

The Maturing of Indian Microfinance

Findings of a microfinance impact assessment study (baseline) - implications for policy and practice

Study by EDA Rural Systems, for SIDBI Foundation for MicroCredit

The role of microfinance in improving the life of the poor has been widely discussed. Key questions about who microfinance reaches and what it can achieve are still open, although expectations of poverty reduction and women's empowerment are widespread. EDA recently conducted an extensive baseline study as part of SIDBI's National Microfinance Support Project that reviews these issues in the context of Indian microfinance institutions. The main findings of this baseline report are summarized here. The full report is available on www.edarural.com/impact.html

Impact study of the National Microfinance Support Project (NMFSP)

This study seeks to contribute to a better understanding of the challenges faced by MFIs in India. Many of the findings are also applicable to other developing countries. The study employs a mix of quantitative and qualitative research methods. The large baseline sample (nearly 4,000 clients, 1,400 non-clients, 280 dropouts, 150 case studies) drawn from 20 MFIs, provides strong evidence for its findings.

Microfinance Models in India

Indian MFIs utilize different models of microfinance: Group-based: Self Help Groups (SHGs) and Grameen replicators, and Individual Banking. The SHG model predominates, accounting for 65% of 1.4 million total clients. Differences between models are reflected in varying foci (development versus financial sustainability focused) and scale of credit. These factors affect outreach, access to and use of credit, and potential impact.

Microfinance Outreach in India

At the household level, few clients (8% of the sample) have access to formal credit. Slightly more (+19%) have savings in a bank or post offices. Group-based MFIs (SHGs and Grameen models) target women. A substantial number are from poor and socially marginalized households, including some very poor. Individual banking MFIs usually target men with larger financial products; clients in this model tend to be from better-off households.

Reaching the Unreached		
Client households	SHG & Grameen	Indiv. Bank
Sample households	3,020	888
No bank credit	93%	94%
No formal savings (Bank/Post office)	83%	67%
Below national poverty line	43%	15%
Below \$1/day at PPP	61%	23%
Scheduled Caste/Tribe	36%	17%

Small loans and (lower) interest rates are not determining factors for enhancing outreach to the poor. Instead, the study shows that responsiveness to client financial needs (e.g. the range of products offered) along with operations in poor areas, prove to be the main factors.

The data broadly supports the perception that there is a trade-off between outreach to the poor, and operational self sufficiency. Yet, there are 2 important exceptions: 2 SHG MFIs, and 2 Grameen replicators that combine sustainability with substantial depth of outreach.

How has micro-credit been used?

Largely for enterprise investment: non-farm, animal husbandry and agriculture. Also, substantial use for household needs and consumption smoothing In the SHG model.



Microfinance Enhances Choices Available to the Poor

More significant findings for the poor on many indicators comparing clients of different wealth ranks and non-clients indicate that microfinance has:

- Enhanced the opportunity to save
- Enhanced the opportunity to acquire a productive asset,
- Reduced dependency on moneylenders, and
- Reduced the interest burden on total borrowings.

Microfinance can Help Clients in Coping with Vulnerable Situations

Building of assets, new livelihoods and accumulated savings help the coping strategies of the poor. Nevertheless, It is the most vulnerable (those with irregular income sources, women headed households, existing indebtedness) who are the least creditworthy. Such very poor households may struggle as MFI clients and their vulnerability can lead to dropout.

Microfinance can be an Empowering Opportunity for Women Clients

Targeting women for financial services is a good start on the road to women's empowerment, enhancing opportunities for their individual growth, economic activity, decision-making in the household and the community. Case studies give clear examples of this, although gender roles and opportunities tend to reflect socio-cultural (patriarchal) norms. Women are disadvantaged by lack of exposure to the world of business and enterprise, and by perceptions about what women can do and where. In such situations, credit may be available but credit alone is not a solution.

Microfinance Helps in Reducing Client's Dependence on Money Lenders (though use of this source continues)

In comparison with non-clients, fewer client households are borrowing small loans from high cost informal sources. Nevertheless, one-third of 'old' client households borrow from moneylenders especially for larger amounts (for example, needed to meet marriage obligations) or for amounts needed urgently (for example, needed for medical costs). Microfinance, so far, has not reduced either the business or the terms of moneylenders. There is some evidence for the reverse, that microfinance may in fact increase informal money lending, if clients need to 'top up' micro-loans, or borrow to repay according to the instalment schedule.

What about the impact on poverty?

These are clear effects of microfinance, but whether they are sufficient to move households out of poverty is unclear. Comparison of endline data with this baseline study will enable more substantial conclusions on this issue. The data shows some movement of clients into less poor wealth categories in 4 MFIs, but continuing poverty of about one third of clients (including 12% very poor) after five years of microfinance. Involvement in microfinance may reduce poverty for some clients, but not for all.

Policy Implications

From the baseline analysis, the study draws some implications for policy and practice, including the challenges of:

- Extending microfinance to under-served and poorer regions within India, which include areas (especially in the north) where women face severe gender barriers;
- Balancing what is manageable and sustainable for the MFI with systems that can be flexible and responsive to the needs of diverse clients;
- Identifying and responding to the differences in client financial needs that arise from varying economic circumstances, livelihoods and household cash flows;
- Building better communication and transparency for a clientele which is often unschooled (60% of women clients have not completed primary level schooling);
- Enabling safe savings mechanisms and sustainable interest rates for micro-credit that can effectively meet the needs of the large numbers of people that remain outside the formal banking system.

