Sanghamithra

A Micro Finance Institution With A Difference

By
Aloysius P. Fernandez

July 2004

"Sanghamithra envisions a society that supports a sustainable and vibrant financial and development environment where every Self-help Affinity Group of the poor has the ability to access credit at competitive terms as well as skills and linkages in order to maximise the livelihood opportunities of its members."

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Sundramma

Sundramma is a SAG member since 5 years, living with her husband and two children in Holalkere of Chitradurga district. The family was landless and lived in a rented house in front of which they set up a small provision shop. She and her husband also worked as agricultural labourers. After 6 months of regular savings Sundramma asked for and got a loan of Rs.5,000 from her group to expand her provision shop. After repaying this loan she took another of Rs.10,000 of which she used Rs.5,000 to further improve her shop and Rs.5,000 to buy a cow. She then took a third loan to buy 6 sheep which soon expanded to a flock of 12. She sold 7 sheep for Rs.10,000 which she invested in a chit fund since she still owed some money to the SAG and was not yet eligible for a fourth loan. With the chit amount she purchased a small house site and also took a 2 acre coconut plot on lease for one year. Her husband started selling tender coconuts. By then she settled her earlier SAG loan and got another loan of Rs.15,000 of which she used Rs.5,000 to buy a buffalo, Rs.5,000 to further expand her provision store, and Rs.5,000 to purchase wholesale bakery items which her husband then started selling along with the tender coconuts. She continues to be a responsible SAG member and her family now has assets worth Rs.1 lakh.

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राष्ट्रीय कृषि और ग्रामीण विकास बैंक
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Managing Director

FOREWORD

Providing the underprivileged access to financial services serves as one of the practical measures to alleviate poverty and micro finance is a powerful tool in that process. Notwithstanding a broad convergence - international and domestic - on how financial services for the poor can be best provided, there are nevertheless gaps in the delivery of these services within the disaggregated poverty matrix.

The World Bank's *World Development Report 2003* estimates that of the world's six billion people, 2.8 billion live on less than US$2 a day. In the next 25 years, population is predicted to grow by a further two billion, with an emphasis on countries in the developing world. The 'Millennium Development Goals' (MDGs) powered by the UN is a comprehensive agenda for reducing the causes and manifestations of poverty by 2015 and encompasses micro finance as one of the means for fostering social development and eradicating extreme poverty.

In India, we stand at a critical crossroad in the evolution of the micro finance effort. A variety of experiments have taken place in various parts of the country to provide micro finance to the poor. This book is about one such institution established for demonstrating that the 'poor are bankable". I have known the author for over a decade and have been an admirer for much longer. He and his team at MYRADA have been at the forefront of experiments in micro finance. They were innovators when the term was not fashionable and have inevitably chosen to travel the path of maximum challenge.

Establishing micro finance institutions of excellence is not always an easy task. Innumerable issues require attention and Murphy's law operates at its severest. In such a context this book serves as a 'ready-made' reference for agencies and institutions that would like to enter the arena. The book gathers the experiences of institutional building by the author and his team and for this reason will prove of value and worth to policy makers, researchers and practitioners alike.

Dated: June 24, 2004
Place: Mumbai

Y.S.P. Thorat
Managing Director

INTRODUCTION

SANGHAMITHRA –
A MICRO FINANCE INSTITUTION WITH A DIFFERENCE

By

Aloysius P. Fernandez

Introduction:

The decision to name the micro finance institution (MFI) **"SANGHAMITHRA"** was welcomed by all those who were involved in setting it up. Sanghamithra was the daughter of Emperor Ashoka who sent her to Sri Lanka on a mission; the MFI also has a Mission - to ensure that the poor have easy, quick and transparent access to all their credit needs. The name also projects the core strategy of the MFI, namely, to build a relationship of trust directly with the Self-Help Affinity groups – "Sangha" means group and "Mithra" a friend.

This booklet traces the growth of Sanghamithra Rural Financial Services (SRFS) from the time it was conceived till the fourth year of operations. However the process of setting up the MFI during the preparatory period between 1993 to 1999 has been described more in detail than the performance of the MFI after 1999 when it became operational. The reasons for this are that this booklet is written in response to several requests for guidance on how to start an MFI. Further, the process of formation has not been documented by outside rating agencies and evaluators who are all concerned with Sanghamithra's performance after 1999; these documents are available. If Sanghamithra's performance has been above par, this writer is of the opinion that the major reason is the effort that went into preparation between 1993 and 1999.

Further, the lessons that can be drawn from a study of the preparatory period are more useful (and perhaps unique) than those which emerge from a study of the experience post 1999 when it began to function along the lines of MFIs of which there are several examples and studies. However, even though the Chapters on Sanghamithra's performance between 1999 1and 2004 may not provide all the details of Sanghamithra's experiences, they are adequate to provide evidence that the MFI is moving along the path to sustainability and towards achieving the objectives it set for itself. To be seen to be objective, the Chapters on Sanghamithra's performance draw heavily on studies conducted by outside consultants and commissioned by financial institutions that supported Sanghamithra. It may be, however, too early to draw firm conclusions in these areas. Briefly, this booklet attempts to provide insights into a unique experiment in the micro finance sector. "It has important lessons on how an intermediary organisation can be structured, on the impact it could have on the banking system and on its own growth and sustainability" (M.S. Sriram[1]).

Sanghamithra was incorporated as a not-for-profit company in February 1995, under Section 25 of the Indian Companies Act of 1956.

The broad objectives of Sanghamithra initially agreed to were the following (these objectives were refined and elaborated during 1993-95 and the final version is given in Chapter 4):

1. To work with the poor and to build on and reinforce their efforts to rise and remain above the poverty line.
2. To provide credit to groups of poor persons who come together on the basis of affinity, with the support of self help group promoting institutions.
3. To create replicable models in the area of financial services for the economically poor and socially exploited sections of society.
4. To mobilise initially from other sources and later from its own resources, all types of support and linkages which the poor can use to promote and sustain their livelihoods, build the institutional capacity of their institutions, develop their skills and increase the level of self reliance and empowerment in order to overcome poverty of all kinds (economic poverty, poverty of values and poverty of relationships with people and organisations)
5. To work with the Government, Banks, Financial Institutions and NGOs to bring about changes in public policies and practices in favour of the poor and deprived, particularly in the area of rural finance and livelihoods.

Several questions were raised during the course of forming Sanghamithra. Why separate it from MYRADA? Why register it as a not-for-profit entity? Will it address the needs of the poorer sectors? Is the model replicable? How large will Sanghamithra grow? Some of these questions will be considered and perhaps answered satisfactorily in the following Chapters. But there are one or two which need to be highlighted here.

SRFS has been kept distinct from MYRADA since MYRADA did not want to enter directly into lending transactions. MYRADA has consistently held the position over the past 10 years that lending operations should not be conducted by NGOs managing development programmes; it should be left to Financial Institutions including Companies set up for this purpose. Further, if SRFS is to demonstrate

[1] M.S.Sriram: "Building Bridges between the Poor and the Banking System" - A study of SRFS.

that Banking with the poor is indeed profitable and sustainable, it has to function as a distinct institution so that cross subsidisation — which is often well hidden — can be avoided.[2]

Sanghamithra is registered under Section 25 of the Indian Companies Act. Its management, however, is not satisfied with the degree of supervision that this Act envisages. Regular, preferably monthly monitoring of Sanghamithra's performance is considered critical for its healthy functioning. Alongside this concern is the vision of the management that Sanghamithra should not grow beyond a loan portfolio of Rs.25 crores. Instead, other similar MFIs should be started in different parts of the State and elsewhere where there is need and potential. To meet this concern and to work towards the vision, the management plans to set up a Fund Management Company which will promote new MFIs, supervise all of them, raise resources and allocate them, monitor their performance and support them to build their institutional capacity. This would meet the concern of the management that it is critical for financial institutions to be monitored regularly. Unfortunately, a follow up project which was under consideration by the Canadian International Development Agency (which helped to start Sanghamithra) and which included a component to set up a Fund Management Company and a loan to Sanghamithra returnable to the Fund Management Company for on lending to other MFIs did not materialise. Plans, therefore, have been on hold.

Sanghamithra will endeavour to target the poor. The primary responsibility of organising the poor into affinity based self help groups devolves on the NGO. Sanghamithra makes its own assessment prior to lending to ensure that the SAG members are poor. But what is the definition of poor? Many of those on the "below the poverty line" list of the Government are not considered to be "poor" by others in the community and many, in fact, earn an income way above the poverty line. The Government of India brought out a Statewise "Poverty Line" benchmark in 1996-97. According to this, families of five below the poverty line are those with annual incomes of less than Rs.12,960 (Andhra), Rs.15,300 (Karnataka) and Rs.16,140 (Tamil Nadu). However, this list did not gain wide acceptance by the States. The World Bank considers all those who earn less than US 1 $ per day to be below the poverty line; at purchase power parity (December 2002), 1 USD = Rs.13.47. This means that a family of five with an annual income of less than Rs.24,582 is below the poverty line. People, however, have their own assessment. A family with two sick or disabled children may earn above the figures quoted but is considered poor because of the extra expenditure incurred. Families with unsteady incomes, with livelihoods which are at high risk coupled with comparatively high expenditure are often considered poor. Besides, several families rise and fall above the poverty line depending on the annual status of their major income or livelihood source. Sanghamithra does take the income per capita into consideration, but it also balances this with the opinions of the SAG members, before it lends to a group.

[2] For more on this, refer to "Is Micro Credit Leading to a Macro Mess" (1999) by the Author.

Many members in the SAGs also rise and remain above poverty within a few years, yet they decide to remain in the SAGs. Should Sanghamithra continue to lend to such groups where a majority are in this category? Or should it continue to explore areas where the Banks have not reached and where poverty is evident? This has to be debated, but at present, the thinking veers towards the latter position.

One concern arising from focusing on the poor and moving continuously to neglected areas is that the costs of transactions will rise and remain high. The implications, therefore, have to be analysed and a balance maintained between achieving the objective of sustainability and that of being ready to fill gaps. Sanghamithra's Management is aware that even in these market-obsessed times, an MFI that has social objectives cannot be run entirely like a business enterprise. Maintaining a balance may imply that the rate of growth is slower than what could have been achieved if Sanghamithra operated like a pure business enterprise; this has to be factored into its long-term strategy. One reason, among others mentioned later, for the decision to opt to be a "not-for-profit" company is because of the concern to strike this balance.

The significant features that identify Sanghamithra are the following: (a) its client is only the SAGs; it lends to the SAG as an institution and not to individuals in the SAG; (b) the client profile is overwhelmingly women (98%); (c) the initial contact and the training of the SAGs is done by the NGO with its own funds — SRFS has provided financial support to NGOs to train SAGs, especially those formed under various Government programmes; (d) the appraisal of the SAG prior to extending a loan is done by the SRFS Credit Manager; (e) the instrument of Credit Disbursement and repayment is always a cheque – never cash; (f) the interest rate to the SAG is 12% on a declining balance — the SAGs on-lend at rates which they decide in each case — SRFS also levies a service charge of 2% on the loan amount with a ceiling of Rs.200; (g) the repayment is done through post-dated cheques — at any time there are two cheques with SRFS; (h) the frequency of repayment is monthly and the repayment terms are 1/10 of the principal per month for a one year loan, 1/20 of the principal per month for a two year loan and 1/30 of the principal per month for a 3 year loan; the additional instalments cover the interest; (i) SRFS has one major loan product — a general purpose loan product to the SAG. It does not offer any savings product to its clients. However, the SAGs have the practice of regular savings; their performance in the regularity of savings is an important parameter in assessing their performance. The group decides on the amount of savings. SRFS does not have an insurance product; however, it recognises the value of such a product and encourages the Resource Centres[3] to mobilise insurance coverage both for people and livestock; as the Resource Centres earn a commission on this product, they are actively engaged in promoting it. SRFS has also introduced a housing loan product which runs concurrently with the general service loan to SAGs.

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[3] One Resource Centre supports 100-150 CBOs, including SAGs and Watershed Associations which pay a monthly fee for membership, as well as for all services rendered. Membership is open to CBOs formed by any NGO or institutions but they are assessed by the Management Committee of the RCs before they are accepted; they are also rated annually. Each RC has its own Management Committee comprising representatives from the CBOs, an office with a computer, an RC Manager and Community Resource Persons.

As on March 31, 2004, Sanghamithra has a cumulative loan portfolio total of Rs.16.15 crores (Rs.161 million) and 37,944 borrowers. Ninety eight percent of the borrowers are women. The size of loans is increasing with every cycle. In the last year 2003-2004, 1312 loans to SAGs ranged from 0 – Rs.50,000; 291 loans from Rs.50,001 to Rs.100,000/-; 94 loans from Rs.100,001 to Rs.200,000/- and 12 loans from Rs.200,001 to Rs.300,000/-.

Finally, all studies and ratings indicate that the performance of Sanghamithra during the past four years has been consistently good. These studies and ratings have been quoted extensively in Chapter 6 since assessments by this writer may appear to be biased. If Sanghamithra has achieved this high level of performance, the credit must go to the members of the Board who have spent hours to keep Sanghamithra on track, to the two CEOs and their staff, to the guidance of Banks and Desjardin and above all, to the SAGs who managed their affairs with a degree of professionalism and commitment that is difficult to emulate.

This introduction cannot end without an expression of sincere thanks to the Canadian International Development Agency for taking the risk to financially support SRFS in 2002 and to NABARD for the initial guidance and support between 1993 and 1999.

Sanghamithra has two programmes managed independently: an urban programme in Bangalore which started with assistance from Mrs.Rohini Nilekani and subsequently took a loan from SIDBI and the Rural Programme with its Head Office in Mysore which started with assistance from the Canadian International Development Agency and thereafter continued with loans from NABARD and the Canara Bank. **This booklet is about the Rural Programme only, which is the major one.**

CHAPTER 1

THE BIRTH OF AN IDEA - 1993

How did the Sanghamithra idea originate? From a high profile Financial Expert? From a creative Working Group? These questions are often asked by visiting Micro Finance Experts. It really originated over an everyday lunch – not a high profile power one - in the MYRADA office in mid 1993 when two senior Programme Officers reported, with a degree of pain and frustration, that the Banks were very slow in establishing links with the Self-help Affinity Groups (SAGs)[1]. What a let down! And like the lunch, which is shared by staff from five different communities bringing five different cuisines, the original suggestions to fill the gap, created by the reluctance of the Banks, were diverse. By the time lunch was over, there were two camps. The first stressed that MYRADA's strategy over the past 8 years had been to open the path for Banks to link up with the SAGs as part of their corporate strategy. MYRADA should continue with this effort instead of starting a Financial Institution; attempts to do so would compromise MYRADA's position. This writer was a part of this group. The second emphasised the situation on the ground where Banks were raising several objections to link with well performing groups, in spite of the efforts of MYRADA; if these groups of the poor were being deprived of credit which they needed in the short run, the group argued, MYRADA should be open to an alternative strategy even if it required a new Financial Institution. The second group won the day.

Sanghamithra did not start in a formal planning situation, with a clinically defined problem tree or situation analysis; it was created from the bias in MYRADA's approach to let the real situation where the poor needed quick access to credit on their terms takes precedence over MYRADA's 'ideology', at least in the short to medium term, until the SHG-Bank linkage programme gained wider acceptance and momentum. The commitment of MYRADA to support a financial environment in which the poor have access to credit, easily and quickly, from financial institutions has

[1] When these affinity groups emerged in MYRADA projects in 1984, largely as a result of the cooperative societies organised by MYRADA, in its rehabilitation projects, breaking down, they were called Credit Management Groups. The focus was on the management of credit rather than on its provision. When MYRADA entered into an agreement with NABARD to launch the R&D initiative related to these groups – NABARD provided MYRADA Rs.1 million in 1987 for this purpose – the name was changed to Self-Help Groups. However, MYRADA continued to stress that the members should be linked by affinity (mutual trust and support) and not because they were eligible beneficiaries. After 1999 when MYRADA realised that SHGs were being promoted without any concern for affinity and with little or no training to build their institutional capacity, MYRADA changed the name of the groups it promoted to **Self-help Affinity Groups or SAGs.** In this document the term SAGs will be used throughout, except where it refers to "SHG-Bank Linkage Programme" of NABARD and in quotations.

not decreased. Sanghamithra, therefore, was a 'gut' response from MYRADA staff with long experience of the complexities that the poor have to cope with in the rural situation where strategies which look 'professional' in a workshop atmosphere have to make way in some situations to meet the needs of the people.

To add to its lowly origins, the first two background notes which appear below fall far short of what major development agencies consider 'proper'. Are the end results of this poor and diverse beginning any different from those that originate in a specialised and often 'pressure cooker' atmosphere? No definite answer can be given after only four years of Sanghamithra's operations; but the achievements of Sanghamithra at this point have been analysed and evaluated by high profile Consultants and a Rating Agency, (M-CRIL), commissioned by Banks and donors before agreements were signed. These assessments are quoted liberally in this document to balance the built-in bias of this writer who is closely involved with Sanghamithra; they indicate that Sanghamithra has achieved what it set out to do within the first 3-4 years of its operations. What the future will hold is difficult to foresee, but the institution has learned much through experiencing the pains of growth, while responding to emerging situations in a constructive manner - many of which normally would have been categorised as 'threats'. It is, therefore, reasonable to assume that it will manage to survive and to achieve the goals it sets for its own growth and health in the future.

An overview of the process that began in 1993 till 2004, when this booklet was written, indicates that it could be divided broadly into three periods or time slots, the defining instrument of division being the major thrusts that were pursued during a particular slot. Within this framework the major thrust between 1993 and 1996 was to develop a conceptual base as well as the guidelines of a strategy which clarified how MYRADA could start a separate financial institution. If it started a separate financial institution, what would be the nature of this institution – for profit or not-for-profit? How would MYRADA balance and promote both the SAG Bank Linkage Programme as well as an independent financial institution? The consequences of promoting a financial institution like Sanghamithra would be that it would enter into competition with the Banks in lending to SAGs. Could MYRADA's engagement with Sanghamithra still keep a space open for it also to remain committed to the SAG-Bank Linkage approach so that both Banks and SRFS could provide quality services to SAGs? These issues, some of which were genuinely troubling, were debated during this period by the staff in MYRADA who were keen on promoting both approaches. A critical mass in MYRADA comprising staff from Head office and the major Projects debated these issues and contributed to the focus and mission that Sanghamithra would eventually adopt. Why did the management invest time and resources to involve a critical mass? Well, the simple and short answer is that is in keeping with MYRADA's style of functioning. The implications of the final choice, namely a Not-for-Profit Section 25 Company, were also analysed in relation to Reserve Bank of India (RBI) and Income Tax regulations.

Once these issues were resolved, the next period from 1997 to 2000 was devoted to setting up the support structure, clearing policy hurdles and raising resources. A CEO was recruited, the institution registered, clearances were obtained from Income Tax and RBI, a Manual of Operations and Software developed and a donor was identified to finance the start-up. From 2000 to 2004 all efforts were focused on recruiting, training and positioning staff, negotiating with Banks to mobilise resources and to streamline credit operations, starting and expanding lending operations (the first loan was given on February 25, 2000), moving from grants to loans, and breaking even as soon as possible.

CHAPTER 2

THE IDEA TAKES SHAPE

As already mentioned, the idea of Sanghamithra originated over lunch, but it had to be put down on paper, if it had to go further. Of the two background papers, both produced in 1993 (and reproduced below), one is from the writer and the other from Dr. Puhazhendhi of NABARD, who at that time was based in Bangalore. The latter's involvement right at the inception was not accidental. NABARD's involvement with MYRADA in leading the strategy to obtain recognition of the SAG model began in 1987 when NABARD provided a grant of Rs. 1 million to MYRADA for an R&D programme related to credit groups. This was the first research project that led to a pilot project in 1992 involving several NGOs and finally to mainstreaming the Bank-SHG Linkage Programme in 1996.

Self Help Groups, initially called Credit Management Groups, emerged in MYRADA in 1984-85 and drew the attention of NABARD in 1986 when MYRADA applied to NABARD for a Research and Development Grant of Rs.1 million which was sanctioned in October 1987 (Annexure 1); it was used for institutional capacity building of SAGs, and to match the groups' savings. The credit for this decision to support MYRADA's R&D initiative in a formal manner and for leading negotiations with various Banks and the Reserve Bank of India (RBI) between 1987 and 1991 goes to Shri P.J. Nayak, the then Chairman and Managing Director of NABARD, and his team at the NABARD Head Office. Between 1987 and 1991, NABARD was involved with MYRADA in assessing the SAG R&D initiative, supported by its grant, and in several meetings with the RBI and major Commercial Banks to sell the idea and to influence change in official policy. These changes included the following:- to allow the Banks to: a) lend to groups (and not only to individuals in groups), b) lend without asking for the ultimate purpose in advance and c) lend to groups which, even though not formally registered, functioned according to the norms of a registered institution. These were the three structural features of the SAG-Bank Linkage model and required policy, institutional and attitudinal changes to be introduced in the financial system and operationalised.

Interestingly, a perusal of books and articles emerging during the past three years from well known institutions and experts engaged in micro finance leave out completely the efforts between 1987 and 1990-91 to change official policy. In fact, RBI's notification related to SAGs dated July 24, 1991 and NABARD's launching of the SHG-Bank Pilot Linkage Programme in 1992, were preceded by several years of analysis of NABARD's R&D initiative with MYRADA, (which started in

1987), as well as by several meetings in NABARD and with the RBI and Senior Officers of Commercial Banks where hurdles that came in the way of extending loans to groups were discussed. This writer remembers one meeting presided over by Shri P.R.Nayak, Chairman of NABARD and attended by several senior officers of NABARD and Commercial Banks which was held in late 1998 in the Canara Bank Headquarters in Bangalore concerning three issues: a) lending to groups (and not to individuals in groups) b) lending to groups without recording in advance the purpose of loans which the group would advance to individual members and c) lending to unregistered groups; these were the three issues that met with a great deal of scepticism from bankers even though NABARD Officials approved of them in the light of the feedback from the R&D initiative. Major policy changes, therefore, were set in motion during the period 1987 to 1991. After 1992, when NABARD launched the pilot SHG-Bank Linkage Programme and after the major policy directives related to the above three basic or structural issues from RBI and NABARD were in place, the focus changed to training the bankers and on continuously removing administrative and attitudinal obstacles in banking practice to the growth of the SHG-Bank Linkage Model. During this period Shri Kotaiah and later, Shri. Y.C. Nanda, both Chairmen and Managing Directors of NABARD and other officials like Mr.Prakash Bakshi (CGM, Micro Credit Innovations Department) played a major and leading role in collaboration with an increasing circle of NGOs and, during the past four years, with MFIs and micro-finance supporting institutions which have sprung up in several parts of the country.

The background note from Dr. Puhazhendhi of NABARD given below on the need for a financial institution was, therefore, part of the ongoing effort of NABARD to develop a supporting framework for a system of micro-finance where the SAGs play a major role in decision making and where Banks play a supportive one. Shri. Subash Wadhwa, the Chief General Manager based in NABARD Bangalore during 1993-1995, which was the period when the idea of Sanghamithra was taking shape, was very supportive of this initiative. Both NABARD Bangalore and Myrada realised that a private micro-finance institution lending directly to groups could play a role in the ongoing effort to create conditions where the poor could continue to access credit at competitive rates and in a friendly or win-win situation. If the Head Office of NABARD played a major role in changing official policy during 1987-1991 related to the SHG-Bank Linkage Model, then it must be said that the Regional Office of NABARD Bangalore played a similar role in promoting Sanghamithra during 1993-1996.

The first two notes that attempted to put "some thoughts" on paper are reproduced below. These two notes were circulated to a few staff from Myrada. During the informal discussions that took place before the note was prepared, two possible names emerged for the proposed institution: Sanghamithra and GROFIN (Group Finance).

Note 1.

A NOTE ON GROUP FINANCE (GROFIN/SANGHAMITHRA)

A Proposed Strategic Intervention

MYRADA

August 20, 1993

As you are aware MYRADA*'s strategy as outlined in its Mission Statement is to support the emergence of appropriate institutions. The Credit Management Groups (or Self-Help Groups) is one such example. Others are the Watershed Management Groups and Village Forestry Committees.*

This note refers to the CMGs/SHGs which have been moving towards self-reliance and therefore need other sources of financing when MYRADA *withdraws. This is where the banks came into the picture and related directly to the groups.*

MYRADA*'s mission of supporting the development of new institutions is one part, the other is to help existing institutions (like Banks in this case) to relate to the new institutions that emerge. Our effort to establish this linkage has been going on for the past three years. NABARD supported this strategy and made serious and sustained efforts to evolve policy changes that would help to establish this linkage between Banks and the groups. As a result of this effort, the RBI issued a circular dated July 24, 1991 and NABARD followed it up with guidelines to all the Banks dated February 26, 1992. To acquaint Bankers with this new strategy, NABARD has organised several workshops, some of which have been run by* MYRADA *on our projects. I have also written a Rural Management Series paper entitled, "Guidelines for Linking Banks with CMGs", which you should have given to every Bank Manager in your area (revised on April 13, 1994 and numbered RMS Paper 19). Inspite of this effort, the Banks have not responded as expected. So far only about 150 groups of* MYRADA *have been linked with groups when there are at least 1500 groups out of our 2300 which could have been linked.*

The need for another strategic intervention has therefore emerged. MYRADA *proposed to set up a Non-Banking Institution under the Company's Act, Section 25 to fill this role. This organisation would be an independent one, though* MYRADA *staff would be involved with it at all levels. To facilitate this intervention, on our request, NABARD deputed Dr.Puhazhendhi for a period of 3 months to* MYRADA.

This proposed organisation has not yet been named; suggestions are welcome. Its primary role however, will be to receive loans from financing institutions and on-lend directly to groups.

At a recent meeting with NABARD officials, they proposed that the RRBs in the area where GROFIN is operating could also be involved possibly through a window dedicated for this purpose. GROFIN, however will serve not only MYRADA's groups but concerned groups of other NGOs that have emerged and are operating well in the area.

The mechanics regarding the working of GROFIN are being worked out and will be shared for discussion with all.

There are certain structural concepts however, which must be clarified at this stage to avoid necessary doubts and the tendency to overload any organisation.

There are broadly, three areas of activities related to the CMG/SHG strategy; these three areas are:

1. Formation of Groups: *This set of activities can never become viable; it cannot pay for itself. It involves several interventions over a 2 to 3 year period in a declining profile as groups take over responsibilities and function independently or with the support of Apex Groups. These interventions therefore will have to be provided by NGOs with project funds or from other sources. I cannot visualise the Banks undertaking any role in this area.*

2. Training of Group Members: *Once again this activity is not viable, at least not in the first two years; though the groups should be encouraged to pay for the training; but a start should be made. As I repeatedly say; it is difficult to move from free service to Re.1; but it is easier to move from Re.1 to Rs.5. This cost of these activities will also have to be borne by the NGOs.*

3. Financial Transactions: *This involves primarily the funding of groups and recoveries. This could be a viable set of interventions and this is what GROFIN will undertake. If GROFIN succeeds and earns surpluses, these could be ploughed into training activities or even into activities required to form groups.*

I have divided these three sets of activities since it is important not to overload GROFIN.

There is another set of activities which the groups require – namely financial audit and performance audit.

The financial audit is now done by MYRADA staff; but gradually the groups should be asked to pay for this service.

The performance audit is a responsibility which I have suggested the Apex groups could perform; this has started in some projects, but it has not developed into a clear strategy in MYRADA as yet.

Aloysius P. Fernandez

Project Proposal for Establishment of a Financial Service

From Dr. Puhazhendhi, (NABARD,Bangalore) – October 5, 1993

Introduction:

1. The concept of Self-Help Groups has been widely recognised and has emerged as a new approach for lending to the rural poor for their socio-economic development with active support for Non-Governmental Organisations. MYRADA has already achieved the task of implementing the credit management groups at the field level. The SHGs formed by MYRADA have registered significant improvement in terms of its socio and economic status. The initial consumption requirements of the group members were met from their own savings and the group members are now in search of economic activities to improve their income level. The concept of group pressure is working very well and the thrift habits have been encouraged. The marginal propensity to save by the group members is showing a positive trend. Many case study experiences revealed the positive impact of Self-Help Groups in rural upliftment.

2. Financing to the rural poor through self-help groups has been identified as a viable alternative in the Institutional Credit Delivery System and NABARD is implementing the pilot project with a specific objective to link the Bank with the Self-Help Groups. During the initial years of the pilot project implementation, many commercial banks and RRBs came forward to provide financial support to the SHGs. The experiences of bankers in financing these Self-Help Groups are quite impressive and the specific aspects like effective utilisation and better repayments were ensured for the Bank loan.

NABARD Letter Head, Bangalore

Dated: October 5, 1993

Dear Mr.Fernandez,

Sub: Non Banking Financial Institution for Self-Help Groups

1. Kindly recall our discussion on 30th September, 1993 regarding the need for separate Non-Banking Financial Institutions for Self-Help Groups. I have presented some of my random thoughts in the enclosed note. If you agree the proposal in principle then we may discuss the modalities and other procedures for launching the institution.
2. When the Grameena Bank model established in Bangladesh is widely discussed, I strongly feel that we should also come out with the acceptable model for banking with the poor under Indian conditions.
3. I am expecting your initial reaction at the earliest.

With warm regards,
Yours sincerely,

V. Puhazhendhi, NABARD

Need for a separate Financial Service:

3. Despite the efforts taken by NABARD, the progress of financing of Self-Help Groups by the banks is rather slow. Inadequate staff strength, lack of motivation by the branch managers, rigid lending norms and their past experience in group lending might be some of the factors which restrict the Banks to finance SHGs. Many Self-help Groups formed by MYRADA have attained the stage of maturity in terms of age of the group, savings, financial strength, etc. Hence, MYRADA proposes to gradually withdraw their support from such groups. Apex group concept has been introduced by MYRADA to take care of the interest of the Self-help Groups in the absence of MYRADA's involvement. The withdrawal proposal of MYRADA is on the assumption that the financing Banks will take care of the requirements of the groups in terms of credit support. However, this does not seem to be forthcoming at present. For example, out of 1500 groups which are mature enough to absorb credit only less than 200 groups have received credit support from Banks.

4. The above discussion brings out the fact that if MYRADA withdrew from the SHGs, the commercial Banks, as at present may not be able to support the groups in full. Hence, it is very much essential that a separate financial institution needs to be established for the benefit of the Groups, which were formed with the strenuous efforts of MYRADA. This specialised institution would help the groups to take care of their savings and also help for group sustainability at a long run.

5. Conceptually the proposed financial service is not adding more tiers in the financial structure. The existing institutional credit structure will be effectively used by the financial services and only the loaning operation will be undertaken by this financial services.

sd/-

V. PUHAZHENDHI,
NABARD, Bangalore Office

The above note goes on to suggest the objectives of the proposed institution, the legal implications and the operational aspects. Since this note played a key role in the formation of Sanghamithra, it is reproduced in full in Annexure 2.

Apart from these two background notes, MYRADA also requested Ms. Sunanda and Shri Sheshadri, Chartered Accountants who had experience of working with MYRADA for over 10 years, to advise the organisation

Sunanda & Seshadri
Chartered Accountants - Letterhead

Ref: No.165/93
The Executive Director
MYRADA
Bangalore 560 071.

Dear Sir,

Sub: Non Banking Financial Institution for self help groups

Ref: Your letter No.15-1-54/93-06 dated 11-10-1993

With reference to the above we enclose a note, working on the viability and draft memorandum and articles of association in duplicate for the discussion on 28-10-1993 at 11:30 a.m.

Thanking you
Yours faithfully,

Sd/
K.Sheshadri)
Partner

on the implications for MYRADA in launching such an initiative. They submitted a note on October 27, 1993. Among other insights, the note pointed out that (a) MYRADA, being a charitable society registered under the Societies Registration Act, would lose its income tax exemption if it invested by loan or equity in the proposed micro-finance institution, (b) the Members of the Governing Body of MYRADA should preferably not be on the Board of the proposed institution. Several other helpful comments, related to the financial institution which was at that time viewed as a potential Non Banking Financial Company were also made.

The two notes and the advice from the Chartered Accountants served as part of the agenda for a Meeting of MYRADA Programme staff held on October 28, 1993. The meeting decided to name the proposed institution 'Sanghamithra'. It also asked for further clarifications regarding the nature and scope of the proposed institution and the alternatives legally available from which the most appropriate could be selected. The choices were (a) an NBFC, (b) a Not-for-Profit Company and (c) a Mutual Benefit Society.

On MYRADA Letter Head

Ref: 15-1.54/93-06 **Dated: October 11, 1993**

1. Dr. V.Puhazhendhi, NABARD, Bangalore
2. Mr. Aloysius P. Fernandez
3. Mr. A.K.Shivaraja
4. Mr. William D'Souza
5. Ms. Yasmin Master
6. Ms. Vidya Ramachandran
7. Ms. Chandra Singh

Sub: Non Banking Financial Institution for Self-Help Groups

The discussion with regard to establishing a separate Non Banking Financial Institution for Self-Help Groups will be held on 28th October, 1993 at 10:30 a.m. at this office. Kindly make it convenient to attend the same.

With best wishes,

Yours sincerely

Harry D'Souza, Chief Accounts Officer

MYRADA requested its statutory auditors M/s. Nambiar and Associates for advice on the option to incorporate Sanghamithra as a Mutual Benefit Society. The auditors submitted a note on Nov 9, 1993 on the option of forming a Mutual Benefit Financial Company (under Section 620A of the Companies Act 1956) in which every SHG would become a member of the Company by subscribing to the share capital of the Company. The note suggested that a Mutual Benefit Society would not be an appropriate institution; accordingly this option was dropped.

From:

M/s. K. B. Nambiar & Associates

Dated: November 09, 1993

Kind Attn.: Mr.A. P. Fernandez

Dear Sirs,

Sub: Non-Banking Financial Institution for Self-Help Groups (SAGs)

This has reference to your letter dated October 19, 1993 seeking our comments on the above mentioned subject.

We have gone through the note on SAGs sent by you along with your letter. Our opinion in this regard are given in the enclosed note.

We shall be glad to furnish any further details you may require in this regard.

Thanking You,

Yours faithfully,
for K.B.NAMBIAR & ASSOCIATES
Partner

CHAPTER 3

1994 To 1996 - Searching For A Way

The period 1994-1996 was devoted to the following activities: (i) To carry the idea of an independent Financial Institution to the staff of some of MYRADA's projects where the SHG-Bank Linkage Programme had developed, like Holalkere, Challakere, Huthur, Talavadi, and Kamasamudram with a view to elicit their reactions and to work out a strategy whereby both approaches could flourish and 'compete' with one another to improve efficiency and to provide better service to the poor; (ii) to train staff for Sanghamithra; (iii) to finalise the type/nature of the institution; (iv) to start the process for incorporation; (v) to obtain the required clearances from RBI, Income Tax Department; and (vi) to raise financial support. Some of these objectives were achieved; others were started but took time — even up to 1999 — to reach a conclusion. Examples of the latter are the search for a Donor and the clearances from the RBI and IT Department.

Two issues were decided rather rapidly; these were: (i) whether MYRADA itself should get into the business of lending or start a separate financial institution, and (ii) whether, if it decided to start a financial institution, it would be for-profit or not-for-profit. As regards the first, a clear stand had been taken since the late 1980s by this writer that an NGO engaged in other types of development activity cannot be in the business of lending, as its culture and systems do not support a 'lending' portfolio. Several financial institutions have offered MYRADA loans which it was expected to on-lend through its wide rural network which covered over 3,700 villages. MYRADA has consistently refused. The only option, therefore, would be to start a separate financial institution.

The second issue was more easily resolved since the MYRADA staff, who were deeply involved in the process, all opted to start a not-for-profit institution. They realised that the implications of having such a body could in some cases retard the rapid growth of the organisation, but given its close proximity to MYRADA, it should share its not-for-profit character. M.S.Sriram, (Professor, IIM, Ahmedabad), who studied Sanghamithra, identified the reasons, in his opinion, why the decision was taken to start a not-for-profit company. To quote the relevant part of his study:

> *Why was Sanghamithra set up as a not-for-profit company if it were to demonstrate profitability and sustainability? The answer possibly is in a mix of the following factors:*

1. *Legally MYRADA could not invest in the equity of Sanghamithra. Therefore, capitalising the project would have been difficult as a for-profit entity. The people who conceived this institution were people who had spent a lifetime in working in the non-profit sector and therefore did not want to invest their personal resources in this company, as they were not looking for returns in any way. No external private investor would be interested in investing in a demonstration model, unless of course, the larger plan was to rapidly grow in this direction in the future.*

2. *Following from the above, funding was sought from developmental rather than commercial sources both for capitalisation and growth. Donor money could only flow in to not-for-profit entities. Sanghamithra was incorporated with zero equity – the liability of the entity limited by the guarantee provided by the promoter members*[1] *as against investment of even a token amount of capital.*

3. *Since this was conceived as a demonstration model, there would be no pressure on aggressive growth plans. Therefore growth rates fuelled by internal accruals were sufficient. The need to access capital markets for growth was not there.*

4. *Keeping it as a not-for-profit entity avoided a possible strategic drift in the future, where the organisation having tasted early success wants to grow rapidly as a proper financial institution, thus losing the initial developmental orientation. The basic objective of MYRADA was only to demonstrate and encourage existing players to participate in banking with the poor; not create parallel systems.*

5. *The thinking during that time also indicates this: "if the project succeeds and earns surpluses, these could be ploughed into training activities or even into activities required to form groups".*[2] *This statement turned out to be providential, as the urban programme of Sanghamithra now pays partner NGOs an amount of Rs.5000/- for promotion and linking of these SHGs.*[3]

Prof. M.S.Sriram, IIM, Ahmedabad in
"Building Bridges between the Poor and the Banking System

There was one more issue which was raised but did not get resolved — namely whether the financial institution should lend only to SAGs or to individuals as well. There was a strong and major lobby to restrict lending only to SAGs since

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1 The term member is somewhat loosely used in the microfinance sector. Usually it refers to borrowers with current outstandings and in several cases, borrowers who have been registered by the MFI. However, the term member in the context of a company specifically means a shareholder who has subscribed to the capital of the company. In case of Sanghamithra, since there is no capital, all the promoters who have given a guarantee would be treated as members. When we use the term member in this paper, we are using the term in the context of a stakeholder-promoter rather than in the sense of client-beneficiary.

2 Fernandez A.P. (1993): Internal note to the staff of MYRADA.

3 M-Cril (2004): Risk Assessment Report of Sanghamithra Rural Financial Services.

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MYRADA's Mission was to build people's institutions and the entire SHG-Bank Linkage strategy which MYRADA had promoted was based on this thrust. There was, however, a significant number who opted to keep the policy open. During this period (1993-1996) it was not clear which position would finally prevail, though it was decided to project the first to avoid confusion — namely, that loans would be given only to SAGs.

Emerging trends in the financial sector during this period supported MYRADA's decision to start an independent institution. For example, the trend to amalgamate unprofitable bank branches was emerging; there were also signs of a growing reluctance to open new branches in rural areas. A Circular from MYRADA Head Office to all the MYRADA Staff dated September 29, 1994 indicated that this trend would have an impact on the ability of banks to cope with the expanding number of SAGs. The SHG-Bank-Linkage Model was based on the assumptions that banks would recognise this model as part of normal banking practice and that the Bank branches would increase in number and not decrease as the trend indicated. The opinion that there was need for a financial institution to fill this looming gap was beginning to gain strength in MYRADA. A note describing these emerging trends was circulated to MYRADA staff on September 29, 1994; an extract is given below.

A NOTE ON SANGHAMITHRA – SEPTEMBER 29,1994

... Once the Self-Help Groups are working satisfactorily, MYRADA links them up with the banks which are within a radius of 4 to 8 kms. This strategy is consonant with MYRADA's decentralised approach. However, this approach was based on the assumption that the number of Bank branches would increase. Within the last 2 years, however, with liberalisation catching on, banks are restructuring in an effort to operate professionally and to make a profit. This does not mean that they are throwing aside all their social objectives; they are still continuing to extend credit to anti poverty programmes

However, as a result, some Banks have "amalgamated" several rural branches. This has been a set back since in many areas the Self-Help Groups do not have a bank in the vicinity any longer. It is these gaps that Sanghamithra is attempting to fill.

Sanghamithra is a separate organisation and not part of MYRADA, though MYRADA staff will be on the Board; it will be registered under the Company Act, Section 25 and will operate like a Non-Banking Financial Institution. It will receive loans from Government and banks including NABARD and on-lend to groups... ...

Aloysius P. Fernandez
September 29, 1994

In hindsight it will appear that Sanghamithra took a long time to be grounded. MYRADA's management sought to bring as many of the staff as possible on board and to set up a Financial Institution whose culture and approach would mesh with its own. This took time. Further, a Not-For-Profit Finance Institution which was engaged in lending was a 'new animal' especially to the Income Tax Department; it also did not fit into the categories of financial institutions recognised by the Reserve Bank of India which put it under the category of Non Banking Financial Institutions which took deposits from the public, whereas Sanghamithra did not intend to do so. The problems that plagued many Non Banking Financial

Institutions during 1996 and 1997 further delayed the process of recognition by the RBI. Besides, it must be noted that till mid 1997 no staff was recruited for Sanghamithra since MYRADA did not have the resources. The entire preparatory work between 1993 and mid 1997 was done by senior staff of MYRADA particularly Ms. Vidya Ramachandran, Ms. Yasmin Master, Ms. Chandra Singh, Col. M.S. Ashok and Mr. William D'Souza (with assistance from Dr. Puhazhendi of NABARD, Chartered Accountants and Tax Consultants) who had to manage their existing programme portfolio besides devoting time to Sanghamithra. Besides, during this period, MYRADA did not focus only on promoting Sanghamithra; it devoted considerable time and resources to strengthen SHG-Bank Linkages and to promote a pilot initiative where one Regional Rural Bank (Cauvery Grameena Bank) took up the responsibility of itself forming groups before linking up with them.

There was another major development directly related to MYRADA but which had an impact on the progress of Sanghamithra during 1994-1995 and must therefore be recorded here:

MYRADA ran into rough weather during 1993-1994 which continued into 1995; looking back, it is surprising that the initiative to start Sanghamithra originated during this critical period. Two prominent politicians were encouraged to "harass" MYRADA. Staff in one project in Tumkur District were physically attacked, the MYRADA Head Office was vandalised, private home telephone lines were used to abuse family members and pressures were brought on Government Departments to harass the organisation. Somebody once wrote that there are no necessary evils in government; its evils exist only in its abuses. MYRADA had the opportunity to experience both good governance and its abuses during this period from which it emerged stronger and more robust as an institution. It also realised that when the chips are down, the organisation has to fight alone and its strength lies in the respect that its Board Members command, in its open systems of management including personnel policies, and finally on the strength of people's institutions at the base. The politicians involved unfortunately recognise and respect (with a degree of uneasiness) only the last. Whatever the rights and wrongs of this affair, its impact on management was to divert its energies to cope with the problem, leaving little time for creative thinking and planning especially of a major venture like Sanghamithra, though, to the credit of the organisation, it went ahead during 1994 with the following initiatives which were required to set the framework for a financial institution to take off.

The SHG-Bank Linkage Programme was promoted both within MYRADA's Projects as well as in other areas where MYRADA had provided training to Bankers and NGOs and at times, follow up support. The growth in the SHG-Bank Linkage programme, took off only from 1999-2000. In 1998-99, the total amount mobilised by SAGs in MYRADA's projects was only Rs.0.9 crores. In 2001-02 it rose to Rs.8.4 crores, in 2002-03 it was Rs.10 crores and in 2003-04 it rose to Rs.11.7 crores. However, there are indications that the rate of growth is declining.

Progress, therefore, was slow till 1999; even after that year there were many large gaps. For example in Dharmapuri District, MYRADA had promoted over 1500 SAGs, of which at least 1000 were eligible for loans, but the Banks were reluctant to extend loans to these groups; there were also other areas where the progress was slow.

While, Myrada was establishing SRFS it also continued to train Bankers with financial support from NABARD and to promote the SHG-Bank Linkage Programme. Bankers from several Commercial Banks and RRBs from various States attended these courses which were held on Myrada's Projects where the SAGs had multiplied, some of which were linked with the Banks. The feedback from these training Programmes, both as a result of interaction with the SAGs and with the Banks linking with them, helped NABARD to continuously update and fine-tune its guidelines on the Linkage Programme. NABARD provided the funds, motivated the Banks to send their staff and selected the participants from across the country with a focus on areas, where the potential for linkage on their return was high, either because a development programme including micro-finance was operational in the area or because SAGs had been formed by NGOs and through Government sponsored programmes.

Another pilot initiative was undertaken during 1994 and 1995 to strengthen the links between Banks and SAGs. Although it will entail a digression, it is worthwhile recording it here as it played a part in establishing Sanghamithra; it also substantiates Myrada's claim that it continued to promote the SHG-Bank Linkage Programme even after it decided to start Sanghamithra. NABARD and Myrada promoted a pilot experiment where one Regional Rural Bank (Cauvery Grameena Bank of Mysore District) took up the programme of forming SAGs (before linking with them) for the first time in the country. This initiative was in keeping with Myrada's thrust to spread the SAG movement and to mainstream it in all financial institutions. Myrada assumed that if some Banks were willing not only to link with the groups but also to form and train them, it would help considerably to expand the programme's coverage. If this pilot experiment succeeded, NABARD was willing to promote it with other RRBs across the country and to provide financial support to help them to start a similar programme. Myrada was keen to promote this approach because it had the potential to involve a large number of RRBs and to utilise their vast rural network. While Myrada was consistently arguing against Banks and Financial Institutions lending in bulk to NGOs for on-lending to SAGs — a practice that was gaining momentum — it was also promoting other channels to meet the demand. The proposed pilot where the RRBs would take the lead was one. Since this pilot was related to the formation of Sanghamithra, it will be described in some detail below:

Myrada had started to acquaint its staff with banking matters so that they (i.e. the staff) could work, if they so decided, for Sanghamithra. To make this initiative more hands-on and practical, it was decided to link it to the pilot project to orient Regional Rural Banks to promote SAGs on their own. When NABARD and Myrada discussed the possibility of encouraging a Regional Rural Bank to take up the formation of SAGs directly, to be followed by credit linkage. Myrada suggested that a pilot initiative be taken up with the Cauvery Grameena Bank (CGB) which covers Mysore District mainly because MYRADA had two major projects in the District which would serve as a useful context for a pilot programme. To start the pilot experiment with the CGB, a Mission comprising NABARD senior officials and MYRADA visited the CGB in October 1994.

> *"Shri S.K. Kalia along with 2 senior officers of NABARD HO held discussions with officials of MYRADA (NGO) and the Cauvery Grameena Bank on 7th and 8th October 1994.They also visited a few branches of the bank to firm up a model for experimenting the new credit delivery innovation through selected branches of the RRB" (Document of CFSF Cell of the NABARD Regional Office sent to MYRADA by Shri S. Panda, Asst. Gen. Manager, NABARD).*

There were four agencies involved in this pilot project with the Cauvery Grameena Bank (i) The CGB itself, (ii) The sponsoring bank — namely, The State Bank of Mysore, (iii) NABARD, and (iv) MYRADA. The role envisaged for the CGB was outlined in a NABARD document as follows:

> *"To identify suitable branches and officers to be associated with the project, to implement the project in co-ordination with MYRADA, NABARD and the Sponsoring Bank, and to bring out a well adapted model replicable in the rest of the RRBs in the country."*

MYRADA's role was restricted to provide training to CGB staff (Managers and Cashiers) in the SAG concept and to support the CGB staff to form groups. The decision was taken to depute 3 to 4 Resource Persons from MYRADA for a period of 3 months to guide the CGB branches to form groups. Several preparatory sessions were held between November 1994 and March 1995 between MYRADA and the CGB. MYRADA placed 4 resource persons in CGB branches in April 1995 and withdrew them on June 1, 1995. MYRADA's objective in placing these staff in the Banks was twofold: (i) to train the Bank Staff to form SAGs, and (ii) to provide MYRADA Staff with an opportunity to learn how Banks function so that they could be considered for employment in Sanghamithra if they so desired. Since the objectives of this assignment included MYRADA's own concern to prepare staff for Sanghamithra, the salaries of these staff (including a lumpsum allowance of Rs 2,500 per month) were paid by MYRADA even during the period of their deputation to the CGB. An Orientation Workshop for Cauvery Grameena Bank Officials on the concept of SAGs was conducted from January 30 to February 1, 1995 and a follow up workshop from 20th to 22nd February at the MYRADA Training Centre in HD Kote in which the Staff placed in the CGB branches also participated.

In spite of all these initiatives to promote the SAG Bank Linkage programme, the gap between the number of SAGs linked to Banks and the number of eligible SAGs which could not establish this linkage continued to grow. The MYRADA Management finally decided to incorporate Sanghamithra Rural Financial Services (SRFS) as a corporate entity under Section 25 of the Companies Act of 1956. The two founder members or promoter directors were Mr. Aloysius P Fernandez

(Executive Director of MYRADA) and Lt. Col. M.S. Ashok who had joined MYRADA as Deputy Director. Accordingly an application for the issue of licence was prepared and submitted to the Office of the Regional Director (Ministry of Law, Justice and Company Affairs) Southern Region, Madras. **SRFS was incorporated as a corporate entity under Section 25 of the Companies Act of 1956 in January 1995.**

GOVERNMENT OF INDIA
MINISTRY OF LAW, JUSTICE AND COMPANY AFFAIRS
OFFICE OF THE REGIONAL DIRECTOR, SOUTHERN REGION, MADRAS

No.2/B-7026/94

Shastri Bhavan, Block 1, V Floor
26, Haddows Road, Madras 600 001.
Dated: January 20, 1995

Sri N.Jayaraman
9, Vinayaka Building
Sampige Road, 1st Cross
Malleswaram, Bangalore.

Sir,

Sub: Application for the issue of licence under Sec.25 of Companies Act 1956 – M/s.Sanghamithra Rural Financial Services.- reg.

Ref: Correspondence resting with your letterNo.S.4.95.421 dated 17-1-1995

With reference to the subject cited, I am enclosing the licence under Sec.25 of the Companies Act, 1956 along with the approved draft Memorandum of Association and Articles of Association for registering the company under the name "Sanghamithra Rural Financial Services" with limited liability without the addition of the word "Limited".

Yours faithfully,

Sd/-

R. Aghoramurthy
Regional Director

Encl. As above.

The Board of Sanghamithra was constituted in 1995 and held it first meeting on February 28, 1995. The Members were Mr. Aloysius P. Fernandez, Lt. Col. M.S. Ashok and Mr. Ravi Vishwanath (Chartered Accountant).

Relevant Extracts from a Circular to all MYRADA Programme and Project Officers informing them of this development dated August 30, 1995 reads as follows:

As you know, an organisation called, 'Sanghamithra' registered under Section 25 of the Companies Act has come into existence. Their operations are yet to commence.

A number of possibilities for cooperation between MYRADA *and Sanghamithra have been examined. The experience gained in* MYRADA*'s collaboration with the Cauvery Grameena Bank and generally with credit groups could form valuable inputs to a new institution like Sanghamithra.* MYRADA *has been able to train a few personnel as Credit Managers.*

Many models and options are open to us for such collaboration. We need to now crystallise our options, obtain the opinion of legal experts and auditors, and put the matter to our Board for a decision. I am going to circulate very soon a note to the members of our Governing Body on the subject. We hope to have a decision, one way or another, within a few months.

As you know, no funds have been or are to be transferred by MYRADA *to Sanghamithra. Nor is any activity being undertaken as yet by Sanghamithra. The status of our activities in* MYRADA *is that we engaged in simulation exercises on a small scale by way of experimentation, which could provide models for future operations by us, or other agencies like Sanghamithra. The whole exercise is part of our withdrawal strategy.*

Sd/-
M. S. Ashok, Deputy Director

3.1. MYRADA STAFF CONTRIBUTE TO THE PROCESS:

On June 20, 1995, it was decided to organise a Workshop of staff from six MYRADA Projects who were actively promoting the SAG-Bank Linkage Model and who had already supported the formation of Sanghamithra, in order to consider their suggestions to carry the process forward and to clarify several issues that were emerging related to Sanghamithra. The meeting was facilitated by M.S. Ashok Deputy Director, MYRADA, Vidya Ramachandran and Yasmin Master, both Programme Officers of MYRADA who were supporting the six projects represented at the meeting. Prior to this meeting the following note was circulated:

> *When MYRADA and NABARD discussed the need for an Alternative Credit System to meet the credit needs of the poor in the mid 1980s, it was understood that this alternate system which came to be known as "Banking with the Poor" through Self Help Groups (SHGs) would relate directly with the existing Banking structure. This is the major reason why MYRADA has consistently avoided becoming an intermediary financing institution like a Bank.*
>
> *This strategy was based on the following assumptions:*
>
> 1. *That the banking network in the rural areas would not only expand but also change its policy in order to cope adequately with the credit needs of the poor; that transaction costs to the borrower in terms of time and money spent would decrease.*
> 2. *That the Bank staff would realise their social responsibilities and make every effort to relate to SAGs once it was proved that repayment rate was over 90%.*
> 3. *That the official Banking policy would shift from providing loans to poor individuals to lending directly to groups of poor people; it follows that the criteria for lending could no longer be dominated by the assessment of a "productive or viable asset", but would have to include indicators of the effectiveness of a SAG and of interlinking institutions which support and sustain the productivity of the asset and ensure repayments.*
> 4. *That the Banking system would redefine its role to make its lending more user friendly especially to the poor.*
>
> *While most of these assumptions have been realised, the Banking network has not expanded adequately to cope with the number of SAGs. On the contrary, with the amalgamation of branches that are considered non-viable, the network has actually contracted and indicators are that it will continue to do so.*
>
> *Secondly, the bank staff have not responded adequately to the needs of the poor. The pressure that they are now operating under, namely to improve the recovery rate, leaves them with little time and less incentive to make*

the effort to increase lending, even though the experience of several banks who have lent to SAGs has indicated that the recovery rate is over 95%; it is for this reason that MYRADA has set up "Sanghamithra".

Sanghamithra will relate with SAGs formed by any NGO, not only the MYRADA SAGs.

Aloysius P. Fernandez
April 22, 1995

The Minutes of the Workshop recording the discussions, conclusions and clarifications will not be given here as they are rather long. The Workshop, however, took the process further in some areas; for example it proposed criteria for advancing loans and the procedures that Sanghamithra could adopt. As these proposals form the basis on which subsequent formats were evolved, it will be useful to list them below for the record as well as to follow how the process developed.

Minutes of the Workshop held on June 20,1995, as minuted by Ms Vidya Ramachandran:

Criteria that Sanghamithra could adopt for Advancing Loans to Self Help Groups

1. The SAG should have had lending and recovery transactions (i.e. credit transactions) with own or mobilised (from other sources) funds for at least one year.
2. The SAG's internal overdues of principle and interest on loans taken from own Common Fund must not be more than 20%. Length of overdues must not exceed more than one season. (This was later revised)
3. At least 80% of the group members should have taken loans from the SAG's own Common Fund (i.e. loans should not have been monopolised by a few members only).
4. The trend of borrowing within the SAG should be in favour of production activities (amount loaned should maintain a minimum ratio of 60:40 between production and consumption activities).
5. The SAG should be a member of the Apex Body.
6. The SAG's books should be maintained independently or with assistance paid for by the group.
7. Savings (individual) per member in the group should be at least Rs.500. (Later modified as minimum savings prescribed per member per week multiplied by the age of the group.)
8. **Preferably, the SAG should have approached a bank branch with the same request and its application should be pending in the bank for at least 4 weeks (or turned down for reasons that Sanghamithra regards as inadequate).**
9. The SAG can take more than one loan from Sanghamithra provided: (a) The total of all loans is within the prescribed credit limit; (b) There have been no overdues in repayment of earlier loans of either principle or interest.

Other Lending Criteria/Conditions:

- Sanghamithra will charge an interest of 14% on loans to SAGs.
- Repayment of both principal and interest will be at not more than quarterly intervals.
- The repayment periods for loans offered by Sanghamithra will presently be: 1st Loan: 18 months; 2nd loan onwards: upto a maximum of 36 months.
- The credit limits offered by Sanghamithra will (in the initial phase) be a maximum of:

1st Loan	Amount equal to internally generated Common Fund.	Less any other out-standings to any other agency.
2nd Loan	1.5 times the internally generated Common Fund	
3rd Loan	2 times the internally generated Common Fund	
4th Loan	2.5 times the internally generated Common Fund	
5th Loan onwards	3 times the internally generated Common Fund.	

(Note: These limits were subsequently revised. The initial loan was related to the cash flow of the SAG. The second loan was based on a variety of indicators and usually exceeded the internally generated common fund by several times.)

Procedures that Sanghamithra will follow with regard to Loan Requests:

- The Credit Manager will attend the Apex Body Meeting at which the SAG loan requested is discussed by the Apex Body, modified if required, approved, and submitted to Sanghamithra.
- Thereafter, the Credit Manager will attend the next SAG meeting to carry out an independent appraisal of its performance.
- At the following SAG meeting the Credit Manager will communicate Sanghamithra's decision (with intimation to the Apex Body and Myrada or any other promoting agency) and will hand over the cheque if the loan has been approved.

> Cheque will be handed over in SAG meetings only, in the presence of as many members as possible.
>
> At the time of handing over the Cheque, Sanghamithra will obtain a promissory note on stamp paper, signed by all members.

Sources of Finance to Sanghamithra:

- From Grants for infrastructure and for lending in the initial stage
- Operational expenses for the first two years will be provided by Myrada (including setting up a separate office outside the Myrada project campus to create a separate identity for Sanghamithra). Thereafter, they will be met from income earned by Sanghamithra.

- From surpluses earned by Sanghamithra after all costs are met.
- Soft loans from other financial institutions in the second stage
- Loans from Financial Institutions at commercial rates in the third stage

As regards the relationship with Banks, point 8 of the above Minutes deserves to be particularly noted. It states, **"Preferably the SAG should have approached a bank branch with the same request and its application should be pending in the bank for at least 4 weeks (or turned down for reasons that Sanghamithra regards as inadequate)".** It was made clear to the participants in the workshop that Sanghamithra was not intended to replace banks. It would seek to extend credit on commercially viable terms to SAGs that have proved themselves to be responsible and creditworthy. Sanghamithra would develop norms for evaluating the creditworthiness of SAGs - norms that would be realistic, objective, measurable and demonstrably effective. Sanghamithra would attempt to prove to banks that SAGs are 'bankable", on a commercially viable basis. Should any bank come forward with an offer of credit to SAGs in a given area on terms that matched Sanghamithra's, the institution would be only too glad to step aside, having done its work. Sanghamithra would seek to prove to banks that rural credit operations could be profitable and sustainable if credit were provided to stable and reliable SAGs.

3.2. Could Sanghamithra be Registered Under Section 12 A Of The Income Tax Act, 1961?

There were two major issues that arose during the period 1994-1996 that took time to resolve which delayed the operationalisation of Sanghamithra. The first issue related to the need for clearance from the Income Tax Department. The second related to Sanghamithra's application to the RBI for registration as an NBFC. The experience of Sanghamithra in resolving these two issues is briefly described below.

A major issue that arose with the Income Tax Department was whether Sanghamithra could be recognised as a charitable entity. Myrada initiated a major initiative to obtain this recognition. The problem put briefly was the following: even if its Board Members agreed to work without any remuneration, even if they did not claim sitting fees or transport allowances, even if Sanghamithra itself did not distribute any dividend, yet it was still lending money. Though the service/interest charges were to be used to cover administrative and development costs only, would the Income Tax Department recognise Sanghamithra as a charitable institution? Myrada commissioned a leading Senior Advocate Shri G.Sarangan to give his learned opinion. His note dated September 9, 1994 dealt with the issue thoroughly. Only three paragraphs will be quoted here - as they may be of use to others attempting similar initiatives - though they do not do justice to the entire note:

> *"In explaining the charitable concept, courts have repeatedly held that eleemosynary element is not essential. In order to sustain charity, it is not necessary that the NBFC should give away money to the poor or even that the NBFC should not charge any interest at all. The NBFC may charge interest on certain loans but may not on other loans, depending upon some objective criteria while conferring a benefit on the poor.*
>
> *"One of the prime requirements is that the institution cannot serve to obtain private profit. Though the expression 'existing solely for charitable purpose and not for the purposes of profit' is not there in the section, it is undoubtedly implied. The general idea is that there should not be persons who derive profit for themselves under guise of running the institution. The institution will no doubt not distribute such profits as it makes (assuming it does) by way of dividend. There may or may not be a clause suggesting that the business that is run 'incidental' to the attainment of the objects of the institution is not run and is not designed to run to make profit. The object of the institution in running the institution is not to make profit. Profit is not the motive or object of carrying on the business. It will be seen that Section 10(23C) (iv) starts with the words "<u>any income</u> received by any person on behalf of....".*

There is no need to exempt the income of an institution if the institution makes no income at all. Only when an income is in fact made is it necessary to exempt the income so that income tax is not paid. In other words, the Act does not *forbid income being made by charitable institutions. What it forbids is a private profit and profit which is not impressed with the character of the trust or obligation to be applied for charitable purposes. As long as the NBFC does not distribute dividend and as long as all property, accretions, income derived therefrom are impressed with the character of trust and are to be applied for charitable purposes only, there can be no denial of exemption under section 10 (23C)." (Shri G. Sarangan).*

An application for registration as a charitable entity was made to the Income Tax Department on July 31, 1995. This matter took a long time to resolve. Initially the Income Tax Department was reluctant until the promoters were able to demonstrate their credibility. Once Senior Officers in the Department realised that this was a genuine effort to support the poor, their response changed to one of constructive suggestions for which Sanghamithra and its client SAGs will be ever grateful. The story of Sanghamithra's interaction with the Income Tax Department is briefly summarised in a note from MYRADA's auditors, M/s.Nambiar and Associates, who worked with MYRADA to carry this application through the Income Tax Department. Relevant parts of this note are quoted below:

Note from M/s.Nambiar & Associates: *From the very nature of its incorporation and its objectives it is clear that Sanghamithra is a company incorporated with the object of promoting rural welfare by uplifting the rural population based on the concept of Self Help Group with no profit to the company. Based on this conceptual belief the company made an application under section 12 A of the Income Tax Act, 1961 to the Honourable Commissioner of Income Tax, Bangalore on 31-07-1995 for its registration as a Charitable Entity. For a considerable time there was no response from the Income Tax Department on the application in spite of several reminders. On 05-11-1996, the Assistant Commissioner of Income Tax informed the company that consequent to change in jurisdiction, the file had now been transferred to Income Tax Officer (Trust Ward), Trust Circle – 3(1), C. R. Buildings, Bangalore. Based on the above information the company took up the matter with the above said officer on 18-11-1996. After several visits to his office the company was made to understand that the original application filed on 31-07-1995 had been misplaced and the company was asked to re-submit the same once again, for needful action. The same was filed by the company on 04-08-1997.*

On 27-09-1997 the company was asked to file a detailed note on Sanghamithra Rural Financial Services regarding the nature of company's constitution, background under which it was conceived, proposed activity and work, main objects and the charitable nature of its activities. In response to this request, a detailed note prepared by one of the Directors viz., Mr. Aloysius P. Fernandez was submitted to the Honourable Commissioner of Income Tax through the Income Tax Officer on 27-09-1997. To this note, a communication was received from the Income Tax Officer, Trust Circle on 21-10-1997 with the following observations.

1. "Object No.A (I) (a): To carry out and undertake the financing of and providing credit on interest or otherwise to group of persons.
2. Object No. 3: To establish, maintain and run social clubs, theatres, laboratories, workshops, shopping complexes etc.

It is also submitted by you in letter dated 27-09-1997 that your company is a non-profit financial institution, as such the main object of your company and other object as stated above are not charitable within the meaning of section 1 (15) of the Income Tax Act. 1961. Hence there is no scope, for granting Registration u/s 12 A and Recognition u/s 80G to your company. This is for your kind information".

On receipt of this communication the company made a further representation on 10-12-1997 to the Honourable Chief Commissioner of Income Tax stating that:

(a) The order of the Income Tax Officer was not a speaking order.

(b) This refusal to grant registration was based on extracts for objects clause drawn out of context and by not giving reasons why the objects were not charitable in nature in support of the claim of the company.

The company further brought to the notice of the Honourable Chief Commissioner of Income Tax the decided case laws on the issues by the Karnataka High Court in CIT Vs. Gayathri Women's Welfare Association – 203 ITR 389 and also the decision of the Supreme Court in CIT Vs. Saurashtra Art Silk Cloth Manufacturing Association – 121 ITR and CIT Vs. Andhra Pradesh State Road Transport Corporation – 159 ITR. The said representation made to the Honourable Chief Commissioner of Income Tax was forwarded to the Honourable Commissioner of Income Tax, Karnataka – II on 31-12-1997 for necessary action. In response to this the company received a communication on behalf of the Honourable Commissioner of Income Tax, Karnataka –II from Income Tax Officer, Trust Ward – 3(1) that the Honourable Commissioner of Income Tax, Karnataka – II has rejected the application for registration under section 12A of the Income Tax Act, 1961 and also registration under Section 80G of the Income Tax Act, 1961, for reasons stated in the said communication.

Reasons are:

(a) "It wants to step in where loss making branches of the banks have failed. Hence, object of the company is mainly a financing activity and credit giving company".

(b) "It is said in Trustees of Govardhan Das, Govindram Family Charity Trust (1959) (21 ITR 231) (Bombay) that it is not possible to say that poor man cannot do without matrimony and that matrimony is a bare

> *necessity of life. Considering the above decisions sport complexes, shopping complexes, industry, theatres, social clubs cannot be called as a bare necessity of rural poor and hence not charitable.*
>
> *In response to the above commun-ication, the Director of the company Mr. Aloysius P. Fernandez and the company's auditors personally represented the matter to the Honourable Commissioner of Income Tax, Karnataka – II and explained the need to provide credit on interest or otherwise to Self Help Group belonging to the poorer sections in rural areas and that no portion of the interest earned thereon be paid or transferred directly or indirectly by way of bonus, dividend profit or otherwise to the members of the company. Consequent to this representation the company was advised to file a fresh application for registration under Section 12A of the Income Tax Act, 1961 together with note containing the representations made before the Honourable Commissioner of Income Tax, Karnataka – II. The said application was filed on 17-08-1998* ***and the same was considered favourably by the Honourable Commissioner of Income tax, Karnataka – II and the registration was granted on 18-12-1998.***

The registration under 12 A of the Income Tax Act implies that Sanghamithra is recognised as a charitable entity and that its income is exempt from taxation subject to utilisation norms and certain other conditions like the need to file annual returns.

Prof.M.S. Sriram's comments on the issue of what makes an activity "commercial" throws further light on this issue. "What is commercial, largely turns out to be a matter of interpretation. One school of thought refers to the possibility of distributing profits, or residual claims to the members of the organisation. The other more conservative view is whether the inherent activity is "charitable" or "commercial" in nature. One of the arguments laid out by an advocate commissioned by Sanghamithra was that the tax status is to be established by the criteria on whether the organisation is serving to obtain private profit. He had argued that there is no need to exempt an organisation that makes no income and therefore by the very nature of granting explicit exemption, one is recognising that income is accruing, but tax is not being imposed. His opinion was that as long as the organisation does not distribute dividend and as long as all property is used for charitable purposes as laid out be the objects of the trust, there should be no doubt about the exempt status of the organisation for the purposes of taxation.

While the argument was tenable, it took some effort by Sanghamithra to convince the tax authorities, before they could get an exemption. This exemption was obtained before the RBI defined what micro finance was for its regulatory purposes. Now that the RBI definition of what could be construed as micro finance is readily available, the taxation interpretation may also follow suit, but we have to recognise that this is still an issue that officers of the Income Tax Department might interpret either way."

(Prof.M.S.Sriram – Building Bridges between the Poor and the Banking System)

3.3. Is SRFS a Non Banking Financial Company (NBFC)?

The second issue related to securing NBFC status for Sanghamithra. Though discussions with the Reserve Bank of India to register Sanghamithra as an NBFC were started informally, the problems related to NBFCs in general had assumed alarming proportions especially during 1996-97 following a major scam; this delayed the formal application from Sanghamithra for incorporation as an NBFC till 1997.

The year 1997 started with an announcement of amendments in the Reserve Bank of India Act in respect of NBFCs. Several changes were made in Chapters III B, III C and V of the RBI Act with effect from January 9, 1997; these Amendments received Presidential assent on March 28,1997. MYRADA's Tax Consultants M/s Sunanda & Sheshadri advised on April 24, 1997 as follows:

"Some amendments to the RBI Act which require the immediate and urgent attention of Sanghamithra Rural Financial Services are given below:

1. No Non-Banking Finance Corporation (NBFC) can carry on/commence its business unless it:

1.1. Obtains a certificate of registration issued by the Reserve Bank of India under Chapter III B.

1.2. Has net owned funds ranging between 25 lakhs and Rs.200 lakhs as may be fixed by a gazette notification for registration.

The application for registration in the case of an existing company has to be made before July 9, 1997 although it can continue with its business. The application form is not yet notified.

Under the circumstances we request you to take up the matter with the RBI, clarify/settle your status and seek exemption, if possible, from the applicability of NBFC regulations/RBI Act."

sd/- Ms.Sunanda & Seshadri.

After several preliminary meetings with the RBI, on May 8, 1997 a letter was written to Shri P.K.Biswas, Chief General Manager, RBI, Bangalore. After explaining the proposed activities and main objectives of Sanghamithra and stressing that the activities of the company were purely charitable in nature, the following questions were raised for RBI's consideration.

4.1. *Under the circumstances explained above, is Sanghamithra a NBFC/ Financial Institution covered by Chapter IIIB of the RBI Act at all? The company will not carry on business in its normal sense to make profit and distribute dividends/bonus. In our opinion, under the overall scheme of the RBI Act the provisions cannot apply to a non-commercial entity which has no share capital and which cannot distribute its profits. The company's corpus will be out of donations/grants from India and abroad from non-governmental development organisations. No public or private equity is involved.*

Under the circumstances, we request you not to treat us as an NBFC governed by Chapter IIIB of the RBI Act and other consequential directions issued by RBI. Our case is not one of exemption but of non-applicability of the relevant provisions of the RBI Act and the consequential directions to us.

4.2. If our plea not to treat us as an NBFC/Financial Institution is not acceptable, we request you to grant us complete exemptions from the directions issued by RBI to NBFC, MNBC and RNBC namely:

a) The non-banking Financial Companies (Reserve Bank) Direction, 1977.
b) The Miscellaneous Non Banking Companies (Reserve Bank) Direction, 1977.
c) The Residuary Non Banking Companies (Reserve Bank) Direction, 1987.

The power to grant exemption is vested in RBI under clauses (17), (14) and (19) of the three sets of directions respectively.

As the company has no share capital it cannot obviously meet the criteria of net owned funds being Rs.25 lakhs in terms of Section 45 IA(1) (b) of the RBI Act. The Company will receive grants and donations from India and abroad. The donations received from abroad will be subject to the provisions of the Foreign Contributions Regulation Act (FCRA). Thus it will have no share capital of its own. The company is limited by guarantee.

Thus we request you to specify the minimum amount of Rs.25 lakhs as the amount to be brought in by us as Corpus through grants and this amount will be invested by us in securities which are permissible under Section 11(5) of the Income Tax Act to ensure that the investment pattern meets with the requirements of the Income Tax Act also.

In our opinion retaining a Corpus of Rs.25 lakhs would meet the requirements of the law as in the explanation to Section 45 IA the term 'net owned funds' includes not only paid up by equity capital but also free reserves. Thus, technically the major or even substantial portion of the net owned funds can be in the form of free reserves. As we are prepared to invest the money in securities/investments the question of net owned funds being diluted will not arise except when there are losses.

4.3. The third alternative which we propose is of extending the time limit for meeting the criteria of net owned funds while granting us complete exemption from the directions issued by you to NBFCs, RNBCs and MNBCs.

5. We request you to consider our plea of complete non applicability as sought by us in para 4.1 above favourably. The alternatives in 4.2 and 4.3 are also offered by us by way of suggestions if 4.1 is not found acceptable.

Yours faithfully,
Sd/- Aloysius P. Fernandez, Director, Sanghamithra

The formal application for registration as an NBFC was finally sent to the RBI on June 28, 1997. As no response was received, a second letter dated June 18, 1998 was sent seeking conditional registration. RBI's letters of March 10, 1998 and May 29, 1998 asked for several clarifications, mainly related to acceptance/ mobilisation of public deposits. Sanghamithra also tried to explain why it was "different".

RBI's letter dated July 6, 1998 reads as follows:

RESERVE BANK OF INDIA
DNBS(BG) 65/KT/LC/S-971/97-98

Department of Non Banking Supervision
Regional Office, 10/3/8, Nrupathunga Road
Bangalore 560001.

6 July 1998

The Director
Sanghamithra Rural Financial Services
2A, Service Road, Domlur Layout
Bangalore 560 071.

Dear Sir,

Application for a certificate of registration to commence the business of a Non Banking Financial Institution under Section 45 IA of the Reserve Bank of India Act, 1934

Please refer to your application dated 28th June 1997 for issue of a certificate of registration to commence the business of a Non Banking Financial Institution. In this connection, we advise that you may approach us for registration **after complying with the requirements under Section 12A of the Income Tax Act** which are applicable to Charitable Trusts and also after attaining the minimum level of net owned funds of Rs.25 lakhs out of the grants said to be receivable by the Company.

2. As regards the request for issue of a conditional Registration contained in your letter dated 18th June 1998, **we regret our inability to accede to your request.**

Yours faithfully
Sd/
(C.S.Murthy)
General Manager.

The RBI also sent a special investigating officer who made a thorough scrutiny of the policy and objectives of Sanghamithra and of the preparations made to start the institution.

Given the urgent and prior need to obtain recognition under Section 12A by the Income Tax Department, MYRADA made renewed and intensive efforts during 1997 to obtain this clearance. As described in a preceding paragraph, a new application was made on August 7, 1997 to the Income Tax Department and several representations were made between 1997 and 1999. The registration under 12 A was finally granted by the Income Tax Department on December 18, 1998. This cleared the way to approach the RBI once again. Several letters were exchanged and meetings set up between RBI and Sanghamithra; only the major letters will be referred to or quoted here.

Meanwhile, in order to clear up the rather messy situation in which some of the NBFCs had landed, which also contributed to a distortion of the entire sector, the RBI had put in place a comprehensive regulatory and supervisory framework in January 1998 which sought to protect the interests of depositors and to ensure that the NBFCs function properly. Responding to feedback, the following statutory change was announced on January 13, 2000, with reference to those NBFCs engaged in micro finance and registered under Section 25 of the Companies Act.

> *In the backdrop of the need for a suitable national policy framework for implementation of many credit linked poverty alleviation programmes to meet the needs of hard core and assetless poor, a High Powered Working Group on Micro Financing in India was constituted by NABARD to recommend a policy framework for sustainable growth of micro finance in the country with participation of community based organisations at the grass root level. The Task Force submitted its report on October 18, 1999.*
>
> *The Working Group has, inter alia, recommended that the policy and regulatory framework should give a fillip to the self-help groups (SAGs) or Non Governmental Organisations (NGOs) engaged in micro financing activities. Accordingly, it has been decided to exempt such NBFCs which are engaged in (i) micro financing activities, (ii) licensed under Section 25 of the Companies Act, 1956, and (iii) which are not accepting public deposits from the purview of sections 45-IA (registration), 45-IB (maintenance of liquid assets) and 45-IC (transfer of profits to Reserve Fund) of RBI Act, 1934.*
>
> *(Ref: Amendments to NBFC Regulations. Ref.DNBS (PD). CC.No 12/ 02.01/99-2000.)*

The final letter to the RBI written on September 8, 1999 is quoted below; a reminder followed on January 7, 2000.

> *The General Manager*
> *Department of Non Banking Supervision*
> *Reserve Bank of India*
> *Regional Office*
> *10/3/8 Nrupathunga Road*
> *BANGALORE – 560 001*
>
> *Dated September 28,1999.*
>
> *Sub: Our application for Certificate of Registration under Sec.45-IA of the RBI Act, 1934*
>
> *Dear Sir,*
>
> *Kindly refer to your letter DNBS (BG) No.1158/B 79/09.01.10/99-00 dated September 8,1999 read with your letter NDBS/(BG)65/KT/LC/S971/ 97-98 July 06, 1998.*

In response, we are glad to enclose copies of the following, as desired by you:

1. Letter No. Trust 718/10A/Vol.A-1/S-742/98-99/CIT-II, dated 18.12.1998 from the Office of the Commissioner of Income Tax, Karnataka II, Bangalore granting us Registration under Section 12 A (a) of the IT Act, 1961.

2. Letter No. Trust/718/10G/695/98-99/CIT-II dated 06.04.1999 from the same authority granting us recognition under section 80G of the IT Act, 1961.

3. Certificate in original No.DR/1131/99 dated 23.09.1999 from the manager, Corporation Bank, VV Mohalla Branch, Mysore confirming that we hold a balance of Rs.60,27,101, as on 23.09.1999, of which we have earmarked Rs. 25 lakhs as our NOF as prescribed by you.

In view of the above, we request that the RBI be pleased to grant us the required registration under section 45-IA of the RBI Act early so that we may commence our operations without any further delay.

We remain grateful to you for this favour.

Sd/-
Vijay Nath Bhat,
Chief Executive,
Sanghamithra

In January 2000, the RBI passed a notification that Sec 45 IA, and IC will not apply to a NBFC which is a) providing credit not exceeding Rs 50,000 for a business enterprise and Rs.125,000 for meeting the cost of a dwelling to any poor person b) licensed under Sec 25 of the Company's Act and c) not accepting public deposits.

This exemption recognised that not-for-profit companies could undertake micro finance activities and that loans to SAGs fall under the category of micro finance. This is an implicit recognition that some categories of micro financing activities apart from the Bank-SHG linkage model can be recognised as, "not-for-profit".

> *To quote M.S.Sriram once again, "The exemption benefited Sanghamithra. Other players in micro finance were registered as Trusts and Societies and continued to function through this period. However, even after such a major exemption was granted based on a high power committee recommendation, there were hardly any companies operating, using this exemption. Apart from Sanghamithra and Indian Association of Savings and Credit (IASC), there is no micro finance programme worth a decent size being carried out under this norm. Even IASC is trying to establish a for-profit entity as most of its loaning activities go beyond the small loan size specified in the exemption clause. IASC may want to move out because its portfolio is largely housing and loan sizes for housing are usually beyond the limit prescribed by the RBI. However, this exemption ensures that micro finance companies fall with certain very limited*

size and range of activities and therefore have to be isolated examples rather than large replicable models.

(Quoted from "Building Bridges between the Poor and the Banking System)

The Reserve Bank of India wrote to SRFS on February 28, 2000:

> Sub: Application for Certificate of Registration under Section 45-IA of the Reserve Bank of India Act, 1934.
>
> Please refer to the correspondence resting with your letter No.SAN/GEN/99-2000 dated January 7, 2000 on the above subject. We advise that the provisions of Sections 45-IA, 45-IB and 45-IC of the Reserve Bank of India Act, 1934 are not applicable to your company in terms of Notification No.DNBS.138/CGM(VSNM)-2000 dated January 13, 2000.
>
> Please acknowledge receipt.
>
> Yours faithfully,
> Sd/-
> S.Athmaraman
> Deputy General Manager

Thus a major hurdle was removed satisfactorily, thanks to bold initiatives taken by several players from the RBI, NABARD and from the NGO and Micro Finance Actors who understood and supported a viable strategy to establish a supportive institutional environment that could provide quick and friendly access to credit by the poor.

CHAPTER 4

1997 – 2000: SANGHAMITHRA DEVELOPS AN IDENTITY SEPARATE FROM MYRADA

This story now needs to back track a few years. The few staff from MYRADA Head Office (Vidya Ramachandran, Yasmin Master, William D'Souza, Chandra Singh) who participated in the first meeting to discuss Sanghamithra, devoted what time they could spare from 1995 to 1997 to follow up the Cauvery Grameena Bank experiment and to carry forward the decision to start Sanghamithra with their project staff. The intense debate that took place in some MYRADA projects regarding Sanghamithra was the most constructive development during 1995 -1996. These debates helped to deepen the understanding of Sanghamithra at all levels in MYRADA as well as in some SAGs; they also helped to identify several potential strengths as well as weaknesses and threats that could undermine the process that the management sought to promote in order that Sanghamithra could emerge as an institution relevant to people's needs and aspirations. This writer decided to accept an assignment in the World Bank in Washington and moved there in August 1995 (he had to return in May 1996); the responsibility of managing MYRADA and of directing and co-ordinating the Sanghamithra initiative was taken up by Lt. Col. M.S. Ashok, who had joined MYRADA a few years earlier as Deputy Director.

By 1997 it became necessary for Sanghamithra to have a full time Officer to push it forward; it could no longer be managed by MYRADA staff who had a host of other responsibilities. Besides, the intricacies of managing an MFI required a different set of skills from what MYRADA possessed. A senior officer from Corporation Bank, Mr. Vijay Nath Bhat, who had the expertise and commitment required to set up Sanghamithra, was identified by this writer who was one of the Directors of the Bank in the mid nineties. Mr.Bhat agreed to join Sanghamithra after his retirement in early 1997. MYRADA also managed to raise a small amount to pay for his services and for other costs involved in setting up the institution.

Mr.Vijay Nath Bhat joined MYRADA as a part time consultant in May 1997 and took over some of the responsibilities of dealing with the RBI and Company Affairs. He became full time consultant from April 1999 to August 1999 and then was appointed as Chief Adviser of Sanghamithra (with all the functions of a CEO) from October 1999 to September 2002. Mr. S.M. Adiga who had worked in Syndicate Bank for several years and had extensive experience in rural banking took over as CEO of Sanghamithra in October 2002; he continued the good work of Mr V.N. Bhat and is currently heading the institution.

The Board of Sanghamithra was also reconstituted and expanded. Three Programme Officers from MYRADA who had nurtured the SAG movement in their respective projects since its inception in the mid-eighties and contributed to the process of establishing Sanghamithra joined the Board on April 11, 1997. They were Ms.Yasmin Master, Ms.Vidya Ramachandran and Mr.William D'Souza. Mr.M.K.Bhat, Nuclear Scientist and Social Activist also joined the Board on April 11, 1997. The Board was further expanded with Mr. Ramesh Ramanathan joining on June 11, 1999 (further details about Ramesh are given below). Mr. K.R.Pradeep a well respected Chartered Accountant and Tax Consultant joined on October 6, 2000. Mrs. Rohini Nilekani, a well-known writer, philanthropist and Founder of an NGO, Akshara which has a major programme to improve the standards of education, joined on August 2, 2002. These prominent members who are committed to good governance, the eradication of poverty and to promote self-reliance, have been of immense support to Sanghamithra; they have provided guidance and financial contributions.

Mr.Ramesh Ramanathan came into contact with MYRADA and Sanghamithra in mid 1998. He saw the need to start a micro finance programme in the Urban areas and approached this writer with his "dream". He decided to build on the basis that Sanghamithra had established which could cover both the urban and rural areas and to branch out independently in the urban area at a later date. The Sanghamithra Board welcomed this approach. He was invited to join the Sanghamithra Board and was formally appointed to the Board of Directors with effect from June 11, 1999.The urban programme of Sanghamithra has since proceeded with the establishment of an urban office with contributions from MYRADA and Ramesh. Funds for lending to SAGs were donated by Mrs.Rohini Nilekani who had, in the past, often stressed the need for a Micro Finance Programme in the urban and peri-urban areas; in spite of many commitments she agreed not only to support the Urban Programme with funds but also to devote time as a Director on the Sanghamithra Board and to be involved actively in the Urban Programme. The development of the urban programme is an interesting and informative experience which will be recorded separately.

An extract from a letter from Mr.Ramesh Ramanathan dated November 26, 1998 reads:

> *To A.P Fernandez: Over the past few weeks, I have spent time with you as well some members of your team. I thank you for the time and effort that you have given in educating me on the various activities of MYRADA. I must state that I am very impressed with the work that your institution is doing, as well as with the open approach that permeates your endeavours, one that welcomes new ideas to penetrate the system.*
>
> *I am writing this letter to you to express interest in working with you and your team on a specific area: Micro Credit. Within this fairly vast field, I am specifically keen on applying this methodology to urban areas (Bangalore). I understand that MYRADA itself is in the process of*

creating a separate entity - Sanghamithra – to work on Savings and Credit programmes for the poor. I would like to be involved in this effort."

Meanwhile, to acquaint Mr.Bhat and the new Directors with the progress of Sanghamithra, as well as to draw from the experience of the Project staff of MYRADA, in order to develop a Mission and a strategy for operations, MYRADA decided to organise a Workshop on August 1 & 2, 1997. The facilitators were Mr. V.N. Bhat, Ms. Vidya Ramachandran and Mr. William D'Souza.

The full report of the Workshop makes useful reading but it is too long to reproduce here in its entirety. It may, however, be useful to quote the part where strategies are suggested by the 3 working groups:

I. *Broad base the Sanghamithra Board to bring in successful entrepreneurial talent and skills in the areas of training and development by inducting at least one representative each from:*

Commercial Bank
Regional Rural Bank
Industry
Profession (Engineering, Law, Accountancy, etc.)
Training Profession (al)

- *Hold a one day financial programme for non-financial members of the Board (strategic planning exercise.)*
- *Hold a one day orientation programme for non-NGO members of the Board.*
- *Identify and prepare a list of competent and committed workers from MYRADA and select administrative and field staff after a selection process to form a core team.*
- *Obtain on deputation one person each from a Commercial Bank and MYRADA with experience in the field of micro-finance for a short period to work with Sanghamithra.*
- *Recruit young qualified people to be developed into a cadre (which would be both less expensive as well as more productive).*
- *Develop a core training team from amongst the available staff and hold regular programmes for staff to coincide with the regular* review.

II.

- *Hold frequent interaction with Commercial banks, RRBs and other MFIs on the techniques and technologies required to support "Banking with the Poor".*
- *Persuade Commercial banks and RRBs to establish separate SAG Cells in their Head Office to develop and finance SAGs and to provide the necessary conceptual and other skills.*

- *Provide repeat training programmes to SAGs/Apex bodies to enhance their capabilities to approach banks and MFIs on their own.*
- *Evolve a proper product mix by using Differential Rates of Interest techniques for different term loans.*
- *Evolve loan-related savings schemes to make loans as far as possible self-liquidating.*
- *Lend to groups and (perhaps) individuals through appropriate products.*
- *Adopt "kiosk" banking to spread fast geographically.*
- *Lend to all SAGs who fulfil our assessment standards irrespective of the NGOs promoting them in our focus areas. (Therefore Sanghamithra should lend not only to MYRADA promoted SAGs but also to SAGs promoted by other NGOs)*
- *Train adult children/wards of the members of the SAG in managing enterprises to expand long-term credit absorption capacities.*

III.

- *Deploy operating funds in loan funds as well as in investment portfolios to optimise earnings.*
- *Adhere strictly to laid down systems and procedures and review and revise those systems and procedures as required to avoid wastages/leakages.*
- *Use IT extensively to save on HR costs and commercial delays.*
- *Follow up borrowers carefully to avoid NPAs.*
- *Explore the refinance route to augment lendable resources.*
- *Pursue with monetary authorities the question of awarding special categorisation to exempt Sanghamithra from impounding provisions and requirements.*
- *Pursue with fiscal authorities to grant the required concessions and exemptions.*
- *Maximise tax-planning to conserve resources.*

The relationship of Sanghamithra to the Banks was also debated; this debate continued through 1999 and the approach adopted will be explained at the end of this chapter.

The years 1996 to 1999 were comparatively slow ones as far as the progress of Sanghamithra was concerned. On the other hand the major policy and organisational issues that had to be tackled to pave the way for Sanghamithra to be grounded and operational could not be solved in a short time; these issues have a momentum of their own, especially when large institutions and Government are concerned. What is highly encouraging, however, is that the responses from the major institutions involved like the RBI and IT Department took the process forward; none of them closed the door permanently even though on paper it seemed to be so at a given point of time.

This writer returned from the World Bank to MYRADA in May 1996 and took over the responsibility of steering Sanghamithra, since Lt. Col. M.S. Ashok decided to start his own organisation and consequently left MYRADA. He however, continued to support MYRADA's work with advice and occasional visits. As his workload increased, he also resigned from the Board of Sanghamithra. Both organisations were sorry to lose his full time services.

4.1. A Donor Responds

In late 1996 this writer approached the Canadian International Development Agency (CIDA) - one of his previous employers that had supported MYRADA whenever it had launched a new initiative with the potential for innovation and policy change - with a proposal to provide a grant to set up Sanghamithra. In response, a consultant engaged by CIDA visited Bangalore for an initial assessment in April 1997.

In 1996 - 1997, CIDA sought micro finance partners with a clear commitment to: (a) Reaching the poor; (b) Financial self sufficiency; (c) Leveraging other sources of funds from the formal financial system (local or international); and (d) Influencing financial sector lending practices to the poor. These selection criteria were in line with the emerging best practices in micro finance.

The latter half of 1997 was devoted to interactions with CIDA. Sanghamithra submitted a concept note to CIDA in October 1997 and followed it with a draft project proposal which was revised, based on comments and suggestions from CIDA officials. On March 9, 1998, SRFS received a communication from CIDA that it would support SRFS in principle and that Developpement International Desjardins (DID) had been selected to be the Canadian Executing Agency (CEA) for the project **Banking With the Poor.** The purpose of engaging the CEA was to provide co-ordination and support to project implementation. During a brief visit to Ottawa in May 1998, this writer had further discussions with officials from CIDA and DID.

DID's website states:

> *Developpement international Desjardins (DID), a component of the Mouvement des caisses Desjardins du Quebec which is the largest financial institution in Quebec (Canada), is one of the world's leaders in establishing partnerships designed to set up financial institutions. DID is currently carrying out projects in over 25 countries in Africa, Latin America, the Caribbean, Asia and Central and Eastern Europe. In the regions where it intervenes, DID is helping empower the disadvantaged by fostering access to financial services. DID's role: a lever for action. DID's strength: achieving results.*
>
> *Developpement international Desjardins has concentrated its creative energies on finding solutions to the following problems: How can long-term mobilisation of local savings be encouraged? How can the security of those savings be guaranteed? How can micro-finance activities be made viable? What are the best ways to maximise the credit recovery rate? How can women be given greater access to financial services? How can effective training for local staff be ensured? Does the use of plastic money have a place in micro-finance? How can lines of credit be managed effectively?*

With this background, MYRADA assumed that DID was an obvious choice to support the growth of Sanghamithra.

Developpement International Dejardines informed SRFS of a pre-inception Mission in October 1998. Representing DID were Mr. Pierre Emond, Vice President, DID and Mr. Yves LaFond, a Consultant engaged by DID. Following this pre-inception Mission, DID decided to field a mission of two National Consultants to undertake the preparator work for the Inception Mission which DID proposed to launch early in 1999. Thi Mission took place between January 8, 1999 and February 14, 1999. Representing DI in the Mission were Mr. Pierre Giguere, Director - Asia and Credit and Risk Managemen Specialist and Mr. Yves LaFond, Project Director. The expected outputs of this Missio were the following:

- Effective project implementation schedule, inputs, outputs, budget, Logic Framework Analysis and the Work Programme Structure (WPS) on a result based framework.
- Detailed formulation of verifiable indicators of performance to monitor an evaluate progress as the project proceeds.
- Detailed work plan and budget for the first year of the project
- Disbursement schedule by quarters for the first fiscal year.
- Operational project management and coordination.
- Project monitoring and reporting framework.
- Letter of understanding between DID and Sanghamithra specifying the roles ar responsibilities and determining the plan of action for the whole project.

The result of the mission was an updated and completed inception plan, including strategic overview of the project, detailed work plans for the first year and a result based framework.

Over a period of five years, DID collaborated in setting up and implementin Sanghamithra. DID mainly provided professional services and organised study visits Desjardins in Canada.

The main elements of this collaboration between Sanghamithra and DID were:

- A study visit to the movement of Desjardins for the CEO of Sanghamithra member of the Board (Vice Chairman), one representative of NABAR and the Chairman of one RRB.
- Technical assistance by a Canadian expert from DID on audit, control a inspection.
- Technical assistance by a Canadian expert from DID on the elaboration o business plan for Sanghamithra.
- Technical assistance by a Canadian expert from DID on strategic plannin for the future of the organisation and the possibility of creating new simi entities.
- Adhoc technical assistance provided by the Project Director on each of t visits to Sanghamithra.
- Commissioning and financing of various researches and studies:
    - Gender Study
    - Feasibility Study

- Impact Study
- Case Study

- Study tour in Bangladesh for the CEO of Sanghamithra.
- Participation in the elaboration of systems, procedures and MIS.

Meanwhile CIDA had gone ahead with processing the Sanghamithra proposal. **It must be noted that negotiations with CIDA began much before the idea of launching an urban programme took shape. CIDA's support, therefore, was restricted to the rural programme.** A letter from CIDA committing a grant to Sanghamithra was required in order to apply to the Home Ministry, Government of India, for permission to receive foreign funds. This letter was given on February 2, 1999 and reads as follows:

Letter Head:

Canadian High Commission, NEW DELHI
February 2,1999

Over the past several months, we have noticed a marked increase in the visibility of micro-finance in India, especially at the policy level. Particularly encouraging are the facts that Finance Minister Yashwant Sinha, in his Budget speech last year, made a specific reference to the need for mainstreaming the concept of Self-Help Groups lending by the banking sector, and later, at the India Forum Policy session held in November 1998, the Governor of the Reserve Bank of India, Mr.Bimal Jalan, stated that providing micro finance was a 'national priority' and asked NABARD *to set up a task force for submitting recommendations.*

In this context, we note with satisfaction the progress that has been made in our recent discussions with MYRADA *regarding Sanghamithra. Particularly the recent discussions held in Bangalore between representatives of Development International Desjardins (DID) and* MYRADA *were highly productive. We understand that during the last meeting a lot of ground was covered and a thorough discussion on all elements of the Inception Plan was organised. Based on those discussions, you have now submitted a draft of your Business Plan and projections for review by the DID representatives.*

Although the final draft of the documents are currently under preparation, we are pleased to inform you of CIDA's commitment to supporting Sanghamithra (through DID) in the amount of one million Canadian Dollars (C$1,000,000/-) over a period of five years. Under this initiative, Sanghamithra will develop profitable credit delivery models targeting the poor to be adopted by the formal banking sector. This involvement will, a) facilitate the implementation of Sanghamithra's plan of setting up an institutional capability for providing credit support to the rural and urban poor in India, and, b) cover your both start up expenses and lending activities. Please treat this letter as representing CIDA's commitment to this involvement.

Please note that the release of approved funds to Sanghamithra will be pursuant to the finalisation of the Business Plan as well the obtainment of all the necessary approvals.

Let me also take this opportunity to convey our best wishes for the speedy implementation of a promising initiative.

Sincerely,

Faisal Beg, Development Officer/Economist

The Government of India did not require an MOU for this project. Therefore, it did not fall under the category of a "bilateral project", even though the funds came from the bilateral division of CIDA.

4.2. A BRIEF OVERVIEW OF SANGHAMITHRA'S POSITION

By the end of 1999 Sanghamithra was ready to start operations. It obtained clearance from the Home Ministry to receive the grant from CIDA. At this point it may be useful to recapitulate briefly;

i. the basic features and objectives of Sanghamithra,

ii. its growth policy,

iii. the position taken regarding its relationship with Banks and other financial institutions involved in lending to SAGs,

iv. its concern to remain focused on the poor, and

v. its products and services.

i. Sanghamithra is a "not for profit" finance institution incorporated under Section 25 of the Indian Companies' Act of 1956; it lends directly only to self-help affinity groups. Originally classified as a non-banking financial company (NBFC), it was re-classified later as a micro-finance institution (MFI) and is exempt from compliance with requirements under Section 45 of the Reserve Bank of India Act.

The objectives of Sanghamithra are:

- To work with the poor to build on their efforts to rise and remain above the poverty line.
- To provide credit, on interest or otherwise, to groups of poor persons who come together on the basis of affinity, both in rural and in urban areas, with the support of SAG promoting institutions like NGOs and Banks (SHPIs).
- To create replicable models in the area of financial services for the economically poor and socially exploited sections of society in rural and urban India.
- To support the rural and urban poor to overcome poverty of all kinds (economic poverty, poverty of values and poverty of relationships with people and organisations) through capacity building, skill development and attitudinal changes.
- To encourage and collaborate with people and institutions with objectives similar to those of Sanghamithra.
- To collaborate with governmental and non-governmental organisations to bring about changes in public policies and practices in favour of the poor and the deprived, particularly in the areas of economic, fiscal and social administration.

Sanghamithra's approach is guided by the following principles:

- It provides a service - reaching clients who would otherwise have difficulty in accessing credit.

- It fosters innovation - developing flexible and sustainable credit systems that the poor can access easily and quickly.

- It has faith in the poor - proving that the poor are bankable, that they have credit discipline, that they have the potential to improve incomes, increase productivity and make profits.

- It seeks to influence systems and policy change - transferring new credit delivery practices to the formal banking sector, more particularly to regional rural banks and co-operatives and advocating policy changes where absolutely necessary and expedient.

ii. As far as its policy for growth is concerned, Sanghamithra does not aspire to be a monolith; this philosophy underlies and informs all policy decisions. Sanghamithra will grow to a certain size, where the economies of scale will help it to achieve sustainability without losing its flexibility. The appropriate size to achieve this balance is assessed to be an outstanding loan portfolio of about Rs.25 crores. Efforts will be made to start new Sanghamithras in other parts of the State/Country wherever the SAG movement has spread and where the banks have not been able to establish adequate linkages. Each Sanghamithra will have a separate legal identity and operational independence. It is also proposed to start a Fund Management Company. This company will supervise the Sanghamithras, mobilise resources, plan for new Sanghamithras and allocate funds efficiently among them. There are some donors who wish to lend to Sanghamithra; they do not want their money back but would like it to be returned to an organisation within the country which could on-lend to MFIs. The proposed Fund Management Company would perform this function.

It must be stressed that while Sanghamithra does intend to break even and make surpluses through its credit operations, its intention is not simply to demonstrate this fact but to create an impact by being at the cutting edge of ethics-based innovation in the micro finance sector -"not monopoly but excellence".

iii. Sanghamithra does not intend to replace banks. It seeks to extend credit, on commercially viable terms to SAGs which have proved themselves to be responsible and creditworthy. Sanghamithra has developed norms for evaluating creditworthiness of SAGs — norms which are realistic, objective, measurable and demonstrably effective. It attempts to prove to the banks that SAGs are 'bankable' on a commercially viable basis. Should any bank come forward with an offer of credit to SAGs in a given area on terms that match Sanghamithra's, the institution steps aside, having done its work. Sanghamithra seeks to prove to banks that rural credit operations can be profitable and sustainable, if credit is channelled through stable and reliable SAGs.

Myrada identified emerging trends in the financial sectors during 1999-2000 which had the potential to undermine the quality and to slow down the progress of the SAG-Bank Linkage Programme. On one hand, the Banks were beginning to discover that lending to SAGs was "good business"; on the other hand, the quality of their service was declining since they had a monopoly over the SAGs in their service area – although the service area rule was removed for the Bank Linkage programme, yet in practice it continued. Banks began to depend increasingly on NGOs for dealing with SAGs; bulk loans were being given to NGOs for on-lending; even where Banks lent directly to SAGs, there was increasing reliance on NGOs to follow up on repayments. Banks were unwilling to issue cheque books to the SAGs, and restricted their service to SAGs to one or two days a week, thereby causing great inconvenience to the members. Given this scenario, Myrada felt that it is necessary to keep bankers on their toes by servicing SAGs which had problems with the Banks; however, in keeping with its philosophy, it would withdraw if and when the Bank's performance improved. It would help to create a competitive environment so that the poor can access credit according to their needs and schedules and on the best terms.

With the Voluntary Retirement Scheme catching on in Banks, and the delay in filling up vacant positions, the staff in the branches of Commercial Banks reported increasing pressure of work. As one Branch manager wrote: "I am required to canvas LIC's life policy, canvas New India's general insurance policy, sanction loans to scores of prospective cycle owners, attend to directions of the executives of LIC and Hero Cycles Company, entertain women who want to buy gold, conduct home loan fairs, sell ECGC policy, collect BSNL's telephone bills, income tax and excise duty and send newer and newer statements to HO." He implies that he has little time to attend to his important customers or to secure larger loans with reduced risk, leave alone coping with the SAG members. Myrada's analysis of these emerging trends indicated that Commercial banks would withdraw from directly linking up with SAGs over the next 3-5 years and resort to bulk lending to MFIs/Intermediate organisations; Regional Rural Banks would continue for a few years more but they too would be under pressure to scale down direct linkages with SAGs; this creates opportunities for the Cooperative Banks and Societies and MFIs in the field of micro finance.

iv. SRFS will constantly endeavour to tailor its operations so that they continue to be appropriate and "friendly" to meet the needs of the poor. The decision to lend only to SAGs helps to sustain this focus, since the members of SAGs are poor. The size of the loans they require are not large initially, though it increases from the third year. The transaction costs of managing small loans to individuals will not make Sanghamithra's operations sustainable; therefore the way to proceed is to advance one loan to the group which is comparatively large when compared to individual loans. The NGOs forming the SAGs are primarily responsible to ensure that the members are poor and linked by affinity. Sanghamithra checks on their status in the course of the group's assessment prior to lending. Sanghamithra's first loan to the group is small; it's size depends on the cash flow of the group; it does not endeavour to push funds into SAGs at a rate and in amounts that the members cannot absorb without excessive risk to their existing livelihoods.

This focus on the poor has at least two major consequences which attract the criticism of Micro Finance experts. These are :

(i) that the loans are small and do not contribute to the sustainable increase in livelihoods for which larger size loans are required and

(ii) the loans are used largely for "consumption".

An analysis of the trend in the size of loans in SAGs promoted by MYRADA indicates that while the loans are small and a large number opt for consumption during the first year, the members graduate to comparatively larger loans and to investments in income generating activities including trading in the second and third years. There are several studies in MYRADA to substantiate this trend.

As regards the size of loans, the trend in the size of loans to SAGs in Sanghamithra's portfolio confirms this. For example in 2000-01, Sanghamithra gave only **3 loans** to SAGs which were between Rs.1 and 2 lakhs. This number increased to **44** in 2001-02 and to **155** in 2002-03. With respect to loans between Rs.2-3 lakhs, in 2000-01 and 2001-02 no loans were advanced in this category. However, in 2002-03, there were **18** loans. With respect to loans above Rs.3 lakhs, there was only one in 2002-03. However, the trend is obviously towards larger loans. Loans between Rs.2 -3 lakhs would work out to an average of Rs.12,000 to Rs.15,000 per member; though some get larger loans even up to Rs.25,000-Rs.30,000 since the money is not equally distributed among the members. In fact, if patterns in lending indicate that the money is equally distributed, then it is a major indicator that the group is below average and should not be asking for or receiving loans in the first place. However, to impose a package or a product in the first year which is considered "viable" partly because it is a large investment, does not respect the need that the poor express for at least a year of training and experience in managing SAGs which gives them the confidence and skills required to invest in large, "viable" income generating initiatives. Sanghamithra's position is that the people are the best judges of the timing and size of loans that they are free to access.

The second issue which needs to be addressed relates to loans taken by members for "consumption" purposes. An analysis of the trend in the purpose of loans made yearly by MYRADA, indicates a clear shift from a bias towards "consumption" in the first year, to trading, cottage industries, agriculture and on and off farm activities thereafter. Even in the first year, though the average number of loans for consumption is around 50% of the total number of loans taken by members, the average amount works out to only 20%. However, the question also needs to be asked: "What exactly is consumption?" Under this category are included loans for food, clothes, socio-religious ceremonies, as well as loans for education and health and to repay loans taken from moneylenders (which are usually taken mainly for "consumption" purposes). MYRADA holds that loans for education and health are investments. It is ironical that if a student at the prestigious Indian Institution of Management takes a loan for his/her education, it is considered to be a sound investment, whereas if a poor person takes a loan to send a child to school it is considered to be "consumption". Repaying high interest loans to moneylenders through borrowings from the SAG is surely not consumption; it is good management of money. Loans for urgent needs like food and clothes are precisely what puts the poor in the clutches of the moneylenders; they are able to repay only the interest given their earning capacity; many eventually loose their lands which were placed as security. The SAGs are willing to provide loans for these purposes. To undervalue the impact of loans for these purposes that the poor require to break the poverty cycle by calling them "consumption" loans is unjustified.

MYRADA's studies indicate that even when loans are taken for "productive purposes", the repayment instalments do not come entirely from these investments, since the cash flow of earnings from an investment often differs from that of the prescribed schedule of repayments. In fact one study showed that over 60% of the repayments came from sources other than the income-generating asset for which the loans were taken. This is because the monthly income from an asset is variable – no cow for example gives the same amount of milk every month. Hence, the SAG members repay their loans from other sources of income including labour. The argument therefore that loans for consumption should not be given since they are not investments, is not valid. The records of SAGs indicate that the repayments on consumption loans is as good as loans for any other purpose.

v. Sanghamithra's Products And Services: It is often reported – as a veiled criticism - that Sanghamithra "offers only one loan product to the groups". This is true in the sense that Sanghamithra gives a loan to SAGs as institutions (the loan is credited to the SAGs common fund) without knowing the purpose in advance for which the members will borrow from the common fund. However, the SAGs are free to decide for what purpose to advance loans to members. The SAG model provides the space for members to take the decision regarding the purpose of the loan given to each member, the interest rate and schedule of repayment and the sanctions for delays. To provide a balanced response to this criticism it is necessary therefore to separate the end use of the loan which is decided by the members, from the need for Sanghamithra to design a loan product which may be required in cases where the SAG members require larger sums than what the SAG is willing to lend and where the SAG decides that a particular purpose may increase its risk to a level that it is not willing to bear –at least at a particular point of time.

The generally understood content of the term "loan product" is that it is designed with the following features: " 1. A defined purpose (for example: housing or insurance) and , 2. A detailed framework guiding the process of loan approval which includes at least the unit cost, the interest and the schedule of recovery. These features are generally standardised by the lending institution with reference to a particular "loan product". In Sanghamithra's case, all these decisions are taken by the SAG and differ from group to group depending on what each group thinks is appropriate at that particular time; accordingly the group may decide that the member is not able to manage a large loan for the entire house, so it will break it down into smaller loans which allows the house to be constructed in stages over a longer period. This occurs in several similar loans. For example, to quote the experience of a member asking for a loan of Rs.10,000 to put up a small wayside tea shop . The group decided to lend the first instalment of Rs.3,000 only to cover the cost of a stove, fuel, vessels, cups etc and to keep investment in a stable (pucca) structure for later.

An analysis of the purposes for which the SAGs give loans to members shows that they cover a wide range. They have many "products". In fact this writer was once approached with the idea of launching a Housing Loon Product for Sanghamithra. He pointed out that SAGs receiving loans from Sanghamithra had been lending to members for house construction, house repair, electrification and extension. In fact MYRADA's records, which cover several years indicate that SAGs lend for a variety of purposes or "products". MYRADA realised that the wide variety in the local situation related to costs and availability of materials and land, to size of family and customs and to cash flow which is seasonal, demands that the lending policy adopts a model which allows and can cope with this variety. The SAGs have proved to be the appropriate institution to cope with this variety; they have done it for the past 15 years and continue to do. A standard "product" design is surely not appropriate in the rural areas; at least not for the poor in the initial stages of their development.

The issue of Sanghamithra designing a loan product for housing emerged recently when groups in the peri-urban areas of Mysore requested for larger loans (approx Rs.45,000 per member) for housing. The proposal from the SAGs was that the housing loan should run parallel to a loan that the group had taken from Sanghamithra. The housing product should have a longer repayment period and possibly a lower interest rate than the standard loan. This proposal was approved by the Board and introduced as a "product" in November 2003. By March 2004, 4 loans to SAGs totalling Rs.6 lakhs were advanced for housing. Please refer to Annexure 3 for a description of this "product".

The need for an "insurance product" to cover at least the assets like livestock purchased by group members from loans and life insurance for the borrowers is unquestionable. However in MYRADA's strategy, this product is increasingly being provided by the Resource Centres (RCs) which have emerged in areas from which MYRADA is scaling down its programmes. Each Resource Centre covers 120–150 SAGs and Watershed Management Associations (WMAs). These institutions pay for all the services that the Resource Centres provide. Within the past 24 months, fifty-three Resource Centres have emerged in MYRADA's project areas from which it is withdrawing. Each RC is staff by a Senior MYRADA staff and several Community Resource Persons drawn from the SAGs. Each RC has a Board composed of SAG/WMA representatives and a separate Bank Account. The RCs have established a relation with various Insurance Companies, which have a presence in their area – usually through Agents - and help the members to carry out all the transactions required for insurance. Several innovative insurance products have been promoted by Insurance Companies which are appropriate to rural areas; but their coverage is still limited and people need confidence and support to access them. The RCs are now in the process of working out an agreement with Sanghamithra to promote insurance of its borrowers. Similar RCs are being promoted even outside MYRADA where Sanghamithra is operating.

"One of the key elements of Sanghamithra's approach is the policy of no restrictions on the purpose of the loans, allowing the women to decide on who gets the loans, based on need and ability to repay. This policy is 180 degrees from many MF, donor and Government operations which insist on the loans being used only for specific "productive" purposes. Client uses of loans within the SHGs are mixed; petty trade, micro business working capital or assets, medical or educational expenses, HH consumption, paying off old loans to moneylenders.

Purpose-driven policies can sometimes lead to misleading responses to staff or external evaluators in questions regarding the purposes of the loans. Many MF "loan use" surveys of clients are full of errors.

What was remarkable in discussions with SHG members was the transparency (and their confidence) in stating the loan purposes. For example, some women said that they have used the loan to pay off debts to moneylenders (a fresh start), others that they had used the loan to make a down payment on an autorickshaw for their husband. These uses are often considered by outsiders as "non-productive", or gender insensitive. It is much more pragmatic and accurate, need and data-wise, to allow the client to be fully transparent on loan use. A policy of no restrictions on loan purpose, only the ability to repay, addresses real needs and is productive. Certainly, clearing up old debts are productive investments. Women want these types of loans, are open on uses and will repay them.

The key necessity is a credit system that can address multiple needs on a sustainable basis. Sanghamithra is effectively on the frontiers of providing this service".

(Project Evaluation by Robert Mitchell & Shipra Goyal)

4.3. FROM GRANTS TO LOANS:

Sanghamithra's management, from the very beginning was aware that it had to achieve operational and financial self-sufficiency; a period of four years was considered to be adequate to achieve these objectives. Efforts towards achieving financial self-sufficiency – which partly relates to the cost of funds – can be undermined if the institution only focuses on mobilising grants where the cost of funds is zero. This could introduce a culture in the institution which does not promote efforts to achieve financial self sufficiency. Sanghamithra's management decided to adopt a strategy which has three stages. In stage one (up to a loan portfolio of Rs.5 crores) Sanghamithra would mobilise grants partly to train staff, install infrastructure and partly to on-lend. In stage two (up to a portfolio of Rs.10-15 crores) subsidised loans would be mobilised and in stage three, Sanghamithra would go in for loans at commercial rates. However, even when the cost of funds is zero, a policy was adopted of imputing the cost of funds at 6% so that a more realistic picture of performance would emerge.

In the take off stage, therefore, Sanghamithra opted to mobilise grants. With CIDA offering to support Sanghamithra, the programme was able to take off. The first grant from CIDA was received on August 12, 1999. Subsequently, between this date and May 2002 a total of Rs.30.26 million was received in 10 instalments. Thirty percent of this amount was used to pay salaries, purchase/hire infrastructure and seventy percent to on-lend.

Sanghamithra then approached NABARD for a loan at subsidised rates. Its proposal to NABARD was accepted on May 29, 2002 and a loan under the Revolving Fund Assistance (RFA) programme was sanctioned to the extent of 75% and 50% of Sanghamithra's funding requirements for on-lending to SAGs during 2002-03 and 2003-04 respectively, subject to a maximum of Rs.2.51 crores (Rs.25.1 million). The RFA was released in two equal instalments every year. A moratorium period of one year was provided for the repayment of the capital. However, service charge on the principal amount inclusive of the period of moratorium was payable. The total amount was to be repaid in 5 years with one-year moratorium, in 8 equal half-yearly instalments. The RFA was secured by Sanghamithra assigning its book debts by creating a floating charge in favour of NABARD and by agreeing to hypothecate to NABARD its movable assets to the extent of a shortfall. Sanghamithra is required to maintain the list of book debts assigned to NABARD and to ensure that no second charge/additional charge is created on them and also that the book debts do not become time barred.

The Agreement with NABARD also requires the setting up of a Project Implementation and Monitoring Committee (PIMC) comprising representatives of NABARD, one or two leading Bankers and MYRADA. The Committee meets quarterly and reviews the implementation of the programme and recommends the release of further instalments. The committee has met six times so far. The last meeting being on March 30, 2004. The Reports from the PIMC indicate that Sanghamithra's loan from NABARD has been well managed and repaid on time. More importantly, the overseeing of this loan has been a learning experience for both parties, particularly for the Sanghamithra staff who have benefited greatly from NABARD's and the Bankers suggestions and guidance.

Sanghamithra then took the third step and approached a Commercial Bank, viz., Canara Bank, though by this time the gap between the interest rates of Commercial Banks and Financial Institutions focusing on development like NABARD was closing. On June 10, 2003 the Canara Bank sanctioned a loan of Rs.3 crores as a term loan in tranches of Rs.50 lakhs each over a period of 24 months. Each tranche of Rs.50 lakhs is to be repaid in 36 monthly instalments of Rs.140,000. The loan initially carried an interest rate of 7.75%. There is a repayment holiday of six months from the date of the first disbursement or three months from the date of last disbursement whichever is earlier for each tranche of Rs.50 lakhs. By March 31, 2004 Sanghamithra had drawn a sum of approximately Rs.2 crores from Canara Bank against the sanctioned amount.

In early 2004, however, Sanghamithra appealed for a reconsideration of the Terms and Conditions in order to improve its liquidity position and to give it more flexibility. Accordingly, Canara Bank revised the Terms and Conditions on April 15,2004 as follows: (1) the term loan of Rs.30 million was converted into an overdraft account against receivables/book debts; this is to be renewed yearly. (2) The interest was reduced from 7.75% to 7% with effect from April 01, 2004. The response of Canara Bank will go a long way in supporting Sanghamithra to improve the credit flow to the poor and to lay the basis for sustainability of the institution. The willingness of the Canara Bank Management to offer a similar level of flexibility to the rural poor as currently exists in the retail and urban sector is adequate evidence that at least some of our Commercial Banks have not forgotten development priorities.

4.4. RELATIONSHIP WITH NGOs:

SRFS depends on NGOs to identify affinity groups and to train and nurture them for about a year before it extends credit to them. During the first two years of operations, SRFS linked up mainly with SAGs formed by MYRADA. Thereafter it increasingly related to SAGs formed by other NGOs. During 2003-04 over 59% of SAGs borrowing from SRFS were formed by other NGOs.

Many of these NGOs and Resource Centres which have undertaken to train and upgrade groups formed under the Government sponsored Stree Shakti programme requested SRFS to provide funds for SAG formation and training. SRFS agreed to this request because it was already part of its over all strategy to support other institutions promoting SAGs even before it began to meet its costs. Accordingly, SRFS has provided a sum of Rs 28,916 received from NABARD and a further sum of Rs 2,23,471 from CARE-India for training to these institutions.

In July 2002, SRFS introduced a "scheme" called Sammaan Dhan. The objective of this scheme was to meet, at least partly the cost incurred by NGOs in training the SAGs. To begin with, SRFS divided its NGO partners into two categories. Category A includes all those NGOs who have formed and linked at least 50 SAGs with SRFS. These NGOs receive a sum equivalent to 8% of the total administrative charges earned by SRFS on those accounts of SAGs introduced by the NGOs concerned, provided the accounts are successfully closed. Category B includes those NGOs who have introduced less than 50 SAGs. Such NGOs receive 6% of the total administrative charges. SRFS proposes to increase the percentage under the "Samman Dhan" on a yearly basis depending on its surpluses.

CHAPTER 5

From 2000 – 2004: An Overview of Sanghamithra's Operations

The reader who has had the patience to reach this page will breathe a sigh of relief. Processes are necessary to lay a broad and deep foundation for an institution, but they can get tiring and painful and need a degree of stubbornness to pursue; they can also be extremely costly in terms of both time and money. The promoting organisation has to be able to allocate the space and resources required and to be fortunate enough to have a supportive organisational policy to promote these processes. Fortunately, MYRADA had enough of stubbornness as well as the support of its Board to carry the idea of Sanghamithra through from 1993 to 2000.

The first loans were given to three SAGs in a MYRADA Project in Chitradurga District on February 24, 2000. The three SAGs were: (1) Sri Gowridevi MSSS, Visweshwarapura, which received a loan of Rs 15,000/-, (2) Maramma Devi MSSS, Gowdrahatti, which received a loan of Rs 60,000/-, and (3) Sri Manjunatha MSSS, Ramaghatta, which received a loan of Rs 20,000/-.

From 2000 to March 2004 SRFS moved ahead steadily. The ability of the CEOs, Shri V.N. Bhat and Shri S.M. Adiga, to negotiate agreements with Banks in order to cut down on transaction costs while reducing the time taken in fund transfers to the remotest corners where SAGs were functioning, to put in place appropriate and adequate systems to manage fund flows so that funds were not lying idle and to monitor the progress of the Credit Managers on a day-to-day basis played a major role in the rapid growth in coverage, in reducing costs and in motivating the field staff to work with commitment and efficiency. MYRADA staff also took a lead in promoting Sanghamithra's lending portfolio in their project areas where the Banks were not sufficiently active in promoting the SHG-Bank Linkage Programme. From 2003 Sanghamithra increasingly established relationships with SAGs formed by other NGOs and under Government programmes, in many cases after investing in their training and upgradation.

This writer is given the privilege to describe the progress and achievements of Sanghamithra during these years. He is aware that a new organisation tends to take off and function well initially and, therefore, its performance during the first few years is not a valid indicator of its progress thereafter. However, the facts and figures provided by Rating and Assessment institutions and by Sanghamithra management related to its progress so far indicate that it has performed well, even exceeding expectations. To avoid the accusation (or at least the suspicion) that this writer is biased, as he could well be given his close involvement with the institution, it may be in the fitness of things to draw largely from assessments made by outside sources that were engaged to study Sanghamithra's performance. It will also provide the reader with the opinions of outside sources which carry the flavour of greater objectivity than the opinions of insiders, as well as a higher degree of expertise in the field of micro finance.

The following pages therefore will draw extensively from three reports:

1. The Impact Assessment of Sanghamithra (Rural Programme): This study dated July 2003 was done by Ms. Girija Srinivasan who has worked in major Financial Institutions, advised Governments abroad on micro finance and provided consultancy in micro finance to several national and international organisations. It was commissioned by DID, Canada and was included as part of the contractual obligations with CIDA. The Impact Assessment (as it will be called in references) was carried out on Sanghamithra's Rural programme only.

2. A Capacity Assessment (credit rating) carried out by M-CRIL and commissioned by SIDBI (Small Industries Development Bank of India) in the context of Sanghamithra's Urban programme's proposal to SIDBI for a loan. This credit rating covers the whole of Sanghamithra and includes both the Rural and Urban Programmes. It will be referred to hereafter as the M-CRIL Rating report.

3. A research study by M.S. Sriram, Faculty member at the IIM Ahmedabad entitled, "Building Bridges between the Poor and the Banking System". This study was carried out under the Sir Ratan Tata Trust Fund for Research Collaborations in Micro Finance; hereafter referred to as "Building Bridges".

(Note: All figures and ratios pertain only to the Rural Programme of Sanghamithra unless indicated otherwise.)

5.1. SANGHAMITHRA'S PHYSICAL PROGRESS FROM 2000 TO 2004 (MARCH). THE RURAL PROGRAMME.

Sanghamithra's Rural Programme is operating in the revenue Districts of Mysore, Chamarajanagar, Chitradurga, Shimoga, Mandya, Davangere, Kolar, Bangalore Rural and Shimoga - all in Karnataka State and in Dharmapuri and Krishnagiri Districts of Tamil Nadu. It also started operations with SAGs formed by MYRADA Kadiri Project in Anantapur District of Andhra Pradesh but withdrew in 2003 since the local RRB decided to expand its SAG Bank Linkage Programme.

There has been a steady growth in the area covered, in the number of SAGs linked to Sanghamithra and in the performance of staff as the following table indicates:

	2000-2001*	2001-2002*	2002-2003*	2003-2004**
Operational Districts	7	7	8	11
Number of groups assisted against whom loan is outstanding	465	795	1052	2108
Number of branches	4	6	12	15
Number of groups per staff	85	159	150	151
Number of villages per staff	49	83	98	88
Value of loans outstanding per staff (Rs. in lakhs)	18	46	59	60
Cumulative loans disbursed (Rs. in lakhs)	122	386	837	1617
Outstanding Portfolio (in lakhs)	92.30	230.53	412.85	725.40
Growth rate in Loan Portfolio		216%	116%	93%

Sources:

* **Impact Assessment by Ms.Girija Srinivasan pg 7 As on March 31,2003.**

** **Sanghamithra data from April 1 2003 to March 31, 2004**

There has been a steady increase in the cumulative loans disbursed. The outstanding loan portfolio also shows a healthy trend. The number of groups serviced by one staff has gone over the figure of 100 to 120 as originally envisioned. The number of villages per staff has risen steadily. However, as the number of groups increases in a village, as is the experience in large villages where new groups emerge as a result of a "demonstration effect", it is expected that the number of villages per staff will decline. This will reduce transport time and costs to service the SAGs; the field officer will also have more time to devote to each group.

Commenting on the growth rate and the potential for expansion, the M-CRIL Rating Report states: "Sanghamithra has experienced tremendous growth over the past one year." ... "This growth has resulted from a clear and focused strategy of lending to self help groups promoted by partner NGOs and sharing a clear understanding of responsibilities with them." ... "For its rural operations, the organisation plans to expand in the areas where the banks, especially the RRBs have not linked with low income clients. This gives a huge business opportunity to Sanghamithra to expand given the continued reluctance of banks to provide credit linkage to such clients" (pgs 8 & 9 M-CRIL Rating Report).

The performance of SRFS is obviously related to the quality of management it fosters. Commenting on the performance related to management of the Rural and Urban programme, the M-CRIL Rating Report states: "Sanghamithra displays good performance on managerial factors. This results from a sound managerial system and accurate operationalisation of the policy and strategy of the organisation. Sanghamithra has highly qualified and professional managerial staff. The training and induction system for all staff members in the rural programme is systematic and thorough. The understanding of the staff of the various operational and procedural aspects is adequate. Commitment and motivation at all staff levels is high."

"Sanghamithra can bank upon the huge experience of its promoter MYRADA in the field of development and micro finance. Apart from the institutional experience of MYRADA, it also has very experienced bankers and development experts on its board. Their input on issues related to policy and strategy has a significant impact upon the overall performance of the organisation". (M-CRIL Rating Report Page 9.)

5.2. DO THE RURAL POOR BENEFIT?

According to the Impact Assessment, carried out by Ms.Girija Srinivasan, the poverty profile of the SAG members indicates that 65-70% of the members are agricultural labourers and 82% hold less than 2 acres (of dryland). It can be reasonably assumed, therefore, that they belong to the category "poor" if not to the category "poorest".

	2000-2001*	2001-2002*	2002-2003*	2003-2004**
Percentage of clients who are poor as defined by occupation (agricultural labourers)	33%	57%	70%	65%
As defined by land holding of less than 2 acres	64%	70%	82%	82%

Sources:

*** Impact Assessment by Ms.Girija Srinivasan pg 7 As on March 31,2003.**

**** SRFS data**

MYRADA's experience gained while conducting hundreds of Participatory Wealth Ranking exercises in the field indicates that people divide the "poorest" broadly into two categories, namely **a)** those who are old, sick and infirm/disabled; they prefer to form separate groups and to get involved in activities which are more social in nature; many also are involved in savings and credit but on terms that suit their conditions, and **b)** those who have the capacity to earn provided they have group support; these usually join the SAGs involved in savings and credit. Studies indicate that the second category of the "poorest" in the SAGs where savings and credit is the major "product" has been able to move upwards both economically and in terms of overall "empowerment".[1] Since Sanghamithra has adopted the strategy of lending to SAGs as groups, the focus on the poor has to come from the NGO which identifies an "affinity" group of poor people and then provides the institutional capacity building required. Sanghamithra, on its own, also factors indicators related to the poverty status of the members in its assessment of the SAGs. The focus on the poor, therefore, is a major dimension in Sanghamithra's strategy.

[1] Refer to **"Putting Institutions First – Even in Micro Finance"** by this writer which incorporates two studies by outsiders and one by MYRADA. All the three studies support this trend; it must however be noted that the SAGs covered by these studies were all formed and trained by MYRADA.

5.3. A Few Key Financial Ratios/Indicators of the Rural Programme

Cumulative Repayment rate: (Ratio of cumulative principal recovered -net of pre-payments -to the cumulative principal due till the date of measurement). The Cumulative on time repayment rate of the **Rural** programme is noteworthy as the following table indicates:

	2000-2001*	2001-2002*	2002-2003*	2003-2004**
On time repayments (%)	99.95	99.99	99.31	98.48

Sources:
*** Impact Assessment till March 31st 2003 and**
** SRFS data from April 1, 2003 to March 31 2004

Portfolio At Risk (PAR): (Ratio of the principal balance outstanding on all loans with overdues greater than or equal to 90 days to the total loans outstanding on a given date)

	2000-2001	2001-2002	2002-2003	2003-2004
Portfolio at risk		Nil	Nil	0.64

Source: SRFS data

M-CRIL's rating report for the whole of Sanghamithra (Rural and Urban Programmes) gives a figure of 98.9% under Cumulative Repayment Rate. It states: " This is primarily due to a very strong credit culture, high levels of discipline at all levels and a zero tolerance policy that Sanghamithra has been able to maintain, despite rapid expansion even in the drought prone areas of Southern Karnataka" (pg 12). The reference to the drought is valid and relevant here as seven of the eleven Districts where Sanghamithra is operating are badly affected by drought; most of them have experienced drought conditions for three successive years.

Operating Expense Ratio (OER): (Ratio of salaries, travel, administrative costs and depreciation expenses to the average loan portfolio).

	2000-2001	2001-2002	2002-2003	2003-2004
Excluding depreciation		11.35%	12.73%	6.38%
Including depreciation		12.82%	13.35%	6.72%

Source: SRFS data

For the whole of Sanghamithra (Rural and Urban Programmes), the OER is 9.6% (Sept 2003) according to the M-CRIL Rating report. Maintaining an operating expense ratio below 10% is an achievement which any MFI can be proud of.

Yield on Portfolio: The interest income on loans, divided by the average loan portfolio for the year

	2000-2001	2001-2002	2002-2003	2003-2004
Yield on Portfolio		14.18%	14.58%	14.57%
Return on Average Asset			4.44%	6.68%

Financial Self-Sufficiency: Ratio of total income to total adjusted for expenses for the year. Adjustments are made for subsidised cost of funds imputed at 6%.

	2000-2001	2001-2002	2002-2003	2003-2004
Financial Self-Sufficiency		71.57%	72.33%	102.05%

Source: SRFS data

To quote the comment of M.S. Sriram:

> *"It is important to highlight that these returns were achieved after paying bank charges for leveraging the banking infrastructure. If the banks were to do these activities themselves, the costs would be lower. The banks would be absorbing these costs on a marginal basis as the infrastructure would be in place. The cost of funds for banks would be lower than the figures used for Sanghamithra's cost of capital – banks can access relatively low cost deposits – a window not available to Sanghamithra."* (Building Bridges page 6)

To quote M.S. Sriram again:

Sanghamithra achieved the above performance by following some unique procedures including:

1. *Identifying the customers: This was done in close association with local community based organisations (CBOs). These organisations used participatory appraisal techniques in identifying client groups. By collaborating with the CBOs, Sanghamithra created an institutional control mechanism. The loan disbursal was done by the SHG through a process of consultation. The involvement of a CBO was crucial because it provided a referral system.*

   While the process of targeting the ultimate clients was left to the SHGs, Sanghamithra did assessments, ensuring the safety of the money being lent. The process was as follows:

   - *First a CBO introduced the SHG. Based on a visit and appraisal, the credit officer determined and classified the SHG into three categories.*

     - *Category A: Ready to be linked;*
     - *Category B: Some parameters have to be me to be linked, but can achieve the standards with some inputs; and*
     - *Category C: Not suitable for linking at present.*

- *The category A groups were registered. The advantage of this system was that potential clients go to know where they stood and how they could qualify for linkage. This feedback put the burden of correction on the collaborating CBO. While this feedback was useful, it impaired Sanghamithra's ability to seek and nurture category C clients.*

2. *Keeping the procedures simple: The procedures followed by Sanghamithra were:*

   - *Introduction by a CBO, visit by an officer for assessment. If the SHG was A category then they passed a resolution and applied for a loan.*
   - *The decision to grant a loan was based on the recommendation and the data given by the credit officer.*
   - *Once the decision was made, cheque was delivered to the SHG by the Credit Officer.*
   - *The documentation was done at the time of delivering the cheque.*
   - *The interest incidence was from the date of the cheque and not from the date of handover. The date of handover preceded the date of the cheque.*
   - *Keeping documentation simple – the objective of documentation was to establish that the money was disbursed on certain terms and conditions. Documentation was not done with an objective of going to court. Therefore back ending all expenses pertaining litigation (which would be exceptional) was the strategy. This saved stamp duty on non-defaulting accounts (expected to be more than 98% cases) and in the unlikely event of default leading to litigation, imposed a penalty on those that actually sought legal recourse.*

3. *Keeping products and repayments simple: The loans were usually in round figures. The terms of the loans were fixed in a manner that the instalments were easy to understand. All repayments were through post-dated cheques. However, the contact with the SHGs had to be regular – therefore only two post-dated cheques were taken. Every time a cheque was banked, the SHG was informed to ensure that there was a sufficient balance. While this ensures regular contact, it gave flexibility to Sanghamithra to use the cheque on the due date. The principle was to devise a product that could be rolled out fast and could be easily understood. "Building Bridges between the Poor and the Banking System*

Annexure 5 carries the Balance Sheet of SRFS and the Income and Expenditure Statement for the year 2003-04.

CHAPTER 6

SANGHAMITHRA'S OPERATING PROCEDURES AND THE IMPACT ON THE BANKS

6.1. SANGHAMITHRA'S DELIVERY SERVICE - A COMPARISON WITH THE BANKS

This Chapter deals with SRFS operating procedures and the impact they have had on Financial Institutions particularly Regional Rural Banks which are the leaders at present in promoting the SHG Bank Linkage programme. As mentioned in the Introduction, just as the previous Chapter drew largely from studies by outside consultants and the rating report of M-CRIL, this Chapter also will draw from studies made by two outside consultants, one commissioned by a donor, CIDA, and the other by a researcher from the Indian Institute of Management, Ahmedabad. Since the results of the studies tend to be largely positive, this writer hopes that the findings will be viewed with a little less scepticism than the findings from studies done by MYRADA (or reports from Sanghamithra), which may be considered biased

Sanghamithra's involvement in an area begins with an invitation from an NGO to lend to the groups it has promoted especially when there is reluctance by the local bank to lend to the groups or when the number of groups is too large for a branch to handle. Sanghamithra conducts a survey of potential business in the district and opens a one person residence cum office. Depending on the potential for business in the district, additional persons are posted; a guiding norm is a caseload of 120 groups per credit officer.

Sanghamithra lends to groups which are a year old. The credit officer carries out a comprehensive assessment of the group each time a loan is requested. There is a standard format for assessment of SAGs. It is designed to assess the performance in savings and lending, the monthly cash flow, regularity of meetings and attendance, etc. The Assessment Formats are attached in Annexure 5. In case the group is found to be weak, the reasons for not sanctioning a loan and the areas for improvement are explained to the group as well as to the NGO with a request to support the SAG with training for institutional capacity building. Funds for this training are mobilised by Sanghamithra if required. If the group is strong, the necessary papers are processed and the loan application is filled. The loan amount is usually discussed with the group and the size and terms of lending mutually agreed upon. The papers are sent to the Sanghamithra HO for processing so that they reach well in time for the weekly meeting of the Loan Committee.

If the loan is sanctioned, the cheques/demand drafts are sent from HO to the credit officer who hands it over to the groups and gets the necessary documentation completed. The objective of documentation is to establish that loans are disbursed on certain terms; it is not done with an objective of protecting an officer's position if the case went to court for default. The loan cheques are post dated to cut down to the minimum the interest on transit time. The loan disbursement is usually completed within ten days to a fortnight of the initial assessment by the credit officer.

Keeping Products and Repayments Simple

"The loans were usually in round figures. The terms of the loans were fixed in a manner that the instalments were easy to understand. All repayments are through post-dated cheques. However, the contact with the SHGs has to be regular – therefore only two post-dated cheques are taken. Every time a cheque is banked by Sanghamithra, the SHG is informed to ensure that there is sufficient balance. While this ensures regular contact, it gives flexibility to Sanghamithra to use the cheque on the due date. The principle was to devise a product that could be rolled out fast and could be easily understood."

(M.S.Sriram – Building Bridges between the Poor and the Banking System)

The system adopted for repayment of loans is as follows: The credit officer collects post-dated cheques from the SAGs while disbursing the loan amounts and thereafter he/she ensures that two post-dated cheques are always with SRFS. The cheques are kept with the Credit Officers except in areas covered by the Cauvery Grameena Bank with which SRFS has collection arrangements. Cheques of other Banks are presented by the Credit Officer on the 15th of every month. The due date for repayment is the 30th of every month with a grace period of 7 days. The entire process takes into consideration the convenience of the borrowers. The transaction cost to the borrower in getting a loan is kept to be minimum and the delivery of loans is at the doorstep of the SAG during a scheduled meeting.

SRFS has developed a Manual of Operations which gives detailed guidelines related to all financial transactions as well as personnel policies.

A comparison of the policies and procedures governing loans from Banks and from Sanghamithra to SAGs is presented in the following table taken from the Impact Assessment by Ms. Girija Srinivasan (September 2003).

Aspect	*Banks*	*Sanghamithra*
Savings to credit ratio	*Ranges between 1:1 to 1:2 usually*	*Sanghamithra sanctions loans on the basis of savings and loan management capacity.*

Aspect	Banks	Sanghamithra
		Savings to loan ratio tends to be higher than what the banks are used to at 1:4 to 1:5 in well functioning groups.
Loan term	Ranges between 6 months to 36 months. Many branches sanction loan for 36 months. They don't sanction a second loan till the first loan is repaid and they don't allow pre payment of the existing loan also.	Initial two loans are for 10 months. Thereafter depending on the loan size it could be 20 months. Prepayments are possible to avail of larger loan.
Rate of interest	Varies from bank to bank – 9 to 13 percent.	The rate of interest is 12 percent.
Service charge	Depends on the bank – can vary from 5 to 1 percent of the loan amount.	2 percent of the loan amount charged up front.
Loan sanction time	Varies on the sanctioning powers of the branch manager. If the loan amount is within the powers of the manager, then within three to four days. Other wise it can be upto one to one and half months. Many branches don't allow the groups to lodge an official application; they are made to wait for seven to eight months some times. Thus the actual loan sanction time from expression of interest can be very long.	Within ten days of loan application and usually within one month of expression of interest to take a loan. branch
Collateral	Branch managers adopt a variety of practices to take collateral in terms of deposits of the groups.	No collateral
Maximum loan size	Around Rs. 75000 to Rs. 1 lakh even for older groups since the branches are	The maximum loan size is Rs. 3 lakhs so far.

Aspect	***Banks***	***Sanghamithra***
		not comfortable to lend larger collateral free advances to the groups.
Follow up	*Usually desk based monitoring.*	*Every two months visit to the groups is made to collect post-dated cheques.*
Penalty for non repayment	*Nil.*	*Rs.100 for each bounced cheque.*
Repeat loans	*Not sure.*	*Repeat loans ensured.*

6.2. Sanghamithra's Operational Relations with Banks:

Sanghamithra has no choice but to work through the Banking system. The bank charges added considerably to the transaction costs and the delay in fund transfers severely affected the working schedules of the SAGs. Sanghamithra therefore began negotiating with banks to offer at par discounting facility in respect of the loan cheques issued by Sanghamithra to the groups as well as immediate transfer of funds. The Regional Rural Banks were approached for these facilities because they have a wide network of branches in the districts, as well as a large number of SAG accounts.

Three RRBs (The Cauvery Grameena Bank and Chitradurga Grameena Bank in Karnataka and the Adhiyaman Grameena Bank in Tamil Nadu) agreed to offer the at par facility waiving commission and discounting charges as well as to transfer funds immediately to the SAGs. Agreements to this effect were entered into with all three Banks. Accordingly, Sanghamithra opened an account in the main branch of the respective bank where it maintains adequate balances and issues cheques (drawn on the main branch) to the self help groups. A list of the SAGs which have been sanctioned loans and the names of the branches where they have accounts is given to the bank at the time of issuing of the cheques. The at par facility ensures that the accounts of the groups are credited with the cheques' proceeds without commission or discounting charges; the postal charges, however are collected. It also ensures that the SAGs' account is credited within a day of the deposit by Sanghamithra in the main branch. Thus the transaction time and the cost to the borrowers are reduced significantly. To illustrate: the normal commission for a cheque of Rs one lakh is Rs 150; the discount charge is even higher and differs from Bank to Bank, but it averages Rs 400. These amounts are saved. Besides the SAGs would have to pay interest on the loan for the period of 12 to 15 days which is the average time it takes for collection. The interest for this period works out to Rs 400-Rs 500; this too is saved. The savings resulting from the availability of funds immediately so that SAG members can borrow to meet urgent needs, also has to be factored in.

The collection of loan instalments is through cheques. There is no handling of cash at any point of transaction. Credit officers collect the post dated cheques in advance ¯ at least two cheques are with Sanghamithra towards loan instalments at any point of time ¯ and present them to the branch where the groups have accounts, on the 15th of every month. The groups are aware that they have to ensure enough cash balance by the 15th or else they pay a penalty of Rs.100 for each cheque bouncing. This system has ensured that the risk of cash transactions for the MFI is nil; on-time repayment of loan instalments is also very high. However, there have been cases where the Banks have delayed in cashing the repayment cheques received from the SAGs; this results in inadequate funds in the SAG accounts to honour the cheques presented by Sanghamithra on the 15th of every month.

As the Banks began to realise that the SAGs were opting to borrow from Sanghamithra and that recoveries were prompt, several of the Branch Managers began to exert pressure to capture the "market". The agreements with two RRBs (the Cauvery Grameena Bank, Mysore and the Adhiyamman Grameena Bank, Dharmapuri) have lapsed, and the Banks refused to renew them. They are now demanding full charges - namely commission, discounting and postal – in order to credit the loan amount to the SAG within a day. If the SAG decides not to pay the discounting charges, then the cheques take the normal 13-15 days for collection. There are also several cases where the Banks have refused to provide chequebooks to the SAGs. The Chitradurga Grameena Bank Officers complained that the workload in their main branch increased significantly when the cheques of the groups were presented for collection. They asked Sanghamithra staff to post ledger entries in their books for all the cheques to be sent for collection. In response, the Credit officer of Sanghamithra spends two to three days with the main branch posting the entries for collection and attending to other transactions.

As a result of these pressures the Banks have increased their lending portfolio to the SAGs, but Sanghamithra's has decreased. Sanghamithra's management does not consider this a set back; in fact it is precisely what was intended. The main concern is to ensure that the SAGs have access to credit easily, quickly and transparently rather than to promote the market driven growth of Sanghamithra which can lead to unfair practices arising from aggressive competition in a particular area. In any case, Sanghamithra has the flexibility and the commitment to move to areas which are neglected by the Banks.

Whether the Banks will continue this aggressive approach is uncertain. Much will depend on the pressures to liberalise and on the increasing concern to earn profits as well on the number of SAGs within the Bank's service area. Bank Chairmen are no longer focusing on performance in the SHG Bank Linkage Programme; they are focusing on the bottom line. This in turn will demand a shift to larger loans than what the SAGs are accessing. The increase in the number of SAGs also provides space for Sanghamithra since the Bank branches are generally not too comfortable to extend loans to a large number of SAGs. Finally Banks are reluctant to extend loans over Rs 1-1.5 lakhs while many SAGs in the third round of loans require much more, which Sanghamithra is ready to offer.

Sanghamithra opens its account in a Bank branch when around 30 groups in the vicinity are to be financed from that branch. To cope with some of the obstacles mentioned above, Sanghamithra is also opening accounts in areas where local cheque clearing is possible so that the groups in the vicinity can be financed irrespective of which branch they keep their accounts with. Thus the number of bank accounts of Sanghamithra kept with various branches has increased to 59 (March 31, 2004). This is beneficial to the groups since they do not have to pay for collection of cheques.

However, with this increase in the number of Bank accounts, it is necessary for Sanghamithra staff to manage cash in each of the branches so that idle funds are kept to the minimum.

6.3. Impact On The Banking System

One of the major objectives of Sanghamithra is to demonstrate to the Banks that lending to SAGs is good business. However, Banks are shifting priorities and "better" business is increasingly attracting the bankers' attention. Several Bankers find that the intensity of transactions with SAG members is far higher than what the margins justify. SAGs members also belong to a different class of clients than what they are accustomed to relating with; they are poor and not viewed as potential clients for large loans. Several Branches are therefore restricting SAG transactions to one or two days a week only. There are other structural obstacles as well in the Banking system which will make it difficult to pursue aggressively the SHG Bank Linkage Programme in the long term. Some of these obstacles are identified by M.S.Sriram below.

> *Is it possible to understand the reluctance of the banks to take on the task of lending to SHGs? After all Sanghamithra has demonstrated that the portfolio is attractive, has excellent repayment rates and is cost effective. In fact the banks may be more efficient in costs because they do not have overheads of the channel; they own the channel.*
>
> *The reason for the banks not taking the SHG portfolio in a manner similar to the housing portfolio is to be traced to the nature of physical activity involved. The banks are used to operating from counters – the activity is centralised. This is so with good reason – banking involves handling of large amounts of cash on a day-to-day basis. This needs security and is to be done in a place with adequate infrastructure. The micro finance models, including the SHG models are decentralised – they reach out to the clients in their setting. This change is a major paradigm shift for the banks. Even if one gets attitudinal changes in the banks, it might not be sufficient because adapting to the methods of micro finance means getting out of the counter. Banks having a diverse portfolio may not afford this change.*
>
> *The documentation and loaning procedures followed by Sanghamithra cannot be readily adapted by banks as they are bound by larger guidelines. There would be need for a general exemption for dealing with micro finance clients for banks to adapt to the types of documentation of Sanghamithra.*
>
> *The staff of Sanghamithra cost much less than the average cost of bank personnel. This is a reality one has to live with. The only way the bankers can address the issue of costs is by outsourcing micro finance activity.*
>
> *Therefore, even though the portfolio looks attractive, it involves a major shift in the operating procedures of the banks. The banks may be unwilling to make the investment in the internal re-orientation. Since micro finance ultimately is a small part of the bank portfolio, it does not make sense for the bankers to make changes in the procedures. The bank staff gets transferred and move from branch to branch and division to division. So the procedures should therefore be easy to adapt and replicated mechanically across a large*

number of staff members. Unfortunately, the procedures of micro finance are so unique that it is difficult to spread it across all staff members. Therefore, we find that the success of SHG linkage programme in a given bank is person dependent; not system dependent. Till we can convert the activity to be system dependent, it is difficult to scale up, irrespective of the attractiveness of the portfolio.

(M.S.Sriram – Building Bridges between the Poor and the Banking System)

There are indications already that this analysis is largely correct and that the internal pressures are having an impact on lending to the SAGs in some parts of the country which are growing at a faster rate and where other opportunities for investment are emerging. However, given the present fall in interest rates for loans to the private sector and individuals, it is quite possible that rural lending will end up cross-subsidising loans in the urban market. This is a trend which may exert some pressure on Banks to promote, with a degree of aggression, the SHG-Bank Linkage Programme at least in some areas where other opportunities for larger investments are not emerging.

It is however, evident that the Banks will continue to view Sanghamithra's operations as competitive in the sense that Sanghamithra is entering their territory or service area where they were comfortable with the monopoly they hitherto enjoyed. Sanghamithra's management however, intends to keep the pressure on Banks to perform so that the well functioning SAGs can continue to access loans quickly, easily and transparently. This requires that the Banks continuously revise their policies and practices and condition their staff to ensure that the links with the SAGs flourish. If the bankers relax and fall back into their old ways, as has happened in some areas, Sanghamithra enters the area once again. A brief analysis of whether this strategy worked during the first three years of Sanghamithra's operations is given below. What will happen in the future, given the change in the new Government's policies, is difficult to predict at this point of time (June 2004); however, Sanghamithra's management will review the situation as it emerges and decide on future strategy.

6.4. Did This Strategy Work? – Three Case Studies

The impact on the Banks (and bankers) was included in the terms of reference given to Ms. Girija Srinivasan who did the Impact Assessment of Sanghamithra. Her report which attempts to answer this query was published in July 2003. The hypotheses tested were the following:

- Sanghamithra has brought about changes in banker's attitudes towards financing self- help groups.
- Sanghamithra's working has influenced changes in banker's role in the capacity building of groups.
- The nature of Sanghamithra's relationships with competitors is for the benefit of clients.

Ms.Srinivasan appreciated the problems involved to attribute any impact entirely to Sanghamithra; however she decided to adopt the following methodology:

Key person interviews were held with various stakeholders. The focus of the interviews was to ascertain – *what is it that the banks do additionally and differently that was not done earlier and what are the reasons for the changes*. The changes as articulated by the banks – Chairmen of RRBs, branch managers of RRBs and commercial banks – were considered and given maximum weightage. The results were validated by triangulating and reconfirming with other stakeholders such as District Development Managers of NABARD, NGOs and SAGs. Some basic data maintained at Myrada and Sanghamithra regarding lending by banks and Sanghamithra was also used. There are limitations to any methodology adopted; what is important is that the methodology used is explained up front so that the reader is able to assess for herself/himself the degree of credibility that the conclusions enjoy.

The following quote is taken from the Impact Assessment Report by Ms.Girija Srinivasan (September 2003); it is long, but this writer decided that it would be better to quote it in full rather than to edit it and add his own comments. Attaching it as the annexure was an option, but given the experience that annexures are rarely referred to by the average reader, it was decided to include it in the text. This quote covers three RRBs which work in areas where Sanghamithra and Myrada have major programmes. They are 1) the Cauvery Grameena Bank (in South Karnataka) which was involved in the pilot project described above where the Bank took up the role of an SAG Promoting Institution in the late nineties. This Bank was slow to take up the SHG Bank Linkage Programme in the early to mid 90s even though there were hundreds of eligible SAGs in its service area; however progress has been significant since the late 90s; 2) the Chitradurga Grameena Bank (in Central Karnataka) which at the time of the report had an enterprising Chairman, Mr.Narasa Reddy; this took the "competition" with Sanghamithra to a new level which resulted not in conflict but in expansion of the SHG-Bank Linkage programme and to a focus in neglected areas –this is explained in more detail below, and 3) the Adhiyaman Grama Bank in Dharmapuri District, Tamil

Nadu where the progress in the SAG –Bank linkage Programme was slow till 2000 even though MYRADA had promoted over one thousand SAGs of which at least 900 were eligible for a loan; during the past three years however, the progress has been remarkable.

6.4.1. CASE STUDY - CAUVERY GRAMEENA BANK

To quote from the Impact Assessment:

> *The Cauvery Grameena Bank (CGB) is working in three districts of Karnataka Viz., Mysore, Chamarajanagar and Hassan districts. As on 31 March, 2003 as many as 3463 groups had savings account with CGB in Mysore district out of which 1483 have been credit linked. During the year Rs. 472 lakhs have been lent to 1612 groups and thus the average loan size works out to Rs. 29,000. Almost all the branches are participating in the SHG linkage programme.*
>
> *The bank has been participating in SHG linkage banking since the year 1992. It was also a forerunner in experimenting with the concept of branches acting as Self-Help Promoting Institutions (SHPIs). The bank has been winning the state level award for best linkages for three years in a row starting from 1999–2000. Though the bank has been a forerunner in SHG linkages in the state, the bank especially the branch managers, did not recognise that SHG lending was a good business proposition. The SHG linkage programme was seen as the interest of the Chairman and the SHG Promotion Cell Officials. Ever since Sanghamithra entered the fray, there is lot of change in the branch managers and even at senior management level, change has set in.*
>
> *There is greater awareness among the Senior management - area managers and General managers - of the bank that the competition for a profitable segment of the business has to be met. The need to efficiently organise the marketing campaign at the bank level in order to retain and expand the SHG portfolio has been felt. This has resulted in the branch managers being asked to lend more to the self-help groups. ("If Sanghamithra can lend to the groups which have savings account with us, why can't we?").*
>
> *The savings to Credit ratio which was hovering around 1:1 to 1:2 even in the case of older groups is being hiked to increase the loan amount to the groups. As per a senior official of the bank "If SRFS offers Rs.1 lakh in the third loan cycle for a good group, the branch manager is forced to give at least Rs. 75,000 whereas earlier it would have been not more than Rs.50,000".*
>
> *The transaction time is being brought down with the loan applications being sanctioned quickly.*
>
> *The bank is stepping up the client contact level to ensure that the groups that are presently customers of Sanghamithra are persuaded to take the next loan from the bank. Some of the branch managers have identified that Sanghamithra visits the group only two to three times after the loan disbursement, and they*

plan to meet the groups at least once in a month to market their loans and woo the customers back. At Head Office level credit linkage camps and motivation camps have been initiated for the self help groups in which a large number of clients are addressed and the bank's loan product for the groups is explained.

"The Chairman of the RRB has welcomed Sanghamithra's presence which is bringing in the necessary attitudinal change in the staff especially in the rural branches of the bank. According to him "RRB branches enjoyed a monopoly in the service area villages and the tendency of monopolistic behaviour was prevalent among the staff. This was to the detriment of the customer who didn't get the best of services. Sanghamithra's presence in only 25 percent of the branches has brought about a sea change not only in branch staff but also in the senior management of the bank who now consider SHG linkage programme as a worthy pursuit. Branch managers know that they have to be on their toes to ensure continuity of business. Sanghamithra's presence has brought about the much needed attitudinal change in many of the branch staff who have become more active and dynamic and also more compassionate to the needs of the poor. The rate of linkages has been higher ever since Sanghamithra came into the picture." Impact Assessment.

The Study continues:

In terms of hard numbers, Sanghamithra is operational along with Cauvery Grameena Bank in respect of 21 branches where as in respect of other branches either Sanghamithra or Cauvery Grameena Bank lend exclusively to the groups. The lending pattern by branches of CGB and Sanghamithra in respect of MYRADA groups for the past three years clearly demonstrates that in respect of some of the rural branches Cauvery Grameena bank is taking over the groups which were initially financed by Sanghamithra, as a result, the growth rate of the number of groups linked has been higher in the case of Cauvery Grameena Bank when compared to Sanghamithra.

However, there are some branches where Sanghamithra continues to have higher growth rate which are predominantly town or city branches of CGB. There is very little incentive for these branch managers to lend to self help groups where more lucrative business opportunities exist and the competition from other commercial bank branches for larger loans is severe. There are also some rural branches where the groups once establishing relation with Sanghamithra[1] *are not keen to take bank loan.*

One can conclude based on these very basic data that Sanghamithra is achieving its objective of bringing about increased linkages of self help groups with the banking system. However, final conclusions can be drawn only on systematic data maintained at the corporate level as to the number of groups being taken over by the banks, in which cycle of lending and why.

[1] During the field visit, Mellahalli village was visited which had 32 groups formed by MYRADA. The branch was half a kilometre away from the village and nearly 28 groups are financed by Sanghamithra. The banker is now approaching the groups for providing them loans but most of the groups are not keen to shift from Sanghamithra. There is a general fear to take bank loan among the villagers.

6.4.2. Case Study - Chitradurga Gramin Bank

To Quote from the Impact Assessment

Chitradurga Gramin Bank is working in Chitradurga and Davanagere districts of Karnataka state. All the branches are participating in the SHG linkage programme. Out of 5500 groups which maintain savings bank account with the RRB branches, 3248 have been cumulatively credit linked. During the year a total of 1413 have been credit linked with a bank loan of Rs.472 lakhs and the average loan size works out to Rs. 33,000.

Chitradurga Gramin bank has been involved in SHG lending for about ten years. The bank also took on the SHPI (SAG Promoting Institution) role and participated in the NABARD project where the bankers are playing the SHPI role. However, the bank was clearly lagging behind in both the linkage banking and in the role of SHPI. Even the targets being given to the bank under the lead bank scheme were not being met till the year 1999 - 2000.

The entry of Sanghamithra into the district has almost coincided with the taking over of the bank by a new Chairman who has made turning around of the ailing bank as the major goal. Under his stewardship, the branches and other staff have taken the competition head on. The Chairman candidly admits that the credit goes to Sanghamithra for building the pressure on the bank to lend to the groups. This shows in the statistics as well - 836 groups were credit linked cumulatively (in the past eight years) as on March 2000 –01 and the figures jumped to 1633 at the end of March 2001-02 registering a near 100 percent increase in the number of groups linked by the bank. From an in insignificant presence, the bank has secured second position in the state in terms of SHG linkages.

"The bank has responded to the competition in a variety of ways - some of them positive and a few them are outright negative pressure tactics".

The policy for linking self help groups has undergone a sea change with higher loan amounts being sanctioned as per the need and eligibility of the groups. Since Sanghamithra was sanctioning larger loans of more than a lakh, many of the branches also started to lend similar amounts. The average time for sanction of a loan which was one month was brought down and in some of the branches where the competition was severe it came down to 6 days. Adequate sanctioning powers were given to area managers and branch managers. Large loans of Rs. 1.5 lakhs still take about a month to get sanctioned and disbursed. The bank developed its own rating norms. The bank has dispensed with the letter of introduction from the NGO for the second and subsequent loans. The loan term which was 36 months has been changed – the first loan is for 6 months, second loan 9 to 12 months and the third loan is 1 to 2 years. The major change has been in the attitude of the branch managers who now consider that SHG linkage is good business. They have increased the client contacts, commenced participating in important events *of the SAGs like SHG anniversary day. Chairman is encouraging the groups to get in touch with Head Office of the bank directly in case of need. "They need to be given due attention" he says.*

The not so positive responses are - a few of the branch managers studied Sanghamithra's system of operating through the banking system and using the negotiable instruments especially the cheque system for collection of loan instalments. To inconvenience Sanghamithra, they have refused to issue cheque books to the groups forcing them to purchase demand draft for remitting the loan instalment. In a few branches the branch managers refused to honour the loan cheques issued by Sanghamithra. This has increased the transaction cost and time of the groups. Some of the branch managers also indulge in other subtle ways of harassing such as not issuing Demand Draft in time and also singling out these groups and delaying their normal banking transactions. These have made the groups and the promoters wary of Sanghamithra. They preferred linking with the banks. A few branch managers also warned that groups which took loans from Sanghamithra would not be provided loans under SGSY. Some groups preferred to take even a smaller loan provided by the branch though Sanghamithra was issuing a much larger loan. All this has resulted in decrease in lending portfolio of Sanghamithra in the district.

– Impact Assessment.

"Discussions with DDM, NABARD, and NGO members of the SPIN network (a network of NGOs and development institutions in Chitradurga District promoted by MYRADA) reveal that there is a sea change in the attitude and practices in the branch managers and the very threat that Sanghamithra can any time come in to lend to the groups is making them keep up the good practices. The momentum which was built up in the past two years for linking self help groups is stabilising and in some branches where more than 100 groups are credit linked there is a realisation that SRFS will not be a serious threat to their business and both Sanghamithra and the branch can co exist." Impact Assessment

The NGOs that have formed the groups are very happy with the competition SRFS has brought about. The positive feature is that the NGO's time and cost in forging linkages with the banks especially Chitradurga Gramin bank has come down. Opening of savings bank accounts with the branches has become a routine affair instead of the long drawn process it used to be. RRB has changed its policy, made the loan accessing less cumbersome and more user friendly. The bank is now keen to sanction upto Rs. 5 lakhs for a group which has a good repayment record in the past three loan cycles. Some of the old practices such as insisting on savings as collateral has come down. A few of the branch managers are yet to change some of the bad practices such as making groups wait for a long time before allowing them to put in a loan application, forcing groups to keep a part of the loan amount as fixed deposit etc.,

Since some of the NGOs are working with SRFS as well as the banks they could bring out the relative strengths and weaknesses. They point out that even now the bank managers don't actively canvass for loan applications: they sanction *when groups pursue them whereas Sanghamithra is very pro active. Similarly they have to follow up on the bank loans to ensure that the loans are repaid in time whereas in the groups where Sanghamithra has financed, Sanghamithra follows up and hence the NGO's work load is limited. They find that Sanghamithra's assessment system ensures only good groups get linked which gives the promoting NGO also a level of comfort.*

Chitradurga Gramin Bank invests in the capacity building of the self help groups especially those formed under the Government of Karnataka programme. This is to ensure the quality of the client base. They have also started financing watershed development associations even those from where the MYRADA has withdrawn. MYRADA feels that this confidence in people's institutions has come about due to the success they have tasted in lending to the SAGs.

Thus the Chitradurga Gramin bank has benefited from the competition of Sanghamithra as well as the stewardship of the Chairman. Nearly 25 percent of the loan portfolio of the bank is of lending to SAGs. As far as Sanghamithra's objective of making banks to lend to SAGs, it has been achieved in Chitradurga. SRFS which was financing 350 rural groups as on 2001, is now financing only 150 rural groups and most of them are new loan accounts. The groups earlier linked to SRFS are now linked with the bank. Similarly, SRFS was lending along with 40 branches of the RRB in 2001 and it has come down to 21 branches in 2003. This affects Sanghamithra's business and this is discussed later in this section. Though the interest of the bank in lending to SAGs is very visible, the long term impact can be measured the bank's continued interest to cater to the self help groups even after the change of guard at the top level.

6.4.3. CASE STUDY - ADHIYAMMAN GRAMA BANK

To quote from the Impact Assessment.

Adhiyamman Grama bank is functioning in Dharmapuri district with 25 branches. All of them are participating in the SHG linkage programme. As on 31 March 2003, as many as 2836 SAGs hold savings bank account with the branches out of which 1202 (nearly 45 percent are credit linked). The average loan size works out to Rs.95,000 per SHG during the year 2002 - 03. In ten branches the groups are formed by the branch managers; the concept of Bank acting as SHPI is being implemented in these branches. Nearly 39 out of the 47 officers in the bank are well trained in SHG concept.

To meet the competition posed by Sanghamithra, the bank brought about policy changes in SHG lending. It increased the average size of loan to match that of Sanghamithra. The discretionary sanctioning powers of the branch managers have been increased from Rs.20,000 to Rs.50,000. The transaction time for the groups to get a loan sanctioned has been brought down to a range of 4 to 7 days in respect of those cases where the branch managers need to refer the cases to the Head office. The share of SHG loan portfolio of the bank is 22 percent of the total loan portfolio.

Regarding working with Sanghamithra, Head office officials opine that the bank has funds which they can deploy in SHG lending. In some of the branches the groups which were linked to banks have been delinked by MYRADA to promote SRFS is the district. However, the branches are quite willing to lend along with SRFS in their service area. The major reason being the average number of groups per branch (113) is quite high with some branches having accounts of more than 250 groups. There is a feeling at the branch level that the branch may not able to cater to the needs of all the self help groups in its area of operation.

According to the staff of MYRADA (Sanghamithra works only with MYRADA in Dharmapuri), the banks are now alert to the competition. Sanghamithra demonstrated that groups are able to absorb and repay larger loans of Rs. 1 lakh and this proved to be an eye opener for AGB and Indian bank and consequently they have increased the loan size. This in turn has enabled the group members to take up larger enterprises. A few branches of the AGB and Indian bank are now lending Rs. 1 lakh to new groups and since the promoting NGO is not keen to recommend such large amounts, the banks are lending without the recommendation of NGO. Regarding continued presence of Sanghamithra in the district, if (as per the suggestion of Adhiyamman Grama Bank) Sanghamithra withdraws from the district the bankers would slacken the lending.

Thus Sanghamithra's presence in the district is acting as a catalyst for the bank branches to be responsive to the needs of the self help groups. – Impact Assessment.

The overall conclusions of Girija Srinivasan's Impact Assessment Report as regards the impact of Sanghamithra's operations on the Banking System coincide with the conclusions of M.S. Sriram's study. The conclusions of Srinivasan's report are given below:

1) *While the response from the top management has been with policy level initiatives, the response from branch staff depends on their motivation, their comfort in lending to self help groups and how they perceive the costs and benefits of lending to this segment. Hence, much of the action is branch centric. While some branch staff are convinced of SAGs as viable business and try to retain and expand the number of groups, there are still many who find that dealing with SAGs involves more transaction time. Thus where there are opportunities for lending to other more lucrative businesses the branch managers give preference to such customers.*

2) *The competition is branch specific and directly proportional to the number of credit worthy groups in the command area. If the number of groups are many say more than 200, the branch managers do not mind Sanghamithra lending to the groups since they realise that they can't cater to so many groups and they may also avoid over exposure to one segment. However, if the number of groups is only 25 to*

50, there is very severe competition which results some [illegible] withdrawing from the groups under the branch.

3) *The response of the bank depends to a large extent on the measures adopted by the Chairman and senior management of the bank. The long term impact can be measured after a change of senior management especially the Chairman. The long term impact of Sanghamithra's competition would be measured by whether the branch managers continue to lend to the self help groups with the same vigour and tempo.*

4) *Bank specific issues like merger of branches, VRS etc, also affect the ability and interest of the branch manager to link groups. For example, two branches of Cauvery Grameena Bank – a rural and town branch - have been merged and the staff apparently find it difficult to cater to the large business. Since at present the town branch is capable of attracting larger customers, the emphasis on lending to self help groups is less. VRS in commercial bank branches has reduced the available number of staff in many of the branches, where as the computerisation of operations has not been fast enough. The commercial bank branches have been slow to take up the challenge of competing with Sanghamithra.*

5) *Similarly the competition is expected to be severe where good groups are functioning. All the branch managers interviewed are keen to link* MYRADA *groups and are not equally enthusiastic about the other SHPI promoted groups.*

To conclude, the impact of Sanghamithra has been articulated by the banks themselves which in fact shows how Sanghamithra even with the small size of operations[2] is seen as a serious competitor to their business. There have been other MFIs and wholesalers who are lending to the self help groups but the banks have not perceived them as serious competition. This has been primarily because the competition has not been localised[3].

Sanghamithra has been able to evoke a very strong response primarily because the competition is localised[4]. Sanghamithra involves the banking system in each of the transactions and hence they are able to see the business potential and the competition.

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[2] During the year 2002 – 2003, in Chitradurga district 1688 groups have been credit linked out of which Chitradurga Grameena bank lent to 1100 groups (65 percent) where as Sanghamithra has lent to about 140 groups (9 percent). Similarly, Adhiyaman Grama bank has lent to 1094 groups (25 percent) whereas the figures for Sanghamithra is 210 (5 percent).

[3] For example, FWWB in Ahmedabad lending to the self help groups is not considered as a serious threat. Similarly, some NGOs/ federations lending to the self help groups is also not viewed as a threat since the NGO is seen as a financial intermediary lending to their own groups (territorial) and many of these organisations borrow money from the branch/ bank to lend to the groups thus becoming their customers. Sanghamithra doesn't have any such territorial operations, cuts across different geographical areas and SHPIs and thus is on equal footing to banks in providing financial services to the groups.

[4] In a static perspective, national level operators may enjoy advantages of scale; but the real world is dominated by dynamic conditions, and here it is direct competition that impels firms to work for increases in productivity and innovation; here, anonymous competition often turns into concrete rivalries and feuds, in particular when competitors are spatially concentrated. "*The more localised the rivalry, the more intense. And the more intense, the better.*" (Porter 1990, 83)

They lend to groups through a bank branch so that the branch manager is able to perceive and feel the competition. Even at the Head Office of RRB the competition is felt because the bank is able to appreciate the fact that Sanghamithra can quickly scale up operations being mobile and lean and in a similar way they can move out quickly of an area if the banks have shown willingness to lend. This mobility and flexibility proves to be the motivating factor to many of the branch managers to adopt good practices since there is a threat that Sanghamithra can come in to lend to the groups, if the groups desire.

> "The competition in the short term of two to three years has evoked strong responses - many positive and some negative. Each branch manager is developing his/ her own competition strategy within the overall policy framework. While some use positive methods of wooing a customer, a few use strong-arm tactics including denial of normal banking services to the groups that borrow from Sanghamithra ignoring the fact this is illegal and unethical. However, it is to the credit of Sanghamithra that none of the banks have pointed to any undesirable or unfair practice by Sanghamithra. The only concerns have been that if Sanghamithra lends to the groups, then the earlier bank loans of the spouses of the group members may not be repaid to the banks. Impact Assessment

"As far as the future relationship with the competitors is concerned, it is clear that the senior management of two of the RRBs, which has the wide rural branch network in the districts, feel that since banks are now lending to the self help groups, Sanghamithra is not needed. However, this may not be in the interest of the bank or the groups in the long run. The attitudinal changes in the branch managers and the senior officers (area managers and the general managers) have been possible only when the competition has been localised. The lending to SHG had not been internalised as a Regional Rural Bank's major programme by many branch managers and the senior officials in spite of the efforts of the Chairman of the bank, NABARD and lead bank. The entry of Sanghamithra has spurred them into action. It is really commendable that a relatively small organisation with a small presence in the district has been able to generate desired responses from banks through direct competition. The direct competition should remain so that the groups continue to have a choice and the banks have a benchmark for quality of customer service. Existence of competition would ensure that the bankers don't slip back into the old ways bred by near monopoly over the market." – Impact Assessment.

Commercial banks – *A brief reference to CBs needs to be made since they have also played a major role in the SHG-Bank Linkage Programme. SAGs formed by* MYRADA *have received loans amounting to Rs 111,602,313/- from Public Sector CBs and Rs 15,635,750/- from Private Banks. Among the Public Sector Banks, The Indian Bank(Rs 38 million), Canara Bank (Rs 25 million) and State bank of India ((Rs 13 million) have been the leaders and among the Private Banks the Vysya Bank (Rs 9 million) is ahead of the others. This is a significant contribution to the programme. However, there are indications of a declining trend in the investment of the CBs in this sector. Some of them like the*

Canara Bank, Indian Bank and Corporation Bank are also opening channels with Sanghamithra for bulk lending. Sanghamithra has already entered into an agreement with the Canara Bank.

Most of the Commercial Bank branches were slow in responding to the challenge that Sanghamithra posed to their business in the initial two years of its operations for a variety of reasons. Some of them are listed here. The voluntary retirement scheme left many branches with inadequate manpower. Banks were asked by Government to undertake a variety of services. Self help group lending has not been acknowledged as a core business proposition by many of these branches. These branches were passive watchers when the initial size of the loans by Sanghamithra was small. When Sanghamithra's loan size increased to more than a Rs.1 lakh with regular repayments, the branch managers started appreciating that the groups are credit worthy. They began trying to woo the groups with prompt services and large subsidised loan schemes of Government. The attitudinal change in the branch managers has been noticed and articulated by the groups. One of the groups has commented, "earlier the branch manager was insisting that the loans of our husbands had to be repaid before we could access the loans. Now that we are taking Rs. 2.5 lakhs from Sanghamithra and repaying promptly, the branch manager has promised us SGSY loans of Rs. 5 lakhs."

CHAPTER 7

The Future

Sanghamithra Rural Financial Services (SRFS's) cumulative disbursements up to March 31, 2004 amount to Rs.16.15 crores (Rs 161.5 million); the loan outstanding as on March 31, 2004 is Rs.7.25 crores (Rs.72.5 million). This is reasonably good progress within 4 years, given all the unexpected obstacles encountered, especially during the past two years mentioned below which impinged on the MFI's growth.

What does the future hold for SRFS? To begin with there is the need for liquidity. How will this be met? There are certain trends which are clear enough to factor into future plans. The Management's plans for 2003-2005 included a follow up project for re-deployable funds which was sent to the Canadian International Development Agency for support; it was scheduled to start in 2003 but it did not materialise. Fortunately by early 2004 an increasing willingness was expressed by Commercial Banks to lend in bulk to SRFS on terms and conditions which SRFS is willing to accept. There is evidence that this trend will translate into adequate liquidity for SRFS's lending operations. For example, Canara Bank has lowered its interest rates from 7.75% to 7% as of April 2004 and converted its term loan into a cash credit account. This will provide Sanghamithra with added flexibility as well as liquidity at reduced cost.

Other Commercial Banks especially the Indian Bank and Corporation Bank are also willing to lend at competitive rates; however the major stumbling block is the legal requirement from Banks for a guarantee. In the case of Canara bank, the loan to Sanghamithra is against receivables /book debts. This closes the door to approach other Banks. The initial grant for on lending which CIDA provided has increased to Rs.3.29 crores (Rs.32.9 million) as on March 31, 2004. This amount is taken as the company's own capital or margin money by the Canara Bank. Consequently unless other Banks are willing to lend by clean or unsecured draft, Sanghamithra will have to depend only on Canara Bank for its liquidity needs. Fortunately the Canara Bank is willing to meet the requirements of Sanghamithra in toto provided its performance continues to be good. Another suggestion is to borrow from a particular Bank with the understanding that loans will be advanced in an exclusive zone, so that the receivables are clearly demarcated. However, the Canara Bank will have to agree to this.

Will SRFS continue to expand its operations in breadth and depth? It will; but the pace of its progress will depend to a significant extent on the reaction of the RRBs. The problem of having to work through banking channels, especially through the

RRBs will continue to cause tensions, at least in the short term, and to have an impact on Sanghamithra's lending portfolio which needs to be sufficiently large in an area so that its office is self supporting. How long RRBs will continue to promote the SHG-Bank Linkage programme aggressively, however, is an open question. Sanghamithra's Management thinks that with the increasing pressure in RRBs to boost the bottom line, with the growing rationalisation of branches, and with the growth in the number of SAGs in the Branch service area beyond a number that the Branch can cope with, there will be space for Sanghamithra to function together with the RRB Branch and to maintain a level of competition which ensures that both financial institutions continue to provide a high quality of service to the customers. Hence Sanghamithra will focus on areas where there is a large number of SAGs and in areas which are neglected by the Banks. This may lead to a District or even to a Taluka approach as part of its strategy. Further Sanghamithra is willing to offer larger loans than most Banks are prepared to do, especially in the third round of lending, when SAGs require and can manage loans of Rs.3 lakh and above. This offers another window for future investment. There is yet another potential group that Sanghamithra is considering, namely, the Watershed Management Associations which, in MYRADA's projects, function like SAGs. They save and lend for land treatment on private lands and for agricultural related activities.

Recruiting and keeping staff is not a major problem, but funds required for training new staff which covers a period of six months at least, are not easy to mobilise. Currently the costs are being met from the surplus that Sanghamithra generates, but this cuts down on the re-deployable funds available for lending. The surplus also needs to meet the cost of providing new infrastructure. The initial proposal to CIDA which was accepted in 2000, served to launch Sanghamithra and to achieve the project's objectives much before the planned project period. As a result, CIDA was willing to support a follow up project for about Rs.3.5 crores (Rs.35 million) which would meet with the requirement of expansion and training of newly recruited staff as well as with the need for low cost funds which would be repaid to a financial institution which MYRADA proposed to set up for promoting new Sanghamithras. However, this follow up project did not materialise. As a result, the spread of SRFS into new areas has been slower than anticipated. A proposal to the Sir Dorabji Tata Trust for a sum of Rs.82 lakhs (Rs.8.2 million) to partially offset this shortfall is under consideration.

Sanghamithra does not intend to grow into a financial super market. It has set its sights to achieve a loan portfolio of around Rs.25 crores with its own capital of Rs.9 crores. With a loan portfolio of over Rs.7 crores and its own capital of Rs.3.29 crores as on March 2004, it has covered about one third the distance in four years, but hopes to speed up and achieve its target within the next four years. The next few years will also see efforts to start new MFIs along the model of Sanghamithra in other parts of the State and country. There are already several requests followed up by visits of qualified and committed NGOs who want to replicate the Sanghamithra model. The management has offered all support to these interested parties including software, staff training and initial visits to monitor progress.

"How is the Sanghamithra model useful to us for large scale replication of micro finance in India" asks M.S.Sriram; he attempts to provide an answer:

> *"This question helps us to focus and decide if the strengths were specific to the promoters of Sanghamithra or if they were system driven. Conceptually, this model followed logic. It did not believe in replicating structures, used existing structures and encouraged banks to actively participate in building linkages with the poor. It acted as an intermediary demonstration model. Since it was not-for-profit, there was scope to plough back residual revenues for the development of new groups, expand and deepen the client base. However, this model was based on the assumption that NGOs would be interested in forming SHGs and linking them. Mr.Fernandez has explicitly stated that "formations of groups cannot pay for itself ... these interventions therefore will have to be provided by NGOs (in an internal note to the staff of* MYRADA*). One could therefore say that if NGOs are willing to bear the cost of investing in groups, the model should be able to run on its own steam. This also precludes the bank promoting SHGs under the assumption that the process of SHG formation and training is intensive if quality was to be achieved. There are arguments that the cost of SHG formation has to be paid by the bankers and it could be recovered in due course, but* MYRADA *did not believe so.*
>
> *The second issue is of intermediation by an institution like Sanghamithra. It is evident from their performance that there was space for an intermediary organisation that could pay for itself. The question of whether this should be membership based or externally induced is open. Possibly there is scope for a federal organisation of the SHGs to eventually operate in the place of Sanghamithra. That form is left to individual preferences, but it might be difficult for other promoters to get a tax-exempt, micro finance company to operate, since a part of whether certain objects of the entity are tenable as charitable activity or not, are tax exempt or not are subject to open interpretations. The precedence of Sanghamithra can be used by other organisations."*
>
> *(Building Bridges between the Poor and the Banking System"* M.S.Sriram *)*

Apart from the possibility of others replicating the Sanghamithra model, MYRADA supported by Sanghamithra Management, also intends to promote similar MFIs in the three Southern States of Karnataka, Tamil Nadu and Andhra Pradesh and to set up a Fund Management Company to co-ordinate and supervise these MFIs. A Senior Bank Officer who had availed of the Voluntary Retirement Scheme, with the qualities and skills required was identified; the preliminary steps to set up a Company were taken. The plan was to set up the Fund Management Company first, so that it could in turn set up other Sanghamithras in North and Central Karnataka; however given the set back the plan received due to the closing down of the Canadian Bilateral programme, the Fund Management Company may have to follow the setting up of other MFIs or hopefully, the two can progress together. In any case this delay has resulted in MYRADA having to continue to play a major role in supporting SRFS and in promoting new MFIs along the same model - which the Fund Management Company would have taken over and hopefully will within the next two years.

Why set up this Fund Management Company (FMC)? Myrada and SRFS Management believe that the functioning of any Financial Institution should be supervised regularly, apart from the audits required by statute. Monthly meetings should consider and assess progress and compliance as well as identify deviations or emerging weaknesses so that timely corrections can be made. Scheduled Banks have this practice. At present SRFS has not incorporated this practice in its management structure. Quarterly meetings of the Board are expected to fulfil this function. While these quarterly meetings may be adequate at this time, when the Board Members are in close touch with SRFS and the MFI is still small, they will not be adequate when the situation changes. Besides regular monitoring of particular geographical areas and of new initiatives, periodical compliance audits to assess whether SRFS is complying with the rules and procedures, are required. The reports generated will also serve as a basis for future plans. At present this role is fulfilled sporadically by outside Consultants. The Fund Management Company is expected to take over this role of regular supervision.

There are also other roles that it will have to be taken on by the FMC; for example, initiating contacts with financial institutions in India and abroad to get the best terms possible for credit, balancing the credit needs of the several MFIs so that idle funds are kept to the minimum, holding repayments from the various MFIs which the original donor provided as loans returnable to an Indian institution - the last grant from CIDA which did not materialise, adopted this model; it was meant to be a loan to Sanghamithra returnable to the Fund Management Company for on lending to new Sanghamithras. The FMC would help the MFIs to introduce new and innovative products and mechanisms, to train staff and to network among the MFIs under its supervision as well as to foster wider networks with others.

Should SRFS morph into a full-fledged NBFC? The question is easily put, but the implications are enormous and as is customary there are two opinions. One group opines that SRFS has the entry level capital required to become an NBFC; why not go ahead? This would raise its profile, draw respect from the set of micro finance experts who tend to disparage a not-for profit MFI, allow it to mobilise credit at lower cost and improve its liquidity position; it would also bring SRFS under the close "watch" of regulatory institutions. The other group stresses that a NBFC would require a different structure and culture as well as a new type of staff – this would take time to put in place and would entail start up costs. This group also points out that, in spite of SRFS's achievements, there is a lack of adequate credibility, as it still has to prove itself; there is also a lack of confidence in its stability which is required to attract and keep deposits even from SAGs. The ever present threat of rumours, which, even if false, are easily floated, would have a negative impact; SRFS is too small and does not have other businesses to cope with the cash flow required in such eventualities. Further, the pressure on a For-profit institution like a NBFC to grow and to compete aggressively with other financial institutions would be a total reversal of SRFS's original mission to create conditions for the poor to access credit quickly, easily and transparently- no matter from which institution. The pressure to grow would also undermine its ability to move in an out of an area in response to changes in the Banks performance. This group also points out that the plan to set up several Sanghamithra's and a Fund Management Company would ensure that the service area of SRFS grows and that adequate control and monitoring is in place. The discussion will continue.

Since the inception in 2000, the annual interest on loans advanced by SRFS to SAGs in the rural area has remained at 12%; with additional service charges, it amounts to an effective interest rate of 14.23% This figure was arrived at based on the cost of credit which was expected to average around 3%, NPAs expected to be less than 2% and transactions costs estimated to be around 9%. The other major factor that determined this rate of interest was the prevailing rates of RRBs during 2000-2001 which averaged around 14% including service charges. SRFS was expected to be competitive by providing better services, by offering larger loans than the Banks were willing to advance and by adopting flexible policies in response to people's needs. The Bankers willingness to advance loans to SAGs was enhanced not only when they realised that the repayments were good –above 96%, but also because such loans were classified under the priority sector portfolio which enabled them to reach official targets and opened the way for expansion in urban areas. This sharpened the competition between Banks and SRFS during 2000 and 2001 onwards. However, with interest rates being comparable and with the better services that SRFS offered, the SAGs preferred to establish a relationship with SRFS.

From 2003,the situation began to change, particularly with reference to interest rates levied by the Banks which fell rapidly to 10% and in some cases even lower, while SRFS continued to remain as before. This had an impact on the number of clients that approached SRFS; several SAGs shifted to the Banks which also became more active in approaching the SAGs. However, the SAG members and SRFS soon realised that banks began to levy higher transaction costs, including higher commission and discounting charges; these costs differed among Banks and even among branches of the same bank and often between individual clients. Bankers began to restrict the days for SAG transactions, often to two in a week; several branches refused to issue cheque books to the SAGs, several delayed to credit the repayments from the SAGs to their bank accounts; in general their attitude towards and interactions with SAG members began to change for the worse. The comments of M.S.Sriram pointing to the reasons for this change are relevant here: "Even though the micro finance portfolio looks attractive for the Banks, it involves a major shift in operating procedures…the Banks may be unwilling to make the investment in internal re-orientation… since micro finance is a small part of the bank portfolio, it does not make sense for the bankers to make changes in the procedures…. The Bank staff get transferred, ... unfortunately the procedures of micro finance are so unique that it is difficult to spread it across all staff members. Therefore we find that the success of the SHG linkage programme in a given bank is person dependent, not system dependent", and further …"The bankers are used to operating from counters ……the SHG model is decentralised…; and he concludes, "the margin of profit is not proportionate to the time spent with the SHG members".[1] As a result, many SAGs returned to SRFS. The bottom line however is that the interest rates levied by Banks has fallen to 10% and below, while that of SRFS has remained at 12%. This difference is visible, unlike the transaction costs and is the first question that SRFS staff have to answer which leaves them at a disadvantage. Transactions — costs and relationships — where SRFS has a competitive edge – come later.

What of the future? The Reserve Bank of India has said that it will pursue an interest rate environment that is conducive to maintaining the momentum of growth and macro economic and price stability. The general consensus is that the fall in interest rates has bottomed out, even though there is ample liquidity in the system. There are also emerging signs, abroad and within, including industrial recovery that will tend to push inflation upwards; interest rates will follow. Therefore, while in the short term, interest rates may still be held as they are at present by Banks, partly due to political compulsions, they may not be able to hold them down for long. The pressure to boost the bottom line is also pushing Banks towards larger commercial loans. Besides, lending to SHGs is no longer the "in thing". The first question from visitors and Senior Officers to Branches is no longer "How much have you lent to SHGs?"

How will this scenario impact on SRFS? In the short to medium term, SRFS is not inclined to lower its interest rates. However, the final decision will depend on the trend in the responses of the SAGs who will balance the current problems they are experiencing when they borrow directly from Banks, with the higher interest rates of SRFS. SAG response will differ from area to area, depending on the attitude of the branch manager, the distance to the bank and other associated factors. The problem area that SRFS has to manage on an on-going basis is its dependency on banking instruments since it has a clear policy not to deal in cash. This dependency forces the SAG members to deal with the Bank even though they decide not to borrow from the Bank; it also results in extra transaction costs to SRFS which the Banks largely absorb when they lend directly to SAGs.

The relationship of the Rural and Urban programmes is another area which will draw attention in future. SRFS, as it very name implies, focuses on the rural area. This was and continues to be MYRADA's mission area. However MYRADA also realised that it needs to respond wherever poverty and oppression is evident. The credit scenario in the urban area is one example, where interest rates are so high that accretion of capital by those who borrow daily to support their livelihood enterprises is extremely difficult if not impossible, often resulting in a negative cash flow. However, MYRADA had no one on staff who could take the lead to start and sustain an urban credit programme. Ramesh Ramanathan, being particularly interested in urban development issues, took the lead in initiating the urban programme and continues to support its professional

[1] Building Bridges between the Poor and the Banking System.

growth and development. He also contributed 50% of the costs to construct an office for the Sanghamithra Urban Unit. Rohini Nilekani provided a generous grant with which to begin loaning operations. MYRADA initially supported the urban programme by helping to identify and train the urban NGOs in forming SAGs; the initiative to continue this was then fully passed on to the Urban Unit.

The Rural Programme linked largely with SAGs formed and trained by MYRADA during the first 2 years and then included SAGs formed by other NGOs and under Government programmes like Stree Shakti, often after supporting their capacity building. The Urban Programme works with SAGs formed by over twenty NGOs, many of whom had no experience in SAG formation and micro finance before coming in contact with Sanghamithra. This difference, coupled with others that arose due to the urban situation, required that the Urban Programme come up with appropriate strategies and supporting systems, which it is doing on an ongoing basis. The cumulative loan portfolio of the Rural Programme as on March 31 2004 is Rs.161,596,000/- and that of the Urban Programme is Rs.42,100,650/-.

The Urban Programme Office in Bangalore has created a network of its partner NGOs in the city – largely working in slums and in peri-urban areas. The Rural Programme has its office in Mysore. The CEO of Sanghamithra is the overall head of both programmes in addition to being Head of Operations of the Rural Programme, and is based in Mysore; he works closely with William D'Souza who is one of the two Vice Chairs of SRFS and is based in Mysore. The Urban Programme has a separate Head of Operations who is based in Bangalore and reports mainly to Ramesh Ramanathan who is also Vice Chair of SRFS. This arrangement worked reasonably well during the period that the Urban Programme was taking off. However, as is to be expected, the differences in the strategic requirements of rural and urban areas, as well as the way in which the two teams have developed due to their distinctive environmental influences is reaching the stage where the nature and timing of decisions taken in one context are not always appropriate to the other. In the future, it is logical that this will raise issues related to organisational management to which increasingly more time will have to be devoted. To some extent, the Chair of SRFS plays a coordinating function, but this is not his/her role, besides which, the function will require far more time as the two programmes grow. The issue of coordination between the two programmes was already identified as a potential risk by M-CRIL in its rating exercise conducted in 2003.

It did not really require M-CRIL to point out this fact; even at the time of starting urban operations, such a situation was anticipated and it was agreed that the urban unit would hive off as a separate legal entity as soon as it was confident that it had found the right type of institutional format to suit its culture and approach. No time frame had been decided, but it had made a reasonable projection that this would happen in around five years. Thus, if matters go according to plan, the rural and urban programmes of Sanghamithra will separate by 2005.

Annexure 1

ECONOMIC ANALYSIS AND PUBLICATIONS DEPARTMENT

Ref.No.NB.EAPD/1434/R&D/Proj.56/97-98
24 October 1987
02 Kartika 1909(S)

NABARD, Mumbai
R&D Fund Division

Shri Aloysius P. Fernandez
Executive Director
MYRADA
Bangalore

Dear Sir,

Sub: Request for financial support from R&D Fund of NABARD for Credit Management Groups

Please refer to your letter No.15-1.66/86-4 dated August 29, 1986 and the subsequent correspondence (c.f. our letter No.NB.EAPD/1074/R&D/Proj.56/87-88 dated September 24, 1987) and discussions on the above subject. We advise that our sanction of a lumpsum grant of Rs.10 lakhs to MYRADA to be used as a seed money support to the Credit Management Groups is subject to the following terms and conditions:

1. The seed money should be provided to as many Credit Management Groups as feasible at a time and depending upon the growth of individual groups, it may be rotated among different groups over a period of time.

2. The seed money provided to the Credit Management Groups may be utilised for helping the members of the groups to borrow from the formal credit system, vis. either Cooperative Societies, Regional Rural Bank or Commercial Bank branches through meeting margin money/share capital contribution requirement.

3. MYRADA should maintain separate accounts of the seed money assistance provided from the R&D Fund of NABARD and its uses.

4. Statements of audited accounts and progress reports on the overall project shuld be submitted to NABARD on a half-yearly basis.

5. The detailed experiences of the CMGs assisted under the project especially with reference to mobilisation of savings, lending operations reducing dependence on moneylenders, economic activities, management of funds, supported linkage with banks/cooperative societies, etc. and the lessons learnt therefore should be suitably documented by MYRADA and furnished to NABARD annually.

6. MYRADA should undertake full responsibility for receiving the grant from NABARD and for its proper utilisation. MYRADA should refund to the National Bank the balance amount of the grant, which is either not required or cannot be utilised for the project and until such refund,

it should hold the amount in trust for the National Bank.

7. The grant should not be used for any capital expenditure, including construction of building, purchase of land or any other fixed asset.

8. The National Bank shall be entitled to depute one or more of its officers to the MYRADA and/or the Credit Management Groups to verify the progress of the project at any time and if necessary suggest modifications in the approach or methodology or contents of the objectives of the project, which shall be considered by the MYRADA and implemented to the extent possible without causing any loss or damage to the MYRADA or the Credit Management Groups. The National Bank shall also have the right to depute its officers to verify the books of accounts, etc. to ascertain the proper utilisation of the funds provided under the grant.

9. The National Bank shall have the exclusive right to utilise the findings or outcome of the project in such a manner as may deem fit. The MYRADA shall not utilise or publish the findings or the outcome of the project without obtaining prior approval of the National Bank in writing.

10. The amount of grant sanctioned will be released to MYRADA in convenient instalments. The first instalment not exceeding 50 per cent of the grant will be released initially and the remaining amount in one or more instalments, depending upon the receipt of progress reports from the MYRADA, indicating utilisation of the grant to the satisfaction of NABARD.

If you are agreeable to the above terms and conditions, you may confirm accordingly by returning the enclosed copy of this letter duly signed by you, to enable us to take action for releasing the amount.

Yours faithfully,

(M.R.Krishnamurthy)
Manager

Encl. As above

Endt.No.NB.EAPD/1435/R&D/Proj.56/87-88 of date
Copy forwarded for information and necessary action to the Deputy General Manager, National Bank, Indian Express Building, No.1, Queens Road, P.B.No.5324, Bangalore, in continuation to our letter Endt.No.nb.EAPD.1075/R&D/Proj.56/87-88 dated 24 September, 1987.

(J.C.Mishra)
Deputy Manager

Annexure 2

PROJECT PROPOSAL FOR ESTABLISHMENT OF A FINANCIAL SERVICE

NABARD Bangalore, Letterhead
From Dr. Puhazhendhi

Introduction:

The concept of Self-Help Groups has been widely recognised and has emerged as a new approach for lending to the rural poor for their socio-economic development with active support for Non-Governmental Organisations. MYRADA has already achieved the task of implementing the credit management groups at the field level. The SHGs formed by MYRADA have registered significant improvement in terms of its socio and economic status. The initial consumption requirements of the group members were met from their own savings and the group members are now in search of economic activities to improve their income level. The concept of group pressure is working very well and the thrift habits have been encouraged. The marginal propensity to save by the group members is showing a positive trend. Many case study experiences revealed the positive impact of Self-Help Groups in rural upliftment.

1. Financing to the rural poor through self-help groups has been identified as a viable alternative in the Institutional Credit Delivery System and NABARD is implementing the pilot project with a specific objective to link the Bank with the Self-Help Groups. During the initial years of the pilot project implementation, many commercial banks and RRBs came forward to provide financial support to the SHGs. The experiences of bankers in financing these Self-Help Groups are quite impressive and the specific aspects like effective utilisation and better repayments were ensured for the Bank loan.

Need for a separate Financial Service:

2. Despite the efforts taken by NABARD, the progress of financing of Self-Help Groups by the banks is rather slow. Inadequate staff strength, lack of motivation by the branch managers, rigid lending norms and their past experience in group lending might be some of the factors which restrict the Banks to finance SHGs. Many Self-help Groups formed by MYRADA have attained the stage of maturity in terms of age of the group, savings, financial strength, etc. Hence, MYRADA proposes to gradually withdraw their support from such groups. Apex group concept has been introduced by MYRADA to take care of the interest of the Self-help Groups in the absence of MYRADA's involvement. The withdrawal proposal of MYRADA is on the assumption that the financing Banks will take care of the requirements of the groups in terms of credit support. However, this does not seem to be forthcoming at present. For example, out of 1500 groups which are mature enough to absorb credit only less than 200 groups have received credit support from Banks.

4. The above discussion brings out the fact that if MYRADA withdrew from the SHGs, the commercial Banks, as at present may not be able to support the groups in full. Hence, it is very much essential that a separate financial institution needs to be established for the benefit of the Groups, which were formed with the strenuous and efforts of MYRADA. This specialised institution would help the groups to take care of their savings and also help for group sustainability at a long run.

5. Conceptually the proposed financial service is not adding more tiers in the financial structure. The existing institutional credit structure will be effectively used by the financial services and only the loaning operation will be undertaken by this financial services.

Objectives:

6. The banking financial service is proposed to set up with the overall objective to provide credit support to the SHGs organised by NGOs. The specific objectives of the financial services are:

   i. To carry out and undertake the business of financing and providing credit to groups of persons belonging to the poorer sections joined together based on the concept of SHGs both in rural and urban areas with active support of NGOs.
   ii. To carry on the business of consultancy and to provide needed infrastructural and training facilities to group members.
   iii. To receive money on deposit at interest and provide financial and other support to the members of the groups.

7. In pursuance of the above objectives of the financial service may undertake one or more of the following activities.

   i. To organise, survey and investigation for assessing the scope and expansion of existing rural industries and establishment of new industries for the benefit of group members.
   ii. To formulate plans for providing required credit to the group members.
   iii. To raise necessary funds for carrying out the objectives of the financial services by borrowing or otherwise.
   iv. To provide finance for economic activities relating to production, trade and business undertaken by the group members.
   v. To arrange for direct financing of the group members by the Commercial Banks and other financing agencies and provide necessary guarantee to them, and
   vi. To undertake such other activities as are conducive or incidental to the attainment of the main objectives of the financial service.

Legal Strength:

8. The proposed financial service will be a 'Charitable Registered Body' under the Companies Act, section 25 and would obtain required permission from the Reserve Bank of India (as per section 45 of the RBI Act to function as a Non-Banking Financial Institution). The unique feature of the financial service is having self-help groups only as members. The entire surpluses will be distributed for the development of the rural poor through self-help groups. The advantages of the financial service under the Company Act are:

   i. It enjoys perpetual succession like societies and any other company formed under the Companies Act 1956.
   ii. It can own property in its name.
   iii. It can contract and defend legal proceedings in its own name.
   iv. The affairs can be carried out more effectively as the Companies Act, 1956 governs it.
   v. There is no personal liability attached to the members.
   vi. Many provisions of the Companies Act, 1956 do not apply to this company due to specific exemption granted to it.

Sources of Funds:

9. The SHGs organised by the NGOs form the members of the financial service. The financial service may raise funds from the following sources:
   i. Contribution by sponsoring institution and from other organisations.
   ii. Admission fees and miscellaneous fees.
   iii. Loans, subscriptions and refinancing facilities from the Government, Financial Institutions and Government undertakings.
   iv. Deposits from members, institutions, corporations, companies and the Government.
   v. Subsidies and grants from Central and State Governments and any other donor agencies.

Operational Aspects:

10. The company shall be managed by a Board (maximum of 10 members). The constitution of the Board may be:
    1. Chairman
    2. Vice Chairman
    3. Project Coordinators from MYRADA Projects (2)
    4. Members from Major Banks (2)
    5. Members from other NGOs and similar bodies (2)
    6. Member from NABARD (1)
    7. Managing Director on a full time basis (1)

    The Chairman of the Board will be the overall in-charge of the financial service and the Board will take all decisions relating to the policy. The organisation shall be administered and managed by the Managing Director.

11. The Head Office of the Financial Service will be in Bangalore, affiliated to the MYRADA Office for an initial period of 3 to 5 years. The staff strength at the Head Office will be 3 members, viz., 1 Accounts Officer, 1 Typist cum Steno, and 1 Maintenance staff, besides the Managing Director. Initially the area of operation of the Financial Service will be confined to the area of operation of MYRADA (States of Andhra Pradesh, Karnataka and Tamilnadu) and will be extended to other areas based on the business potential available. To start with the Financial Service will provide support to 5 of the selected project areas of MYRADA and each project office will have one credit manager who will undertake the credit operations under the supervision of the Project Officer.

12. The entire financial service from Head Office to the SHGs will be operated through Bank account. The instruments available with the banks such as cheques, Demand Drafts, Mail Transfer facilities will be used for smooth flow of the fund from the Financial Service to the SHGs and also to recover the instalments from the group to the institution. For example, the Head Office will have a main account and the Project Office will have a nodal account. The budgeted amount for loan disbursal will be transferred from Head Office to the nodal account through giving instructions to the Bank. The Credit Manager at the Project level will appraise and sanction loans for SHGs with active support of the Project officials and Project Coordinator and the sanctioned amount will be credited to the SB Account from the Nodal Account in the project area by giving necessary instructions to the Bank. Similarly, the SHG will instruct its bankers for repayment of the loan and the specified amount will be transferred from the SB Account of the SHG to the Financial Service account either to the Nodal Account or to the Head Office account. The above mentioned procedure is conceived with a specific idea to have smooth flow of funds without using any currency and also to have an effective monitoring system through preparing periodical statements at different levels.

Viability:

13. The Financial Service may provide credit to an extent of Rs.50 lakhs per year. It is expected that the initial contribution of Rs.20 lakhs should come from the group members as well as from Myrada and other donors free of interest, the remaining amount and also the future requirements will be met by NABARD, Government of India and other major banks at reduced interest rate. A statement indicating the fund flow and also the extent of income generation for the period of 5 years is enclosed. The profit received till the 5 year period of the Financial Service will be kept in reserve which will be used for the benefit of the groups after five years.

Major Innovations:

14. The proposed financial service distinctly differs from other banking institutions mainly through having SHGs as its members and the credit assistance will be extended only to the groups. The merit of informal credit sources such as timely and adequate credit flow and also scientific lending norms followed by formal credit institutions will be appropriately built in while developing the appraisal system and loan delivery in the financial service. Other specific innovations are:
    a. Exclusive focus on the very poor through SHGs.
    b. Flexible lending norms
    c. The banking at the borrowers doorstep.
    d. Timely and adequate credit.
    e. Close supervision of the borrowers and their activities.
    f. Better awareness of lending rules and procedures by borrowers.
    g. Compulsory savings.
    h. Active participation of borrowers in open discussion.
    i. Vigorous practical training both for borrowers and staff members.
    j. No influence from any quarter entertained.
    k. Adopting group pressure for recovery rather than cohesive methods.

15. The functioning of the institution is totally informal and both loan disbursement and recovery will be effected at the borrowers doorstep by the field level staff of the institution. Many innovations in loan appraisal, disbursement and recovery will be effected keeping the borrowers benefit in mind.

s/d

(V.Puhazhendhi) NABARD, Bangalore Office

Annexure 3

Sanghamithra Letterhead
Corporate Office:
916, 8th Main, 3rd Stage Gokulam
MYSORE 570 002. Karnataka.

CIRCULAR NO.44

Sub: Housing Loan

Sanghamithra would like to introduce a new loan scheme to enable group members to avail housing loans, which will be effective from 14th November 2003 on the occasion of "Children's Day".

This loan scheme can be availed by the groups who have already availed general group loans subject to regular repayment of the existing group loan.

This scheme is called **"Sanghamithra Griha Nirmana Loan Scheme".**

Salient features of the scheme:

1. **Purpose of the Loan:**
   i) Site purchase
   ii) New house construction
   iii) Repairs to existing house
   iv) Extensions/renovations to existing houses
   v) Construction of bathrooms/toilets
   vi) Creation of workspaces within the house.

2. **Eligibility Criteria:**
   i) The group should have effectively functioned for a minimum of 3 years.
   ii) The group should have availed and repaid loan either from SRFS or other Financial Institutions at least twice before availing housing loan.

3. **Amount of the Loan:**

   The loan will be for a minimum sum of Rs.75,000/- and a maximum of Rs.1,50,000/- per group. The loans within the group to an individual member is subject to a minimum limit of Rs.5,000/- and maximum of Rs.30,000/-. Atleast 5 persons in a group should avail the loan.

4. **Period of Loan:**

   3 Years including moratori7m period of 3 months plus upto 6 months for repayment of interest on an even basis.

5. **Interest:**

   Rate of interest will be 12%on reduced balance basis as per the Sanghamithra procedure.

6. **Service Charges:**

   Service Charges are as applicable to the general loans payable upfront as follows:
   1st Year 2%

2nd Year 1%
3rd Year 0.5%

7. **Repayment:**

The loan is repayable in 3 years. Monthly repayment will be Rs.5000/- for a loan of Rs.1,50,000 which will proportionately come down depending on the size of the loan.

8. **Repayment Holiday:**

Repayment holiday of 3 months are allowed from the date of disbursal of the first installment of the loan. The amount should be utilized within 3 months and the construction should be completed.

9. **Security:**

Clean, but a copy of the record of right is to be submitted to Sanghamithra which should not bear any other encumbrances.

10. **Other Conditions:**

(i) Group should ensure that all documents relating to the house/land are to be in the name of the borrower or spouse and disputes if any are to be settled by the group itself, which in any way should not effect repayment of the loan to Sanghamithra.

(ii) Average repayment capacity of the members to the SHGs of existing loans should be more than the average repayment per month to SRFS by the group inclusive of general loan.

(iii) The borrower of housing loan should not have defaulted to the groups at any time.

(iv) Group is entirely responsible for the repayment as in the case of other loans

(v) Group should ensure that the individual members or spouse are not having any liability with any other Financial Institutions.

(vi) The group should maintain a list of borrowers purpose wise (as mentioned above) location, site amount of loan to each member etc., under Housing Loan Scheme.

(vii) Sanghamithra will have the right of access to inspect assets created out of the loan proceeds availed by members and to verify documents related to the property, obtained by the group to create charge.

(viii) Sanghamithra will have the right to recover the loan amount from the group either partly or fully if it is found during inspection that the asset is not created or the work is not completed within the holiday period of 3 months.

(ix) Until the closure of the Sanghamithra Housing Loan by the group, members/spouses should not be allowed to alienate the property to third party by sale , mortgage and pledge or in any other direct or indirect manner.

(x) All other rules, regulations and procedures existing or that may be amended from time to time by the Sanghamithra Board in future will be applicable to this loan scheme also.

All the Staff Members are hereby required to go through the circular properly and implement the same with the true spirit of the scheme and explain to all the stakeholders each and every aspect correctly. Any doubt or suggestions may be directly referred to Corporate Office for clarification and improvement of the scheme and make it a grand success.

sd/-

S.M.Adiga
Chief Executive Officer

Encl: 1

(Repayment Schedule for a loan of Rs.1,50,000/-)

Date	Particulars	Debit	Credit	Closing Balance	No. of Months Repayment
10 Nov 03	Disbursal		150000	150000	
30 Nov 03	Accrual	838		**150838**	
31 Dec 03	Accrual	1509		**152347**	
31 Jan 04	Accrual	1524		**153871**	
29 Feb 04	Accrual	1539		**155410**	
15 Mar 04	Repayment	-	5000	**150410**	
31 Mar 04	Accrual	1505		**151915**	
15 Apr 04	Repayment	-	5000	**146915**	1
30 Apr 04	Accrual	1470		**148385**	
15 May 04	Repayment	-	5000	143385	2
31 May 04	Accrual	1484		**144869**	
15 Jun 04	Repayment	-	5000	139869	3
30 Jun 04	Accrual	1449		**141318**	
15 Jul 04	Repayment	-	5000	136318	4
31 Jul 04	Accrual	1414		**137732**	
15 Aug 04	Repayment	-	5000	132732	5
31 Aug 04	Accrual	1378		**134110**	
15 Sep 04	Repayment	-	5000	129110	6
30 Sep 04	Accrual	1342		**130452**	
15 Oct 04	Repayment	-	5000	125452	7
31 Oct 04	Accrual	1305		**126757**	
15 Nov 04	Repayment	-	5000	121757	8
31 Dec 04	Accrual	1268		**123025**	
15 Jan 05	Repayment	-	5000	118025	9
31 Jan 05	Accrual	1231		**119256**	
15 Feb 05	Repayment	-	5000	114256	10
28 Feb 05	Accrual	1193		**115449**	
15 Mar 05	Repayment	-	5000	110499	11
31 Mar 05	Accrual	1155		**111604**	
15 Apr 05	Repayment	-	5000	106604	12
30 Apr 05	Accrual	1117		**107721**	
15 May 05	Repayment	-	5000	102721	13
31 May 05	Accrual	1078		**103799**	
15 Jun 05	Repayment	-	5000	98799	14
30 Jun 05	Accrual	1038		**99837**	

Date	Particulars	Debit	Credit	Closing Balance	No. of Months Repayment
15 Jul 05	Repayment	-	5000	94837	15
31 Jul 05	Accrual	999		**95836**	
15 Aug 05	Repayment	-	5000	90836	16
31 Aug 05	Accrual	959		**91795**	
15 Sep 05	Repayment	-	5000	86795	17
30 Sep 05	Accrual	918		**87713**	
15 Oct 05	Repayment	-	5000	82713	18
31 Oct 05	Accrual	878		**83591**	
15 Nov 05	Repayment	-	5000	78591	19
30 Nov 05	Accrual	8360		**79427**	
15 Dec 05	Repayment		5000	74427	20
31 Dec 05	Accrual		795	**75222**	
15 Jan 06	Repayment		5000	70222	21
31 Jan 06	Accrual	753		**70975**	
15 Feb 06	Repayment		5000	65975	22
28 Feb 06	Accrual	710		**66685**	
15 Mar 06	Repayment		5000	61685	23
31 Mar 06	Accrual	667		**62352**	
15 Apr 06	Repayment		5000	57352	24
30 Apr 06	Accrual	624		**57976**	
15 May 06	Repayment		5000	52976	25
31 May 06	Accrual	580		**53556**	
15 Jun 06	Repayment		5000	48556	26
30 Jun 06	Accrual	536		**49092**	
15 Jul 06	Repayment		5000	44092	27
31 Jul 06	Accrual	491		**44583**	
15 Aug 06	Repayment		5000	39583	28
31 Aug 06	Accrual	446		**40029**	
15 Sep 06	Repayment		5000	35029	29
30 Sep 06	Accrual	401		**35430**	
15 Oct 06	Repayment		5000	30430	30
31 Oct 06	Accrual	355		**30785**	
15 Nov 06	Repayment		5000	25785	31
30 Nov 06	Accrual	308		**26093**	
15 Dec 06	Repayment		5000	21093	32
31 Dec 06	Accrual	261		**21354**	

Date	Particulars	Debit	Credit	Closing Balance	No. of Months Repayment
15 Jan 07	Repayment		5000	16354	33
31 Jan 07	Accrual	214		**16568**	
15 Feb 07	Repayment		5000	11568	34
28 Feb 07	Accrual	166		**11734**	
15 Mar 07	Repayment		5000	6734	35
31 Mar 07	Accrual	118		**6852**	
15 Apr 07	Repayment		5000	1852	36
30 Apr 07	Accrual	69		**1921**	
15 May 07	Repayment		1921	0	37
	TOTAL	**36921**	**186921**		

Annexure 4

SANGHAMITHRA RURAL FINANCIAL SERVICES - RURAL PROJECT
INCORPORATED UNDER SECTION 25 OF THE COMPANIES' ACT, 1956
COMPANY LIMITED BY GUARANTEE

BALANCE SHEET AS AT 31st MARCH, 2004

	SCHEDULE NO.	31.03.2004 Rs.	31.03.2003 Rs.
SOURCES OF FUNDS:			
Reserves & Surplus			
Capital Reserve	1	30,783,046	30,009,618
Donor's Fund - Care India, New Delhi	2	705,099	1,830,424
Development & Training Fund	3	953,073	300,000
Anniversary Celebration Fund	4	101,000	-
		32,542,218	32,140,042
Secured Loans			
Corporation Bank Cash credit a/c (On Security of Fixed Deposits)		-	1,729,361
NABARD, Bangalore Secured against Book Debts)		23,362,500	13,900,000
Canara Bank - Overdraft a/c (Secured against Book Debts)		19,143,227	-
		42,505,727	15,629,361
Total		75,047,945	47,769,403
APPLICATION OF FUNDS:			
Fixed Assets:	5		
Gross Block		1,970,722	1,620,267
Less: Depreciation		1,040,588	893,885
Net Block		930,134	726,382
Investments	-	-	
Current Assets, Loans & Advances:			
A. Current Assets	6	15,356,171	5,958,952
B. Loans and Advances	7	74,521,329	42,502,300
		89,877,499	48,461,252
Less : Current Liabilities and Provisions	8	15,759,688	1,418,231
Net Current Assets		74,117,811	47,043,021
Miscellaneouse Expenditure	-	-	
Total		75,047,945	47,769,403

For and on behalf of the Board

As per our Report of even date
For Hariharan & Co
Chartered Accountants

(Aloysius P. Fernandez)
Chairman

(William D'Souza)
Vice-Chairman

(Ramesh Ramanathan)
Vice-Chairman

(H. Ramachandra)
Partner

(Vidya Ramachandran)
Director

(Yasmin Master)
Director

(S M Adiga)
Chief Executive Officer

(Cecil Lazarus)
Head-Operations

Bangalore
2nd July 2004

SANGHAMITHRA RURAL FINANCIAL SERVICES - RURAL PROJECT
INCORPORATED UNDER SECTION 25 OF THE COMPANIES' ACT, 1956
COMPANY LIMITED BY GUARANTEE

INCOME AND EXPENDITURE ACCOUNT FOR THE YEAR ENDED 31st MARCH 2004

	SCHEDULE No.	31.03.2004 Rs.	31.03.2003 Rs.
INCOME:			
Charges Collected from SHGs	9	8,359,356	4,822,206
Interest & Other Income	10	766,871	489,053
Reiceived from - CIDA DID		151,000	30,360
A		9,277,227	5,341,619
EXPENDITURE:			
Remuneration and Benefits to Employees	11	1,332,557	943,029
Repairs & Maintainance	12	47,056	33,665
Operational & Administrative Expenses	13	1,751,880	1,504,162
Financial Expenses	14	2,524,165	785,491
Depreciation		173,239	182,762
B		5,828,897	3,449,109
Surplus Before Provisions A-B		3,448,330	1,892,510
Less : Provision made against Financial Assistance portfolio		1,373,902	546,995
EXCESS OF INCOME OVER EXPENDITURE FOR THE YEAR		2,074,428	1,345,515
Less : Appropriations :			
Development & Training Fund		1,200,000	599,061
Anniversary Celebration Fund		101,000	
		773,428	746,454
Less: Excess of Expenditure ove Income brough forward from earlier years		-	1,004,236
Surplus/Deficit Transferd to Capital Reserve		773,428	(257,782)

For and on behalf of the Board

As per our Report of even date
For Hariharan & Co
Chartered Accountants

(Aloysius P. Fernandez)
Chairman

(William D'Souza)
Vice-Chairman

(Ramesh Ramanathan)
Vice-Chairman

(H. Ramachandra)
Partner

(Vidya Ramachandran)
Director

(Yasmin Master)
Director

(S M Adiga)
Chief Executive Officer

(Cecil Lazarus)
Head-Operations

Bangalore
2nd July 2004

Annexure 5

SANGHAMITHRA RURAL FINANCIAL SERVICES

Assessment Formats

Questionnaire to Assess a Self-Help Group

1. **Assessment no.** | | | | | | | | | | | | |
2. **Assessment date** | | | | | | |
3. **SHG code** | | | | | | | | | | | | |
4. **Name of the SHG:**______________________________
5. **Full Address :**______________________________

Village : ____________________**Post Office:**__________

Taluk : ____________________**Pin Code :**__________

District :____________________**Telephone :**__________

CATEGORY 1 : PRELIMINARY
QUESTIONS- A SCORE TICK(-/)
SCORE GIVEN

1.1 Age of the Self-Help Group

a. 2 years and above	*8-10*	☐	
b. Between 1 and 2 years	*4-7*	☐	
c. Less than 1 year	*0-3*	☐	________

1.2 Genuineness and Awareness

What was the purpose of forming the group?

a. To organise individual members/ group/ community for economic activity	*8-10*	☐	
b. To inculcate saving habits and avail need based loans	*4-7*	☐	
c. To take loans from NGO/Govt.	*0-3*	☐	________

1.3 Level of Savings

The formula to be used to assess the level of savings is $\frac{SA}{S*N*M} * 100$

Where

SA = actual savings

S = monthly savings/member as promised/planned by SHG

N = number of members

M = number of months elapsed since inception
Of the group/or the last three years whichever is less

If the result is

a. 90 percent or above	8-10	☐
b. Above 80 percent but less than 90 percent	4-7	☐
c. Between 70 and 80 percent	**0-3**	☐ ______

1.4 Control Over Funds

a. Loans are sanctioned by all the members of the group in a meeting	8-10	☐
b. Loan decisions are taken by a committee which includes some non-members	4-7	☐
c. Loan decisions are made by people other than the members of the group	0-3	☐ ______

1.5 Recovery Rate

Recovery rate (%) is calculated on the loans extended by SHG to its members is follows

Total amount actually collected/recovered * 100
Total amount due

Marks assigned as below:

	Marks
79 or less 80	0
80-90	10 - 20
91-100	22- 40

If the marks under category 1.1 to 1.4 are less than 24 or the marks under category 1.5 is 0, the interviewer has to stop the inquiry here.

The total marks for the first category is **80**

Category 2 : Internal non-financial information

2.1 Continuity in membership

a. Of all the members who created the group more than 90 percent are still part of it — 8-10 ☐

b. Of all the members who created the group, between 70 and 90 percent are still part of it — 4-7 ☐

c. Of all the members who created the group, less than 70 percent are still part of it — 0-3 ☐ ______

2.2 Regularity

During the last year, all the meetings scheduled have been held — 8-10 ☐

a. More than 80 percent of the meetings have been held — 4-7 ☐

b. Less than 80 percent of the meetings have been held — 0-3 ☐ ______

2.3. Attendance

a. More than 90 percent — 10 ☐

b. Between 70 and 90 percent — 7 ☐

c. Less than 70 percent — 3 ☐ ______

2.4. Range of activities

a. The group undertakes also social/lobbying activities apart from the financial activities — 8-10 ☐

b. The group undertakes only savings and credit activities — 4-7 ☐

c. The group only undertakes savings activities — 0-3 ☐ ______

2.5. Governing Structure

a. The leaders of the group are elected democratically and rotated periodically — 8-10 ☐

b. The leaders of the group are elected democratically but are not rotated — 4-7 ☐

c. The leadership is always cornered by the same members — 0-3 ☐ ______

2.6. Literacy

a. 60 to 100 percent of the members have functional literacy — 8-10 ☐

b. 30 to 60 percent of the members have functional literacy — 4-7 ☐

c. Less than 30 percent of the members have functional literacy — 0-3 ☐ ______

2.7. Self-reliance

a. The members of the group conduct meetings, maintain books and deal with outside agencies without supporting organisation — 8-10 ☐

b. *The group needs some support from the supporting organisation in terms of accounting and resources*	*4-7*	☐	
c. *The group is totally depending on the supporting organisation for meeting, accounting and resources*	*0-3*	☐	______

2.8. Financial Autonomy

a. *Group pays for all its costs of operations like stationery, meeting costs, travel etc.*	*8-10*	☐	
b. *It meets more than 50% of the cost, but it also needs some external support*	*4-7*	☐	
c. *The group does not pay for its operating costs*	*0-3*	☐	______

The total marks for the second category is	**80**

Category 3: Borrower Appraisal Information

3.1 Loan Sanctioning -Are all or some of the following conditions practised while sanctioning a loan in the SAG:

a) Use of collateral or asset as guarantee 2 ☐

b) Eligibility period before availing a loan 2 ☐

c) System of guarantor and co-guarantor 2 ☐

d) Clearing of previous loans 2 ☐

e) Proportion to the amount of savings of the borrower 2 ☐ ______

3.2 Distribution of the loans

a) More than 50 % of the members have taken a loan 7-10 ☐

b) Between 25 and 50% of the members have taken a loan 4-7 ☐

c) Less than 25% members have taken a loan 0-3 ☐ ______

3.3 Purposes of the loans

a. More than 70 percent of the loans are for productive purposes 7-10 ☐

b. Between 50 and 70 percent of the loans are for productive purposes 4-7 ☐

c. Less than 50 percent of the loans are for productive purposes 0-3 ☐ ______

3.4 Interest rate

a. Variable depending upon the purpose, amount or borrower 10 ☐

b. More than 36 percent 8 ☐

c. 24 to 36 percent 6 ☐

d. 12 to 24 percent 4 ☐

e. No interest charged 0 ☐ ______

3.5 Interest earned on savings

a. The income is shared by the members proportionally to the level of their savings 10 ☐

b. The income is added to the savings of the group 6 ☐

c. No decision has been taken about this yet 0 ☐ ______

3.6 Savings History

Amount/ member/ month

a. More than Rs.40 8-10 ☐

b. Between Rs.20 and Rs.40 3-7 ☐

c. Less than Rs.20 0-3 ☐ ______

3.7 Utilisation of the Savings Mobilised:

Loans advanced as a proportion of the savings

a. Above 100 percent 8-10 ☐

b. Between 50 and 100 percent 4-7 ☐

c. Less than 50 percent 0-3 ☐ ______

3.8 Funds Availability

Amount of funds

a. *More than 3 times the savings of the groups*	*8-10*	☐	
b. *Between 1 and 3 times the savings of the groups*	*4-7*	☐	
c. *Less than the savings of the group*	*0-3*	☐	____

3.9 Overdues on internal lending

a. *The overdue is less than 5 percent of the loans advanced*	*8-10*	☐	
b *The overdue is between 5 and 10 percent of the loans advanced*	*4-7*	☐	
c. *The overdue is more than 10 percent of the loans advanced*	*0-3*	☐	____

3.10 Records Maintained

a. *Attendance Register*	*1*	☐	
b. *Minutes Book*	*1*	☐	
c. *Loan Ledger*	*2*	☐	
d. *Savings Ledger*	*2*	☐	
e. *Cash Book*	*1*	☐	
f. *General Ledger*	*1*	☐	
g. *Bank Pass Book (group)*	*1*	☐	
h. *Individual Member Pass Book*	*1*	☐	____

3.11 Quality of maintenance of records

a. *Good*	*8-10*	☐	
b. *Satisfactory*	*4-7*	☐	
c. *Poor*	*0-4*	☐	____

The total marks for the third category is **110**

Category 4 : External non-financial information

4.1 Economic Level

Average annual income per member

a. The income is less than Rs. 10,000	8-10	☐	
b. The income is between Rs.10,000 and Rs.20,000	5-7	☐	
c. The income is more than Rs.20,000	0-4	☐	____

4.2 Land Holding- No. of Members holding land

a. Less than 80 percent	8-10	☐	
b. More than 80 percent	5-7	☐	
c. Every member holds land	0-4	☐	____

4.3 Irrigated Land

a. Less than 50 percent of the land is irrigated	8-10	☐	
b. Above 50 percent of the land is irrigated	5-7	☐	
c. All the land held is irrigated	0-4	☐	____

4.4 Purpose of the Supporting Organisation/NGO

a. The only purpose is promoting SHGs	8-10	☐	
b. Promoting SHGs is one of the main purposes	5-7	☐	
c. Promoting SHGs is not one of the main purposes	0-4	☐	____

4.5 The organisation has been promoting and supporting SHGs for

a. More than 3 years	8-10	☐	
b. Between 1 and 3 years	4-7	☐	
c. Less than 1 year	0-3	☐	____

4.6 The organisation visits the SHG

a. Twice or more, a month	8-10	☐	
b. Once a month	4-7	☐	
c. Less than once a month	0-3	☐	____

4.7 According to the NGO, the creditworthiness of the SHG is

a. Good	8-10	☐	
b. Satisfactory	4-7	☐	
c. Poor	0-3	☐	____

4.8 The organisation is ready to provide some support to Sangamithra regarding the operations with the SHG

a. Yes	6-10	☐	
b. Yes with some incentives	1-5	☐	
c. No	0	☐	____

The total marks for the fourth category is	**80**

Category 5 : External Financial Information

5.1 Previous Experiences with Formal Credit Institutions
The group has already been linked to a bank for loans

a. *Yes*	*8-10*	☐	
b. *No, but the group has opened a savings account*	*4-7*	☐	
c. *No*	*0-3*	☐	______

If the group has never been linked to a bank, the three following questions must be given the mark 0

5.2 Amount of loans provided by the bank

a. *More than 4 times the owned funds of the group*	*8-10*	☐	
b. *Between 2 and 4 times*	*4-7*	☐	
c. *Less than 2 times*	*0-3*	☐	______

5.3 Repayment rate on bank loans. The marks attributed to assess the *repayment rate is given by the formula (r-70/30)*10*
where r: repayment rate on loans taken from bank.

$$\text{Marks} = \frac{\dfrac{\text{Amount actually repaid to bank} \times 100}{\text{Amount due to the bank}} - 70}{30} \times 10$$

5.4 Overdue of SHG with the bank is

a. *Less than 10 percent of the funds advanced*	*8-10*	☐	
b. *Between 10 and 20 percent of the funds advanced*	*4-7*	☐	
c. *More than 20 percent of the funds advanced*	*0-3*	☐	______

5.5 Awareness about Banking Procedures among Members

a. *More than 80 percent of the members have already dealt with a bank*	*8-10*	☐	
b. *Between 30 and 80 percent of the members have already dealt with a bank*	*4-7*	☐	
c. *Less than 30 percent of the members have dealt with a bank*	*0-3*	☐	______

The total marks for the fifth category is **50**

TOTAL MARKS

Summary of marks	*Maximum*	*Scored*
Category 1	*80*	
Category 2	*80*	
Category 3	*110*	
Category 4	*80*	
Category 5	*50*	
Total Marks	*400*	

Poor/Satisfactory/Good/Very Good

Signature

Place:
Date:

DEMAND PROMISSORY NOTE

Rs.__________

Place :__________

Date :__________

On demand I/We____

____

____

jointly and severally promise to pay ________________________ a sum of Rs.__________ (Rupees______________________________) with interest at___ percent per month / compounded monthly for value received.

Name: 1.

2.

3.

Affix Revenue Stamp

WITNESS

1.

2.

3.

RECEIPT CUM LINK LETTER

Received with thanks Rs ______________ (Rupees: ________________ ________________________________ only) from Sanghamithra Rural Financial Services by Cheque/DD no. ________________ Dated (date of Cheque/ DD) drawn on ________________ (Bank). ____________ Branch, on ____________ (date of receipt of F.A) being the Financial Assistance as per the document executed by me/us on________ (date of execution of agreement).

Affix Re. 1/- Revenue Stamp

Date:
Signature/s of Borrower/s:
(Authorised Representatives)

1.

2.

3.

Name of Borrower account : ________________________

F.A. No. ________________________________

Witness 1.

2.

FA09/01

Regn. No. Appl No.
F.A. No. Repeat Group

SANGHAMITHRA RURAL FINANCIAL SERVICES

916, 8th Main, 3rd Stage, Gokulam, Mysore 570 002

SHG APPLICATION CUM APPRAISAL FORM

Date: ____________ For Office use only

To: Credit Manager
SANGHAMITHRA, ____________ Unit. ________ ________

Dear Sir,

We, ______________________________(Name of SHG), hereby apply for financial assistance for further extending loans to members of our Self-Help Group. We furnish below the necessary particulars.

I. PARTICULARS OF SHG AND FINANCIAL EXPERIENCE

1. SHG Code: | | | | | | | | | | | | |
2. CM /CSA ref: | | | | | | | | | | | | |
3. Product code: | | | | | | | | | | | | |
4. Full Address:

Village: ____________ Post Office: ____________
Taluk: ____________ District: ____________
Pincode: ____________ Telephone: ____________

5. Our Bank Accounts are operated by :

1. Smt./ Shri. ____________ ____________
(NAME) (DESIGNATION)
2. Smt./ Shri. ____________ ____________
(NAME) (DESIGNATION)
3. Smt./ Shri. ____________ ____________
(NAME) (DESIGNATION)

6 a. Total no. of members at the commencement of the group (state the year of formation ________) Female ________; Male ________
b. No. of members since joined ________ No. of members since discontinued ________
c. Total no. of members at present is : ________; Female ________; Male ________

7. Receipts & Payments a/c for the period ____________ to ____________

Receipts		Payments	
Opening balance – cash		Loans given	
Opening balance – bank		SHG expenditure – Revenue	
Savings of Members		SHG expenditure – Capital	
Membership Fees		Repayments of Loans taken by SHG	
Fines		Interest repayments on taken loans by SHG	
Bank Interest		Savings withdrawn by members	
Loan Interest		Other uses	
Loan Recoveries		Closing balance – cash*	
Loans taken by SHG		Closing balance – bank*	
Grants received			
Other sources			
Total		Total	

8. List of all agencies from whom grant was received

Name of the Agency	Amount Received	Date of Receipt
Grant		
Total		

9. Particulars of loans currently outstanding to outside agencies:

Source of Loan	Loan date	Amount of Loan	Outstanding Amt as of dt.______	Repayment periodicity	Repayment Amount Rs.

10. Saving history of SHG for the period ______________ to ______________

Year	No. of members	No. of months	Total saving of SHG	Avg. Monthly saving per member
OB				
Total				

11. Internal lending and recovery of the SHG for the period ______ to ______

Year	No. of members	No. of months	No. of loans disbursed Internally	Loans disbursed Rs.	Loan recovery Rs	Average monthly recovery Rs	FA due As on ..
OB							
Total							

II FINANCIAL ASSISTANCE APPLIED FOR:

Rupees________________________________Rs.__________

III REPAYMENT

We hereby undertake to repay the Financial Assistance as follows:

a) Equated monthly / quarterly / half-yearly / annual / irregular installments as scheduled below.

Installment amount: Rs.________________________________

No. of Installments: ________________________________

Last Repayment date : ________________________________

A copy of the resolution to borrow executed by all the members of the group authorizing us *interalia* to borrow on behalf of the SHG is enclosed.

DECLARATION

We hereby declare that the particulars given above are true and correct to the best of our knowledge and belief.

We hereby authorize Sanghamithra Rural Financial Services, hereinafter called Sanghamithra, to disclose all or any particulars or details or information relating to our Financial Assistance a/c with Sanghamithra to any other financial institution /govt. or any agency(ies) as may be considered necessary or desirable by Sanghamithra.

Sanghamithra may disqualify us from receiving any credit facilities in case it is proved that the declarations of our outside borrowing made above contain misrepresentation of facts.

We hereby declare that we have no borrowings from any other agency on the date of application, for the same purpose, other than what has been indicated above.

We undertake not to borrow from any other agency without the permission of Sanghamithra.

We hereby undertake to pay at the time of the first disbursal of the Financial Assistance, service charges equivalent to 2% of the total Financial Assistance amount calculated for every year or part thereof over which Financial Assistance installment repayments are spread/ scheduled.

(Authorized reps)
Place:
Date:

Applicants Name & Signature

1. ________________________
2. ________________________

Note: * : Where closing balances on hand /at bank are unusually high as at a particular date , please explain change, if any, in those positions subsequently.

**: Whereever there is sudden abnormality in periodic average recoveries, attach month-wise recovery statistics and explain abnormalities, if any

APPRAISAL REPORT

I have visited ______________________ (SHG) and have inspected their working..

2. Observations of Credit Manager:

   Savings from members:
   Rs.______________________

   Loan outstanding against members:
   Rs.______________________

   Amount in default, if any, against members:
   Rs.______________________

   Recovery percentage: ______________________

   Cash/ Bank Balance:
   Rs.______________________

3. Record whether the following items were found satisfactory/ unsatisfactory

   Use a scale of 1 to 5 (where 5 denotes highest satisfaction and 1 denotes lowest)

Frequency of Meetings (a)	Average Attendance (b)	Regularity of Meetings	System of Accounting	Recording of Information related to members	Savings History of the Group	History of Credit to its members	Auditor's Report about the Group

4. The particulars furnished by the applicant have been verified and are found to be satisfactory. I recommend that a Financial Assistance of Rs. ______________________ may please be extended, under the following terms:

   - Repayment Installments : Rs. ______________________
   - No. of installments : ______________________
   - Frequency of installments : ______________________
   - Probable date of final repayment : ______________________

   Place : ______________________

   Date: ______________________

Credit Manager

FOR OFFICE USE ONLY

Financial Assistance Committee's Decision

- Sanctioned Rs.______________________
- Rejected

Reasons for rejection: ______________________________

____

Place: ______________

Date: ______________

Signature	Signature	Signature

(On Rs.50 non-judicial stamp paper)

AGREEMENT FOR FINANCING SELF-HELP GROUPS

The articles of Agreement entered into on this ___________day of ___________

200____ at ____ by and between

________________ ____________________ (name of the SHG) an unregistered

association of persons having its office at ______________________________

village, ____________________ district, represented by its authorized representatives

Shri/Smt. ______________________________ ______________________________
(Name) (Designation)

Shri/Smt. ______________________________ ______________________________
(Name) (Designation)

Shri/Smt. ______________________________ ______________________________
(Name) (Designation)

who are fully authorised by all the members of the SHG, (a copy of such Authorisation is annexed hereto and forms part of this agreement), herein after referred to as "Borrower", which expression shall, unless repugnant to the subject or context thereof, mean and include members of the unregistered association for the time being, their respective successors, legal heirs, administrators and assigns of the one part

and

Sanghamithra Rural Financial Services, registered under the Companies Act, 1956 with its corporate Office at #916, 8th main, III stage, Gokulam, Mysore-570012 and District Office among others at____
represented by its Manager, Shri/Smt.____________________ hereinafter called "Sanghamithra" which expression shall,unless repugnant to the subject or context thereof, mean and include its successors and assigns of the second part

Whereas the Borrower is an association of unregistered persons / SHGs who have agreed to help each other with a view of developing and ameliorating the socio-economic conditions of their members.

Whereas having formed the SHG, the Borrower as per application dated__________ made by the above mentioned authorized representatives, and duly authorized to borrow in terms of its resolution no. _________dated. ___________ (Copy enclosed) requested Sanghamithra to grant Financial Assistance of Rs.__________ (Rupees______________________ only) for on-lending to its members.

And whereas Sanghamithra has agreed to grant the Financial Assistance to the Borrower on certain terms and conditions.

And whereas Sanghamithra and the borrower are desirous of reducing the agreed terms into writing.

Now therefore, this agreement witness as follows:

1. Sanghamithra has agreed to lend and the borrower has agreed to borrow Rs.__________ (Rupees____ only)
2. The borrower hereby agrees with Sanghamithra that they shall repay to Sanghamithra the principal sum of Rs.__________ (Rs.____________________________ only) along with

interest, service charges, commission, cost, charges and expenses on or before the due dates described in the schedule A given below. The schedule excludes any charge or expense that may be charged by Sanghamithra, as penal charges on account of Borrowers default, if any.

3. In case the credit facility availed by the borrower is a term financial assistance the same shall be repayable in installments in the manner specified in the repayment schedule. Besides the borrower will pay administrative charges at the rates that may be payable as per Sanghamithra specified rates that are in force for the time being and applicable to such transactions.

4. Sanghamithra is entitled to charge service charges on every financial assistance account equivalent to 2% of the total financial assistance sanctioned for every year or part there of for the period over which the repayments are scheduled, at the time of the disbursement of the 1st installment itself.

5. That Sanghamithra shall be entitled to charge interest at the rate of 1% p.m. or such other rates as are in consonance with its policy and controlling authorities, directives or as determined by Sanghamithra at its discretion from time to time by notice in writing. These charges are compounded monthly and are chargeable on the balance outstanding due and repayable at the end of the last day of the previous month except:

   a) In the first month when the financial assistance has been taken, the administrative charges shall be levied at 12% p.a. for the actual number of days the financial assistance is availed during that month.

   b) Where the financial assistance account is being closed in any month by way of full repayment the administrative charges shall be levied at 12% p.a. for the balance outstanding due and repayable as at the end of the last day of the previous month for the number of days in that month upto the date of full repayment.

6. The borrower should utilize the proceeds of the financial assistance facility exclusively for the purpose of lending to its members for the identified economic activity/ income generating activity to promote the socio-economic conditions of its members and member's families.

7. In the event of the Borrower committing breach of any of the terms and conditions stipulated by Sanghamithra or mis-utilization, non-utilization or only partial utilization of the proceeds of the financial assistance, notwithstanding anything herein contained and notwithstanding the stipulation, if any, that the Borrower is allowed to pay the amounts due in installments, Sanghamithra shall have right to demand repayment of the entire liability forthwith.

8. The borrower shall repay the financial assistance availed together with administrative and other charges payable as per Sanghamithra prescribed rate/s that may vary from time to time. In the event of failure to repay the financial assistance facility availed in the stipulated manner and or failure to pay minimum charges as stipulated, the borrowers shall be liable to pay penal charges at the rate of 6% p.a (over and above the normal applicable rates on financial assistance) with monthly rests on the balance principle outstanding, from the date of default till the financial assistance account is regularised or complete repayment of the financial assistance.

9. Not withstanding anything contained here above the borrower shall be liable to repay the financial assistance amount on demand together with the administrative and other charges payable by the borrower to Sanghamithra in accordance with its rules.

10. The borrower has produced a copy of the resolution passed by the borrower in their regular meeting accepting the terms and conditions of the financial assistance sanctioned and authorizing the representatives to execute the necessary documents

Schedule A

REPAYMENT SCHEDULE

Install No.	Due Date	Amount Rs.	Install No.	Due Date	Amount Rs.	Install No.	Due Date	Amount Rs.
1.			13.			25.		
2.			14.			26.		
3.			15.			27.		
4.			16.			28.		
5.			17.			29.		
6.			18.			30.		
7.			19.			31.		
8.			20.			32.		
9.			21.			33.		
10.			22.			34.		
11.			23.			35.		
12.			24.			36.		

IN WITNESS WHEREOF the parties hereto have affixed their respective signatures on the ______________ day of ______________________ 20___ first herein above written.

For SHGs
Name **Signature**

1. ______________ ______________

2. ______________ ______________

Witness:

1. ______________ ______________

2. ______________ ______________

For Sanghamithra
Name **Signature**

______________ ______________

______________ ______________

Witness:

______________ ______________

______________ ______________

(Normally taken on Rs.100/- stamp paper)

INTER-SE AGREEMENT EXECUTED BY THE MEMBERS OF THE SELF HELP GROUP

This Agreement made at ______________ on this ______________ day of ______________ 20______ between

1. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
2. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
3. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
4. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
5. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
6. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
7. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
8. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
9. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
10. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
11. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
12. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
13. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
14. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
15. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
16. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
17. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
18. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
19. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years
20. Shri/Smt/Kum. ______________ Son/Wife/Daughter of ______________ aged ______________ years

who are members of the ____________________ group, hereinafter referred to collectively as the Self-Help Group Members, or SHG Members in short, which expression shall, unless repugnant to the context or meaning, include every member of the said SHG and their respective legal heirs, executors and administrators.

WHEREAS all SHG Members are residents of ____________________ village, ____________ Taluk of ____________ District, ____________ State and are known to each other;

WHEREAS the SHG Members above named have joined voluntarily together and formed the SHG with intent to carry on savings and credit and other economic activities for mutual benefit subject to the terms and condition hereinafter appearing.

NOW THERFORE THIS AGREEMENT WITNESSETH THAT

1. Each member of the SHG shall save a sum of Rs.__________ (Rupees ____________ ____________________ only) or such sum as may be decided by the group by general consensus from time to time on weekly/ fortnightly/ monthly basis which shall be deposited with the authorized member of the group.

2. Each member shall strive for the success of the SHG and shall not act in any manner detrimental to the business interests of the SHG.

3. The SHG members shall be jointly and severally liable for all the debts contracted by the SHG.

4. All assets and goods acquired by the SHG shall be in the joint ownership of all the members of the SHG and shall ordinarily be in the constructive custody of such member as may be authorized by the group.

5. The SHG members hereby duly elect and appoint

   Shri./Smt./Kum.____________________ as ____________

   Shri./Smt./Kum.____________________ as ____________

   Shri./Smt./Kum.____________________ as ____________

   hereinafter called as authorized representatives to look after and manage the day to day affairs of the SHG's activities and also act in their name and their behalf in all matters relating thereto. The authorized representatives may, however, be changed at any time by majority vote of the members and new representatives elected in keeping with the management practices of the SHG.

6. Each of the SHG Members hereby agrees to abide by and ratify all such act, deeds and things as the authorized representatives may do in the interest of the group.

7. The authorized representatives shall take decisions in the day to day working of the SHG and each representative shall actively involve herself or himself and co-operate in looking after the day-to-day affairs of the SHG activity, in particular to attend to the following activities that are delegated to them.

8. The SHG members hereby specifically authorize the representatives:

   a) To keep or cause to be kept, proper books of accounts of the savings made by the SHG members, financial assistance/ loans granted to them and the recoveries made from them and render every year the full accounts to the SHG members for their approval and adoption.

   b) To receive all payment due to the SHG and issue requisite receipts or acknowledgements for and on behalf of the SHG.

   c) To institute and defend on behalf of the SHG Members, any legal proceedings and safeguard the interests of each member of the said SHG and for this purpose engage or disengage any lawyer or advocate or agent and incur the necessary legal expenses in connection therewith.

9. The SHG members hereby specifically authorize the above authorized representatives to open savings bank account, fixed deposits and other account in ________________ Bank and operate the same under the joint signature of any two of the above authorized representatives

Or

The SHG members hereby specifically authorize the following representatives to open savings bank account, fixed deposits and other account in ________________ bank and operate the same under the joint signature of any two of the representatives authorized for this purpose

Shri/Smt./Kum. ________________

Shri/Smt./Kum. ________________

Shri/Smt./Kum. ________________

10. Every member of the SHG hereby authorises the representatives to

a.) apply for financial assistance from Sanghamithra on behalf of the SHG and execute necessary agreements/documents and valid acknowledgement of debts/liability on behalf of the SHG for the purpose.

b.) collect financial assistance amounts from Sanghamithra on behalf of the SHG, deposit the same in the savings account of the SHG for onlending to members in accordance with the decision of the SHG and

c.) repay installments of SHG towards the settlement of financial assistance account of SHG with Sanghamithra

11. In the event of death of any of the members of the SHG, his/her legal heirs shall be entitled for the benefits and be liable for the obligations of the deceased member under this agreement.

12. It is agreed that no new person shall be included as a member of the SHG without consent of all the existing members.

IN WITNESS WHEREOF the aforesaid members of the SHG have set their respective hands hereunto at ________________ (place) on the ________________ (day) of ________________ (month) ________________ year.

Sl.	Name of the member of SHG	Signature
1		
2		
3		

Sl.	Name of the member of SHG	Signature
4		
5		
6		
7		
8		
9		
10		
11		
12		
13		
14		
15		
16		
17		
18		
19		
20		

INTRODUCTION LETTER

Date

From:

____

____

____

To:

Sanghamithra Rural Financial Services,
916, 8th Main, 3rd Stage,
Gokulam,
MYSORE- 570 002.

Dear Sir,

We have pleasure in introducing the following SHGs to you for a possible credit linkage. We know and have assessed them and find that their institutional strengths are adequate to make them viable institutions, which can use and repay loans effectively.

Sl.No.	Name of the SHG	Village
1		
2		
3		
4		
5		

We are confident about good credit behavior from the above-mentioned parties.

Thanking you,

Yours sincerely,

____

(Signature with seal)

FA01/01

SANGHAMITHRA RURAL FINANCIAL SERVICES

916, 8th Main, 3rd Stage , Gokulam, Mysore 570 002

SHG REGISTRATION FORM

Date : ____________________

To: Credit Manager
Sanghamithra, ____________________ Unit.

For Office use only

Regn. No.:
Regn. Fee chq ref.:

Dear Sir,

We are a group of people, organised in the form of a Self-Help Group We would like to collaborate with Sanghamithra to extend credit facilities to our members. Kindly register us as a linked SHG to Sanghamithra. We understand that this in no way binds us to borrow from Sanghamithra, nor does Sanghamithra agree to provide financial assistance for all or any of the purposes indicated in the form below.

1. Name of the Group ____________________
2. SHG code | | | | | | | | | | | | |
3. Type of Group : Men/Women/ Mixed
4. Specify Rural or Urban ____________________
5. Full Address:

   Village : ____________________ Post Office : ____________________

   Taluk : ____________________ District : ____________________

   Pincode : ____________________ Telephone : ____________________
6. Village Code : | | | | | | | | | | | | |
7. Date of Initiation ____________________
8. No. of members in our group: Female: __________ Male: __________ Total______
9. Meeting Place / Day / Time :____________________
10. Associated with NGO/ Other Development Organisation : ____________________
11. Group Leader(s) Name (in BLOCK LETTERS)

    Smt./Shri (1) ____________________ Smt./Shri (2) ____________________ and

    Smt./Shri (3) ____________________
12. Our Savings Bank Account details :

    Account No. ____________________

    Bank name: ____________________,

    Branch ____________________,

    Place____________________

    (enclosed xerox copy of bank Pass book)
13. We have taken-up some of the following group activities in addition to our Savings & Credit activities.
14. The following books of accounts / records are being maintained regularly and upto date by us/our group.(pl.tick)

a) Admission register b) Attendance register c) Minutes Book
d) Individual Pass book e) Cash /Bank Book f) Petty Cash Book
g) Individual Savings & Loan ledger h) General Ledger i) Trial Balance
j) Balance Sheet

15. Particulars of our members at present is given below. In case there are changes in our membership, we will inform you accordingly.

	Name (Start with Group Leaders)	Age	Sex	Caste# (Cat)	No . in the family		Land Holding (Acre)	Primary Occupation **(Category)	Activity under-taken with loan of the group (use code)x
					Adult	Children			
1									
2									
3									
4									
5									
6									
7									
8									
9									
10									
11									
12									
13									
14									
15									
16									
17									
18									
19									
20									

1-SC, 2-ST, 3-OBC, 4-Minority Community, 5-General
** 1-Rural Artisian, 2-Landless labour, 3-Marginal farmer, 4- Small farmer, 5-Other farmer, 6-Trade, 7- Service, 8-Wage Employment, 9-Fixed Employment
X 1-Farm Labour, 2- Cultivation, 3-Artisan, 4-Animal Husbandry, 5-Petty business, 6-Consumption, 7-Asset creation, 8- Others.

Kindly register us as a SHG linked to Sanghamithra.

Name and Signature of SHG Representatives

Name Signature

1. ____________________ ____________________
2. ____________________ ____________________
3. ____________________ ____________________

STATEMENT OF CONTINUITY

From

____

____

________________________________ Date: __________

To
Sanghamithra Rural Financial Services,
916, 8th Main, 3rd Stage Gokulam,
Mysore-570 002.

Dear Sir,

Sub: Continuity of Inter-se Agreement dated ________ regarding our SHG

We the undersigned office bearers hereby state that the constitution of the SHG remains unchanged and is as per the Inter-se Agreement executed on __________. We, the office bearers of this SHGs shall remain jointly and severally liable for the agreements made by this SHG/Federation.

Or

The following changes in the office-bearers of our SHG have taken place effective __________ vide the SHGS resolution no. ________ passed in our meeting held on __________.

Out going office bearers		Incoming office bearers	
Names	Signatures	Names	Signature
1.________	________	1.________	________
2.________	________	2.________	________
3.________	________	3.________	________

We jointly and severally affirm that while the incoming office bearers whose names and specimen signatures are detailed above will deal with you in all matters relating to our SHG with you, all the documents signed/ executed by the outgoing office bearers, including those who signed original documents remain and continue to remain valid and binding on us throughout the life of the transaction in reference.

In case of any further change in the constitution of the SHG for any reason whatsoever, the change will be made known to you within reasonable time.

Thanking You.

Yours faithfully,

Name & Signature of Office Bearers		Witness
1.________	________	1.________________
2.________	________	2.________________
3.________	________	3.________________

This booklet traces the growth of Sanghamithra Rural Financial Services (SRFS) from the time it was conceived till the fourth year of operations. However the process of setting up the MFI during the preparatory period between 1993 to 1999 has been described more in detail than the performance of the MFI after 1999 when it became operational.

Sanghamithra Rural Financial Services

916, 8th Main, 3rd Stage, Gokulam,
Mysore 570 002. Karnataka. India
Ph : 0821-2512300, 2512419
Fax : 0821-2512419
E-mail : sanmitra@sancharnet.in
Website: www.sanghamithra.net