An Assessment of Microfinance among Poor Groups in Bangalore

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Introduction: Microfinance, earlier known as microcredit, has been studied in terms of its impact on women's bargaining powers in the household, empowerment, overall wellbeing, and mobility along the spectrum of poverty (Helen Todd; Jasmine Burnley; Naila Kabeer).

Our study has been conducted over a period of two years between 2006 and 2007 in Bangalore. The impact of microfinance in rural areas can be mapped more easily owing to many years of its operation there. In contrast, microfinance in cities is a relatively new phenomenon. Further, the situation in cities is laced with many more complexities. This is unlike the case in rural areas where power equations and political relationships are clearer than what they are in cities. In our study, we have tried to outline some of these complexities. We have tried to explain that urban poor groups, owing to the instability of their incomes, need access to multiple sources of finance. But it also matters what degree of poverty individuals and groups are. This is because if they are just moving out of absolute poverty and are trying to stabilize their situation, accessing multiple sources of finance can be precarious owing to increases in likelihood of debt. A serious event such as death/ill-health of a family member can push them down the spiral of poverty.

In this paper, we have tried to explain why more and more institutions are entering microfinance, how microfinance loans are used and whether microfinance is purely a savings and credit exercise. If this is so, what happens to its claims of enabling the poor groups to become entrepreneurs? In all the areas that we surveyed, we found that apart from microfinance, other forms of finance also existed. This includes chit funds, private financiers and moneylenders. We have explained how each of these systems works and how the poor plug into each one of them.

MFIs are expected to follow certain procedures and stipulations laid down by the RBI. However, there is gross violation of this. We have detailed the existing violations. NGOs and activist groups need to pay attention to these. Else, MFIs are turning out to be the very moneylenders that they demonize.

In our fieldwork, we found that the poor are increasingly falling into the debt trap. Some of them use the microfinance loans to repay other loans. Most women are usually part of more than one *sangha*. Some of the people are forced to leave the locality overnight and go elsewhere in an effort to escape their debts. We also encountered cases of suicide owing to increasing debts in one area. At the same time, microfinance is not accessible to all. Its reach is limited to bankable women and regularized slums. This alerts us towards understanding the nature of poverty and what implications a intervention like microfinance can have on people at different levels of poverty. This requires more detailed research. We hope this paper goes some way toward informing such a research agenda.

Fieldwork Description: Fieldwork was undertaken in Rajendranagar, L. R. Nagar and Ambedkarnagar (Ejipura Ward), Vandimode (K. R. Market) and Nakkalbande (Jayanagar). We interviewed women who are members of *sanghas* and also some of the local leaders in the areas. This allowed us to understand how microfinance was impacting the targeted beneficiaries. Sepcifically, we were interested in understanding how women access finance through various circuits and the role that slum leaders play in facilitating this access to finace. Our hunch was that in some slums, it is the leaders who are also moneylenders and/or running finance companies. If this was truly the case, we were keen to explore the power relationships that existed between the leaders and the poor groups and examine if microfinance was influencing these power eqautions.

We also investigated other sources of finances in these areas including private financiers, non-registered finance companies and moneylenders. This was done to understand what are the various avenues through which the poor access finance. We also wanted to compare the interest rates charged by these various networks/institutions. This helped us to analyse whether the interest rates charged by microfinance were truly less than the rates charged by "exploitative moneylenders."

Interviews with private and nationalised banks, microfinance institutions and individuals researching on microfinance were also conducted to understand the intricacies involved in the operation of microfinance and how microfinance policies are formulated.

By interviewing these different actors, we attained a relatively rich and complex picture of how microfinance operates.

Increasing presence of Banks, MFIs and NGOs in microfinance: Microfinance is increasingly becoming a lucrative proposition. This is because of the increasing emphasis on bringing the poor and their earnings into the mainstream financial system. Banks and microfinance institutions have recognized that the poor have varied and diverse needs. By providing loans of small amounts, their needs for educating their children, accessing healthcare facilities, purchasing commodities for festivals, etc. can be served. *The Hindu Business Line*, October 27 2006 mentions, "Off late, some of the leading commercial banks, such as ICICI Bank, HDFC Bank, UTI Bank and the State Bank of India, have begun focussing on this sector rather aggressively. Even some of the multinational banks operating in India, such as ABN Amro, Standard Chartered, HSBC and Citibank, have moved into the sector. There is a growing realisation among commercial banks that micro-finance is a bankable proposition."

There is an intricate link between private and nationalized banks, microfinance institutions (MFIs) and NGOs. Private banks such as ICICI lend money to MFIs. MFIs in turn, distribute the money as microfinance loans to borrowers on behalf of the private bank. Banks such as ICICI find it very expensive to enter the field directly and organize *sanghas*. Intead, they find it cost-effective to lend to MFIs who in turn do the distribution. The MFI pays the bank interest on the amount lent. Similarly, nationalized banks in cities disburse money through NGOs. In the field however, we came across instances where cooperative banks were directly entering the field and offering money to people.

A MFI is usually a non-banking financial institution (NBFC). The Reserve Bank of India has laid down guidelines about NBFCs and how these can be formed. As a NBFC, the MFI cannot take deposits from its borrowers. Many MFIs find this to be a restrictive clause. In our investigations, we found that usually MFIs hold on to the savings of the poor as deposits and then return it back to them with interest in an effort to bypass this prohibition. MFIs either work through NGOs or independently. In the former case, NGOs are responsible for the formation of *sanghas* and collection of interest and loan repayment. The MFI lends money to the NGO at a certain rate of interest. Within the *sangha*, money is circulated at a higher interest rate. For e.g., MFIs may give the NGO at 3% interest but within the *sangha*, the money may be rotated at 5-8%. The differential is reatined as profit of the group and used in future rotations. The MFI pays the NGO a fixed sum of money for every *sangha* that the NGO forms. Increasingly however, MFIs are directly entering the field. One MFI that we were in touch with mentioned that NGOs are interested in microfinance for the commissions that they get and not for "empowerment".

NGOs receive a large amount of funding for microfinance from donor institutions. In Bangalore, many NGOs are dependent on microfinance as their main funding source. Therefore, most NGOs have a microfinance programme in their portfolio of activities. A C-GAP (Consultative Group for Assistance to the Poor) publication titled "Access for all" mentions that some NGOs have now become "professional MFIs". They are moving away from the donor mode. It is therefore apparent that NGOs have a large stake in microfinance.

Microfinance Interest Rates:

The usual interest rates vary between 24%-36%

Banks such as ICICI charge between 9%-21% interest rates

NGOs offer loans at rates between 1.25%-3%

MFIs such as Janalaxmi charge an interest rate of 24% + 2% service fee

Ujjivan, a MFI, charges 16% + 2% service fee and other expenses related to book-keeping, organizing meetings, etc.

Andhra Pradesh based Spandana charges 36% interest

Nationalized banks such as Canara Bank charge an annual interest rate of 9.5%

Cooperative societies and banks charge 11%

Use of Microfinance Loans:

We found that microfinance loans are largely used for personal expenses such as medical emergencies, payment of children's school fees, marriage expenses, etc.. Some of the women we encountered take small loans from the *sangha* to purchase ration and food items. Microfinance loans are also used to carry out house repairs and for making house rent payments.

A large number of women use microfinance loans to pay for their children's education. Women from one *sangha* in Rajendranagar pay between Rs. 70 – Rs. 100 per month as children's school fees. The admission fee for joining the school is between Rs. 700 – Rs. 1,000. In another *sangha* in the same area, a woman had taken a loan of Rs. 10,000 at 2% interest rate, to pay for her children's school fees. She is now repaying Rs. 500 per month. MFIs have found that there is an increase in loan taking around the time of children's admission to schools and before festivals. Ujjivan, a MFI based in Bangalore, is now launching education loans under its microfinance programme. Loans from the *sangha* are also used for spending during festivals. Ujjivan has now begun to offer a special package of festival advances to its borrowers. Borrowers get Rs. 1,500 as festival advance in the midst of their borrowing-repayment cycle.

However, we did not encounter a single case where *sangha* loan were used for business/enterprise. Advocates of microfinance are arguing that *sangha* loans are useful for stabilizing present conditions. By the second/third cycle, people start using the loans for investing in businesses. But, in the cases that we examined, people had entered the fourth cycle of loan and yet, there were no instances of individuals who were using the loan for starting/advancing business. K, a 60-year old widow residing in K. R. Market, had taken loans of Rs.500, Rs.1,000 and Rs.1,500 from the *sangha* for household and hospital expenses, and also to clear other loans that she had taken from other sources. She pointed out that the *sangha* provides loans of small amounts, which is useful for personal expenses, but cannot be used for business purposes. We found that hawkers dealing in expensive fruit and premium items depend on moneylenders for loans because *sanghas* cannot advance loans of higher amounts, in a short period of time.

Meager Savings – questioning the claims of microfinance:
From the above, we are questioning whether microfinance is simply about savings and credit rather than providing opportunities for moving out of current conditions. During our research, we found that women in different areas save between Rs.20-Rs.250 a week. There were fewer instances of higher end saving and many more of savings between Rs.20-Rs.50. Some of the interviewees mentioned that they do not save much in *sanghas*. For e.g., in one *sangha*, after four and half years, members had savings between Rs.7,000-Rs.9,000. In another sangha, women had saved between Rs.2,500-Rs.4,800 after two and half years of the sangha's existence. A local leader in Rajendranagar who is also a moneylender concurred the same, pointing out that women save much more in chits than in *sanghas*. This is because chits are usually of high value and the women who participate in chits have to compulsorily save the amount of money committed to the chit. We found that women participate in chits during periods when they have a high income and are keen to turn to save larger amounts. In K. R. Market, we found that remittances to the villages had decreased with the entry of microfinance. Each person is a member of two to three groups and in Rajendranagar, we were told that most women were members of between 3-8 groups. In some cases, people are repaying more than Rs. 1,500 per week. This alerts us to the increased debt burdens among the poor.

Multiple Finance Circuits: In all of the areas we surveyed, we found that apart from microfinance, people invest in chits and borrow money from private financiers and moneylenders. This is because groups among the urban poor need money for various purposes and one source may not be enough to fulfill their needs. Moreover, as we mentioned above, the need for money may be greater during certain periods in the year such as festivals, time of school admissions, etc. During these times, urban poor groups may not be able to access money for all their need from one source only. Financiers, moneylenders and now MFIs recognize this phenomenon. Thus, women in a group meeting in K. R. Market pointed out to us that while financiers are present in the market on a day-to-day basis, the number of financiers increase around festival times. This is because those running businesses constantly need money to invest in business during festivals. Procedural requirements have to be completed to obtain microfinance loans. During times of emergency when the need for money is urgent, it may not be possible to fulfill all the procedural requirements. Therefore, people need access to money beyond microfinance.

In our research, we found that women continue to invest in chits. A senior journalist reporting on microfinance also pointed out that chits have not declined with the entry of microfinance. In Ambedkarnagar, an interviewee mentioned that chits are organized in her lane whenever people urgently need money. It is a myth that only the better off among the poor participate in chits. This woman had joined chits ranging from Rs. 100 to Rs. 2,000. She explained that when she had more money in her hands, she would join chits of higher value. When she was out of work or did not have enough money in hand, she would refrain from joining chits or enter chits of lower value. During times of festival, she would join chits to save money to purchase clothes for her children. Diane Singerman (1995) in her work on the Sha'abi community in Cairo found that the *gaamiyat* (same as chits) were organized when a woman was in desperate need of money, particularly for marrying off her children. Women who are clever at playing finances would set up the *gaamiyat* or a woman in need would approach such women to organize a savings group. In Rajendranagar, we found that people participated in year-long chit groups. These chits ranged from Rs. 50 – Rs. 300. Some chits were organized around festival times such as Diwali chits, *aashaadha* chits, *pataaki* (fire cracker) chits. Thus, chits seem to address emergency and seasonal needs.

People also borrow money from private financiers. These private financiers provide daily loans. For instance, a person in need of Rs.100 can approach the private financier who will advance him/her with Rs.90. At the end of the day, the person must return Rs.100. Private financiers and some MFIs deduct the interest amount from the initial principal amount advanced.

Local leaders play a very important role in the case of private financiers and finance agencies. In Rajendranagar, we found that moneylenders enter the area through local leaders. Local leaders introduce borrowers to moneylenders and stand as guarantors for the borrowers. The leaders are then held responsible if the borrower defaults on the payment. In some cases, moneylenders lend the capital to the local leaders at a certain interest rate. The local leaders disburse smaller amounts to people at a higher interest rate. In this way, a finance network is created in the area. In this way, about six people act as middlemen for the moneylender/finance company and each will introduce minimum 10 persons to the company for loan. In Vandimode, local leaders receive commissions for each introduction to the finance companies.

This model is now being adopted by one MFI. The MFI has started identifying local leaders. It gives the leaders a certain amount of money to lend to individual borrowers. If the borrowers default on payments, their properties and belongings can be taken away. This leads us to question the "empowering" aspect of microfinance. The power relations are now being reconfigured. The local leader now has greater control over the borrowers.

In Vandimode, a community organizer informed us that apart from the SJSRY scheme, MFIs such as Ujjivan and Janalaxmi are constantly giving loans of between

Rs.5,000 and Rs.10,000 to the people. According to him, when people are given small loan amounts, they repay promptly. Large loan amounts are however spent on alcoholism, etc. Small loan amounts are often used for paying school fees, social functions and other basic needs. This person organizes thrift and credit groups but has found that despite this, people are still approaching MFIs for loans.

It is important to note that MFIs don't intend to wipe out the moneylender. Their goal is to marginalize the moneylender and to reduce his/her client base. The government realizes that the existence of the moneylender is crucial, esepcially for advancing money in time of emergency.

Are multiple finance circuits increasing the debt burdens? Benjamin and Bhuvaneswari (2001) in their study on industrial clusters and poverty in Bangalore found that access to multiple sources of financing provides urban poor groups with opportunities to move out of their current situation. They explained that the poor, over time, learn to play the finance markets and use the money to invest in their businesses and to acquire more space to carry out their economic activities. However, they also caution to the fact that as some of the poor groups use finance and money to move out of their conditions of poverty, any serious event including ill-health or death of family member, can push them spiraling down into the debt trap.

Internal Moneylenders: During our research, we found that in *sanghas* of 14-20 women, some of the women would appropriate a larger amount of the loan. In turn, they would lend it to other women, hawkers in the market, etc. These women had become moneylenders by roating the *sangha* money. For e.g. in Anjaneappa Garden, we came across 10 members who had turned into moneylenders. They started by charging 10% interest but later reduced it to 5%. Sometimes, instead of collecting interest, they were collecting *raagi* (millet). They asked borrowers for house documents as security. Later, if the borrowers did not repay in time, they would take away the house. Some of the Nakkalbande and Jayanagar hawkers were their borrowers.

Is microfinance truly about access for all?: One of the questions that we were concerned with is whether microfinance reaches out to people at all levels of poverty. We found two trends:

1. **Non-notified slums are excluded from access to microfinance:** Private and nationalized banks as well as MFIs are wary of lending money to non-notified slums. We found that ICICI bank has profiled all slums in Bangalore. Loans are not advanced to people residing in non-notified slums even when people hold genuine documents. Similarly, another MFI explained that before they start operations in a slum, they verify with the BDA and the local police station whether the slum is due for eviction. If it is, then operations are immediately closed. Even nationalized banks don't give loans to non-notified slum dwellers. In an interview with the manager of Canara Bank women's branch, we asked the manager if her bank gives microfinance loans to non-notified/illegal slums. She explained the NGOs do the identification for her bank and they inform the bank not to give money to non-notified and illegal

slums. From this it appears that NGOs also control which groups can have access to microfinance.

2. **Microfinance does not reach the poorest of the poor women:** A reporter on microfinance clearly pointed out that MFIs lend only to "economically active women". They must ensure that their client is creditworthy. During our research, we found that most of the women who were members of *sanghas* had stable jobs such as housemaids, corporation workers, women running petty shops/businesses, stable apprenticeships, etc. Some of the women also had other members in the house who were income earners.

Microfinance Procedures – violation of government regulations and norms: Women borrowing loaning from MFIs have to provide details of all the assets they own and also documents such as *patta*, ownership of the house, electricity bill and identity card. Loans are often advanced to people who possess land/property documents. In the absence of these, rent receipts are accepted. Assets are also accepted for surety. Some researchers on microfinance pointed out that according to the RBI regulations, MFIs cannot demand such documents. This is because MFIs are not moneylenders but are there to provide the poor with relief from moneylenders. By asking for documents, MFIs are acting like moneylenders. Similarly, according to RBI regulations, MFIs cannot fine borrowers for late repayment. Nationalized banks such as Canara Bank offer defaulting borrowers a window period of six months before they can act any further. Ujjivan justifies charging fines by stating that just as a middle/higher income person has to pay a penalty on delayed credit card payments, in a similar vein MFIs fine their borrowers for late repayment.

Similarly, RBI has laid down the interest rates that private finance companies can charge. But these companies often charge interest rate higher than what is mandated. We found that private financers in Vandimode maintain two forms of records. One form of record is that which shows that interest has been collected as per government rules and regulations. But in reality, a higher interest rate is collected. For example, the government in its notification has said that the interest rate should not exceed 2 % but in reality the financiers are charging 20% interest rate, ten times more than the government order.

Conditions of Defaulters: There is a high rate of defaults on repayments. In areas like L. R. Nagar, we found that people had left the area owing to the debt burden. In another case in Rajendranagar, 15 *sanghas* came together form a federation. This was because 12 groups had taken loan of Rs. 2.5 lakhs from Banshankari Cooperative Bank The repayment was irregular. At the same time, Andhra Pradesh based Spandana who was disbursing microfinance loans in the area was facing problems with repayment. The repayment was poor because some of the members of some of the groups had gone out in search of employment and had not returned back for a long time. After the formation of the federation, members in need of loans would be screened by the federation and accordingly, it would be decided whether the member should approach a bank or MFI for the loan.

Linking Microfinance to Clear Land Titling: Microfinance is now viewed as a mainstream form of financing for the poor. The earlier claims of empowerment have now been replaced with the slogan of banking for the poor. International agencies such as C-GAP, a consortium that makes policies on microfinance, is persuading governments to implement these policies. C-GAP believes that governments should step out of the microfinance sector. Their role should be one of facilitating the environment for financial inclusion of microfinance. C-GAP proposed that governments should develop proper legal and regulatory frameworks for clear land titling in order to facilitate the inclusion of microfinance into mainstream financial systems. C-GAP's insistence on clear titles is based on the idea that land can be used as collateral in case of defaults on loans.

Conclusion:

This study is the beginning of a larger research agenda on understanding the various ways in which microfinance impacts the lives of the poor. From our preliminary findings, it is clear that some of the claims of microfinance such as encouraging savings, giving impetus to opportunities for entrepreneurship, etc, are suspect. Apart from this however, microfinance seems to be influencing the various relations that exist within the structure of local politics. This needs to be investigated much more in order to question the "empowerment" claim of microfinance. We hope that this study is the beginning of such a research agenda.