Abstract
High transaction costs (TC) are one of the impediments to bank loans to the poor in low-income countries. As earlier studies have shown (Seibel & Dave 2002), bank TC can be lowered substantially by lending to self-help groups (SHGs) as financial intermediaries. Under the SHG Banking Program of the National Bank for Agriculture and Rural Development (NABARD) in India, over one million self-help groups with 16 million members (90% women), comprising some 90 million household members of the rural poor belonging to scheduled castes, were linked to 36,000 bank branches and financial cooperatives at commercial interest rates (March 2004). As the program, which in contrast to former programs is not mandatory, continues to grow rapidly, the question becomes all the more pertinent whether the success of financial intermediation by SHGs is due to overall lower TC or a shifting of TC to SHGs and their members. In Karnataka State, 78 SHGs with 1160 members were selected for a pilot study. TC of SHGs were found to be low, comprising real costs of 0.62% and opportunity costs of 0.60% of loans outstanding to members. Real costs of members were 0.04% and opportunity costs 2.3%. It is tentatively concluded that SHGs are an efficient intermediary for bank loans to vast numbers of the rural poor. The study provides a methodology that can be used in more representative national and local samples.

1 Support by Deutsche Gesellschaft fuer Technische Zusammenarbeit (GTZ) GmbH is gratefully acknowledged.
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Official exchange rate in February 2004:
Rs45.2 to the US$
Executive summary

SHG banking, the developing world’s largest program of banking with the poor: profitable for whom?

India has a highly differentiated rural financial sector, comprising some 50,000 bank branches and 92,000 cooperatives. Yet, the poorest 200 million and some 180 million of the rural near-poor are largely barred from formal rural finance. To cut across access barriers, the National Bank for Agriculture and Rural Development (NABARD), a rural apex bank, has made a bold move by promoting self-help groups (SHGs) as informal financial intermediaries, which mobilize their own resources and are refinanced by banks. During 1996-2004, SHG banking in India has grown to the developing world’s largest microfinance program for the rural poor, comprising around one million SHGs with a total of 16 million self-selected members, 90% of them women, credit-linked to some 36,000 bank branches and cooperative societies.

SHG banking has proven to be a highly successful social proposition to the poor, NGOs and GOs as facilitators, and banks; but is it also a commercial proposition? Conclusive evidence is lacking, as there is no national study with an agreed-upon methodology. A pilot study of bank transaction costs (TC) in a select few regional rural, commercial and cooperative bank branches, using both average and marginal cost analysis, found that social mobilization costs were largely externalised to non-governmental and governmental organizations, and direct bank TC were moderate. At repayment rates reportedly in the upper 90s percentile range, SHG banking was found highly profitable by the banks – more than any other rural financial product. In stark contrast, a pilot study of a select few regional rural banks, using a different methodology, found “that all the bank branches, irrespective of SHG promotion mechanisms are making substantial losses on this product”; and that this is partly “because banks prefer to carry out the entire scrutiny/appraisal process with each new SHG prior to lending… even when renewing credit lines.” Beyond these divergent findings, there is agreement that rural banks need to be reformed, interest rate structures adjusted, and SHG banking made more efficient.

Meanwhile, the question has been raised whether SHG banking is advantageous to the SHGs; or are they burdened with excessive transaction costs shifted by the banks? To answer this questions, a field study was carried out in Karnataka State (ranking in the middle HDI range among Indian states) in February 2004, comprising 78 SHGs linked to regional rural banks, commercial banks and primary cooperative societies under a district cooperative bank.

Basic SHG data

The 78 groups, on average three years old, comprised a total of 1160 members mostly from scheduled castes and tribes, 15 on average, 97% female. At repayment rates of mostly 98-100%, compared to overall bank repayment rates of 35-83%, they confirmed the paradox that the poor repay their bank loans, while many of the non-poor don’t.

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3 Micro-Credit Ratings International Ltd in cooperation with EDA (UK) Ltd: The outreach/viability conundrum: can India’s Regional Rural Banks really serve low-income clients? Gurgaon 2003; also available as an ODI Working Paper (supported by Overseas Development Institute, London).
4 Human Development Indicators
Internal resources amounted to US$ 1,187 per group, 64% derived from regular savings and 36% from interest earned – confirming that, given the chance, even the poorest can save, borrow and repay. At borrowing rates around 12% and lending rates around 24% (eff. p.a.), the interest rate margin represents a major source of income to the groups. Compulsory savings are credited to individual accounts within each SHG, withdrawable only when leaving the groups. In some groups, members deposit voluntary savings. About 30% of the members have personal bank accounts.

Loans outstanding per group amounted to an average of US$ 2,230\(^5\): 53% derived from internal funds and 47% from bank loans. Repayment problems are minimal. 67% maintained a single loan account irrespective of source of funds. Virtually all members had a loan outstanding, averaging US$148. The groups decide on loan sizes and maturities by consensus, taking need and creditworthiness into consideration.

Regular meetings are an important factor of group dynamics. 55% of the groups meet weekly, 31% monthly. Regular savings amount to US$1.20 per member and per months. Contrary to expectations, weekly meetings generate a mere 16% more in resources than monthly meetings.

**Transaction costs (TC) of SHGs and members**
TC include real costs incurred in Rupees and opportunity costs of time spent on meetings and transactions calculated at the local rate of wage labor. Opportunity costs of time spent are largely fictitious, as members and office-bearers rarely forego any income and are more than offset by indirect and intangible benefits, in addition to direct economic benefits. Main findings are:

- **Minimal SHG transaction costs:** Annual transaction costs of SHGs were found to amount to US$27 per group or 1.22% of loans outstanding to members (averaging US$ 2,230), comprising 51% real costs and 49% opportunity costs. Real costs are 0.62% and opportunity costs 0.60% of loans outstanding. Weekly meeting schedules, compared to monthly meetings, increase real costs by 41%, opportunity costs by 25% and total SHG TC by 34%. As TC are a more or less fixed amount, their relative share decreases as loans outstanding increase: from 4.9% of Rs 25,000 outstanding to 0.1% of Rs one million; or in the case of real TC, from 2.5% to 0.06%. Once outstandings exceed Rs 200,000, TC reach negligible proportions. Existing TC, particularly opportunity costs, are more than offset by indirect and intangible benefits.

- **Negligible member transaction costs:** Annual direct transaction costs of SHG members were found to amount to US$3.50 or 2.3% of loans outstanding (averaging US$148), which are almost fully opportunity costs. Calculating only real TC and adding indirect TC incurred by SHG office bearers, annual member TC amount to US$ 1, or 0.7% of average outstandings.

**Issues and recommendations**
TC of SHGs and members were thus generally found to be low so that immediate intervention is not required, except in the case of banks offering the recently

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\(^5\) Exchange rate in February 2004: US$1 = Rs45.2.
introduced government-sponsored *subsidy loans*, which have interfered with SHG banking and led to undue delays in loan allocations. On the whole, pending confirmation by nationally representative studies which are still lacking, it is tentatively concluded that SHG banking is highly profitable to banks and highly beneficial to SHGs and their members. NABARD, banks and NGOs should therefore continue expanding and deepening the program. Other countries, like Indonesia where SHG banking was first introduced on a national scale by the central bank (and supported by GTZ)\(^6\), may take a fresh look at the experience in India, which demonstrates how banking with the poor can be expanded on a vast scale if promoted with full force. Yet, unlike in Indonesia, most banks in India require SHGs to come to the bank, rather than taking the bank to the SHGs: an issue for the shaping of a demand-oriented banking culture in the framework of rural and agricultural bank reform.

As both internal resources and bank loans continue growing, so does the need for adequate training, control and supervision. NABARD may therefore be encouraged to facilitate, through banks and other cooperating partners, the annual reporting and auditing of key balance sheet and performance data of SHGs, including total assets of SHG, SHG loans outstanding to members, bank loans outstanding to SHG, return on assets of SHGs, and the ratio of non-performing loans.

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Introduction: rural finance and SHG banking in India

Rural finance in India: a highly differentiated sector
India has a highly differentiated rural financial sector, comprising some 50,000 bank branches and 92,000 cooperatives (2000). On average, there is one RFI for every four villages. Since 1982, liquidity is provided by the National Bank for Agriculture and Rural Development (NABARD) as an apex development bank with the mandate of agricultural and rural development. In a climate of incipient liberalization since the early 1990s, this has substantially increased the outreach of RFIs, with an overall saver outreach of 123 million and a borrower outreach of 72 million (2000). Yet, as noted by the World Bank (2003), India’s financial system has not been able to provide adequate access to the 193 million rural poor and another 180 million rural near-poor. Of the landless and marginal farmers, over 70% have no deposit account and 87% have no access to formal credit. Only 1% of all rural households have access to emergency loans. For the lowest segments of the rural population, the scheduled castes, access until recently has been virtually nil. Loan processing by RFIs reportedly takes 6-8 months. Approximately 10% of commercial loans and 15% of priority sector loans are non-performing (2002). At the prevailing (deregulated!) interest rates of 9-14%, rural banking is rarely profitable, and mostly incurs losses. This forces the banks to restrict their services and have their customers come to the bank instead of taking the bank to the customers. Some of the main shortcomings of rural finance in India are thus:

- lack of access to financial services by the rural poor and poorest
- excessive processing times of loans
- high default rates
- lack of profitability
- poor service.

SHG Banking: linking a million SHGs to banks by March 2004
In this situation, NABARD decided to cut across all access barriers and try a new strategy of banking with the rural poorest: linking banks and self-help groups, or SHG Banking. Inspired by NGOs in India and experience with linkage banking in Indonesia\(^7\), it started a pilot project in 1992, with promising results. As of 1996, it mobilized hundreds of NGOs and government organizations as support agencies and entered into national implementation, coordinated by its own Microcredit Innovations Department (MCID). “We either do it with full force – or not at all”, was the directive of the scheme’s initiator, Dr. Nanda, chairman of NABARD, who subsequently became the Raiffeisen, or Yunus, of banking with the poor in India.

The program’s target population are the very poor in rural areas, most of them belonging to the lowest population segments (the so-called scheduled castes and tribes). While the program has no bias-by-design to either men or women, 90% of the self-selected members turned out to be women.

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\(^7\) Seibel 1985; Kropp et al. 1989; Seibel & Parhusip 1992
SHG banking is not a nationally standardized bank product. Banks are free to determine, and change, their terms including interest rates on SHG loans, just as SHGs are autonomous in determining the terms of their loans to members. In recent years, bank interest rates to SHGs have shown a decreasing trend, fluctuating around 10% effective p.a. SHGs lend at around 2% p.m. on the declining balance, which is 24%. Some groups start as high as 36% p.a.; but given a steady increase in internal funds, there is a tendency to lower interest rates to below 20%. Internal funds and interest rates are not nationally monitored.

Groups save regularly for at least six months, using the savings as loanable funds. The groups are encouraged to open a bank account, but are not required to deposit any compulsory savings. To SHGs, the margin between interest paid to banks and interest received on loans to members is a major source of retained earnings. Regular savings and interest income are the two major sources of the groups’ loanable funds.

By March 2004, the time of the study, SHG banking had expanded to 523 districts in 30 states. 2800 partner organizations were involved in social mobilization and guidance. The cumulative number of SHGs credit-linked to banks had risen to 1,079,091 with an estimated 16 million members comprising a population of approximately 90 million of the rural poor. The programme continues to grow in outreach at extreme speed, with 361,731 new groups provided with bank loans during FY 2003-04 (a growth rate of 50.4%). A large, unrecorded number of groups have opened savings accounts with banks, but not yet reached the maturity to obtain bank credit. 38% of the groups are financed from banks’ own resources and 62% from NABARD liquidity credit.

As of March 2004, 560 banks with a total of 36,000 branches (including cooperatives) were involved: commercial banks accounting for 50% of credit linkages, regional rural banks for 39% and cooperative banks for 11%. 20% of the groups were formed and financed by banks; 72% were formed by governmental and non-governmental organizations and financed by banks; and 8% were formed and financed by NGOs, which were in turn refinanced by banks.

**SHG Banking: a social or a commercial proposition?**

Historically, rural banking in India has been driven by a strong concern for rural development and poverty alleviation. The degree of social commitment found in many banks, governmental and non-governmental organizations involved as well as in NABARD is extraordinary. This social commitment, together with liquidity made available by NABARD at market rates of interest, has been a major driving force behind SHG banking. To most bankers whom we met in India, rural banking, including SHG banking, is first of all a social proposition; their service mentality and the social service culture of their banking institutions is unquestioned. This is reflected in the rather limited interest evoked by questions of adequate interest rates,

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8 NABARD reports cumulative numbers of SHGs and cumulative disbursements, not loans outstanding as would be normal banking practice. Of the 1,079,091 SHGs credit-linked to banks, 56.4% were refinanced by NABARD by providing liquidity to the banks. As of March 2004, NABARD reports a cumulative volume of banks loans to SHGs of Rs 390.4 billion and a cumulative amount of refinance of 141.9 billion (36.3%), but not in constant prices. The reported figures cannot be converted into US$ without exact information on the amounts disbursed per year and the respective exchange rates. Applying the exchange rate of February 2004 of Rs45.2 to the US$ can provide but a very rough approximation.
profit maximization and financial incentives as rewards for individual performance, particularly in regional rural banks (RRBs) and cooperative banks.

Yet, there is a consensus in the international, and much of the Indian, rural and microfinance community shared by NABARD that for financial institutions, strategies and products to be sustainable, they must also be commercially viable, over and above any social concerns, lest banking turns into charity. NABARD has realized that if SHG banking is to reach 100, or more, out to 300 million of the rural poor in India and if financial services are to cover all their financial needs in adequate quantity and quality, it must assure adequate returns to all parties involved: banks, SHGs and members. In addition, vast numbers of non-governmental and governmental organizations bear social mobilization and SHG maintenance costs yet to be studied in depth. The overall picture is quite complex and presented in detail elsewhere, eg, by NABARD, Kropp & Suran, Harper, Seibel & Khadka, and Wilson.

To ascertain whether SHG banking is profitable or not, NABARD therefore commissioned a study of bank transaction costs, which was presented at the tenth anniversary celebrations of SHG Banking in India in October 2002. The study (Seibel & Dave 2002), which was indicative and provided a methodology rather than statistically valid results for all of India, arrived at the conclusion that, SHG banking, at repayment rates in the upper 90s percentage range, is highly profitable for the banks relative to other financial products, despite interest rates which are among the lowest in developing countries. In more detail, it was found that:

- Non-performing loans to SHGs reportedly were 0%, testifying to the effectiveness of group lending to the very poor. In contrast, consolidated NPL ratios of the bank branches ranged from 2.6% to 18% (by local standards, presumably higher by international accounting standards); and of Cash Credit (CC) and Agricultural Term Loans (ATL) up to 55% and 62%, respectively.
- Returns on average assets of SHG Banking ranged from 1.4% to 7.5% by average cost analysis and 4.6% to 11.8% by marginal cost analysis, compared to –1.7% to 2.3% consolidated. In contrast, ROA of Cash Credit varied from –10.2% to –0.5% and of ATL from –6.3% to 0.2%;
- The operational self-sufficiency of SHG banking ranged from 110% to 165% by average and 142% to 286% by marginal cost analysis, compared to 86% to 145% consolidated. In contrasts, OSS ratios of Cash Credit and ATL ranged from 54% to 102%.
- SHG Banking was found to be a robust financial product, performing well in healthy and in distressed financial institutions.
- Self-reliance of SHGs based on internal savings and retained earnings was found to be rapidly growing, exceeding in older groups the volume of bank refinance by an increasing margin. In addition SHGs deposit substantial amounts of savings voluntarily in banks as a reserve for bad debts.
- In addition SHG Banking has indirect commercial effects on banks in terms of improved overall vibrancy in banking activities.
- Indirect benefits at village level included the spreading of thrift and financial self-reliance and of a credit culture among villagers, microentreprise

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9 This study did not address the issue of the overall adequacy of interest rates of rural banks in India, but focused on the profitability of SHG banking within the given operational framework of the banks. There is evidence that banks would have to charge substantially higher interest rates to cover all costs, including risk costs and the capital costs of inflation, and to provide an adequate profit margin.
experience, growth of assets and incomes, the spreading of financial management skills, and the decline of private moneylending.

- **Intangible social benefits** were reportedly many: self-confidence and empowerment of women in civic affairs and local politics, improved school enrolment and women’s literacy, better family planning and health, improved sanitation, reduction of drinking and smoking among men, and a decline in adherence to local extremism.

The study left one major question unanswered: Is SHG banking perhaps profitable to the banks at the expense of SHGs? Or phrased differently: have banks shifted transaction costs to SHGs and their members, which now bear the brunt of high access costs?
2. The study of transaction costs in SHG banking

2.1 Objectives

As the programme continues to expand at a rapid pace, it is now deemed necessary to ascertain the suitability of the SHG banking approach, in particular taking into account client transaction costs at the SHG and individual member levels.

In a joint meeting with NABARD and GTZ, it was agreed that the following issues should be explored:

- What are the transaction costs of the SHGs and SHG members?
- What is the level of satisfaction of SHG clients with the existing service culture of the bank staff, an issue dealt with in a separate paper (by D. Rojahn)?
- *If transaction costs are found to be high*: How can transaction costs of SHGs and SHG members be further reduced?

Transaction costs (TC) are of crucial importance in evaluating financial products and their outreach. In SHG banking, there are several categories of transaction costs: those incurred by clients in getting loans and making deposits, the TC of SHGs as intermediaries between client-members and banks, and the bank’s TC. Additional transaction costs are incurred by governmental and non-governmental organizations as social mobilizers, by NABARD as the guiding, refinancing and supervisory agency, and by donors. TC studies, if any, are on banks; very few are on clients and SHGs. The relevance of TC studies lies in the analysis of trade-offs between the TC of clients, SHGs and banks. SHGs are assumed to absorb TC from both banks and poor clients and thereby make the poor bankable. In a new institutional economics perspective, banks, as institutions, are assumed to be *efficient*, ie, overall TC if borne by banks are reduced, through their direct services to SHGs, rather than shifted to clients. As bank TC were the subject of the preceding study in 2002, the emphasis in the present study is on the TC of SHGs and their members. In the same vein, SHGs as informal financial institutions are assumed to be *efficient*, ie, they provide access to bank services for people otherwise unbankable and reduce their TC by saving them many individual trips to the bank.

2.2 Study design

**Sampling:** For the study, NABARD selected three banks in Karnataka State, which in terms of the Human Development Index (HDI) and the Gender Development Index (GDI) ranks in the middle among the states in India (UNDP, 2003). The districts selected vary widely in terms of level of economic development, ranging from Bangalore Rural, one of the most, to Raichur District, one of the least developed district, which also ranks lowest among all districts of India in terms of HDI and GDI. The banks represent the three major types of rural banking institutions in India: regional rural banks (RRBs), commercial banks and district cooperative banks. Kalpatharu Grameena Bank, an RRB, had been selected for test interviews. The sample is not statistically representative for either India or Karnataka State. The study can at best be considered as indicative.

Field research was carried out in February 2004 with the assistance of staff from the NABARD branch office in Bangalore, banks and the Institute for Social and Economic
Change (ISEC), Bangalore. The sample included 78 SHGs in eight bank branches and three primary agricultural cooperative societies (PACS). The 78 SHGs comprised a total membership of 1160, 97% of them female. We estimate that all in all we met with some 800 members of the 78 groups. (Table 1)

<table>
<thead>
<tr>
<th>District</th>
<th>Bank and bank branch</th>
<th>Number of SHGs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bangalore:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bangalore Rural Tumkur</td>
<td>Kalpatharu Grameena Bank: Rajakunte, Brahmasandra Gate</td>
<td>9</td>
</tr>
<tr>
<td>Raichur</td>
<td>Tungabhadra Gramin Bank:</td>
<td>31</td>
</tr>
<tr>
<td></td>
<td>Matmari Branch</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Dongarpur Branch</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Jalahalli Branch</td>
<td></td>
</tr>
<tr>
<td>Mysore</td>
<td>Canara Bank:</td>
<td>19</td>
</tr>
<tr>
<td></td>
<td>Yelwal Branch</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Chamarajanagar Branch</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Bellur Branch</td>
<td></td>
</tr>
<tr>
<td>Hassan</td>
<td>Hassan District Central Co-operative Bank:</td>
<td>19</td>
</tr>
<tr>
<td></td>
<td>Balupet PACS</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Arehally PACS</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Nittur PACS</td>
<td></td>
</tr>
<tr>
<td><strong>Total no. of SHGs</strong></td>
<td></td>
<td><strong>78</strong></td>
</tr>
<tr>
<td><strong>Total membership</strong></td>
<td></td>
<td><strong>1160</strong></td>
</tr>
</tbody>
</table>

Methods and instruments: The study, which is not based on a representative sample, may be considered as a pilot-test of a questionnaire instrument for the study of TC of SHGs and their members (Annex3). The methodology evolved during the study. As new types of costs emerged in new locations and were subsequently included in the questionnaire, we cannot exclude that some cost items escaped our attention in the earlier-studied SHGs.

The questionnaire instrument comprises four parts:

A. General information  
B. Transaction costs of SHGs  
C. Transaction costs of members  
D. Issues and suggestions

SHG TC are covered by items 16-29 in Part B, member TC by items 33-35 in Part C. In both cases, real expenditures in Rupees and opportunity costs of time spend on meetings and transactions are included, the latter on the basis of average local rural wages calculated separately for women’s and men’s groups according to items 31 and 32.

The data are contained in an SPSS data file, which can be made available upon request.

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10 Prof. Rajshekar of the ISEC made invaluable contributions to the design of the questionnaire.  
11 Such is the situation if there is no opportunity for adequate pretests of the instruments and their adaptation to a range of local conditions. This is why we are saying that this is more a pretest of a methodology than a study with finite results.  
12 This data file can only be read by the SPSS program.
2.3 Basic SHG data

Characteristics of groups
78 groups were included in the study. 76 groups were women’s groups, two were men’s groups. The 78 groups comprised a total of 1160 members, 97% of them female.

About two-thirds of the groups were established in 2000 and 2001: 20% in 2000 and 45% in 2001. 26% of the groups were established during 1995-99, and 9% during 2002-03\textsuperscript{13}. On average, the groups are approximately three years old.

Figure 1: Year of SHG-establishment in sample

Group size varied from 10 to 20; the average was 15 members. 97% of the members were female, a slight overrepresentation compared to the reported overall Indian average of 90%. In 88% of the groups, literacy rates are below 40%.

Repayment performance of SHGs
This study has confirmed the excellent repayment performance of SHGs, as reported in the earlier study of Bank TC, which contrasts starkly to the overall (consolidated) repayment performance of the bank branches visited. Repayment rates of the branches and PACS, each taken as a whole, varied from 35% to 83%, repayment rates of the SHGs from 95 to 100%, with six of the institutions reporting repayment rates of 99-100%. (Table 2)

\textsuperscript{13} SHGs established in 2002 and 2003 were mostly left out as linkages with banks were just emerging during their first one or two years in existence.
Table 2: Repayment rates in bank branches and cooperatives, 2003

<table>
<thead>
<tr>
<th>Bank and bank branch</th>
<th>Consolidated</th>
<th>SHG Banking</th>
<th>SHG share of total outstandings in %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kalpatharu Regional Rural Bank:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rajakunte</td>
<td>74%</td>
<td>100%</td>
<td>22</td>
</tr>
<tr>
<td>Brahmasandra Gate</td>
<td>98%</td>
<td>28</td>
<td></td>
</tr>
<tr>
<td>Tungabhadra Regional Rural Bank:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Matmari Branch</td>
<td>67%</td>
<td>95%</td>
<td>1</td>
</tr>
<tr>
<td>Dongarpur Branch</td>
<td>62%</td>
<td>100%</td>
<td>1</td>
</tr>
<tr>
<td>Jallahalli Branch</td>
<td>35%</td>
<td>100%</td>
<td>2</td>
</tr>
<tr>
<td>Canara Bank:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Yelwal Branch</td>
<td>77%</td>
<td>98%</td>
<td>3</td>
</tr>
<tr>
<td>Chamarajanagar Branch</td>
<td>78%</td>
<td>99%</td>
<td>1</td>
</tr>
<tr>
<td>Bellur Branch</td>
<td>67%</td>
<td>99%</td>
<td>4</td>
</tr>
<tr>
<td>Hassan District Central Co-operative Bank:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jammanahally PACS</td>
<td>83%</td>
<td>100%</td>
<td>4</td>
</tr>
<tr>
<td>Arehally PACS</td>
<td>70%</td>
<td>98%</td>
<td>12</td>
</tr>
<tr>
<td>Nittur PACS</td>
<td>72%</td>
<td>96%</td>
<td>6</td>
</tr>
</tbody>
</table>

SHG finances

The 78 groups have accumulated on average internal resources amounting to Rs 53,647 (US$ 1,187)\(^{14}\) per group: 64% derived from regular savings and 36% from retained earnings (from interest earned, fines).\(^ {15}\) The margin between interest paid to banks, ranging from 10.75% to 12.5% p.a., and interest received from members averaging 24% represents a major source of income and dynamic growth of fund.

Given an average group age of three years, internal accumulated resources amount to approximately US$ 24 per member per year or US$ 2 per member per month. Resulting from the savings-driven nature of the groups\(^ {16}\), this is an impressive achievement deserving further study, given the extreme poverty of the members at the time of entering the groups.

Average loans outstanding per group amounted to Rs 100,800 (US$ 2,230): 53% derived from internal funds and 47% from bank loans.

Table 3: Average internal funds and loans outstanding in 78 SHGs

<table>
<thead>
<tr>
<th></th>
<th>Average SHG internal fund: Rs 53,647</th>
<th>Percent savings: 64%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average loans outstanding: Rs 100,800</td>
<td>Percent internal fund 53%</td>
<td>Percent bank loan 47%</td>
</tr>
</tbody>
</table>

\(^{14}\) The official exchange rate to the US$ in February 2004 was Rs 45.2.

\(^{15}\) As there are no balance sheets and income statements, no distinction is made here between “retained earnings in previous years” and “current year profit”. In fact, the current state of bookkeeping does not permit fine distinctions.

\(^{16}\) In credit-driven groups, internal resource mobilization is starkly weaker. In P4K in Indonesia for instance, groups that had been in existence for several years were found to have internal resources of $1 and compulsory bank deposits of $6 per member, and a fraction thereof if calculated per year.
Most groups operate on a zero-cash principle, keeping virtually no cash at hand. The average was found to be US$10. Bank deposits are relative small, amounting to US$160 on average.

**Terms and conditions of SHG loans to members**
67% of the groups maintain a single loan account with identical terms and conditions for loans from internal and bank funds, while 33% differentiate according to source of funds. In Table 3, the loan terms reported in the column *internal resources* pertain to either a single account (where groups do not differentiate between source of funds) or a separate account of internal resources. The column *bank resources* only applies to groups which apply different terms to loans to members from bank resources.

- At the time of the interview, almost all members had a loan outstanding; 94% of members had a loan from internal or single accounts and 84% from separate bank resource accounts.
- Decisions on loan terms were reported to be always based on consensus, taking into consideration a mix of need as expressed by each member and creditworthiness as assessed by the group.
- Loan sizes to members vary in most groups. They were reported to be equal by 5% of the groups in case of loans from internal or single accounts and by 30% in case of loans from separate bank resource accounts.
- Group leaders (usually a chairperson and a secretary, or representative one and representative two) tend to take loans closer to the middle of the scale in case of single or separate internal accounts, averaging 61% of the biggest loan granted to any member; and more at the upper end of the scale in case of separate bank resource accounts, averaging 81% of the biggest loan granted to any member.
- Interest rates do not differ much by source of funds; at an average of 23%, they are slightly lower for loans from separate bank resources, compared to 27% of loans from internal or single accounts; but the difference is not statistically significant.
- Maturities of loans to members averaged 11 months from single or internal accounts and 19 months from separate bank resource accounts.
- Instalment periods in most groups were monthly, regardless of source of funds (63% and 65%, respectively). In most other cases, they were weekly (27% and 35%, respectively). In the few remaining cases, they were fortnightly, seasonally or annually.
- 86% of the groups with single or separate internal resources and 100% of groups with separate bank resource accounts reported that there were no arrears.
<table>
<thead>
<tr>
<th>Table 4: Terms of loans to members from internal and bank resources</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Internal resources</strong></td>
</tr>
<tr>
<td>------------------------</td>
</tr>
<tr>
<td>Number of SHGs</td>
</tr>
<tr>
<td>Percentage</td>
</tr>
<tr>
<td>Members with loan outstanding</td>
</tr>
<tr>
<td>Equal size of loans to members</td>
</tr>
<tr>
<td>Loan size of leaders in % of biggest loan</td>
</tr>
<tr>
<td>Interest rate:</td>
</tr>
<tr>
<td>Mean</td>
</tr>
<tr>
<td>Range</td>
</tr>
<tr>
<td>Loan period (maturities):</td>
</tr>
<tr>
<td>Mean</td>
</tr>
<tr>
<td>Range</td>
</tr>
<tr>
<td>Instalment periods:</td>
</tr>
<tr>
<td>Monthly</td>
</tr>
<tr>
<td>Weekly</td>
</tr>
<tr>
<td>Other</td>
</tr>
<tr>
<td>Overdues:</td>
</tr>
<tr>
<td>Percent of SHGs</td>
</tr>
<tr>
<td>Percent of outstandings</td>
</tr>
</tbody>
</table>

*Single account for both internal and bank resources or separate internal account
**If separate from internal resources, otherwise included in internal resources.

**Group meetings**

Most groups meet weekly (55%); 31% meet monthly and 14% fortnightly. There are major differences between the banks in our sample: through influence by Myrada, a major participating NGO, the groups linked to Canara Bank and Hassan DCCB all meet weekly, while the groups under Kalpatharu RB all meet monthly. Only in Tungabhadra RB is there variation with regard to meeting schedules. Group meetings last from 0.5 to 2.5 hours; the average is 1.5 hours.

In most groups the meetings are held at times when members are not occupied with income-generating activities. 92% of the groups reported that members do not forgo income when they attend meetings; in 8% of the groups, members may forego earnings, but only during high season, which averages around three months per year.

<table>
<thead>
<tr>
<th>Table 5: Meeting schedules of SHGs by bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank</td>
</tr>
<tr>
<td>----------------</td>
</tr>
<tr>
<td>Kalpatharu RB</td>
</tr>
<tr>
<td>Tungabhadra RB</td>
</tr>
<tr>
<td>Canara Bank</td>
</tr>
<tr>
<td>Hassan DCCB</td>
</tr>
<tr>
<td>Total</td>
</tr>
<tr>
<td>Percent</td>
</tr>
</tbody>
</table>

The influence of SHG meeting schedules on savings

Experience elsewhere has shown that the amount of savings mobilized is strongly influenced by the frequency of savings collection, preferably weekly or even daily as opposed to monthly. In our sample of 78 groups, the influence of meeting schedules
on savings mobilized per month is weak, increasing by a mere 16% from average monthly savings of Rs 50 in case of monthly meetings to Rs 58 in case of weekly meetings.

### Table 6: Monthly savings per member

<table>
<thead>
<tr>
<th>Meeting schedule</th>
<th>Amount in Rs</th>
<th>Minimum</th>
<th>Maximum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Weekly</td>
<td>58</td>
<td>20</td>
<td>96</td>
</tr>
<tr>
<td>Fortnightly</td>
<td>46</td>
<td>20</td>
<td>54</td>
</tr>
<tr>
<td>Monthly</td>
<td>50</td>
<td>10</td>
<td>100</td>
</tr>
</tbody>
</table>

Member savings in the group and in the bank

All groups have regular compulsory savings, credit to members’ individual accounts, usually in passbooks issued by the groups. Regular member savings are a major source of loanable funds. They may only be withdrawn when a member leaves a group. In a few groups, we observed\(^\text{17}\) that members may also deposit voluntary savings, which are added to their personal account but cannot be withdrawn at will.

Three main options of regular savings were found in the groups: (i) monthly savings of Rs 50 per member in 31% of the groups; (ii) weekly savings of Rs 10 per member in 32% of the groups; and (iii) weekly savings of Rs 20 per member in 17% of the groups. On average, regular savings amount to Rs 54 (US$1.20) per member and per month.

Individual bank accounts of members were not systematically studied. However, it was found that 240 of the members present at groups meetings during the field research had a bank account. On that basis, we estimate that around 30% of the members have a bank account. About half of them opened their bank account after joining the group.

\(^{17}\) This was not systematically recorded.
3. Transaction costs (TC) of SHGs and members

3.1 Methodology
The study is based on 78 SHGs in Karnataka State in February 2004 (as described above), using a questionnaire instrument (Annex 3). Two types of costs were included: (i) real costs incurred in Rupees \(^{18}\); and (ii) opportunity costs. Only those costs were included that were considered essential for obtaining or servicing a loan. \textit{Real costs of SHGs} included mainly transportation costs of office-bearers, remuneration of external book-writers and auditors, loan documentation, stationery and photos. \(^{19}\) \textit{Real costs of members} included mainly costs of photos, transportation costs and fees for no-objection certificates \(^{20}\); their real costs may be somewhat underestimated, as we cannot be sure to have captured all expenses. Social mobilization costs of establishing new groups and externalised maintenance costs are not included here.

\textit{Opportunity costs} of both, office-bearers and members, are largely fictitious, for two reasons: (i) there is no income foregone, except in rare cases; and (ii) the opportunity costs are more than offset by indirect and intangible benefits, such as self-confidence in private and public spheres, familiarity with financial matters, and personal access to banks and government programs. However, both types of costs, real and opportunity, are being reported here.

Opportunity costs of SHGs or members included the value of time spent on meetings, financial matters outside of meetings and bank-related travel. As the groups are genuine self-help groups with financial and non-financial objectives and activities, only that portion of the meeting time pertaining to financial matters was included. Only the opportunity costs of unpaid office-bearers (usually two) were included in the calculation of SHG opportunity costs. In the case of individual member TC, the time spent on financial matters was included.

The opportunity costs were calculated separately for women and men at their respective rural daily wage rate as stated by each group, weighted according to the number of months of high and off-season. Eg, a wage rate for women of Rs 40 per day during 3 months of high season and of Rs 30 per day during 9 months of off-season yields an average wage rate of Rs 32.5. However, this is an overestimate, as most women are unemployed during low season.

\begin{table}
\centering
\begin{tabular}{|l|c|}
\hline
 & Average daily rural wage rates as stated by 78 SHGs \\
\hline
Women during 4 months of high season: & Rs 36 \\
Women during 8 months of off-season: & Rs 27 \\
Weighted mean: & Rs 30 \\
\hline
Men during 4 months of high season: & Rs 54 \\
Men during 8 months of off-season: & Rs 44 \\
Weighted mean: & Rs 47 \\
\hline
\end{tabular}
\end{table}

\(^{18}\) Borne by the SHGs in case of SHG TC and by the members in case of member TC. \\
\(^{19}\) In a few cases, costs of documentation and stationery were subsidized and not included in the cost calculations. \\
\(^{20}\) Required only by some banks. No-objection certificates are issued by other banks, certifying that the member has no unpaid loans outstanding.
Regarding the opportunity costs of office-bearers, we also asked what would be a fair remuneration if any would be paid. 15 SHGs found it ludicrous to even consider paying remuneration and refused to state an amount. The remaining 63 SHGs gave Rs 50 (US$1.10) as a fair amount per month. We did not use this figure in our calculations, but the rural wage rate instead, which was universally available.

TC of SHGs are presented below in terms of the average of actual loans outstandings of SHGs to their members, amounting to **Rs 100,800 (US$ 2,230)**. TC of members are presented in terms of the average of actual loans outstanding per member, amounting to **Rs 6,691 (US$ 148)**.

### 3.2 Transaction costs of SHGs

Annual TC in terms of average loans outstanding: TC of SHGs amount to 1.22% of loans outstanding to members, or, in real terms, Rs 1,230 (US$27) over Rs 100,800 loans outstanding (or Rs 85 per member). They are equally divided in real costs (accounting for 51% of total TC) and opportunity costs (accounting for 49% of total TC). Real TC are 0.62%, opportunity costs 0.60% of loans outstanding. (Table 8)

<table>
<thead>
<tr>
<th>TC of SHG</th>
<th>Mean in Rs</th>
<th>SD**</th>
<th>Min</th>
<th>Max</th>
<th>TC in %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real costs***</td>
<td>630</td>
<td>518</td>
<td>0</td>
<td>1784</td>
<td>0.62</td>
</tr>
<tr>
<td>Opportunity costs</td>
<td>600</td>
<td>366</td>
<td>0</td>
<td>1782</td>
<td>0.60</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1230</strong></td>
<td><strong>657</strong></td>
<td><strong>230</strong></td>
<td><strong>2968</strong></td>
<td><strong>1.22</strong></td>
</tr>
</tbody>
</table>

*Average volume of loans outstanding to members per SHG: **Rs 100,800 (US$ 2,230)**

** SD = standard deviation. The large size of the SD is related to the small size of the sample and the relative weight of extreme values.

*** Real in terms of actual expenses in Rupees.

More detailed data of the composition of real and opportunity costs are presented below in Tables 9 and 10.

### Table 9: Mean opportunity costs of SHG office-bearers per SHG (in hours per month)

<table>
<thead>
<tr>
<th>Time spent on:</th>
<th>Mean no. of hours</th>
<th>Standard deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial matters in meetings</td>
<td>4.70</td>
<td>3.49</td>
</tr>
<tr>
<td>Financial matters outside meetings</td>
<td>0.34</td>
<td>1.14</td>
</tr>
<tr>
<td>(Regular) bank travel and transactions</td>
<td>9.59</td>
<td>7.89</td>
</tr>
<tr>
<td>Accessing current loan (recalculated p.m.)</td>
<td>1.06</td>
<td>1.11</td>
</tr>
</tbody>
</table>
Table 10: Mean real transaction costs per SHG (in Rupees per year)

<table>
<thead>
<tr>
<th>Cost item</th>
<th>Amount</th>
<th>Standard deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Remuneration of office-bearers</td>
<td>18</td>
<td>93</td>
</tr>
<tr>
<td>External book-writer</td>
<td>200</td>
<td>330</td>
</tr>
<tr>
<td>(Regular) travel expenses to bank</td>
<td>177</td>
<td>332</td>
</tr>
<tr>
<td>Travel expenses for accessing current loan</td>
<td>28</td>
<td>82</td>
</tr>
<tr>
<td>Stationery</td>
<td>76</td>
<td>94</td>
</tr>
<tr>
<td>Loan documentation</td>
<td>78</td>
<td>75</td>
</tr>
<tr>
<td>Other cash expenses</td>
<td>41</td>
<td>120</td>
</tr>
</tbody>
</table>

TC in terms of increasing loan volumes: TC tend to be an absolute amount which does not vary by the size of loans outstanding. Thus, as the financial volume of SHGs increases on a putative scale\(^{21}\), the relative size of TC decreases: from 5% of loans outstanding of Rs 25,000, to 0.25% of outstandings of Rs 500,000, and to 0.1% of outstandings of one million. The respective percentages of real TC are 2.5%, 0.1% and 0.06%. (Table 11)

Table 11: Real and total TC\(^*\) p.a. in % of putative outstandings

<table>
<thead>
<tr>
<th>Loans outstanding</th>
<th>Real TC</th>
<th>Total TC</th>
</tr>
</thead>
<tbody>
<tr>
<td>25,000</td>
<td>2.52</td>
<td>4.92</td>
</tr>
<tr>
<td>50,000</td>
<td>1.26</td>
<td>2.46</td>
</tr>
<tr>
<td>100,000</td>
<td>0.63</td>
<td>1.23</td>
</tr>
<tr>
<td>200,000</td>
<td>0.32</td>
<td>0.62</td>
</tr>
<tr>
<td>300,000</td>
<td>0.21</td>
<td>0.41</td>
</tr>
<tr>
<td>400,000</td>
<td>0.16</td>
<td>0.31</td>
</tr>
<tr>
<td>500,000</td>
<td>0.13</td>
<td>0.25</td>
</tr>
<tr>
<td>1,000,000</td>
<td>0.06</td>
<td>0.12</td>
</tr>
</tbody>
</table>

\(^*\)Real TC: Rs 630; total TC: Rs1230. Real TC means: actual expenditure, excluding putative opportunity costs.

The following graph shows how transaction costs decline rapidly and reach negligible proportions once loans outstanding exceed Rs. 200,000: an amount reached by many groups older than three years. The upper curve shows total TC, the lower curve real TC (expenditures in Rupees).

\(^{21}\) This is not a predictive scale of what will, or should happen in terms of bank refinance over time. In fact, there is evidence that within the given framework of economic conditions (i.e., limited investment opportunities), there is a tendency for increasing internal group funds counteracting the growth of a demand for external finance.
Differences between banks: TC vary by bank. In absolute terms, they vary from a low of Rs. 507 in Kalpatharu RB, where groups were in the immediate vicinity of the bank and meetings were held monthly (as shown in Table 4), to a high of Rs 1583 in the three PACS under Hassan DCCB, where groups were more remote. In relative terms, they range from 0.2% to 2.3%, reflecting sizeable differences in average outstandings varying from Rs 50,000 to Rs 242,000. (Table 12)

Table 12: TC of SHGs by bank (in % of loans outstanding to members)

<table>
<thead>
<tr>
<th>Bank</th>
<th>Amount outstand’g</th>
<th>TC/SHG</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kalpatharu RB</td>
<td>242,000</td>
<td>507</td>
<td>0.2</td>
</tr>
<tr>
<td>Tungabhadra RB</td>
<td>50,000</td>
<td>1139</td>
<td>2.3</td>
</tr>
<tr>
<td>Both RRBs</td>
<td>90,000</td>
<td>997</td>
<td>1.1</td>
</tr>
<tr>
<td>Canara Bank</td>
<td>123,000</td>
<td>1370</td>
<td>1.6</td>
</tr>
<tr>
<td>Hassan DCCB</td>
<td>102,000</td>
<td>1583</td>
<td>1.6</td>
</tr>
<tr>
<td>Grand mean</td>
<td>100,800</td>
<td>1230</td>
<td>1.2</td>
</tr>
</tbody>
</table>

The influence of SHG meeting schedules on TC: TC vary by the meeting schedules of groups: from Rs 962 in groups with monthly meetings to Rs 1,447 in groups with weekly meetings (Table 13). TC of SHGs with weekly meeting schedules exceed TC of SHGs with monthly schedules, in terms of:

- Real costs by 41%
- Opportunity costs by 25%
- Total costs by 34%

Table 13: TC of SHGs by meeting schedule

<table>
<thead>
<tr>
<th>Meeting schedule</th>
<th>N</th>
<th>Real costs</th>
<th>Opp. costs</th>
<th>Total TC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Weekly</td>
<td>43</td>
<td>763</td>
<td>685</td>
<td>1447</td>
</tr>
<tr>
<td>Fortnightly</td>
<td>11</td>
<td>504</td>
<td>463</td>
<td>967</td>
</tr>
<tr>
<td>Monthly</td>
<td>24</td>
<td>451</td>
<td>511</td>
<td>962</td>
</tr>
<tr>
<td>Grand mean</td>
<td>78</td>
<td>630</td>
<td>600</td>
<td>1230</td>
</tr>
</tbody>
</table>
The influence of group size on TC
TC of SHGs (recalculated per member) decline slightly with increasing group size. Statistically, the influence of group size is negligible ($r=-0.22$, sig. 0.057).

3.3 Transaction costs of SHG members

TC of members are largely opportunity costs incurred from attending meetings, amounting to Rs 153 or 2.3% of loans outstanding. Real costs are a negligible Rs 3 or 0.04%; they are marginally higher if adjusted for underestimations (perhaps Rs 12 or 0.16%). Total costs are Rs 156 or 2.3%. real TC of SHGs and members are added, the total is Rs 46 per member or 0.7% of member loans outstanding. (Table 14)

Table 14: Direct TC of members p.a.

<table>
<thead>
<tr>
<th>TC of members</th>
<th>Amount in Rs</th>
<th>% of loan outstanding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opportunity costs</td>
<td>153</td>
<td>2.3</td>
</tr>
<tr>
<td>Real costs</td>
<td>3</td>
<td>0.04</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>156</strong></td>
<td><strong>2.3</strong></td>
</tr>
<tr>
<td>SHG real TC per member</td>
<td>43</td>
<td>0.6</td>
</tr>
<tr>
<td><strong>Grand total of TC</strong></td>
<td><strong>199</strong></td>
<td><strong>3.0</strong></td>
</tr>
<tr>
<td><strong>Grand total of real TC</strong></td>
<td><strong>46</strong></td>
<td><strong>0.7</strong></td>
</tr>
</tbody>
</table>

*Average total loan outstanding per member: Rs 6691 (US$148)

Savings and credit TC: If we differentiated between the TC (in terms of real expenditures) of savings mobilization and lending according to the respective volumes involved, we arrive at savings TC of 0.24% and credit TC of 0.45% per member:

- Real TC on savings balance: 0.24%
- Real TC on loans outstanding: 0.45%
- Total real TC: 0.69%
4 Summary and conclusions

4.1 Summary

(1) TC of SHGs:
- TC of SHGs are minimal
- Half the TC are real costs and half are putative opportunity costs, which are largely fictitious as they do not involve any income forgone
- From loans outstanding above Rs 200,000 TC are negligible

(2) TC of members:
- Direct and indirect TC of members are negligible

(3) TC and intangible benefits:
- TC are more than balanced by intangible benefits of office bearers and individual members

(4) Explicit demands of SHGs:
- Bank loans: bigger loans
- SHG loans: no additional explicit demands
- Training: income-generating activities, financial management
- TC: no specific demands

(5) Implications for NABARD:
- TC of SHGs and members are generally no issue requiring intervention
- However, subsidy loans offered by government have interfered with the smooth functioning of SHG banking, disrupting the sequencing of repeat loans (mostly of increasing size) and imposing, in some banks, undue waiting periods
- Many banks require the SHGs to come to the bank, rather than bringing the bank to the people: an issue not so much for TC, which are small, but for the shaping of a demand-oriented banking culture (dealt with below)

4.2 Issues and recommendations

(1) Auditing and reporting

As internal resources of SHGs from member savings and retained earnings and external resources from bank loans continue growing, so does the need for internal control and external supervision. A number of groups pay already for external control of their books by NGOs or federations; but the external examiners are neither properly trained nor supervised. In particular, no evidence was found of examiners providing, or assisting the book-writers to provide, a balance sheet, which could easily be constructed on the basis of the existing data in the groups’ books. It is
suggested to NABARD to facilitate the following through its cooperating partners in the field including banks:

- The monthly balancing of accounts
- Annual or semi-annual auditing and reporting of balance sheet data.

The following system of auditing and reporting is suggested:

(1.1) **Preparation of balance sheets and profit & loss statements:**

- by SHGs with the assistance of their respective guiding organizations (federations, NGOs, GOs, banks, PACS)
- to be reported to linkage bank branch or PACS

▶ A model balance sheet and profit & loss statement are provided in Annex 5.

(1.2) **Auditing of SHG balance sheet and profit & loss statements:**

- by linkage banks and bank branches

(1.3) **Reporting of key SHG balance sheet and performance data to NABARD:**

- by linkage banks

(1.4) **Key data to be reported:**

- Total assets of SHG
- Total net loans outstanding to members
- Total bank loan outstanding to SHG
- Return on assets (ROA) of SHG (\( \text{Profit/Total Assets} \)) at year-end
- NPA or NPL [to be decided!] of SHG (overdue more than 90 or 180 days?)

(1.5) **Monitoring and supervision of partner organizations:**

- Monitor federations, NGOs and GOs
- Supervise federations and NGOs if financial intermediaries

(2) **Training:**

To guarantee the quality of financial management in groups and prevent fraud, it is recommended to NABARD to organize and facilitate adequate training for

- book-writers
- book-examiners and auditors

(3) **Saving**

(3.1) **Individual savings in the group**
All groups have regular savings, credited to members’ accounts and withdrawable only upon leaving the group. Some groups also accept voluntary savings, which are not withdrawable at will. Savings, together with interest income grow continually and eventually become the main source of loanable funds, exceeding bank funds.

Easy access to voluntary savings would be a substitute for emergency loans by SHGs or moneylenders. To advanced groups, with loans outstanding to members (eg) above Rs 200,000, it is recommended:

- To encourage internal voluntary savings collection
- To manage liquidity alternatively from small cash funds, early repayments and bank deposits.

**(3.2) Graduation to individual bank relations**

The field of individual bank relations for members with investment opportunities beyond the financing capacity of the groups has been prepared by the involvement of office-bearers and members in bank transactions. Approximately 30% of SHG members in our study (presumably more in more advanced areas) have already an individual bank account. Most banks appear unaware of the future potential of having enterprising SHG members graduate to individual bank relations. I

In advanced SHGs, we therefore recommend to banks to provide opportunities to enterprising members for graduation to individual savings accounts and individual loans, based on their track record in the group.

**4.3 Conclusions**

The study has shown that transaction costs of a non-representative sample of 78 SHGs and their 1160 members are low and decrease rapidly with increasing loan volumes. The study provides a methodology that can be used in more representative national and local samples.

- While there is no urgency to intervene, in the interest of overall efficiency the TC of the SHGs can, and should be, further reduced by simplifying and standardizing the repeat loan process for groups with a good track record; and by speeding up the process of loan examination and disbursement.

- Beyond the scope of this study, it has been observed that the relatively smooth process of bank linkages is being disrupted by the easy money of new government-supported subsidy programs, resulting in considerable delays in disbursement, interruptions in the sequence of repeat loans, and higher risks.

- As a by-product of this study, perhaps the most important conclusion is that the rapid increase in internal funds of totally unregulated and unsupervised SHGs with wholly inadequate and intransparent book-keeping practices requires immediate action, presumably at a moderate cost: the standardization of book-keeping, the preparation of annual balance sheets, and annual auditing of the SHGs by the participating banks under the guidance of NABARD.
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