states are often greater than between other neighbouring countries.

Institutional factors are also likely to have strongly influenced differing practice in Bangladesh and India. For example, in Bangladesh the Grameen Bank itself is in part protected from undue regulatory interference by being formally constituted by an act of parliament whose influence extends to others using the same system. In India, self-help groups do not have more than 20 members to avoid the need to register themselves as legal bodies, which might bring with it a whole range of regulatory constraints.

In addition, 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 the state of Uttar Pradesh has mobilised local farmers' clubs to form over 1100 SHGs (Prathama Bank, 2000). Government agencies are active in some states, and financial intermediaries such as BASIX (see Box 4.1 in Chapter 4) 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 (as described in Chapter 5), are themselves spreading the message, and many people observe, learn from and copy their neighbours, without any external intervention.

It would have been difficult, if not impossible, to introduce the SHG system in Bangladesh, where bank-branch coverage is much less and banking management is in general less eager and under less compulsion to identify with new ways of reaching poor people. 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 poor people that demands the minimum of institutional change, and the SHG system is just that for India.

Funding sources have also played a key role. While early experiments with micro-finance in both countries began in the late 1970s without any donor assistance, micro-finance has been largely a donor-driven phenomenon, everywhere. The Grameen system was and indeed still is lavishly supported by donors in Bangladesh. It is an ideal channel for donor assistance, since it is relatively standardised and transferable, it is dominated by a few large MFOs, it depends mainly on subsidised funds and is more or less totally independent of existing local banks.

Development aid to India was US$1.90 per head of the population in 1985, and was at the same level in 1997. The equivalent figures for Bangladesh were US$11.40 and US$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.

Likewise, the two major apex financing bodies in each country have played an important part in determining which system predominates. NABARD in India 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 2000-1, for example, NABARD organised 3200 training courses on SHG linkage, with 166,000 participants (NABARD, personal communication). This single-product approach inevitably imposes some uniformity, and there has been some question whether MFOs which use the Grameen system are eligible for NABARD refinance at all.

In Bangladesh, the reverse may be true. The Palli Karma Sahayak Foundation (PKSF), the wholesale fund that provides almost 20 percent of the on-lending finance to the country's MFOs (Credit and Development Forum, 1998: iv), has set criteria for its partner organisations that raise questions whether organisations that do not follow some variant of what I have called the Grameen system are eligible (Alamgir, 1999: 90). Institutional inflexibility may in both countries have played some part in determining which systems are used.

‘Sustainability’

One of the main reasons for the popularity of micro-finance as a poverty alleviation tool is the belief that MFOs can eventually become ‘sustainable’. This term has many meanings, ranging from the continuing ability to find and retain donors to the 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 MFOs serving poor people. Nevertheless, financial services for poor people 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. It is therefore important to compare the sustainability of the two systems.

The recent M-CRIL Report (M-CRIL 2001) contains information for 10 MFOs that use the Grameen system, three of which operate in India, and for 31 using the SHG system, all of which are Indian (for the detailed results, see Chapter 10). 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 percent, whereas the comparable figure for the MFO working through SHGs is only 8.9 percent (M-CRIL, 2001: Annex Table 3).

Much of this difference arises because the younger MFOs promoting SHGs have large sums of un-lent funds on deposit, and because they are wholesaling funds to the SHGs that perform the retail function. Indeed, when SHG members use financial services for lumpy consumption, or even for micro-enterprise expenditure within a household budget, savings and loans may essentially perform the same role. Members may set aside either small amounts as savings to build up a lump-sum or small repayments to repay a lump-sum loan they have taken (see the introduction to Chapter 3). A system that encourages savings first, as in the SHG system, is likely to accumulate far greater un-lent funds than a system that focuses on credit, accompanied by compulsory but inflexible savings products.

Nevertheless, the difference in yields 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.[3] As suggested in Chapter 5, the SHG system leaves more money with the communities, but, like any retailer, they have to perform many more of the transaction functions in return.

Two writers in the *Microbanking Bulletin*’s issue on efficiency (1999: 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 among MFOs. The SHG system is more flexible; the financial intermediary usually has less frequent contact with the groups, once they have reached the stage of taking loans, but assessing and guiding 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 Grameen system requires more staff per client, because the MFO providing loans is acting as the retailer. In the SHG system, the SHG is the retailer, and thus loan balances from the bank or MFO to SHGs are much higher than those to Grameen group members. The amounts and balances of the loans an SHG makes to its individual members, and of any savings it mobilises from them, need not and usually cannot be recorded by the bank or MFO.

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[4], while the Grameen system requires less qualified and thus lower paid staff.

Ideally, we should compare the costs of two financial service providers serving the same numbers of clients, one of which works with SHGs and the other with the Grameen system. This is not easy. For example, under the system of linking SHGs to banks, loans are mainly extended by bankers for whom such loans are only one of a number of products, and it is difficult to separate out the costs of this product.

More importantly, the promotion of the groups themselves has, at least until recently, usually been 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 MFOs that use the Grameen system is well documented. The Grameen Bank itself made a profit of just over 100 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 19,000 million taka. Over half this capital was provided from concessional sources, the majority at interest rates as low as 2 percent.

SHARE in India is a much younger organisation, and it does not aim to reach ‘financial self-sufficiency’, which is micro-finance language for real profitability, until 2006, long after it has become a very substantial organisation. I 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 (OBC), near Dehra Dun in India, is unusual if not unique in that its only customers are SHGs; it therefore makes it possible 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 Rs 1 crore (10 million), over 80 percent of which was funded by customers' deposits. The branch would have made a loss of just over Rs 5 lakhs (500,000) without any subsidy, but the Bank was able to claim subsidised NABARD refinance against the loans. 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 percent 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 US$30 (Rs 1350) and US$355 (Rs 16,000) (Harper M *et al*, 1998: 73, Fernandez 2001: 35-6). Experiments with dedicated SHG development agents undertaken by BASIX (see Box 4.1 above) and others seem likely significantly to reduce the cost towards the lower end of the range. One Indian banker (Harper M *et al*, 1998: 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 operation 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 Rs 7 per Rs 100 lent, while the equivalent figure for SHARE in September 2000 was Rs 10. While this is obviously an over-simplified comparison, it seems to confirm the general impression that it costs less to do business through an SHG than through the Grameen system.

However, these cost calculations and comparisons take no account of the context in which micro-financial services are being developed, of the capacities of clients targeted or the level of development of the respective organisations, which can all contribute significantly to overall costs, as Mathew Titus analyses in depth in the next chapter.

Likewise, the SHG system requires less long-term investment in organisations. Any existing bank branch can service an established SHG and its members. This in fact further complicates comparison as the full costs in the SHG system are likely to be higher upfront, during the promotion stage, but lower later on when SHGs have stabilised.

‘Sustainability’ is of course 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 percent a year, while most MFOs in Bangladesh charge well over 20 per cent. These figures are not directly comparable with the rate of 12 percent 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. As Chapter 5 makes clear, 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 MFOs using the Grameen system accrue to the MFO 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 bank or MFO that 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. As the cases in the next two chapters clearly demonstrate, SHGs can be very 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.

Likewise, because SHGs are genuinely autonomous independent entities, they have little protection against hijacking or capture (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 (see Chapter 5).

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 Integrated Rural Development Programme (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.

Indeed, well over half the SHGs that were financed in 2000-1 were in the single state of Andhra Pradesh, where the state government has for some years been using SHGs for distributing subsidies. 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 M, 1996: 88-9).

An SHG demands more management capabilities of its members, although probably less time, compared to those of a Grameen-type group. SHG members are running a bank, albeit on a very small scale. This demands significant additional responsibilities, not just of officers but also of members, who must at least understand issues such as interest rates and risk and be able to monitor the performance of their micro-bank. Such responsibilities can be significant for a poor, illiterate women with limited time and computational skills (see Chapters 8 and 9 for many concrete examples).

A Grameen member, on the other hand, 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'etre* 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 intermediary for their savings or loan requirements, and their new supplier may be able to offer a better deal partly because (s)he has not had to incur the initial cost of customer development. Grameen groups, on the other hand, are tied to and kept alive by the MFO that 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, I 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 that is low enough to make them into immediately profitable clients. As the analysis in the next chapter shows, the customer creation investment can be significant, and has to be undertaken by NGOs that benefit from external subsidy, or by the efforts of unusually committed bank staff. In addition, SHGs are more likely to deteriorate or collapse than Grameen groups which are an integral part of a larger and more rigorous system.

However, access is more important than price, and it is therefore necessary to enquire which system is most effective at reaching poorer people.

Outreach to and impact on the poorest

The primary aim of providing micro-financial services 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. 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 or benefiting 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, 1997: 21; Hulme and Mosley, 1996: 115; Wright, 2000: 56, 262).

Poorer people are excluded not only by 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, 2000: 26).

In comparing the Grameen and SHG systems, it is worth bearing in mind that the Grameen system is older and has been subjected to much more rigorous analysis and research. In contrast, there is little published material on the downside of the SHG system. Nevertheless, let us look, first, at the extent to which poorer people are included or excluded from the two different systems.

There is only one case known to me where both systems are operating in the same area. BASIX is working through SHGs in eastern Andhra Pradesh, and SHARE is working in the same part of the state through the Grameen system. Neither organisation can claim to have fully covered the market, and 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 MFOs using the Grameen system, 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, 1986: 110).

For example, Activists for Social Alternatives (ASA) in the state of Tamil Nadu, India serves 12,000 women using a modified Grameen system. It requires that 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. Their field-staff check poverty levels with a 16-point housing-quality index and a participatory wealth-ranking exercise (Hishigsuren, 2000: 29-30). ASA also ensure that the first groups in any village only include Dalits.

Grameen groups are therefore effectively formed or at least quite rigorously screened by bank or NGO staff before acceptance. There is, however, some evidence (Matin, 1997a:

50) that poorer people are gradually excluded from Grameen groups over time, as the staff have less influence over the recruitment of new members than they do when the groups are first formed.

In the SHG system, bankers and NGO staff who promote SHGs are more likely to accept their members without question. Many SHGs are formed from pre-existing groups (Harper M *et al*, 1998: 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. Such issues are obviously of concern to many NGOs, but too much intervention here may undermine the democratic and autonomous functioning of groups that is so much part of the SHG system.

One study (Harper M *et al*, 1998: 27, 41) seems to confirm this. It found that the poorest people are excluded from SHGs, and indeed that many SHG members had suffered as a result of their membership.

There are, however, cases which suggest that the picture may not be as simple as this. Ashrai is one of the few MFOs in Bangladesh which effectively operates with the SHG system (Alamgir, 1999: 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. Likewise the NGO PRADAN (see Chapters 5 and 9) has promoted SHGs among some of the poorest tribal people in eastern India.

Part of the differences between the success of the two systems in including poorer people may arise from differing visions of how to tackle poverty. Unlike Grameen groups, which tend to focus more exclusively on poor people, Indian NGOs promoting SHGs may attempt to promote as many groups as possible in each village and to include every socio-economic level. This is part of their focus on building democratic people's organisations (explored in Chapter 5), not just delivering financial services.

Take the case of MYRADA. Fernandez (2001: chapters 10 and 11) reports that in seeking to include different socio-economic groups from among poor people, MYRADA has found that over half of the poorest families are represented in SHGs after two or three years. Studies of these groups also suggest that there is little discrimination against the poorest members in terms of access to services and leadership (see Chapter 5). It may be significant that MYRADA is also one of the highest-cost promoters of SHGs (Fernandez 2001: 35). Social inclusion has a high cost.

Finally, 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 MFO to influence who is or is not included in such a small group, as well as its operations, than it is to influence an SHG with 20 or more members.

In practice, however, it is suggested that the real unit of operations in the Grameen system is the centre, with 30 or more members (Matin, 1997b: 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 intermediary. This influence can be benign, but is perhaps more likely to be oppressive (Harper A, 1998 and 2000: 25).

In looking at the potential impact of the two different systems on poor people, the operations of Grameen groups beyond their formation remain very much under the control of the MFO. Grameen clients are in effect bound 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.

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 supervision can be a two-edged sword.

SHGs in contrast are much freer 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. The SHG system therefore 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. In Chapter 9, Ajit Kanitkar analyses the demands on local leadership that such a system makes, as well as its rewards.

It is possible that poorer people may be more likely to accept the rigid conditions of the Grameen system and to need the protection they imply, and be less able to cope with SHG membership, than those who are better off. This may indeed exclude the poorest from SHGs in the first place.

However, the impact of micro-finance depends in part on the differing needs of clients. As suggested in Chapter 3, poorer clients generally need greater protective services, such as savings, consumption loans and insurance, including loans to pay off higher-cost debt to money-lenders. The less poor, on the other hand, can benefit more from loans to build or expand their enterprise (see Chapter 4).

The SHG system is built on members' savings, and loans from banks are taken only to increase the pool of capital available for lending to members, which can be for any purpose determined by individual groups themselves. In contrast, the Grameen system insists that micro-loans be used for productive purposes, that is for investment in micro-enterprises, and demands compulsory savings as a condition of accessing such loans.

The broader range of services which is provided by SHGs, and the greater flexibility of members in choosing which services to access, may thus be more appropriate to poorer people. MYRADA, for example (Fernandez, 2001), has found that while poorer members of SHGs enjoy as much access to loans as relatively better-off members, the poorer take smaller loans for consumption rather than investment.

In contrast, the insistence of Grameen-type organisations that loans be used for productive purposes risks forcing poorer members into taking loans for purposes they cannot manage effectively, and hence may push them into further debt.

However, these distinctions are becoming increasingly blurred. Recent experiments with voluntary savings by users of the Grameen system in Bangladesh such as the Association for Social Advancement (ASA) and Buro Tangail demonstrate that there is a substantial demand from members for such services, and that they can be integrated into the Grameen system without difficulty. The provision of voluntary savings is therefore expanding among Grameen-type organisations, including in India. For example, SHARE collects voluntary deposits through a cooperative they have set up in the state of Andhra Pradesh, and these voluntary savings can be withdrawn at weekly intervals.

As for loans, in practice funds within a household are fungible, and, as Grameen-type organisations have discovered, it is often not possible (and usually not desirable) to prevent the 'diversion' of productive loans to other purposes. Moreover, Indian banks lending to SHGs insist that SHG members do not use these loans for consumption needs, making those SHGs that borrow from banks little different from Grameen groups in this regard. However, SHGs can often ignore this stipulation given that they have more flexibility because their initial loans are from their own group funds and their activities are less closely supervised by the banks.

In summary, the evidence seems on balance to suggest that SHGs are probably less likely to include poorer people than Grameen groups; neither system reaches the very poorest. The evidence on impact, however, is too unclear to make a conclusive judgement. 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 some Grameen groups, and, if they do, how to minimise these effects.

'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-financial services have enabled large numbers of poor people to improve their social and even their political status, as Chapters 5 and 9 illustrate.

This effect is 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 under consideration 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 as the next two chapters illustrate. However, if they are successful it seems obvious that this will enhance their status more than the fact of being a client of a bank or MFO, which is what the members of Grameen groups are. The bank of which they are clients has, at least until recently, often been far from customer-friendly. Although competition is forcing Grameen MFOs to be more flexible, they still have rigid loan rotas and repayment schedules. Although this is changing, freely withdrawable savings are still the exception rather than the rule. The analytical framework of sustainable livelihoods is increasing our understanding of the complexities of poor people's financial needs (see Chapters 3 and 4), 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 cost 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 that 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.

At the same time, as the next two chapters clearly show, SHGs are more vulnerable to capture by vested interests, and to inequitable distribution of the benefits, because they are less closely supervised by the financial intermediary where they deposit their savings and from which they may take loans. While it may be possible to avoid such outcomes through effective promotion (see Chapter 5), this only adds to the overall promotional costs.

Moreover, as suggested earlier, there have been many cases in India where SHGs have been used as channels for government grants and other poverty alleviation programmes. These programmes can be very beneficial to 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.

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.

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* organisations. Fernandez (2001: 91) reports that some 200 (about 2.5 percent) of the total of 77,495 members of SHGs sponsored by MYRADA were elected to their *gram panchayats* (elected village councils) in 2000. In 1999, 30 members, almost exactly the same percentage, of the 12,000 members of Activists for Social Alternatives (ASA)'s Grameen-type groups in Tamil Nadu were similarly elected (Hishigsuren, 2000: 71).

In addition, many Grameen-type groups in Bangladesh have switched their business from one bank to another, in search of better services; this is good evidence of their independence and empowerment.

Some Indian NGOs promoting SHGs, such as the DHAN Foundation and MYRADA, encourage and assist 'their' SHGs to come together in clusters and federations (see Chapters 5, 8 and 9). These bodies may or may not themselves be involved in financial intermediation, and some of them have become large and powerful democratic organisations in their own right, which may be able to empower members of their SHGs further.

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 Tamil Nadu (Hishigsuren, 2000: 27-8) also encourage their members to form similar apex groupings, for a variety of non-financial functions.

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 M *et al*, 1998: 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.

Feasibility within a given environment

There is a great need and demand for micro-finance 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 organisational capacity to deliver the services to those who need them. Organisational capacity-building takes time and costs money. A system which requires less organisational 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 organisations which work with the Grameen method in India are also expanding very fast, and it is to be hoped that there will be many occasions in the future when people can make their own choice from two or more competing providers of micro-financial services. 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, my tentative conclusion is 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.

Conclusions

I summarise the pros and cons of each system in Table 7.1. More broadly, Bangladesh is relatively homogeneous and 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, autonomous, readily transferable and dependence-creating system that 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. 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. In making much greater demands on members of SHGs to manage themselves, such groups are more vulnerable to collapse.

As small autonomous organisations they are also more exposed to capture, both from within and from without. In particular, 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 SHG 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 of poverty in India. If not, they will become no more than another milestone in the nation's long list of development failures.

Table 7.1: Summary of the pros and cons of the SHG and Grameen systems

	Self-help groups	Grameen groups
Plusses for clients	• Flexible • No need for bank at all • Highly empowering • Members can save and borrow as needed • Free to chose suppliers • No enforced loan ladder • Can evolve from existing groups, ROSCAs, chit-funds, etc. • Can access the full range of bank services • Can evolve into federations, and cooperatives	• No need for literacy • No need for members' initiative • Protected from internal and external exploiters • Poorer people are included • Belong to and are supported by the bank • Bank can offer a range of additional tailor-made services
Minuses for clients	• Need management skills and time • Depend on good accounts • Can be captured internally or externally • Cash may not be secure	• Must meet frequently • Little freedom or flexibility • Group composition not wholly under members' control • Pressure to borrow • Interest rates inflexible
Plusses for banks	• Lower transaction costs • Can fit into any branch • Graduation easier • Can build on existing groups • Savings mobilisation easier • Groups can absorb odium of expelling members	• Can resist subsidised 'schemes' • Tighter control • Standardised MIS • Standardised procedures • Easier to forecast need for funds • Can use lower-grade staff
Minuses for banks	• Hard to monitor • May be tempted by other banks or by politicians • Slow to develop • May form own federations • MIS more complex • Need NGOs or highly committed staff to develop groups	• Higher transaction costs • Need continuous guidance and presence • Need dedicated system • Hard to evolve and change
Suitable conditions	• Existing bank network in rural and poor areas. • Diffused communities, castes, wealth levels • Tradition of informal financial services • Wide variety of scale and nature of investment opportunities • Some local leadership • NGOs and/or committed bank staff	• Very poor, homogeneous communities • Highly marginalised people with little opportunity and/or initiative • Few traditional informal financial mechanisms • Lack of financial intermediaries • Resource poor, little hope of graduation • Large numbers of small business opportunities • Few NGOs

[1] Group systems are not only predominant within modern micro-finance practice, but are also common in informal financial systems, especially the traditional rotating savings and credit associations (ROSCAs), chit-funds, etc. which are found throughout the world. As suggested later in this chapter, some self-help groups in India have emerged from ROSCAs and similar informal groups.

[2] The Census of 2001 suggests that the proportion has fallen to 26 percent, a significant reduction, although there is still much debate about this figure.

[3] The analysis of operating performance in Chapter 10 seems to confirm that Grameen-type organisations have higher operating costs, largely because of staff costs.

[4] The analysis provided in Chapter 10 suggests that this may not be the case, but that analysis looks only at the number of SHG borrowers that have borrowed as a result of SHGs taking loans from MFOs, and therefore does not include all the other financial transactions that take place in the SHGs, whether they borrow externally or not. Including these in the calculation would make staff of SHG programmes more productive.