APRACA FinPower Program No. 1

COMPLETION REPORT:

FinPower Microfinance Development Forum – Dialogue in Mongolia: Enabling Microfinance Policy Environment and Regulatory Framework

Facilitator:
Benedicto S. Bayaua

Documentor and Expert:
Praful Dholakia

An APRACA FinPower Publication with the Special Sponsorship of the International Fund for Agricultural Development (IFAD)

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This book is published during the incumbency of Mr. Abdurakhmat Boymuratov, APRACA Chairman, and Mr. Won-Sik Noh, APRACA Secretary General.

MESSAGE

Greetings!

APRACA has successfully established among its members machinery for systematic interchange of information on sustainable rural and agricultural financial services, encouraged inter-country studies and provided training, consultancy, research and publication services on matters of common interest in the field of rural finance and microfinance.

The FinPower National Microfinance Development Forum in Mongolia focusing on enabling microfinance policy environment and regulatory framework and interfacing with a technical support to key rural finance stakeholders is a testimony of APRACA's strong commitment to pursue the promotion of efficient and effective rural financial systems and broadened access to rural financial services in order to help reduce rural poverty among countries in Asia and the Pacific.

The International Fund for Agricultural Development or IFAD has played the role of APRACA's strategic partner under the FinPower Program. APRACA and IFAD share that mutual desire to pursue and create conducive rural finance policy environment and regulatory framework. I wish therefore to acknowledge the IFAD support to APRACA.

May we therefore thank Dr. Thomas Elhaut, IFAD Asia Division Director, and Dr. Ganesh B. Thapa, IFAD Regional Economist, for the trust and confidence they have continuously bestowed on APRACA and for their commitment to help alleviate poverty and accelerate rural growth and development among countries in Asia and the Pacific.

We wish to thank the Honorable Governor of Bank of Mongolia and the CEO of XacBank for supporting the conduct of the week-long program.

We sincerely wish that this report will continuously inspire policymakers, practitioners and other stakeholders in the Asia-Pacific region.

Abdurakhmat Boymuratov
APRACA Chairman

Acknowledgement

The International Fund for Agricultural Development (IFAD)-supported APRACA FinPower Program extends its sincere thanks to the Honorable Dr. Lkhanaasuren Purevdorj, Governor, Bank of Mongolia, for his gracious acceptance to host the forum and dialogue. Likewise, FinPower conveys its deep gratitude to Mr. B. Lkhagvasuren, Mr. D. Boldbaatar and other senior officers of Bank of Mongolia who provided guidance to the forum and dialogue.

FinPower gratefully acknowledges the support of Mr. Praful Dholakia, Assistant General Manager of the NABARD Consultancy Services (NABCONS) of India, who acted as international expert and documentor during the National Microfinance Development Forum and Dialogue in Mongolia.

FinPower also conveys its sincere gratitude to Mr. Sorinzonbold Lhagvasuren, 1st Deputy CEO, XacBank for sharing his thoughts on the Mongolian rural financial landscape. Our sincere gratitude is also due to Mr. Chuluuntseren Otgocguluu, Employment Policy Advisor to the President of Mongolia, Ms. Soyolmaa Erdenetsogt, Economist, Bank of Mongolia, Mr. Oyuntsetseg Chuluunbat, Director of Microfinance Banking Department (Retail), XacBank and Mr. A. Serik, Senior Officer, Rural Credit Department, Khan Bank for exchanging their ideas and providing critical field-assistance to APRACA.

I sincerely thank the excellent support provided by Mr. D. Dalantainyam, IFAD Rural Poverty Reduction Programme (RPRP) National Project Director to the successful conduct of the forum and dialogue.

Field assistance and cooperation received from Mr. Timothy Hooper, Executive Director, Vision Fund, Ms. Bayarsaikhan Dembereldash, Executive Director, Microfinance Development Fund (MDF), Ms. Doljinmaa Dorjpurev, CEO, ValueQ of Achid Finance Group, Ms. Oyunchimeg Togoodorj, Executive Director, Mongolian National Cooperative Association and Ms. Uranchimeg Navaansambuu, Program Coordinator (MEDP), ADRA are sincerely acknowledged.

Finally, FinPower conveys its deep gratitude to Ms. Ch. Ariunaa, forum and dialogue interpreter, who made an easier understanding of the Mongolian rural finance landscape.

Won-Sik Noh
Secretary General
APRACA

Acronyms and Abbreviations

APRACA	Asia-Pacific Rural and Agricultural Credit Association
BC	Business Correspondent
BF	Business Facilitator
CDR	Credit Deposit Ratio
CEUs	Currency Exchange Units
FinPower	Program for Accelerating the Financial Empowerment of Poor Rural Communities in Asia and the Pacific through Rural Finance Innovations
FRC	Financial Regulatory Commission
IFAD	International Fund for Agriculture Development
IRVs	Individual Rural Volunteers
JLG	Joint Liability Group
MDF	Microfinance Development Fund
MEDP	Microeconomic Development Program
MFIs	Microfinance Institutions
MFOs	Microfinance Organizations
NABARD	National Bank for Agriculture and Rural Development
NABCONS	NABARD Consultancy Services
NBFCs	Non-Banking Financial Companies
NBFIs	Non-Bank Financial Institutions
NGO	Non-Governmental Organization
RFC	Rural Finance Corporation
RPRP	Rural Poverty Reduction Programme
SBLP	SHG-Bank Linkage Program
SCC	Savings and Credit Cooperative
SCU	Savings and Credit Union
SHG	Self-Help Group
SHPI	Self -Help Promoting Institution
SME	Small and Medium Enterprise

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1. INTRODUCTION

1.1 Background

The rural financial markets of developing countries in Asia and the Pacific are in various stages of development with varying levels of experience. While several countries already have policy regimes that are fully liberalized and deregulated, there are still a number whose policy environment are either fully or partially characterized by credit subsidies, credit allocations and directed loans.

As acknowledged in many policy studies, a country should have a conducive rural finance policy environment that would allow financial institutions to operate in areas where there is demand for their services and, in effect, enable them to allocate their funds from surplus units ("savers") to deficit units ("borrowers") at a price that would make them recover their cost and generate sufficient yield to capital. An enabling policy environment, thus, implies deregulated interest rates, compliance with reasonable performance standards and regulations, especially with, *inter alia*, capital requirements, branching policy and risk management. Within such a policy environment, therefore, banks and other financial institutions will be able to operate prudently while providing adequate, sustainable and timely credit and other financial services to the rural sector, particularly the resource-poor. Simply put, a policy environment and regulatory framework that is conducive would mean increased and sustained credit access for the poor and rural households. Conversely, weak rural financial markets discourage rural growth.

However, despite policy reforms instituted, still some countries continue to experience lack of or limited access by the rural poor to credit. In fact, microfinance institutions (MFIs) still hesitate to lend to agriculture and related projects. Innovative approaches and practices have to be developed so that MFIs will be encouraged to lend to the poor in general and to the small farmers and fishermen in particular. For most MFIs, lending to the agriculture and related sector is deemed risky and, therefore, a costly lending activity. Clearly, microfinance work in agriculture is the biggest challenge.

1.2 IFAD-APRACA FinPower Program

Given these facts, not to mention the increasing importance of microfinance in poverty alleviation as seen from the impact of microfinance programs in some countries, the Asia-Pacific Rural and Agricultural Credit Association (APRACA), in partnership with the International Fund for Agriculture Development (IFAD), is currently implementing the IFAD-APRACA Regional Program of Accelerating the Financial Empowerment of Poor Rural Communities in Asia and the Pacific through Rural Finance Innovations or dubbed as the FinPower Program. This program has three central components:

Component 1: Participatory Dialogue and Policy Forums

Component 2: Pilot Programs, Exposure Visits and Documentation

Component 3: Training, Regional Study and Sharing of Innovative Practices

1.3 Objectives of the National Forum and Technical Support (Dialogue)

In consonance with the main goal of the FinPower Program, which is *to promote the financial empowerment of the rural poor in Asia-Pacific Countries through policy dialogue, innovative pilot program and knowledge-sharing among actors in the rural finance sector,* the conduct of the National Microfinance Development Forum in Mongolia and the corresponding technical support through dialogue had the following specific objectives:

- Sharing of experiences of India and Mongolia in the creation of conducive rural and microfinance policy environment and regulatory framework;
- Assessing the current state of rural and microfinance policy environment and regulatory framework in the country venue of the National Forum;
- Identifying issues, constraints or obstacles to the efficient and effective provision of rural and microfinancial services; and
- Crystallizing recommendations towards the development of rural financial markets, including formulating sound policies and establishing a client-friendly regulatory framework.

2. PROCEEDINGS OF THE NATIONAL FORUM

2.1 Venue and Date

The National Microfinance Development Forum was held in Ulaanbaatar, Mongolia on 16 March 2010. A total of 64 participants (Annex 3) attended the forum.

2.2 Opening Ceremony

The main speakers at the opening ceremony were Mr. Sorinzonbold Lhagvasuren, 1st Deputy Chief Executive Officer (CEO) of XacBank, Mr. Dagva Dalantainyam, IFAD Rural Poverty Reduction Programme (RPRP) National Program Director, and Mr. Benedicto S. Bayaua, then Secretary General, APRACA.

Mr. Sorinzonbold warmly welcomed the APRACA team and Mr. Praful Dholakia, Consultant from the NABARD Consultancy Services (NABCONS) as well as the forum participants. He appreciated the initiative of APRACA in promoting microfinance in Mongolia and hoped that participants would have a lot to learn from the presentation of Mr. Dholakia and the other local resource persons and would extract valuable information to promote microfinance in Mongolia. He also highlighted the proactive role played by XacBank in Mongolia for development of microfinance.

Mr. Dalantainyam provided an overview of the concept of microfinance as they had evolved in Mongolia. He thanked APRACA for its initiatives in bringing the forum to Mongolia. He also exhorted the participants to learn from the deep experience of India in microfinance.

Mr. Bayaua provided a concise background of APRACA and the goal and objectives of the FinPower Program. He stressed the orientation of FinPower towards promoting financial empowerment of the rural poor in Asia-Pacific countries through policy dialogue, innovative pilot programs and knowledge-sharing among members and partners. He stated that the objectives of the forum and dialogue were to share the experiences of selected APRACA-member countries in the creation of conducive rural and microfinance policy environment and regulatory framework and to assist the key stakeholders in their formulation of a plan of action towards the development of the rural financial markets, including sound policies and regulatory framework. He made special mention of the fact that NABARD, the apex-level development financial institution in India, had pioneered several rural finance innovations such as linkage banking and women in enterprise development.

2.3 Forum Presentations

The papers and the corresponding resource persons during the forum were the following:

- **Status of Rural and Microfinance Policy Environment** By Ms. Oyunchimeg, Director, Microfinance Department, Financial Regulatory Commission, Mongolia
- **Role of Rural Finance Companies (RFCs) as Local Community Financial Institutions** by Ms. S. Nergui, Consultant, Achid Finance
- **Together Against Poverty** – By Ms. Onon Deriilaamyatav, Executive Director, Together Against Poverty Foundation/Organic Mongolia
- **Creating Conducive Rural and Microfinance Policy Environment and Regulatory Framework in India** by Mr. Praful Dholakia, Consultant, NABCONS, India;

These presentations were followed by a question and answer period where the participants had sought clarifications on the finer issues of microfinance, especially on the Indian experience. Mr. Bayaua facilitated the forum while Mr. Praful Dholakia documented the proceedings.

3. PROVISION OF TECHNICAL SUPPORT THROUGH DIALOGUE WITH RFIs

3.1 Venue and Date

The technical support was rendered by Mr. Praful Dholakia during the period from 17 to 19 March 2010.

3.2 Objectives

The dialogue was intended as an avenue for reflecting on the experiences shared, key issues raised and innovations learned during the forum, for identifying workable microfinance policies and strategies, and for identifying which of these policies and strategies are feasible and can be further pursued by appropriate regulatory authorities in Mongolia.

This dialogue entailed visits to various key microfinance stakeholders, projects and clients for one-to-one discussions on various microfinance-related issues and field interaction. Mr. Dholakia met a total of 21 officers of various institutions (see Annex 4).

3.3 Key Stakeholders Visited

The consultant conducted dialogue on March 17-19, 2010 with the Bank of Mongolia and several key stakeholders and their clients. The dialogue partners were:

- Bank of Mongolia with Dr. Lkhanaasuren Purevdorj, Governor, and other senior executives led by Mr. B. Lkhagvasuren and Mr. D. Boldbaatar, both Directors
- XacBank with Mr. S. Munhbold, Director of Retail Banking Division and Mr. Oyuntsetseg, Director of Microfinance Banking Department and middle officers of the Eco Productions Unit.
- XacBank's "franchise model" – the Savings and Credit Cooperative *Zoos Hurd* is located in *Henty* province of *Omnodelger* soum, about 150 kms. away from Ulaanbaatar, interacting with Mrs. Narantsetseg, Manager of the SCC, and core staff, members of the Loan and Supervisory Committee and several borrowers,
- Achid Finance Company of Mongolia, with Ms. Doljinmaa Dorjpurev, Chief Executive Officer and ValueQ Company, a rural finance company (RFC) promoted by on the Company's UNDP-

supported RFC innovation. Interacted also with few members of the Board of Directors/Loan Committee of the RFC in *Tarialan soum* of *Huvsgul aimag.*

- Khan Bank with Mr. A. Serik, Senior Officer, Rural Credit Department, and the bank's core staff who directly worked on provision of microfinance in the countryside.
- Vision Fund, Mongolia with Mr. Timothy Hooper, Executive Director and Ms. Tseveg Otgontsetseg, Manager, Internal Control and Assessment Department. Interacted with three women entrepreneurs.

4. COUNTRY AND MICROFINANCE PROFILE OF MONGOLIA

The following information were drawn from the forum presentations and the dialogue with key microfinance stakeholders. The following specific features characterize the economy of Mongolia, particularly the microfinance sector.

Mongolia has a population of 2.75 million (as in March 2010). Ethnic Mongols (*Khalkhs*) account for about 85 percent of the population while the minority groups include *Kazakhs*, *Buryats*, and *Chinese*. In many ways, Mongolia may be considered a "city state," as over 40 percent of the population live in the capital city of Ulaanbaatar, where about 60 percent of the gross domestic product (GDP) is generated. Some 82 percent of the total assets of the financial sector are located in Ulaanbaatar. Poverty is higher in rural areas, especially in the western region, and there are indications that the poverty gap continues to widen.

Since the beginning of the 1990s, substantial structural reforms had been introduced, including currency reforms, price and wage liberalization, privatization of small and medium enterprises (SMEs) and State-owned companies and enactment of a substantial number of new laws and regulations to facilitate private sector activities. The privatization process was accelerated when large state-owned enterprises began to be privatized in 2001.

The Mongolian economy is centered on agriculture (i.e., agricultural crops, herding, and livestock) and mining (the main hard currency export). The country has experienced GDP growth of over 10 percent per year on average over the past six years, with budget surpluses. The country was ranked 115th among 182 countries of the world in the UNDP's Human Development Index 2009.

The financial sector of Mongolia is a two-tier system, composed of the Bank of Mongolia (i.e., the Central Bank) on tier one, and commercial banks, non-bank financial institutions and credit and savings cooperatives on the second tier. With one small exception: there is no deposit insurance. The capital adequacy ratio has been well above the international standard of eight (8) percent set by the Basel Committee. The Central Bank law expressly prohibits the Government from setting interest rate controls on loans. Mongolian law allows for mortgages and other loan instruments backed by securitized collateral. However, rudimentary systems for determining titles and liens and collecting debts make lending based on local collateral risky. Banks frequently complain that onerous foreclosure rules are barely workable and unfair to creditors.

The financial sector is *totally* privatized. As at the end of February 2010, the following commercial banks were operational in the country – Golomt Bank, Khan Bank, Savings Bank, Capital Bank, Agricultural Bank, Trade and Development Bank, Mongol Post Bank, Transport Development Bank, Erel Bank, Credit Bank, Ulaanbaatar City Bank, Zoos Bank, Anod Bank, Capitron Bank, XacBank, National Investment Bank, Chinggis Khaan Bank and State Bank. In addition, there are 11 insurance companies, 209 savings and credit cooperatives, 173 non-banking financial institutions and 48 securities market intermediaries. There is no licensed apex bank in Mongolia. There is, however, a Government-led wholesale lending

institution, the Microfinance Development Fund (MDF). Only one company currently provides financial leasing for smaller enterprises (XacLeasing), only one regulated institution specializes in non-collateralized, group solidarity lending (Vision Fund Mongolia) and only one NBFI specializes in rural finance innovation (Achid Finance).

Of the total loans outstanding as at the end of February 2010, the share of loans to "Individuals" was about 33 percent (down from 41 percent in August 2008). *Loans to individuals are often used for productive purposes, especially within the informal sector.*

According to the Mongolian laws and regulations, all financial operations are divided into two parts: "banking" and "non-banking". The Bank of Mongolia is responsible for the licensing, supervision, and regulation of banks while the Financial Regulatory Commission (FRC) is responsible for supervising non-banking financial institutions, including credit unions and non-deposit-taking lenders, capital market intermediaries and insurance companies. FRC has a Microfinance Department whose main functions include formulating proposals to improve the legal environment of non-bank financial activities/savings and credit cooperatives, developing rules, criteria, procedures, regulation, methodology and recommendations within the scope of its power and ensure the implementation with the aim of providing stability of the NBFIs, SCC, etc., creating competition and establishing trust in the NBFI, SCC and Currency Exchange Units (CEUs) and developing and implementing policy to introduce corporate governance principles, developing proposals and maintaining records on granting, suspending, revoking and terminating the licenses to carry out activities on NBFI, SCC, among others.

According to the Mongolian legislation, "banking" and "non-banking" financial services may only be carried out by the authorized, "for-profit" legal entities. This requirement was established in order to protect consumers' assets, ensure long-term sustainable operation and maintain the overall stability of the financial sector. The only "non-profit" legal entity permitted to provide financial services is SCU. They are allowed to provide such services because they can do so only to their members, not to the public, and because SCUs are not large enough to affect the stability of the financial sector.

Formal microfinance providers such as banks, NBFIs and SCUs are all required to acquire licenses in order to provide banking and other financial services. Once a bank has been permitted to provide banking and financial services, no other permissions are required to provide "microfinance" services. The FRC provides licenses to all financial institutions except banks. NBFIs are not authorized to take deposits from the public. SCUs are only allowed to provide loans to—and mobilize deposits from—members. There is no minimum capital requirement for SCUs, but they should have a minimum of 20 members.

The range of financial products and services available in Mongolia is extensive, with the vast majority available to lower-income households and/or businesses. Consumer lending backed by pensions, savings, salaries, and/or large down payments (i.e., "consumer leasing") has become widely available and is often used either as working capital or for small business improvements by microenterprises. While it appears that a large portion of the population (79 percent of households) has access to financing, financial institutions still have scope to move down market to address the needs of the rural poor. Several products that address the needs of the "bottom of the pyramid," but are not fully developed, are non-collateralized loans, micro-leasing and mortgage lending.

The country has a high-interest regime where both deposit and lending rates are very high compared to other countries. It is not unusual for a microcredit to carry an annual interest rate of 50 percent or so. Even the microenterprise loans where the funds are utilized for some productive purposes carry an interest rate of 40 percent p.a. and it is difficult to envisage a microenterprise in rural area that can generate adequate revenues to sustain such huge interest pay-outs and yet be viable. The scenario in case of consumption loan would be certainly far worse to the borrower who would be required to service

a very expensive loan without any income generated from the borrowed money. However, this is an issue that is linked to a much higher play of economic policies and forces and the microfinance institutions have little leeway. This underlines the need for innovations in resource mobilization in a cost-effective manner.

In Mongolia, as in other countries, informal financial arrangements are widespread. This includes rural moneylenders, pawnshops, middlemen, traders, collectors, friends and relatives. Such informal finance is most visible in case of meat processing, vegetable retailing and cashmere production where the bigger traders/middlemen finance the small producers/herders. Interest rates vary from four (4) percent to nine (9) percent per month (48 percent to 108 percent p.a.).

Banking laws in Mongolia specifically prohibit the Government from engaging in lending activities though multilateral agreements and a particular provision of the Central Bank law provide loopholes that allow the Government to engage in direct intermediation of financial services under some areas like secondary housing market and socially targeted micro and SME lending. However, the Central Bank law expressly prohibits the Government from setting interest rate controls on loans.

In Mongolia, there is neither an official definition of "microfinance" nor any policies, laws or regulations specifically designed to create an enabling environment for microfinance. Instead, microfinance is regulated by the same banking and financial laws and regulations that govern the mainstream financial system. This means that specific laws do not directly relate to microfinance institutions, their creation, or licensing, nor do specific tax breaks or a regulatory or supervisory regime apply to them. Likewise, there is no specific national policy on microfinance.

Over the years, the Mongolian microfinance sector has experienced rapid growth. Despite there being a very low population density in the countryside, nomadic population, harsh climate, seasonality of demand for financial services, high covariance risk and very poor rural physical infrastructure, the achievement of MFIs like Khan Bank, XacBank and the Mongol Post Bank is impressive. Although these MFIs dominate the micro lending market in terms of the number and volume of loans outstanding, other NBFIs like Vision Fund and Trans CapitaI are the leaders in terms of depth of outreach.

Contrary to microfinance loans in other countries, the majority of such loans in Mongolia are individual collateralized loans with terms up to 12 months. Although nearly every financial institution in Mongolia provides a significant percentage of its services to low-income clients, not all classify these activities as "microfinance". Only one commercial bank and three NBFIs specifically market themselves as "microfinance" institutions – XacBank, Vision Fund, Trans CapitaI and Credit Mongol. The typical "microloan" refers more to enterprise loans, which are usually greater in value than the *MicroBanking Bulletin* proxy of 64.90 percent of per capita Gross National Income (GNI) in Central Asian nations.

A considerable portion of the loan portfolio of the key microfinance players is financed through external borrowing, a large share of which is in foreign currency. Since only part of these foreign currency borrowings can be offset by on-lending in foreign currency, these liabilities are a growing concern. With the continuing high inflation, microfinance banks may not be able to rely on deposits as a source of financing.

Estimating the potential demand and supply gaps in microfinance in Mongolia is difficult as no empirical quantifiable demand assessment is available.

The following information were also drawn from the dialogue with key microfinance stakeholders, including the Bank of Mongolia.

Bank of Mongolia

In sequel to the courtesy call by the Consultant on Dr. Lkhanaasuren Purevdorj, Governor, Bank of Mongolia on 15 March 2010, the expert had conducted dialogue with the other senior executives of Bank of Mongolia (Central Bank) on 17 March 2010, especially with Mr. B. Lkhagvasuren and Mr. D. Boldbaatar, both Directors of Bank of Mongolia, for apprising them of the discussions and issues raised in the National Forum and for obtaining their ideas and overall support for the APRACA initiative. The exchange of ideas with the top echelon of the Bank of Mongolia had gone a long way in giving a firm direction to the overall approach and efforts of APRACA.

One specific issue that was brought to the attention of the two Directors of the Bank of Mongolia was that the banks in Mongolia were not in a position to open savings bank accounts in the name of SHGs and subsequently finance them unless the groups were formally registered. Some of the banks and NGOs had previously raised this issue in the national forum. Mr. Dholakia explained that the Reserve Bank of India had resolved this issue way back in January 1993 by way of an advisory to all commercial banks that savings bank accounts could be opened in the name of SHGs, whether registered or not. It was suggested that this issue could be examined by the Bank of Mongolia with reference to the prevailing socio-legal framework in the country.

XacBank – Head Office

Mr. Dholakia interacted with Mr. S. Munhbold, Director of Retail Banking Division and Mr. Oyuntsetseg, Director of Microfinance Banking Department of XacBank. The primary objective of the dialogue was to understand various microfinance initiatives launched by XacBank in Mongolia and to offer suggestions on various operational issues experienced by the bank in the field, more particularly with reference to how the same were being addressed in India. The Consultant had described in detail the concepts and operational issues behind the promotion and nurturiing of self-help groups (SHGs) in India as well as their linkages (both savings-linkage and credit-linkage) with banks. The linkage banking program had become the single largest poverty amelioration program in the world. These discussions were followed by a close interaction with the core staff of the abovementioned XacBank units.

In side discussions with the Xacbank Eco Products Unit, the Consultant had provided the technical details of cultivation, processing and financing of *jatropha* (*jatropha curcus*) for production of bio-diesel as also innovations in solar cooking. Although *jatropha* crop is known for its soil-binding ability and the ability to grow under varied agro-climatic conditions, it was clarified by the Consultant that there would be first a need for close involvement of the local agricultural research bodies/agri-universities in trials to determine its ability to grow in the extreme conditions which, if proven, would have great potential to resist growing desertification in the country, especially in the *Gobi* region.

XacBank Franchise Model

As a part of provision of technical assistance by the Consultant, XacBank had arranged for a day-long visit to a savings and credit cooperative (SCC) that was established under XacBank's "franchise model" in a *soum* (a rural administrative center located far from major settlement areas). The SCC *Zoos Hurd* is located in *Henty* province of *Omnodelger* Soum, about 150 kms. away from Ulaanbaatar. During the course of this field visit, the Consultant had interacted with Mrs. Narantsetseg, Manager of the SCC, and its core staff, members of the Loan and Supervisory Committee and several borrowers, including a young herdsman who lived in isolation on a hillock with difficult access about 15 kms. away from the SCC premises.

XacBank's mission is to provide access to comprehensive financial services to citizens who are normally excluded due to income or location. Through this innovative franchise approach, XacBank aims at deepening outreach to the most remote *soums*. Approximately 50 percent of the Mongolian population reside in remote rural areas, and 70 percent of the rural population work in traditional livestock raising. Demand for financial services far exceeds supply in these areas. Only some Mongolian commercial banks, including XacBank, Agricultural Bank and Mongol Post Bank, have branches in *soums*. Savings and Credit Cooperatives (SCC) are equally sparse in remote rural areas. However, there is growing demand among *soum* residents for reliable access to sustainable financial services close to their communities. To help meet this demand, XacBank has introduced a "Development Guide" Franchise Service. The idea is to help rural residents, primarily the poor, herders and women access financial services in their *soums* by organizing into SCCs with the close facilitation and support of XacBank.

This model entails the establishment of a *soum*-based Savings and Credit Cooperative (SCC) formed and operated by the local residents in a sustainable manner, with technical and operational support from the Bank. This model supports local economic growth and delivers multiple financial services through strengthening of more independent, more democratic and more outreach-capable financial institutions that are initiated, owned, controlled, managed, and shared by local residents.

XacBank provides such services to the franchisee SCCs as technical assistance (training, consultancy, regional demonstration training and seminars), rating, monitoring and evaluation, MIS, financial services (credit line, wholesale loan, leasing), new products and services (money transfer, mobile banking agency, insurance), etc.

The Development Guide Franchise Service involves four main activities:

- organization of extensive training for the creation and establishment of rural SCCs;
- capacity building of existing rural SCCs to enhance financial services;
- provision of basic office equipment for new SCCs established in *soums*; and
- advisory and other technical support for SCCs.

Any SCC seeking to enroll itself under the franchise contract should fulfill certain minimum criteria such as located in a soum, at least 21 members, at least ₮ (tugrik) 2.0 million equity shares, active participation of member and agreement with franchise contract principles.

There is an advisory committee, comprising nine (9) cooperative heads, who represent all the 78 SCCs franchised so far, which has general meeting twice a year to discuss and approve SCC growth policy and action plans.

The SCC specific information that is pertinent is as under:

- Total members were 320 of which, 217 were women. All members were from the same *soum* having a population of 6,000. Membership is open to all the *soum* residents. Non-members cannot get loans or open deposit accounts.
- The membership fee is ₮ 10,000/- for joining besides an additional ₮ 50,000/- towards share capital contribution. This is a dynamic concept and is changed as needed during annual general meetings (AGMs). Share capital is also augmented through a wholesale loan from XacBank.
- Directors are elected during the AGMs by voice votes for a term of three (3) years (by rotation). Besides, there are 3 Risk Committee members who are also so elected for a term of two (2) years. The Risk Committee's functions include scrutiny of loan applications and sanction of proposals. Its decision is final and cannot be overruled even by the Board.

- Additionally, five (5) members of the Internal Audit Committee are also so elected for two (2) years and, upon election, are trained by XacBank.
- All loan products and its terms are decided by the AGM. Presently, loans are mainly for vegetable cultivation (for a maximum of 12 months), herder loan (for 12 months for hay, children's education, etc.) and business loan (18 months). The rate of interest is 3 percent to 3.5 percent per month (36 percent to 42 percent per annum). Maximum loan eligibility is 10 times of the share capital contribution.
- Terms deposits are for a maximum period of five (5) years which allows the highest rate of interest of 21 percent p.a.

Based on the above information and the discussion held in the SCC, it can be said that:

- Women constitute the majority of members. However, this is not because of any special drive for women's enrolment but owing to the fact that in most *soums*, it is the women who run the business;
- The credit deposit ratio (CDR) of the SCC was 4:1 which is considered very encouraging;
- Management of the SCC is on sound professional and democratic lines. However, in practice, and for practical reasons, the same set of people return to man various committees and the overall management remains in their hands only;
- The diversity of the loan portfolio is in synchrony with the needs of the *soum* and is demand-driven; and
- The interest rates on both term deposits and various loans are very high, higher than what the commercial banks allow. At remote *soum* levels, it is difficult to envisage economic activities that can absorb such higher interest rates in the long run. This calls into question the long-term viability of the SCC.

Achid Finance – Rural Finance Company (RFC)

The Consultant also visited ValueQ Company, a rural finance company (RFC) promoted by Achid Finance Company of Mongolia, and had detailed discussions with Ms. Doljinmaa Dorjpurev, Chief Executive Officer, on the Company's UNDP-supported RFC innovation. Achid Finance Group was founded in 2002 with the objective of "helping its clients and customers with specialized technical and appropriate financial assistance that allows them to grow and prosper in sustainable ways". Achid runs its activities through its subsidiary-companies "Achid Consulting" and "Achid Finance" that have their own specific purposes. For better understanding the concept of RFC, the Consultant had also interacted with a few members of the Board of Directors/Loan Committee of the RFC in *Tarialan soum* of *Huvsgul aimag*.

The uniqueness of the model is mobilization of private capital into the rural finance sector. Two RFCs were established in rural Mongolia with special license from Bank of Mongolia to operate as non-bank financial institutions (NBFI). The RFC is owned by the local community and established with pure private capital. Provision of technical assistance to RFCs for its start-up operation is an inherent feature of the model. The first RFC was established in *Tarialan soum* of *Huvsgul aimag*, and the other in *Bayantsagaan soum* of *Bayanhongor aimag*. Most local people in the first area are engaged in agricultural activities such as growing wheat and vegetables, while in the second area, the major activity is livestock herding. The first RFC provides seasonal agricultural loans, the second provides herders loans. The RFC increases access of the rural poor people to the financial services, and it enables the rural people to invest locally by putting their excess capital into RFC as equity investment. The professional management of the RFC convinces rural people to invest and get a return on their investment.

The model has partnered with ADRA, Mongolia for non-collateralized group loans and with Mongol Daatgal for index-based livestock insurance.

Some distinguishing features of the RFC are mobilization of private funds, good governance of community-owned MFIs, community participation, professional supervision and internal control system, free from donor involvement/pressure, free from political influence and diversification of ownership concentration.

Private capital is mobilized through the issuance of shares with low nominal value so as to attract a large number of local residents while the strategic investors invest their funds by buying higher number of shares to keep the liquidity problem at bay in the formative stage. The share of the local residents should be more than 50 percent of the total equity. The microfinance consulting and training institution provides the technical assistance to build the capacity of human resources to manage the local company independently. Training is provided in a process-oriented manner by providing on-the-job trainings. Technical assistance services include training in company by-laws and other internal systems. The RFC has all the features of a limited liability company. It has a Board of Directors (BOD), a Supervision Committee and a Loan Committee. Members of these governance units are elected by the shareholders. There is a high probability of electing the right person for the right position because local people know each other very well. Local residents are the shareholders and RFC provides services to its shareholders up to certain limits, depending on share of equity in total asset. This feature provides an opportunity to develop the demand-driven products and improve the customers' collaboration with the Company. At the same time, it reduces the risk of loan delinquency while improving the repayment rate because clients are the owners.

The comparative advantage of the RFC Model over other prevalent models is depicted in the following Table:

Table 1: Comparison on Certain Features between RFC and Non-RFC Institutions

Non-RFC Institution	Features	Comparative Feature of RFC
Banks	Centralized management system. Expensive top-down business approach.	Decentralized management system, governance decisions made by locals
Cooperatives	Conflict of interest, mission drift. Limited possibility to attract outside investors. Limited outreach	Professional financial management provides services to everyone, not limited to only its members. Profit-driven common interest
Non-Bank Financial Institution	Privately owned by one company or person; no community involvement	Owned by local community, community interest and participation.
Informal Sector	Illegal and lack of potential.	Officially permitted by FRC and supervised, builds human resource capacity

The model appears to be promising and it has reached break-even point in the very first year of its operation. This indicates its sustainability. However, there are certain issues and challenges:

- RFCs are not allowed to mobilize deposit from public according to the regulatory framework of Mongolia. This severely restricts long-term business depth;
- Since RFCs are not allowed to do money transfers and all operational transactions need to be done only through banks; they are dependent on competing banks;

- Needs to have a professional technical assistance in order to build capacities of the RFCs and to operate independently in a sustainable manner; and
- Their unique structure with low capital and high ownership dispersal makes it difficult to get license from FRC/Bank of Mongolia.

Khan Bank, Ulaanbaatar

Khan Bank is the only bank to have established branches in every province and town in the nation. Discussions were held by the Consultant with Mr. A. Serik, Senior Officer, Rural Credit Department, Khan Bank and the bank's core staff who directly worked on provision of microfinance in the countryside.

The factors leading to the success of Khan Bank as a microfinance provider (the same factors also make XacBank a successful microfinance player in Mongolia) are:

- It occupied the market earlier than the other microfinance providers;
- It provides demand-driven products and services;
- It has operated under the direct supervision of the Central Bank of Mongolia since its establishment;
- It organizes regular human resources trainings;
- It has received significant amounts of international donor support and technical assistance; and
- It closely follows international principles and guidelines for prudential and transparent banking, even when it is not required by the Central Bank.

Vision Fund, Mongolia

The Consultant, in his last leg of providing technical consultancy, had visited the HQ of Vision Fund, Mongolia, a part of World Vision, and had discussions with Mr. Timothy Hooper, Executive Director and also Ms. Tseveg Otgontsetseg, Manager, Internal Control and Assessment Department.

Vision Fund, Mongolia has been licensed to function as a limited non-bank financial institutions (NBFI). The Consultant presented a brief profile of the contours of microfinance in India. The Consultant also had a discussion with the Vision Fund Team on its hugely successful program of provision of microloans to solidarity groups. Ms. Tseveg had later on facilitated an interaction with three women entrepreneurs at the Vision Fund's Field Office located on the outskirts of the capital city of Ulaanbaatar. These entrepreneurs had all successfully lifted themselves out of poverty through this program.

There are today over 1,200 solidarity groups financed by the Vision Fund, Mongolia. The program providing for loans to solidarity groups was launched in 2005. Earlier, non-availability of collateral and the consequential absence of credit history on the part of otherwise potential entrepreneurs meant no chance of a business loan. This denied both the individual potential entrepreneurs as well as the society in general a fair chance to grow and develop. However, this issue has been very effectively addressed in the Vision Fund's "solidarity" approach.

Under this approach, eight (8) to 10 qualified entrepreneurs living in development communities come together and form community banks or what is called "solidarity groups" in Mongolia. Once a group registers with Vision Fund, it is provided vocational training in different income-generating activities based on the traditional skills already known to the members. This training also covers other business-related aspects as accounting, management and marketing. Once their capacity has been built up like this, the group then approaches Vision Fund for non-collateralized micro-loans. The loans can be as little

as US$50.00 for a small business to develop or expand. The loans are given only to the proven entrepreneurs who have established their trust worthiness, work ethics and sound business ideas.

This approach ensures that employment is created and the economic engine is re-generated which, in turn, benefits the entire community and helps it come out of poverty. Thriving businesses create more jobs and generate additional goods and services benefiting the whole communities. Borrowers guarantee each other's loans, support each other's businesses and keep their own books. The group screens potential borrowers and tracks each repayment, building its members' leadership skills and sense of pride along the way. Weekly meetings offer accountability and support and also build business skills.

The best tenet driving this approach is that the poor but proven entrepreneurs are a good credit risk which is reflected in the fact that the recovery of loans under the "solidarity" platform is over 98 percent. Further, the recoveries are recycled and reinvested in another entrepreneur, beginning the cycle all over again. The support from the Vision Fund is not limited only to providing the loan; its loan officer regularly visits the members of the group and helps them get the best from their businesses. Borrowers are eligible for repeat loans for higher amounts depending on their individual repayment performance.

Since Vision Fund is registered as an NBFI, it cannot accept deposits from its members under the Mongolian laws. This has been resolved through a partnership with XacBank and each member of a "solidarity group" is expected to open a savings bank account with a branch of XacBank. Loans, when sanctioned, are also first credited to a new loan account opened in the name of the concerned borrower and each disbursement is closely followed up by the NBFI's loan officer to ensure that it is fully utilized for the intended purpose. This prevents mis-utilization or diversion of loans.

Weighing the pros and cons, there is no doubt that the Vision Fund's program of providing loans to the entrepreneurs under the "solidarity group" approach is one of the most successful microfinance initiatives in Mongolia and deserve to be supported at all levels by the Government, Central Bank, other regulators and commercial banks alike.

ADRA, Mongolia

ADRA, Mongolia (a part of a global humanitarian organization of the Seventh-day Adventist Church) has a program-component for Self-Help Groups (SHGs) under its Microeconomic Development Program (MEDP). This program aims to build bridges between financial organizations and rural residents who have no business experience, specialized skills or assets to show as collateral. The program helps rural residents get out of financial difficulty through the SHG model that enables low income earners to find a common solution and work together at a low cost. By working as a group, the members are given the opportunity to start a microbusiness, share experience, increase sales, build professional capacity and improve products to display in local markets. During 2009, the project had supported 191 SHGs in 26 small villages of *Zavkhan, Selenge* and *Bayankhongor* provinces. Overall, project loan repayment stood at 98 percent. Khan Bank, XacBank and Mongol Post Bank have partnered with ADRA International to provide non-collateralized lending to SHGs and individuals. However, adoption of the SHG model has yet to take off in a systematic manner in Mongolia and awareness about its concept, philosophy and practice is very low, especially among bankers.

5. MICROFINANCE IN INDIA

The Gross Domestic Product (GDP) of India ranks 12th among the top 30 global economies due to its large size and population. It is classified as a country of medium human development, ranked 134th among 182 countries of the world in the UNDP's Human Development Index 2009. However, despite overall growth, around 300 million people, or about 60 million households, are still living below the poverty line. It is further estimated that of these households, only about 20 percent have access to credit from the formal sector. Clearly, microfinance services in India have emerged as an effective intermediation tool for financial inclusion and the associated growth process of the masses.

A pilot project for SHG-Bank Linkage Program (SBLP), drawn from the experiences of the Deutsche Gesellschaft fur Technische Zusammenarbeit (**GTZ**) or German Agency for Technical Cooperation and the Asia-Pacific Rural and Agricultural Credit Association (APRACA), was launched by NABARD in 1992 as a partnership model between three agencies, viz., the SHGs, banks and NGOs. By the end of March 2010, over three (3) million SHGs in India had been linked to formal financial institutions.

The primary objectives of the program are:

- to evolve supplementary credit strategies for meeting the credit needs of the poor by combining the flexibility and responsiveness of the informal credit system with the technical, administrative and financial resources of the formal credit set-up;
- to build mutual trust and confidence between the bankers and the rural poor; and
- to encourage banking activity, both on the thrift and credit sides, in a segment of the population that the formal credit institutions usually find difficult to cover.

NABARD is the single largest entity in India that strongly supports SHG formation process and, thus, provides dignified financial and capacity building support to self-help promoting institutions (SHPIs). There is an element of indirect subsidy as NABARD presently supports the costs involved in the formation and nurturing of SHGs up to the stage of credit linkage. This financial support currently is about US$60.00 per SHG.

A major impact study on the SHGs linkage project, commissioned by GTZ and NABARD, brought out several interesting findings:

- Excellent coverage of women (80 percent of SHGs were exclusively all-women);
- 60 percent of the members of all SHGs were the "poor";
- These groups, on an average, reported a growth by 6.10 percent per annum in their incomes;
- They were able to spend 5.50 percent more on education and health per annum each year;
- The average loan amount borrowed grew by 20.50 percent per annum, whereas their savings increased by 14.20 percent;
- Poverty reduction rate among the SHGs was high at 10 percent p.a. for their members; and
- Improved social empowerment was reported by 92 percent of the groups.

Today, India's formal financial sector is amazingly vast and consists of commercial banks, regional rural banks (RRBs) and cooperative banks. As many as 32,885 rural and semi-urban branches of commercial banks, 14,303 branches of RRBs and nearly 92,000 rural outlets of cooperative banks are engaged in microfinance activities. The banking infrastructure has evolved over a period of time through various policy interventions, especially with the objective of reaching out to the poor better and wider. However, despite this massive infrastructure of banks, 36 percent of the rural indebted households are still

dependent on the informal sector. This dependence on the informal sector is much higher in the case of lower-asset groups.

Microfinance in India has grown at a tremendous pace, achieving significant outreach amongst the poor as well as non-poor (but low-income) households across the country. Linkages between banks and self-help groups (SHGs) supported by the National Bank for Agriculture and Rural Development (NABARD), on one hand, and Microfinance Institutions (MFIs), on the other, have emerged as the two most prominent means of delivering microfinance services in India. Growth in terms of outreach across both models has been very high. Under the SHG-Bank linkage model, a substantial amount of US$3.60 billion was disbursed as loans during 2008-09 alone. M-CRILMFI estimates that portfolio of microfinancing institutions in India has grown by 146 percent over the past two years. However, despite the impressive growth of microfinance in India, only a small proportion – 16 percent – of the estimated overall demand of US$21 billion is presently being met. Assuming that a substantial part (even 75 percent) of this demand for credit will be met by the Bank-SHG linkage program, disbursements by MFIs would still need to grow at a phenomenal rate in order to meet the residual demand. Indian microfinance sector would need an investment of $1,415 million over the next five years to increase its effective outreach to a reasonable proportion (30 percent) of the population which has very low incomes.

India so far has been following a policy of non-regulation of MFIs. The requirements applicable to MFIs do not go beyond, as in other non-regulating countries in the region, the administrative and simple accounting requirements of charities, trusts, etc. The country has been relying on self-regulation as an effective way of ensuring the proper functioning of MFIs.

In India, microfinance is provided by apex development financial institutions (such as NABARD, Small Industries Development Bank of India (SIDBI) and Rashtriya Mahila Kosh), commercial banks, regional rural banks, co-operative banks, non-banking financial companies (NBFCs) and various "not-for-profit" entities.

The Microfinancial Sector (Development and Regulation) Bill, 2007 seeks to promote the sector and regulate microfinancial organizations (MFO). The Bill has two broad objectives:

- to promote and regulate the microfinance sector and
- to permit microfinance organizations (MFOs) to collect deposits from eligible clients

It has been proposed in the Bill that NABARD shall regulate the microfinancial sector. Every MFO that accepts deposits needs to be registered with NABARD. Conditions for registration include (a) net owned funds of at least US$10,000 and (b) at least three (3) years in existence as an MFO. All MFOs, whether registered or not, shall submit their annual financial statements to NABARD. Every MFO that accepts deposits has to create a reserve fund by transferring a minimum of 15 percent of its net profit realized out of its thrift and microfinance services every year.

Analyzing the current scene of microfinance services, a new type of loan methodology is seen to be evolving that is somewhat hybrid in nature. It considers itself in the business of improving livelihoods, in which 'livelihood financial services' is one piece. It places equal emphasis on the provision of agricultural, business, development and technical services in addition to the provision of financial services, which includes credit but is not limited to it. Credit is not sufficient alone to guarantee an improvement in the livelihoods of the rural poor. It is believed that other financial and technical services are necessary and can be sustainably provided on a revenue model.

There are several emerging issues and challenges facing the microfinance sector in India that would need to be addressed suitably for sound consolidation and growth of this sector in the times to come. They are as follows:

- Although there has been an impressive expansion, it lacks depth. Growth is confined to credit, with very little insurance and even, less savings coverage offered. Even in credit, increase in client numbers accompanied by increase in geographical coverage did not lead to deeper engagement with clients in terms of larger loans and diversified products. The shallow engagement with the clients on account of the 'touch and move on' business models rendered the operational costs high.
- Mission Drift is often visible. The admiration for the pace of growth is accompanied by unease at the manner and content of expansion. The yearning for organizational transformation in many cases does not seem to be a well thought-out strategy of upscaling operations, but seems an image-makeover exercise.
- Cellular finance might emerge as an alternative to brick and mortar MFIs with significant competition for the medium and small MFIs. Technology and platform providers might take to finance rather than providing a space for MFIs to operate on their technology and infrastructure. In the business correspondent/business facilitator (BC/BF) sphere, such developments have already taken place where technology providers have set up entities to function as correspondents with multiple banks.
- The regulation being attempted through the Microfinance Bill may not protect the large number of clients that borrow from the NGO/MFIs. Regulatory stance must move from the position that only depositors' interests need to be protected. The small borrowers are equally active in the local economies, and they invest their future compared to savers who sacrifice only their past with the financial institutions. The millions of microlivelihoods that critically depend on continued availability of credit need to be protected. This would call for a significant change in the regulatory stance.
- Avenues for savings need expansion. Savings has been an aspect of microfinance service that has, by and large, been left to the SHGs to do by themselves.
- Microfinance has to develop a greater sensitivity to the needs of the poor clients. The small loans should give way to livelihood support loans of a larger size and longer duration. Only when livelihoods and incomes are targeted can the microfinance sector claim that its mission is achieved.

The amazing multiplicity of social structures in India throws open several options for formation and nurturing of diverse kind of community institutions at the grass roots level for absorbing institutional credit and ensuring high end-repayments. However, one has to really focus on training, capacity building and institution building of various stakeholders in right earnest to make any of the proposed models a meaningful success. Some "non-SHG" community institutions that have been successfully tried out in India are as follows:

- **Joint Liability Group (JLG)** – A joint liability group is an informal group comprising preferably of four (4) to 10 individuals from a same locality and with the same socio-economic background coming together for the purposes of availing bank loan, either singly or through the group mechanism, against mutual guarantee. No two members of the group can be of the same family. JLGs can be formed primarily consisting of tenant farmers and small farmers cultivating land without possessing proper title of their land. Each member accepts to take

responsibility for repayment of every loan provided to remaining members. All members sign mutual agreement where the responsibility is assumed jointly.

In this approach, JLG members are financed and not their projects. The members are expected to engage in similar type of economic activities like crop production. The groups must be organized by likeminded farmers and not imposed by the bank or others. JLGs of such eligible farmers can also serve as a conduit for technology transfer, facilitating common access to market information, for training and technology dissemination in activities like soil testing, training, health camps and assessing input requirements. The management of the JLG is to be kept simple with little or no financial administration within the group. Banks can finance JLG by adopting any of the two models – Model "A" where the individuals in the group are financed and Model "B" where the group itself is financed. The finance to JLG is expected to be a flexible credit product addressing the credit requirements of its members including crop production, consumption, marketing and other productive purposes. Banks may consider cash credit, short-term loan or term loan depending upon the purpose of loan. The differences between JLGs and SHGs are depicted in Table 2 below.

Table 2. Comparison between SHGs and JLGs

SHGs	JLGs
Based on trust	Based on joint liability (mutual guarantee)
Savings an integral component	No provision of savings within the group
Larger group – 10-15 members	Smaller group – 5-10 Members
Limited peer pressure for repayment	Strong peer pressure as joint liability
Lower peer pressure, lower repayment	Higher peer pressure, higher repayment

- **Farmers' Clubs** – Farmers' Clubs are grass roots level informal forums of farmers. In India, such clubs are organized by rural branches of banks/NGO's/Govt. extension agencies with the support and financial assistance of NABARD for the mutual benefit of the banks concerned and the rural farmers. The broad functions of the Farmers' Clubs would be to:
  - Coordinate with banks to ensure credit flow among its members and forge better banker-borrower relationship;
  - Organize minimum one meeting per month and, depending upon the need, there would be 2-3 meetings per month. Non-members can also be invited to attend the meetings;
  - Interface with subject matter specialists in various fields of agriculture and allied activities. For guest lectures, even experienced farmers who are non-members from the village/ neighbouring villages could be invited;
  - Liaise with corporate input suppliers to purchase bulk inputs on behalf of members;
  - Organize/facilitate joint activities like value addition, processing and collective farm produce marketing for the benefit of members. They can also sponsor or organize SHGs;
  - Undertake socio-economic developmental activities like community works, education, health, environment and natural resource management; and
  - Market rural products.

- **Common Interest Groups** – It is a group of a minimum of five (5) persons, generally hailing from countryside, registered under India's Partnership Act, 1932 with a common interest, e.g., a group of dairy farmers, group for banana cultivation. Initial corpus amount is raised through equal participation amongst members that builds up the group capital. This could also be

something like an Artisans' Guild. The primary objective is to bring together people with some skills so that they can scale up their enterprises by coming together or for providing services on a larger scale to a wider clientele. These can also be something close to a producers' group or a service providers' group.

It is said that all major changes with wide ranging implications arise from the wisdom of the common person. The idea of SHGs as a viable credit delivery model for the poor is one such path-breaking concept that has fast emerged as a promising tool for financial inclusion even before the term was coined by the financial experts. In India, its microfinance program has made tremendous socio-economic impact on empowerment of women as well as transformation of policies and practices of all related institutions in their approach to banking with the poor. Clearly, the stage in India set for newer innovations and more effective delivery models as microfinance becomes more mature.

In the Consultant's view, here are some reasons why group loans, both in India and in Mongolia, work well:

- **Allows MFIs to go deeper into the pyramid** – Group borrowers are often poorer than individual borrowers. Since the only collateral required of them is a mutual guarantee, group loans allow clients without assets (like appliances, vehicles, or property titles) to access credit. Group loans give MFIs the ability to offer credit to what would otherwise be considered much riskier, collateral-less borrowers. Very poor clients need support in ways that group mechanisms provide, and live in areas where the cost of mitigating risks without group mechanisms would be non-viable. Group mechanism includes a lot of "costs" that in rural areas are not really considered (people don't value their time because the opportunity cost is low), but where monetary costs such as significantly higher interest rates or physical collateral (rather than social collateral) would prevent people from accessing credit.
- **MFI Efficiency** – With group loans, one loan officer can serve multiple people at the same time, which helps keep MFI costs down. Since loan values are small, the fixed costs of doing business are high compared to the interest earned from the loans. Group loans help MFIs like Vision Fund who work with the village banking methodology to be sustainable, especially when they have to travel far distances to visit clients.
- **Mitigated Credit Risk** – The borrowers guarantee each other's loans and, in many cases, the group is responsible for the loan payment from the group savings if the guarantor fails to pay. This mitigates credit risk. In fact, social collateral is far stronger than physical collaterals, more so in rural areas than in urban.
- **Group Education** – One loan officer can effectively teach a whole group on various topics such as financial literacy, business training, family well-being and health.
- **Support and Solidarity** – Group members are mostly neighbors who know each other or become close as they work together in a community bank. Besides guaranteeing each other's loans, group members can support each other with business advice and help in personal issues.
- **Adverse selection before disbursement** – This deals with the question of selecting the right clients. Since people know their neighbors, reliable clients are able to select other reliable clients much more cheaply than MFIs can. If they might end up paying for somebody's irresponsibility, then they make sure they pick responsible people to borrow with. Groups are formed according to risk levels and the groups assume the risk rather than the MFI.
- **Ex-ante moral hazard** – This is the risk of people using money for activities other than those reported to the MFI. Groups ideally monitor the businesses that are chosen so that they do not end up paying for somebody else's business failure.

- **Ex-post moral hazard** – This relates to the risk of people making profits and then claiming that they cannot pay because they did not make any. Group members know if their neighbors are making money and make sure they repay the money because the alternative is paying it all themselves.

6. ISSUES AND RECOMMENDATIONS

Issues

Among the transforming economies, Mongolia is one of the most successful examples of the deepening and broadening of access to financial services. This fact is reflected in impressive statistics like about 750, the number of households per bank branch; 92 percent, the percentage of on-time performing loans; 50 percent, the number of commercial banks significantly involved in microfinance activities; and 100 percent, the percentage of villages and townships with at least one commercial bank providing microfinance services. This high level of penetration of financial services has been achieved in a relatively short period. These achievements are particularly significant given that Mongolia has the 4th lowest population density globally with half of its population living in often inaccessible rural outlands.

Against this backdrop, one might conclude that the "microfinance revolution" in Mongolia was fostered through the creation of a specific microfinance enabling environment at the very beginning. However, there are still issues to be addressed:

- There is no specific national policy on microfinance. Likewise, there are no specific laws that directly relate to microfinance institutions, their creation or their licensing.
- There are no fiscal incentives for microfinance. Similarly, there is no specific regulatory or supervisory regime for microfinance.
- There is no proviso in any law or policy that encourages or motivates microfinance innovation or the role of NGOs in microfinance.
- There is a near-complete absence of any law, regulation or policy related to consumer education, financial literacy or financial consumer protection.

The challenge in developing inclusive rural financial markets in Mongolia goes well beyond simply providing microfinance services in rural areas. MFIs are certainly needed to provide access to financial services by the poor households in rural areas but because the rural poor need deposit and payment services as much as access to credit, commercial banking institutions will inevitably remain the predominant players in rural financial markets. Over time, an improved legal environment, functioning collateral registries and efficient land markets can also make it easier for rural financial providers to serve growing farming enterprises with credit for large-scale agricultural activities.

There exists no serious policy impediments to bank entry or branching or to foreign ownership.

At the microlevel, there all also some pitfalls with group lending that an NBFI should guard against:

- **Adverse selection before disbursement** – Do people know each other too well so that they are not willing to enforce social sanctions? MFIs need to have rules to make sure that the right people are chosen.
- **More work for poor clients** – The benefits mentioned above mean that the poor clients are expected to put in a lot more work. This is an implicit cost that is not associated with individual loans. In rural areas, the opportunity cost of putting time into getting a loan is low. In order to mitigate risks using individual loan mechanisms, interest rates and collateral

requirements would have to be much higher. Poor people are not willing to front these monetary costs.

- **Group Meetings** – Group mechanisms have a lot of meetings, which is also a cost. The low opportunity cost for attending group meetings for rural borrowers seems reasonable, but when the clients are urban, there definitely is a cost associated with leaving one's business stall for half a day.
- **Assuming Other's Risk** – Often, it is not effective for risk-averse people to assume other people's risk. However, educational programs help reduce this problem. If people understand the system, they become less risk-averse.
- **Collusion** – Groups can collude to cheat MFIs. MFIs have to be strict in their monitoring so that this does not happen.

Recommendations

Notwithstanding the success of the Mongolian microfinance evolution as above, there are areas that do offer scope for further suitable action on the part of various stakeholders so that the health of the Mongolian microfinance becomes sustainable without much dependence on donors and foreign currency loans. These areas are as under:

- **Regulatory Framework**

There are some core areas where specific laws and regulations are possibly required or, where some laws do exist, there are some changes therein that would help. These areas are as follows:

(i) Bank of Mongolia may consider, maybe on a pilot basis first, allowing banks to open Savings Bank Accounts in the names of SHGs, both registered and unregistered, and providing finance to them based on group's social collateral and peer pressure;

(ii) Concurrently, limited licenses maybe issued to SHGs to engage in provision of microfinancial services to accord a legal basis to the "internal lending" within a group which is so much vital to a group's maturity, growth and sustainability. This limited license may be subsequently converted into a full license or rescinded based on performance. This will be an important innovation in microfinance in the country and is a felt need.

(iii) Towards mainstreaming the SHG model, it would be also desirable for the Bank of Mongolia to tweak its existing policy framework so as to turn SHG lending into a normal lending activity of banks which would be a part of "desirable" lending portfolio of the concerned bank (without having to define "priority" sector like some countries have done). This could be accompanied by suitable relaxation of margin and security norms for financing SHGs as also adoption of simplified loan documentation by banks for SHGs.

(iv) Issues of contract enforcement and collateral invariably emerge when a country is in a transitional phase from State ownership to a market-based private economy. Mongolia is no exception. Because of Mongolia's return to traditional nomadic herding, most rural land remains under state ownership and, thus, is not available as collateral. Although under the Mongolian laws, banks can seize collateral of defaulting borrowers without going through the court system, SCCs are not empowered to do so. Even the alternative but movable collaterals like animals and inventories are not as good to banks as immovable assets are. In fact, rudimentary systems for determining titles and liens and collecting debts make lending based on local collateral risky. Banks frequently complain that onerous foreclosure rules are barely workable and unfair to creditors. Clearly, there is a need for looking into building up and

revamping of the registries for land. In the interim, Mongolia could follow the path of major Central Asian countries with improvement in its legal infrastructure for consumer leasing and, thus, offer another alternative for moveable collateral.

(v) "Informal providers", i.e., NGOs, individuals, government and donor projects, are all legally prohibited from engaging in lending services in Mongolia. However, despite this prohibition, there are NGOs, moneylenders and projects that do provide financial services to the poor. Although the NGOs and their projects are apparently discouraged by the Government in favour of mainstream providers because of the unprofessional ways in which they operate, the Government and FRC are, at the same time, not much inclined to forthwith stop their operations because they do help alleviate poverty by reaching out to the very poor households who are otherwise not accessed by the formal credit institutions. Informal finance is clearly very important in rural areas, but the full extent of its importance and the possible leverages that it could provide to formal financial institutions have not yet been adequately explored. Hence, there is a need for suitable policy refinement where the strength of the informal sector could be positively dovetailed with the end-arms of the formal credit agencies for better and deeper credit delivery. Besides, this would do away with, to some extent, the existing duality of mutually exclusive approach towards the informal providers. This would also prevent possibilities of excessive credit lines going to fill gaps that may not exist in reality (being filled already by informal finance) which, in turn, may carry the danger of crowding out private sector finance.

(vi) There also appears to be a need for support, built into the fabric of legal, regulatory and policy framework, for the access of the poorest of the poor to mainstream services through innovations and new legal forms of local community groups, other than SHGs that had already been dealt with earlier. Some new local community groups that could be experimented with are farmers' clubs, common interest groups, joint liability groups, self-help promoting institutions (SHPIs) and individual rural volunteers (IRVs) schemes. They have been playing a very important role in reaching out to the poor with much more than mere credit package and have contributed to the overall welfare of the rural communities elsewhere in the world.

(vii) There is no rating agency operational – State-owned or private. Similarly, the Credit Information Bureau in Mongolia, though established in 1996, is still not operating at its full potential. In fact, the lack of credit bureau at the village level in Mongolia is a gap that poses a systemic risk. Supervisory bodies should consider providing the private sector with opportunities to establish service institutions such as rating agency, credit information bureau and a second-tier apex organization under their direct supervision. This would help in intensifying the demand-driven operation of financial institutions. These institutions too can begin with a temporary license which, in due course, can be converted into a full license or revoked, depending upon performance.

(viii) Both Bank of Mongolia and FRC may consider adopting an add-on role of institution building to their existing regulatory functions. Health of the credit delivery institutions, more particularly in the countryside, is of utmost significance inasmuch as this would directly influence the efficacy of the last-mile credit delivery mechanism. The institutional building role may entail supporting, *inter alia*, training to the field staff, technical assistance, financial education and awareness of the rural clientele as also the staff of the credit delivery institutions, new business orientation, conduct of viability studies, etc. For instance, for enhancing the role of SCCs in rural areas, support to it needs to be refocused in the direction of training and technical assistance, including improved transparency. Implementing an appropriate regulatory framework for SCCs and improving the one for NBFIs could also help expand financial services in rural areas. This institution building role may not be as pro-active as it is in case of NABARD in India which has a slew of initiatives flowing out towards institutional development, including some grants, but may nevertheless be proactive and institutionalized through, say, involvement of some professional agency, institution or NGO that could render these services on agency basis.

(ix) The term microfinance is generally understood as the provision of financial services to the poor. However, this understanding equates microfinance with just "credit" for microenterprises while the poor also need savings, consumption loans, housing loans and insurance services. True-blue microfinance institutions are those that provide thrift, credit and other financial services and products of very small amounts mainly to the rural poor for enabling them to raise their income levels and improve their living standards. Credit is not sufficient alone to guarantee an improvement in the livelihoods of the rural poor. In Mongolia, this somber realization needs to percolate among the banks and other microfinance providers so that the policy-making levels in the Government institutionalizes this new philosophy that seeks to turn "microfinance" into "business of improving livelihoods, in which 'livelihood financial services' is one piece". It places equal emphasis on the provision of agricultural, business, development and technical services in addition to the provision of financial services, which includes credit but is not limited to it.

(x) In Mongolia, there is a near-complete absence of any law, regulation or policy related to consumer education, financial literacy or financial consumer protection. There are no microfinance-specific consumer protection rules and this issue is addressed through general financial sector laws and regulations. Since microfinance deals mainly with the poor whose position vis-à-vis the lender is very subordinate, there is a need for suitable but specific policy framework to protect the interests of the micro borrowers who will increasingly be exposed to the marketing pitfalls as newer and newer micro products invade the market.

- **Business Philosophy of Microfinance Providers**

(i) There appears to be a need for a demand-driven diversification of microfinancial services for the poor. Only one company currently provides financial leasing for smaller enterprises (XacLeasing), only one regulated institution specializes in non-collateralized, group solidarity lending (Vision Fund Mongolia) and only one NBFI specializes in rural finance innovation (Achid Finance). While it appears that a large portion of the population (79 percent of households) has access to financing, financial institutions still have scope to move down market to address the needs of the rural poor. Several products that address the needs of the "bottom of the pyramid," but are not fully developed, are non-collateralized loans, micro leasing, micro insurance, productive leasing and mortgage lending. Tourism, especially eco-tourism, is another area that may be ideal for Mongolia given its geography and traditions of herder hospitality.

(ii) Microfinance needs to develop a greater sensitivity to the needs of the poor clients. Contrary to microfinance methodologies used in other countries, the majority of loans in the microfinance sector in Mongolia are *individual collateralized loans* with terms of only up to 12 months. In many cases, the short duration do not enable most borrowers to do much except to ease liquidity problems. The microloans to the poor should give way to livelihood support loans of a larger size and longer duration. Although there has been an impressive expansion, it lacks depth as it is more or less confined to credit, with very little "credit plus" products and even lesser savings coverage. Even in credit, increase in client numbers, accompanied by increase in geographical coverage, has not led to deeper engagement with clients in terms of larger loans and diversified products. The not-too-deep engagement with the clients on account of the 'touch and move on' business models has rendered the operational costs high. Analyzing the current scene of microfinance services in Mongolia, a need for a new type of loan methodology is felt which would consider itself in the business of improving livelihoods, in which 'livelihood financial services' is one piece. It would place equal emphasis on the provision of agricultural, business, development and technical services in addition to the provision of financial services, which includes credit but is not limited to it. Credit is not sufficient alone to guarantee an improvement in the livelihoods of the rural poor. It is believed that other financial and technical services are necessary and can be sustainably provided on a revenue model.

(iii) Adoption of "SHG Model" merits a serious consideration by the bankers as it effectively addresses the issue of delivery of "credit plus" services with thrift built into its very operation. This model has yet to take off in a systematic manner in Mongolia and awareness about its concept, philosophy and practice is low, especially among bankers. This assumes added significance due to the generally high interest rate regime in the country where a rural poor ends up paying a rate of interest as high as 45 percent on his small production loan. The impact of this high interest regime in case of consumption loan would be certainly far worse to the borrower who would be required to service a very expensive loan without any income generated from the borrowed money. Although this is an issue that is linked to a much higher play of economic policies and forces and the microfinance institutions have little leeway, the argument here is not on regulating the interest rates *per se* but on the ever-increasing need for raising local resources that would be cheaper than the foreign currency loans. This underlines the need for innovations in resource mobilization in a cost-effective manner. Adoption of the SHG model could be very effective to address this issue as it would help in pooling and mobilizing the thrift of the members at a low cost which, in turn, would help the banks in re-pricing their products to better suit the poor. The banks would be far more comfortable in financing the poor through this mode as they would find the risk and transaction costs to be low. This would guarantee their sustained interest in the program. The sustainability of the program from the point of view of availability of resources is clearly established.

(iv) Shortage of human resources is undoubtedly a major problem that already seems to be impacting the sector. No serious effort seems to have been taken to create academic courses at universities and management institutes while structured training courses for banking and other concerned personnel to improve their industry readiness is not available in general. The banks and other related institutions have to organize in-house training for the new recruits as well as existing staff. Industry-level investments in training, including infrastructure, may be enhanced.

(v) The providers of microfinance in the country need to be future-ready. Although mobile-based banking by some banks in the country has been successfully grounded, the realization has yet to sink in deep that cellular finance might emerge as an alternative to brick and mortar MFIs with significant competition for the medium and small MFIs. Technology and platform providers might take to finance rather than providing a space for MFIs to operate on their technology and infrastructure. The argument is not as much about how the banks can compete with these technology providers as it is about how the two should explore the possibilities for a mutually beneficial business partnership where the eventual beneficiaries are the clientele.

- **Government**

(i) Far greater challenges than rural finance are related to improving **rural infrastructure** (e.g., roads and social services such as health, education, etc.). Moreover, improving rural roads requires more than funding for building and upgrading roads as incentives to enhance the involvement of local governments or other local groups in road maintenance has proven to be critical virtually everywhere for lasting improvements in rural roads. Likewise, rural education is not only a matter of providing teachers and classrooms but also requires proper incentives, especially for herder boys whose present and future earning potential must be taken carefully into account.

(ii) Clients, despite becoming large in numbers, are still in the fringes of the sector. Supply being severely limited when compared to demand, the market is dominated by the sellers. As a majority of the clients are from vulnerable sections, the presumption is that they are unequal in dealing with any financial institution and would be subject to exploitation. Client protection in such markets should thus be the responsibility of the State. Before the issue becomes a core concern of the State, the sector has to voluntarily introduce safeguards that improve client protection. Grievance redressal mechanisms within each institution and across the sector are necessary. The code of conduct should be strengthened and mechanisms of compliance, put in place.

(iii) The weak regulation of microfinance in Mongolia, especially the efforts of FRC, is not likely to protect the large number of clients that borrow from the microfinance providers. The need of the hour is that the regulatory stance moves away from the position that only depositors' interests need to be protected. The small borrowers are equally active in the local economies, and they invest their future compared to savers who sacrifice only their past with the financial institutions. The millions of microlivelihoods that critically depend on continued availability of credit need to be protected. This would call for a significant change in the regulatory stance.

(iv) For enhancing the outreach of the microfinance services to the needy, the legal, regulatory, organizational, systemic and the attitudinal problems need to be addressed and the desired changes brought about to make them more effective. With a majority of the customers being illiterate, needing consumption loans and a majority of the lenders requiring high documentation and collateral security, the products are not reaching the rural poor. The Mongolian microfinance can be made much more effective through inclusive financial reforms.

7. EPILOGUE

Microfinance recognizes that poor people are remarkable reservoirs of energy and knowledge. Although lack of financial services is a sign of poverty today, it is also understood as an untapped opportunity to create markets, bring people in from the margins and give them the tools with which to help themselves. Although the poor sometimes manage to mobilize resources to improve their economic status very slowly over time, extension of financial services to them enables them to better leverage their initiative by accelerating the process of building up incomes, assets and overall economic security. However, conventional financial institutions seldom lend down-market to serve the needs of low-income families and women-headed households. These disenfranchised social groups are very often denied meaningful access to credit, making the discussion of the interest rates and other terms of finance irrelevant. Hence, the fundamental problem is not so much of unaffordable terms of loan as the lack of access to credit itself.

The lack of access to credit for the poor is attributable to practical difficulties arising from the discrepancy between the mode of operation followed by financial institutions and the economic characteristics and financial needs of the low-income households. Over the last decade, however, successful experiences in providing finance to small entrepreneur and producers demonstrate that poor people, when given access to responsive and timely financial services at market rates, repay their loans and use the proceeds to increase their income and assets. This is not surprising since the only realistic alternative for them is to borrow from informal market at an interest much higher than market rates. Community banks, NGOs and grass roots savings and credit groups around the world have shown that these microenterprise loans can be profitable both for borrowers and for the lenders, making microfinance one of the most effective poverty reducing strategies.

Notwithstanding the success of microfinance institutions, only about two (2) percent of the world's 3.2 billion rural dwellers are estimated to have access to effective financial services. Although there is demand for credit by poor and women at market interest rates, the volume of financial transaction of microfinance institution must reach a certain level before their financial operation becomes self-sustaining. In other words, although microfinance offers a promising institutional structure to provide access to credit to the poor, the scale problem needs to be resolved so that it can reach the vast majority of potential customers who demand access to credit at market rates.

The Indian experience has demonstrated that microfinance can be a participatory exercise and the banking system can deliver it sustainably. Instead of creating new institutions to deliver microfinance, it has enabled linkage of groups of the poor with the existing banking infrastructure. Though there are

emerging issues that need to be addressed to make it sustainable in the long run, it shows that by involving voluntary organizations in social mobilization and creating an enabling and flexible policy environment, autonomy and the space for innovations, microfinance can achieve a vast scale and can become a national movement.

Mongolia, in its first wave of microfinance success, has demonstrated that it has embarked on the right path. The time now is for the mid-stream navigational correction, re-calibration of the crosshairs to bring the future at the centre and unleash a fresh wave of reforms that would truly script the Mongolian microfinance experiment as a global success story. The progressive socio-politico-banking edifice in Mongolia has already done it once and there is no reason that they would not do it again, better.

Annex 1

RURAL AND MICROFINANCE ENVIRONMENT AND REGULATORY FRAMEWORK OF INDIA (Full Text)

By
PRAFUL DHOLAKIA

DISCLAIMER: *This paper is exploratory in nature with compilation of successful experiences in India that have been supported by NABARD through its pan-national presence of partners of diverse nature. However, the paper also constructively critiques different dimensions of the microfinancing scenario, systems, processes and regulation ambience in the country.*

Preface

Microfinance has made tremendous strides in India over the years and it has become a household name in view of the multi-pronged benefits reaped/receivable from microfinance services by the poor in this country.

Self-help groups (SHGs) have become the common vehicle of development process, assimilating all development programs. The SHG-Bank Linkage Program, drawn from the experiences of the Deutsche Gesellschaft fur Technische Zusammenarbeit (**GTZ**) or German Agency for Technical Cooperation and the Asia-Pacific Rural and Agricultural Credit Association (APRACA), launched by NABARD in 1992 and envisaging synthesis of formal financial system and informal sector, has become a powerful movement throughout the country. It is considered as the largest microfinance program in terms of outreach in the world and many other countries are keen to replicate this model.

At present, a large number of self-help promoting institutions (SHPIs), all the banking institutions and MFIs are pursuing this program for the uplift of the poor. This is also recognized as a part of priority sector lending and normal banking business by Reserve Bank of India. Thus, it is synonymous with the microfinance program of the country. This program is also the main contributor towards the financial inclusion process in the country.

As on 31 March 2009, there were more than 6.10 million savings-linked SHGs and more than 4.20 million credit-linked SHGs, thus covering under the program about 86 million poor households. Such a massive outreach and pre-dominance of its position among all other global microfinance programs in various countries make the Indian experience unique.

This paper has borrowed, wherever required, from the data published by NABARD in its annual booklet on “Status of Microfinance in India – 2008-09”. This booklet is, in fact, based on the most authentic data received from the primary sources that have been properly validated and are the nearest to the actual position of microfinance sector in India under both the prevalent models – SHG-Bank Linkage Model and MFI-Bank Linkage Model.

This paper also contains the promotional programs taken up by NABARD to give necessary boost to the microfinance sector in India. This support relates to promotion and nurturing of SHGs by SHPIs, training and capacity building of the stakeholders, equity/capital support and provision of soft loan assistance to MFIs. NABARD is also experimenting innovative projects for further developing the SHG-Bank Linkage, particularly in different areas which are lagging behind.

It is expected that the planners and bankers would find this document useful in getting a sharper focus on microfinance as it plays out in India in its full glory which might, in turn, help them bring about suitable policy initiatives/changes and improvement in operational strategies for the implementation of the programs in their countries/regions.

1. Indian Economy and Microfinance

Home to over 1.1 billion people, India constitutes approximately one sixth of the world's total population. A predominantly rural country, it is classified as a country of medium human development, ranked 134th among 182 countries of the world in the UNDP's Human Development Index 2009 (incidentally, Mongolia's rank is 115th). Life expectancy is 63.7 years at birth, and four fifths of the population live on less than $2/day. The adult literacy rate is 61 percent. It is the world's largest democracy and a key, fast-growing economy alongside China and Brazil. Its picture of growing GDP and rising foreign investments show an environment where wealth is increasing rapidly.

Due to its large size and population, India's GDP ranks 12th among the top 30 economies of the world (Year 2008 Ranking-Global Times). However, despite overall growth, around 300 million people, or about 60 million households, are still living below the poverty line. It is further estimated that of these households, only about 20 percent have access to credit from the formal sector. Additionally, the segment of the rural population marginally above the poverty line but not rich enough to be of interest to the formal financial institutions also does not have good access to the formal financial intermediary services, including savings services. Clearly, microfinance services in India have emerged as an effective intermediation tool for financial inclusion and the associated growth process of the masses.

Broadly speaking, microfinance means providing financial services to the poor, long excluded by mainstream banking and finance market. It can be defined as any activity that includes the provision of financial services such as credit, savings, and insurance to low income individuals who fall just above the nationally-defined poverty line, and poor individuals who fall below that poverty line, with the goal of creating social value. Microfinance is a new reality in the world of development discourse and financial intermediation. Neo-liberals support it as it does not disturb the *status quo*. Commercial banks see in it a new area for credit dispensation with a high repayment rate in a world of mounting non-performing assets and sub-prime hazards. Many governments welcome it as a less burdensome manner of fighting poverty. The most important economic rationale in bringing financial services to the door steps of the poor households is the economy in the transaction costs. For formal banks, it will be costly to mobilize the small savings of the poor families lying widely scattered. Equally prohibitive is the cost to the conventional banks in financing a large number of these families who require credit frequently and in small volume and that too not backed by collateral securities.

Microfinance as a major financial service emerged in the 1970s, notably after Prof. Muhammad Yunus, the Nobel peace laureate, started the Grameen Bank in Bangladesh. The Bank began to offer financial services to the poor once excluded from formal banking primarily because they lacked collateral. Today, microfinance has emerged as an industry in which even big multi-national and national banks are interested because they are sure of repayment and high profitability. The creation of social value through microfinance services includes poverty alleviation, improving livelihood opportunities through the provision of capital for microenterprise, microinsurance, savings for risk mitigation and consumption smoothing. Microfinance thus covers the delivery of banking and other financial services at affordable costs to vast sections of the disadvantaged and low-income groups. Easy access to public goods and services is essential for an open, inclusive and efficient society.

Three different approaches could be identified in the evolution of microfinance in the world: the Latin American Model, the Grameen Bank Model and the SHG-based Model. The Latin American Model is

a commercial model. Emphasis on social and community development of poor women is totally missing in such a model. The Grameen Model, on the other hand, is basically centered on women and poverty. The self-help group (SHG)-based model is the Indian variant of microfinance popularized and institutionalized by NABARD, largely through the commercial banking system.

The microfinance sector in India, largely unfettered by tedious regulation and interference, is young and dynamic. With more and more financial institutions entering the microfinance market, microfinance is growing at a break-neck pace on all fronts, viz., loan outstanding, client outreach, product and service diversification and geographic spread. The aggregate amount of credit outstanding of the poor with the formal banking sector is only 10 percent of the total credit requirement of the poor in India, as estimated by the World Bank. Clearly, the balance is met by informal sources.

2. Historical Background and Present Status of Microfinance in India

Notwithstanding the phenomenal expansion of the banking network in the countryside in India over the years, the rural poor continue to depend on non-institutional credit conduits for their emergent needs for funds. This system, albeit flexible and simpler, is not free from exploitation. At the other end of the spectrum, owing to the huge administrative expenditure involved in imparting individual and small banking facility to such weaker sections, bankers are often not very motivated. Against this backdrop, financing of SHGs in India has emerged as a supplementary credit strategy that endeavors to meet the credit needs of the rural poor by coalescing the flexibility, sensitivity and responsiveness of the informal credit scheme with the technical/administrative strength and financial capabilities of the formal credit structure.

In the Indian context, a self-help group (SHG) is a group of around 15 to 20 poor individuals, usually women, who provide financial support to one another in the form of pooled savings and internal credit assistance. SHG members generally use the loan for both consumption and productive purposes. Given the nature of money, most MFIs do not scrutinize loan utilization. The bank issues a loan to the group, after rating them based on their savings and internal credit behavior. The SHG can also lend internally both before and after the bank linkage takes place. The SHG may choose to keep only part of their savings in the bank account, partly in order to maintain internal financing capability for emergency loans.

While technology and finance hold the key to ameliorate poverty, the poor in India do not have adequate access to the formal banking sector. Inaccessibility of the poor to the formal/institutional banking sector is mainly due to the following reasons:

- Lack of good retail outlets offering banking services;
- Lack of assets with the poor that could be used as collateral; and
- Illiteracy of the poor.

3. NABARD's Role in SHG Movement in India

NABARD has successfully spearheaded the microfinance program in India through partnership with various stakeholders like non-governmental organizations (NGOs), banks, and cooperatives in the formal and informal sector, with support from both the Government of India (GOI) and the Reserve Bank of India (RBI) since the early 1990s. The SHG-Bank Linkage Program (SBLP) was launched by NABARD as a pilot project in 1992 against the backdrop of a huge banking structure being unable to adequately address the microcredit needs of the poor. Encouraged by the positive results of the pilot project, the RBI had advised banks in 1996 to mainstream the SHG-BLP. The program later on acquired national priority from 1999 onwards with successive union budget pronouncements. The program has since come a long

way from the pilot stage and has clearly emerged as the primary model for providing rural microfinance services to the unbanked rural clientele. This is a home-grown model, very flexible and without any dependence on foreign funding. It has truly ushered in a silent revolution in the Indian microfinance sector.

Although it had started off as a small pilot experiment, it is today a large movement with nearly four (4) million SHGs (quick estimates) availing of bank loan and thereby impacting positively the lives of 60 million poor people (quick estimates). It is no more a backyard venture of a few committed institutions but a mainstream movement, wherein numerous stakeholders are playing their part proactively. The pace and quality of its growth has made the government, both in the States and at the center, sit up and take notice. This in itself may not be an unmixed blessing, but it does bring in sustained support to the movement. In fact, the Central and State Governments have made this program a cornerstone of their approaches to deliver development services and products to the poor and marginalized sections of the population. From less than 500 groups to more than four (4) million groups linked to the banking system in the last 18 years, the growth has been phenomenal, to say the least.

Up to 31 March 2009, a total of 3.77 million SHGs, representing 54 million poor families or approximately 221 million people, have received cumulative loans of nearly US$6 billion (Rs298.30 billion) from commercial banks. Currently, roughly 66 percent of the formal supply is disbursed through the self-help group-bank linkage route, largely refinanced by the National Bank for Agriculture and Rural Development (NABARD) while the rest comes from private-sector microfinance institutions (MFIs), increasingly backed by commercial banks.

4. NABARD's SHG-Bank Linkage Program (SBLP)

This program, developed and managed by NABARD, allows SHGs to obtain loans from commercial, rural, and cooperative banks. The banks lend to the SHGs and are eligible for NABARD refinance for these loans at a subsidized interest rate. The strategy involved is simple: forming small, cohesive and participative groups of the poor, encouraging them to pool their thrift regularly and using the pooled thrift to make small interest-bearing loans to members and in the process learning the nuances of financial discipline. Subsequently, bank credit also becomes available to the groups, to augment their resources for lending to their members. It needs to be emphasized that NABARD sees the promotion and bank linking of SHGs not as a credit program but as part of an overall arrangement for providing financial services to the poor in a sustainable manner and also an empowerment process for the members of these SHGs. NABARD, however, also took a conscious decision to experiment with other successful strategies such as replicating Grameen methodology and wholesaling funds through NGO-MFIs.

The guiding spirit behind NABARD's microfinance initiatives has the following contours:

- Offers cost effective approaches to formal institutions for expanding outreach to poor;
- Develops collateral substitutes;
- Focuses on rural poor, especially women;
- Facilitates empowerment of the poor; and
- Effectively pursues the macroeconomic objectives of growth.

A question is often asked as to how this program is different from a regular poverty removal program of the Government. This Indian model of microcredit has some important distinguishing features that set its own unique class:

- Loans under it are very small;
- The emphasis is on poor women as the money in the hands of a woman is better used;
- Credit walks apace with thrift;
- The repayment period is generally short;
- Loans are devoid of any concession bearing a comparatively higher rate of interest;
- The rate of repayment is generally very high, often exceeding 95 percent; and
- Lastly, a striking contrast between sponsored poverty alleviation schemes and microfinance is the admitted fact that the former has failed to make any significant dent on poverty, while the latter has produced positive results. The former bred corruption and the latter promoted honesty and integrity. The world has so far learned to cope with poverty, only one way – through charity. But charity does not change the situation; it sustains poverty.

Another question that naturally comes to the mind is why the focus of the program is on maximum coverage of women in SHGs. For various reasons, there is a positive bias in favour of women in SHG-BLP. These are:

- Women have a better repayment rate as they are more susceptible to peer pressures;
- Women are the solution to many problems;
- Women first use money for the family rather than on consumption/leisure;
- Women look to the future with a planned strategy to improve the family situation; and
- Women experience poverty more than men.

A concern is expressed that with more women getting economic empowerment, there could be more tension within the family. We have to accept that there are complex and sometimes varying interests within households, not only between men and women but between older women and younger women, or between children and their parents. Conflict is a normal part of life. But a lot more attention needs to be focused on working with men to make them understand the changes that are going on, and how they can work together more harmoniously, rather than thinking that the way things used to be are the only way they can be. Gender's not all about women; it involves men too.

5. SHG-Bank Linkage – The Journey Thus Far

NABARD's original goal of supporting one million SHGs under this program by 2008 was achieved in 2005 itself. The growth of the program was slow during the initial years for several reasons. Unlike other subsidized lending programs supported by the government, the program is not mandatory for the banks. Involvement of multiple actors – promoter organizations to form the SHGs, the SHGs themselves, and banks – meant a naturally slow institutional learning process. There was also a paucity of capable promoter organizations and insufficient funds for SHG promotion. Most importantly, the lending methodology was novel for the banks which was in contrast to the individual, activity-based and security-protected lending that the bankers knew. SHG-lending is organization-based. Adherence to organizational practices such as proper maintenance of accounts, regular group meetings and good loan-repayment performance on internal lending were to be used to determinants of creditworthiness. Banks were also hesitant to lend to SHGs because the loans were required to be collateral-free. In fact, the program's main claim to success has been the significant outreach achieved and repayment rates of over 95 percent (compared to other poverty lending programs that have had repayment rates of less than 50 percent).

Several factors explain the rapid increase in program outreach in recent years. Apart from natural learning process of all actors involved, NABARD's extensive training programs for institution building and capacity building to all the actors involved has played a significant role. The Microfinance Development and Equity Fund, a dedicated fund created at NABARD with a fund of Rs2 billion (US$40 million) using contributions from the Reserve Bank of India, NABARD and other commercial banks is being used to consolidate and further expand this program. NABARD organizes or finances each year hundreds of sensitization/awareness programs for bankers, NGOs and government functionaries. The sheer size of this support for capacity building of partner agencies can be appreciated by the fact that during 2007-08 alone, NABARD supported 3 Zonal Workshops, 3,122 awareness programs for SHG Members (covering 0.142 million SHG Members), 324 awareness-cum-refresher programs for CEOs and field staff of NGOs, 591 training programs for the officers of commercial cooperative and regional rural banks, 4 trainers' training programs, 25 exposure visits for bank/NGO officials to other banks and institutions doing pioneering work in microfinance, 193 field visits to SHGs for the members of the block level bankers' committees (BLBC), 54 awareness programs for the elected members of the local self-governments, 45 sensitization programs for the senior government officials and 839 other assorted programs.

The adoption by the central government of the SHG concept as its primary anti-poverty self-employment program, the Swarnajayanthi Gram Swarozgar Yojana (SGSY) also aided the growth of formation and linkage of SHGs, though the sustainability and average quality of SHGs promoted under SGSY is debatable.

NABARD has also been instrumental in promoting a conducive policy environment for promoting the SBLP. The lessons learnt during the pilot phase were mainstreamed by the RBI, on NABARD's initiative. Important guidelines which were issued to mainstream the program include:

- Opening of saving bank accounts in the name of SHGs;
- SHG lending to be a normal lending activity of banks;
- SHG lending by banks to be part of priority sector lending;
- Relaxation of margin and security norms for financing SHGs; and
- Adoption of simplified loan documentation by banks for SHGs.

6. SHGs – Major Issues & Challenges

Overall, the SBLP is one of the most innovative social empowerment and economic development initiatives in the developing world. This initiative – reaching more than seven million families throughout the country – has unleashed the hitherto latent energy of millions of women from poor families, endowed them with the confidence, capital, and capacity to "determine their own destiny and shape their future and those of their children's". The self-help group movement initiated by NABARD has provided a vibrant development platform for the rural poor, especially women, transcending primordial divisions and patriarchal monopoly, thus heralding a fundamental transformation of the place and role of women in the family and the community. The methodology for social mobilization, group formation, capacity development, strengthening group cohesion and allied dynamics, economic development planning, credit management, etc. has evolved through a participatory process by 'listening' to the people without pre-conceived models, which lends authenticity to the initiative and inspires confidence about the long-term sustainability and potential for widespread replication of the project across the country and beyond. Clearly, it is by far the largest microfinance program in the world. However, the program seems to be reaching a plateau and there are certain major issues and challenges that need to be addressed. Some of these issues and challenges are the following:

6.1 Sustainability

The program faces several challenges. Most critical is the issue of sustainability of the SHGs. Many are dependent on the promoter organizations for even routine tasks such as maintenance of account books and conducting of meetings where transactions take place. Others operate at a low equilibrium of low savings and low credit that is unlikely to contribute significantly to improving the lives of SHG members. Most importantly, there has been a decline in numbers of SHG's availing repeat loans. Repeat loans are critical because it indicates that loans to SHGs are not one-time loans as in the case of traditional subsidized loans, but that the banks could be a dependable source of loans for the SHGs. It is only when the number of repeat loans become significant that SHG-based microfinance could be said to be on par with financial services provided by other well-performing microfinance organizations (MFOs).

6.2 Jagged Geo-spread

The program suffers from unequal geo-spread and continues to be concentrated predominantly in South India. As of 31 March 2009, 65 percent of total SHGs and 81 percent of the amount lent was in the four States in South India and 53 percent of total SHGs and 51 percent of the amount lent in the State of Andhra Pradesh alone.

6.3 Need for SHG Federations

SHG federations are different from the general federations in several ways. The major difference is in the size of the primary organization. SHGs are much smaller than the dairy cooperatives, the fishermen societies, or the credit unions. Because of the small size and their membership being mostly or exclusively poor, SHGs also have smaller financial resources and more limited human capacity than other typical primary organizations that form federations. SHGs are also informal organizations, i.e., they are not legally incorporated as in the case of the cooperatives or the fishermen societies. In the initial stages, SHG federations were promoted primarily as an exit strategy, i.e. to allow organizations that had promoted SHGs to withdraw their support to SHGs while also ensuring their sustainability.

The structure of the federations and the functions performed vary and depend significantly on the promoting NGO. In some federations, like those promoted by DHAN, there are more than 200 SHGs as members. The federation provides a wide range of services, including financial services, and employs paid staff. The federation structure is a nested-structure with SHGs as members in cluster-level federations and block-level federations. The block-level is a registered entity, either as a society or a trust. In some cases, new organizations called resource centers have been formed that are similar in operational area and services offered to the block-level federations of SHGs promoted by other NGOs. However, the membership in the resource centers is not restricted to SHGs, though the majority of the members are SHGs, water development associations and other community-based organizations supported by the concerned NGO (MYRADA) are also members. As the name suggests, resource centers are designed to serve as a resource for the services required by community-based organizations in an area. The resource centers are typically governed by executive committees with representatives from the SHGs, other member organizations and MYRADA. The MYRADA federations primarily focus on building solidarity, addressing delinquency and dealing with social issues. Some of the federations offer audit services.

Several government agencies are also promoting SHG federations. The Society for Elimination of Rural Poverty (SERP), an agency formed by the Andhra Pradesh Government, is implementing two World Bank-supported projects – Andhra Pradesh District Poverty Initiatives Project and Andhra Pradesh Poverty Reduction Project. The major objectives of these projects are to support existing SHGs, form new SHGs and federate them at the village and block levels. These projects, together, expect to form

over 500 block-level federations. These federations are similar in size and functions to the ones promoted by DHAN. These projects also provide investment funds to the federations to be lent to the SHGs.

Sa-dhan, a network of MFOs in India, recently studied 27 SHG federations. The federations were from all regions of India, with the majority (13) from the south. Nineteen federations provide financial services, while eight (8) do not. Among the 19 providing financial services, only six (6) have strong member control; others are primarily controlled by the promoter agencies. The study concludes that federations involved in financial intermediation are likely to achieve sustainability while those involved only in social intermediation are unlikely to do so.

The primary purpose of federating SHGs is to ensure their sustainability. SHG federations help SHGs internalize all operational costs and reduce the cost of promoting new SHGs. Federations also build solidarity among SHG members by helping them see SHGs as part of a larger organization. This helps build members' stake in the SHGs. Building ownership is important in SHGs since, typically, they are not self-promoting organizations, and the small size of SHGs makes it difficult for their members to visualize them as sustainable organizations.

7. SHG Promotion and Linkage – Regular Support from NABARD

7.1 NABARD'S Support for Capacity Building and Loanable Funds

NABARD provides capacity building assistance and financial support to its partners for the promotion and broad basing of microfinance operations. As part of its efforts to link larger number of SHGs to the banking system, NABARD also focuses on training and sensitization of partner agencies, through various interventions.

7.2 Liquidity Support to Banks for SHG-bank Linkage

NABARD provides 100 percent refinance assistance to banks for financing SHGs.

7.3 Promotional Grant Assistance to NGOs to Function as SHPIs

NGOs already working in the social sector are encouraged to take up SHG promotion as an **"add-on"** activity. This not only helps in complementing the core areas of activities of the participating NGOs but also reduces overheads costs in formation and nurturing of groups. NABARD provides grant assistance of Rs3,000 to NGOs for promotion and linking of each SHG. This amount broadly covers training of members of SHG, stationery for the group, incentive/part salary of NGO staff, etc.

7.4 Supporting RRBs as SHPIs

In order to widen the spectrum of SHPIs, NABARD encourages regional rural banks to take on the role of SHPIs themselves. Under this program, the bank staff at the identified branches are provided with specific training in promotion, nurturing and financing of SHGs. This successfully grooms RRB staff to form SHGs. This module envisages support from NABARD for training of staff of ten identified branches for each RRB, with provision to partly meet the costs of awareness building, training and stationery for the SHGs, which are promoted by them. NABARD provides grant assistance at Rs1,500 per SHG to RRBs for formation and linkage.

7.5 District Central Cooperative Banks as SHPIs

In India, cooperative institutions like district central cooperative Banks (DCCBs) and primary agricultural cooperative credit societies (PACS) have been in existence for the past several decades. They have the potential to emerge as major partners considering their strong presence in rural areas for integrating SHG-Bank Linkage Program in their existing business activities. NABARD has therefore formulated a scheme for assisting DCCBs to form, nurture and link self-help groups. NABARD provides grant assistance at Rs1,500 per SHG to DCCBs for formation and linkage.

7.6 Farmers' Clubs as SHPI

NABARD has been encouraging informal forums called Farmers' Clubs (FCs) to spread the message of 'development through credit' and inculcate the repayment ethics among farm borrowers. These clubs also have significant potential to work as SHPIs. Accordingly, a module has been developed to support them to function as SHPIs. The module envisages financial support to nodal bank branches and FCs for meeting expenditures on (i) awareness building on SHGs among volunteers and nodal branch staff, (ii) training of identified FC volunteers to work as facilitators, (iii) required stationery for SHGs promoted, (iv) reimbursement of expenditure incurred by the facilitators in promotion of SHGs and (v) incentives to the farmers' clubs for acting as SHPI. The module is now helping available independent facilitators like school teachers and primary health workers to form and nurture SHGs.

7.7 Individual Rural Volunteers as SHPIs

In some regions of India where NGOs are not adequately represented, a special initiative has been launched by NABARD to rope in socially committed individual volunteers like retired and active school teachers, postmasters, village elders, social workers and members of existing credit-linked SHGs for the formation of self-help groups and linking them with banks. This scheme is being implemented in some States of the country through regional rural banks and district central cooperative banks. Volunteers are provided with grant assistance of Rs1,200 per SHG for forming and linking them.

7.8 Capacity Building of Partner Institutions in Microfinance

Comprehensive training of the staff of banks, NGOs and government agencies is the key to collaborative partnership of these agencies. This exercise includes designing of course modules oriented towards a wide range of target audience. Suitable reading material and training aids are developed and updated periodically by NABARD. The programs are regularly evaluated to help modify their contents.

7.9 Revolving Fund Assistance (RFA) to MFIs

NABARD provides revolving fund assistance on a selective basis to NGOs, SHG federations, credit unions and other agencies to help them build their financial intermediation capacity for on-lending to SHGs and to prepare them to take bank loans in the future.

7.10 Distance Education Program on SHGs

NABARD has associated with the Indira Gandhi National Open University (IGNOU) in a distance-learning education program for building up a group of quality grass roots trainers in the field of SHGs. NABARD reimburses the full course fee of Rs1,000 for the first 1,000 successful participants of the six-month Certificate Program on "Empowering Women's Self-Help Groups" conducted by the IGNOU. Besides, NABARD has partnered with Yashwantrao Chavan Maharashtra Open University (YCMOU),

Nasik, Maharashtra State in shaping and offering a six-month Certificate Course for Self-Help Group Facilitators focusing on the promotion and nurturing of SHGs. This comprehensive course on the subject offers coverage of topics like empowerment of women, poverty alleviation and issues on social communication at the pre-formative stage of SHGs and aspects like stabilization of group functions and conflict resolution. NABARD has agreed to support by reimbursing the course fee to the first batch of 500 candidates who successfully pass the certificate course examination in the first attempt.

7.11 Collaboration with External Agencies

To support funding of various initiatives leading to designing of products and services, creation and promotion of delivery mechanisms, setting up of new organizational structures and devising systems and procedures which will help improve the access of the poor to institutional financial services, the Credit and Financial Services Fund (CFSF) was set up in NABARD in 1995, with the assistance of the Swiss Development Cooperation (SDC). Most of the microfinance initiatives of NABARD have been funded through the CFSF. NABARD has also collaborated with GTZ, Germany, primarily for supporting initiatives in the field of training and capacity building and development of an appropriate MIS.

7.12 Technology Support to NGOs for MIS on SHGs

Of late, NGOs, that have promoted a large number of SHGs under SHG-Bank Linkage Program, are expressing difficulties in maintaining proper database of the SHGs under their control. This has led to poor monitoring of the groups and decline in the quality of SHGs in a few areas. Computerized management information systems (MIS) of SHGs are expected to facilitate proper maintenance of database and effective implementation of SHG-Bank Linkage Program. NABARD has come out with a support package for encouraging computerization of good NGOs engaged in formation, nurturing and bank linkage of SHGs. NABARD provides a grant of Rs50,000 for purchasing PCs and the required software to such NGOs that have satisfactorily utilized the grant support from NABARD for promotion and linkage of SHGs and should have promoted a minimum of 500 SHGs.

7.13 Documentation of Success Stories

NABARD has also been documenting success stories/best practices for replication elsewhere. In addition, NABARD, at its own expense, mass-publishes each year reading materials for promoting microfinance in the country. It has also partnered with a leading financial daily of India to periodically bring out “Microfinance World”, a microfinance supplement.

8. Innovative Pilot Projects by NABARD

In addition to the regular support programs listed above, NABARD has also recently unleashed a few innovativions to address some unusual areas concerning healthy growth of microfinance in India. The phenomenal growth rate of microfinance sector, especially through the SHG-Bank Linkage Program, has posed a number of issues and challenges which need immediate attention. These programs are basically investment for posterity.

8.1 Application of IT

There are now many branches of commercial banks and regional rural banks that service more than 200 SHG accounts which were hitherto considered impossible. Howsoever welcome the trend may be, the burgeoning numbers have also brought to the fore a host of issues relating to tracking, monitoring and

adequately servicing SHG accounts. It was felt that the best way to deal with the huge numbers would be to take recourse to new technologies available. It has been felt that use of information technology (IT) in the form of processor/memory cards for SHGs and other clients, coupled with automation in a bank branch, would serve to solve these vexing issues and leave adequate time for business development work for the branch manager. NABARD has therefore decided to launch an experiment through five branches each of two RRBs through the introduction of processor/memory cards for active clients and SHGs and automation of book keeping at SHG levels. This is expected to reduce paper work, save time, improve efficiency of the field workers, lower the scope of manipulation, reduce unintended leakages and help maintain up-to-date books at SHG level. The users of processor/memory cards would include SHGs and other good customers of the bank who are its regular customers. About 500 such customers, who would perform all banking transactions on a fast track, would be selected in each bank branch; time taken for banking by these regular good clients is likely to be reduced considerably. The transaction data of each SHG collected from the field could be consolidated at branch office to generate MIS reports, which the branch staff could effectively use to track the functioning of SHGs, ensure prompt credit linkages and recovery. This, coupled with automation of back-office operations of the branch, would ease the branch manager of a lot of time spent on routine matters and they could use the spare time to build new customers and enhance business relations.

8.2 Scheme to Finance Joint Liability Groups

A joint liability group (JLG) is an informal group comprising preferably of four (4) to 10 individuals coming together for the purposes of availing bank loan either singly or through the group mechanism against mutual guarantee. The JLG members would offer a joint undertaking to the bank that enables them to avail loans. The JLG members are expected to engage in similar type of economic activities like crop production. The management of the JLG is to be kept simple with little or no financial administration within the group. JLGs can be formed primarily consisting of tenant farmers and small farmers cultivating land without possessing proper title of their land. The JLGs of such eligible farmers can also serve as a conduit for technology transfer, facilitating common access to market information; for training and technology dissemination in activities like soil testing, training, health camps and assessing input requirements. Banks can finance JLG by adopting any of the two models – Model A – financing individuals in the Group and Model B – financing the group. The JLG would prepare a credit plan for its individual members and an aggregate of that is submitted to the banks. Banks may evolve a simple loan application for this purpose. The individual members of JLG would be eligible for bank loans after the bank verifies the individual members' credentials. The finance to JLG is expected to be a flexible credit product addressing the credit requirements of its members including crop production, consumption, marketing and other productive purposes.

8.3 Project on "Computer *Munshi*" (Computer Accountant)

Quality and regularity of bookkeeping is one aspect of linkage banking which is affected the most because of the widespread illiteracy amongst the poor SHG women. If ignored for a long time, this has the potential to endanger the sustainability of the groups. Another related issue of almost equal importance is the MIS, which means passing on the relevant information about the functioning of the SHGs to the concerned stakeholders like SHPIs and banks. PRADAN, an NGO, has come up with the idea of Computer *Munshies* (CM). The idea involves the identification of skilled rural youth for the task of higher order accounting by providing training as Computer Munshies. The trained individuals would be equipped with a computer and software to serve 100 to 300 SHGs. The SHG level meeting transaction statement will be sent to the CM after every meeting, which will be keyed in by the trained individual using the software which would generate outputs like trial balance, member savings and loan balances. The SHG promoter and the banker could also access data about SHGs from the CM on payment of

a fee. The software captures all the essential data, both financial and non-financial. It also facilitates financial analysis, drawing a trial balance, balance sheet, portfolio analysis, member level impact – by capturing the base line data, etc. The outputs generated could be useful to all related stakeholders including bankers, social intermediaries and the SHG themselves. To test the idea, NABARD has sanctioned a grant assistance of Rs6.10 lakh to the said NGO.

8.4 Grain Banks and SHGs

The tribal population in some parts of India is known to use the concept of Grain Banks (Grain *Golas*) for saving the grains during the harvesting seasons and using them to meet their consumption requirements during the lean and dry periods. They also use the arrangement for borrowing the grains for seed purposes at the time of sowing. In the past too, some of the State and central government interventions in the backward regions had attempted to create the infrastructure of Grain Banks.

Currently, the need for evolving a participatory food security system for backward tribal regions is being actively debated. The strong emphasis on group savings in kind and borrowing in kind under the Grain Bank approach has significant similarities with the SHG-Bank Linkage Program, with the only difference being that the savings and loans are in kind. The issue, therefore, is how to facilitate monetization of the savings and loans in kind and integrate the traditional approaches into the monetized microfinance system. Such integration would enable the poor tribal population to access need-based financial services and also address the issues of food and seed securities. The project is to enable the poor to save in kind, raise resources against such savings, participate in food security systems and also provide access to seeds for sowing purpose in the times of distress. Apart from the savings in cash, monetization of the savings-in-kind and loans to SHGs against their stock of grains would be considered by the Bank. Members would save and draw loans both in cash and/or kind, depending upon their convenience.

8.5 Rural Volunteers as Book Writers

Low literacy levels of SHG members, resulting in heavy dependence of SHGs on SHPIs for record keeping, is one of the constraints in extending the linkage program in resource-poor areas. Keeping this in view, NABARD, based on interactions with banks and NGOs, has launched a pilot project for associating local rural volunteers as book writers for SHGs to improve the regularity/accuracy in the maintenance of books of accounts, and to explore a possible evolution of MIS between SHGs and banks. A grant assistance of Rs7.50 lakh has been sanctioned to cover honorarium to the book writers, cost of their training and the stationery required for bookkeeping of SHGs.

8.6 Project on *'e-Grama'*

With the aim of equipping and enabling villagers and SHGs members to access information, NABARD has partly funded the establishment of 13 Village Information Centres (*e-Grama*) through an NGO in the southern State of Karnataka. The technology-integrated information network covers various areas like weather conditions, crop inputs, product prices, land records and other useful information for the rural folk. Besides, many add-on services like bookkeeping of SHGs, and scanning are also envisaged to be provided. The NGO has facilitated setting up 50 centers including 13 with NABARD's assistance. Commercial banks and RRB are extending necessary credit support to the entrepreneurs.

8.7 Financing Rythu Mithra Groups

Rythu Mithra Groups (RMGs) or Farmers' Friends Clubs, are being promoted by the Government of Andhra Pradesh to bring about a marked improvement in the lives of small, marginal and landless farmers

through collective action. RMGs are expected to serve as a conduit for its members for technology transfer, facilitate access to market information and market, assist in carrying out activities like soil testing, training, health camps, assess input requirements, etc. All commercial banks, RRBs and DCCBs in the State participating in the project and are extending loans to the Clubs.

8.8 Social Security System for SHG Members

Another innovative project which has been approved by NABARD entails the creation of community-based social security system for members of SHGs in rural areas for improving their livelihood and securing them from uncertainties of life. The project components include the provision of a package of health insurance, life insurance, etc. for SHG households by paying premium generated through discounts offered by service providers like grocery shops and cloth merchants in the project area for SHG members in rural areas. It is being implemented through the Organization for Awareness of Integrated Social Security (OASiS), an NGO, in two villages covering 500 poor households in a district in the Central State of Madhya Pradesh, involving a grant assistance of Rs8 lakh from NABARD. Self-employed groups (SEGs) from SHGs would be formed by the NGO to provide various services involving selling of products at a discount.

As may be seen, there is a wide array of activities and areas with which NABARD is closely associated as the initiator and fund provider with the eventual objective of continuously scaling up the promotion, nurturing, linkage and sustainability of SHGs. No wonder then that more than 400 women join the SHG movement in India **every hour just as one** NGO joins NABARD's microfinance program **every day.**

9. Evolution of Microfinance Institutions (MFI) in India

The provision of credit to the poor people has been one of the main concerns of policy planners in India since independence and cooperatives were the only formal financial institutions providing credit to the poor. To augment the credit flow to this sector, commercial banks were nationalized in phases beginning 1969. Since then, there has been a massive expansion of commercial banks in terms of number of branches in the unbanked areas. In addition to the rural credit delivery structure, regional rural banks (RRBs) have been set up in India since 1975 as a unique institution, in the sense that these are meant to be local institutions, familiar with the local conditions and at the same time being commercial in its range of operations.

Today, India's formal financial sector is amazingly vast and consists of commercial banks, regional rural banks and co-operative banks. As many as 32,885 rural and semi-urban branches of commercial banks, 14,303 branches of RRBs and nearly 92,000 rural outlets of cooperative banks are engaged in microfinance activities. The banking infrastructure has evolved over a period of time through various policy interventions. The main driving force behind these policy initiatives has been to create infrastructure to improve credit flow, particularly to the poorer sections of society. Despite this massive infrastructure of banks, **36** percent of the rural indebted households are still dependent on the informal sector. This dependence on the informal sector is much higher in the case of the lower-asset group.

The mechanism of *directing* credit to the poor through sponsored programs has suffered from poor recovery rates that had made a reverse impact on the recycling of credit. Also, there has been a mismatch between what the poor needed, particularly, in terms of products and product delivery mechanisms and what conventional financial institutions could offer. To fill the gap that has arisen due to this mismatch, microfinance institutions (MFIs) have emerged.

MFIs are broadly understood as the institutions other than banks that are engaged in provision of financial services to the poor. However, this understanding equates microfinance just as credit for microenterprises while the poor also need savings, consumption loans, housing loans and insurance services. True-blue microfinance institutions are those that provide thrift, credit and other financial services and products of very small amounts mainly to the poor in rural, semi-urban or urban areas for enabling them to raise their income levels and improve their living standards.

Analyzing the current scene of microfinance services, a new type of loan methodology is seen to be evolving that is somewhat hybrid in nature. It considers itself in the business of improving livelihoods, in which 'livelihood financial services' is one piece. It places equal emphasis on the provision of agricultural, business, development and technical services in addition to the provision of financial services, which includes credit but is not limited to it. Credit is not sufficient alone to guarantee an improvement in the livelihoods of the rural poor. It is believed that other financial and technical services are necessary and can be provided on a revenue model in order to be sustainable.

10. Microfinance Institutional Structure in India

Different organizations in this field can be classified as "**mainstream**" **and** "**alternative**" microfinance institutions.

10.1 Mainstream MFIs

NABARD, Small Industries Development Bank of India (SIDBI), Housing Development Finance Corporation (HDFC), commercial banks, regional rural banks (RRBs) and the credit co-operative societies are some of the mainstream financial institutions involved in extending microfinance.

10.2 Alternative Microfinance Institutions

These are the institutions that have come up to fill the gap between the demand and supply for microfinance. Based on organizational forms, MFIs can be divided into three categories as under:

- **Not-for Profit MFIs**
  - Societies registered under Societies Registration Act, 1860 or similar State Acts
  - Public Trusts registered under the Indian Trust Act, 1880 or any State enactment governing religious or charitable public trusts
  - Non-profit companies registered under Section 25 of the Companies Act, 1956 that are specifically exempted from registration with RBI

- **Mutual Benefit MFIs**
  - State Credit Cooperatives
  - National Credit Cooperatives
  - Mutually-Aided Cooperative Societies (MACS)

- **For Profit MFIs**

  Non-Banking Financial Companies (NBFCs), registered under the Companies Act, 1956 and as defined in the Reserve Bank of India Act, 1934, whose principal business is the provision of microfinance.

11. Growth of Microfinance in India

Microfinance has made great strides in India during the recent times. The self-help group-bank linkage program (SBLP) has continued to make good progress, but at a slower pace. Based on the "State of the Sector Report 2009 on Microfinance", the following are some of the quick highlights pertaining to the year 2008-09:

- MFIs have recorded about 8.5 million clients during the year 2008-09, a growth of 60 percent over the previous year.
- More than 50 percent of low-income households are covered by some form of microfinance product.
- The total outstanding microfinance loans posted a growth rate of 30 percent (Rs359.39 billion) over the previous year's level of Rs229.54 billion.
- The overall coverage of the sector is estimated to have reached 76.6 million against 59 million in the previous year.
- The SHG loan outstanding has increased by Rs71.5 billion with an addition of 6.90 million clients.
- At the current growth rates, MFIs might outstrip the SBLP in portfolio volumes soon.
- Some parts in India faced entrenched default constituting a portfolio share of less than 0.50 percent.
- MFIs so far have reached 234 of the 331 poorest districts identified by the Government of India.
- SBLP registered a decline of number of women SHGs from 82.5 percent in March 2007 to 80.4 percent in March 2008.
- The microfinance penetration index shows wide variation among States in India and while the southern States have done very well, the progress is slow in eastern, central and other States.
- The sector is thus continuing to experience an uninterrupted growth rate despite several internal and external adversities.
- In the southern States, a point of saturation has been reached with families being in multiple groups, as also borrowing loans from more than one MFI. This leads to the same set of clients being counted by each SHG or MFI with which the client is linked. Precise numbers on the extent of such multiple loans are not available and difficult to estimate. A mechanism for compiling data on the numbers is necessary to produce reliable information.
- However, the expanded outreach and increased loan disbursement have to be seen in the context of the quality of what has been achieved. The quality dimension is basically examined from the width and depth of outreach achieved. The distribution of the microfinance services across the country and also the coverage of the most vulnerable sections of population are matters for closer scrutiny. The north, east and north-east still have considerable headroom to grow. In terms of coverage of the vulnerable, it is difficult to conclude that the most poor have been prioritized. Studies and anecdotal evidence point to the coverage of the upper strata of the poor and not so much of the ultra poor.
- In the case of SHG linkage, except the government-sponsored programs that are mandated to focus on poor, the other efforts do not prioritize the poorest.

- The SBLP has hit a plateau in the southern States, with new groups linked being less than that of the last year, impacting the growth numbers for the country as a whole. The slowing of the pace in SBLP should provide the space and resources for consolidation and deepening of the financial services among the SHGs. In that sense, the lower growth rate should be seen as a positive development in the saturated southern States.
- In terms of geographical coverage, only well-endowed and high-growth areas have been prioritized. The expansion within such areas has also not consciously targeted the poor. The most vulnerable are not clients of choice, for most organizations engaged in SHG promotion or MFI lending.
- The other dimension of quality of expansion is the depth of services. The numbers reached have been significant and to some extent, the volumes have been substantial. But the expansion lacks depth. Needs fulfillment of the clients does not seem to have taken place. The total potential of each client in terms of a variety of loans, savings, insurance and other services has not even been surveyed by the institutions. The average loans per client in both MFIs and SHGs have been low; between Rs3,500 and Rs5,000. The duration of the loan is short, typically one (1) year or less. The small loan size and short duration do not enable most borrowers to do much except to ease liquidity problems.
- The number of institutions providing microfinance has increased. The number of MFIs reporting to Sa-Dhan increased to 233 in 2008. Per information available with NABARD, by the end of March 2007, 334 MFIs had availed loans from the banking system. There is an increased availability of funding from financial institutions and donors. Continuing the trends seen in the last year, there is a heightened activity in the private equity and venture capital spheres.
- A much deeper structural change that is set to sweep the microfinance landscape is the transformation of NGOs into lending institutions. There is a strong movement towards the transformation of NGOs' promotional work in dealing with the poor into commercial microfinance operations through a variety of means. Besides, urban microfinance has also caught the fancy of both MFIs and funders. The industry leaders and mid-level NGOs/MFIs are foraying into urban markets with large business plans.
- The beginning of new funding instruments and new funding avenues are being seen in the market. Equity placements are no longer exceptional and forbidding; they are tending to become familiar and even welcome. Bulk funds have been flowing into the sector from not only the traditional funders but also the public sector, private sector and foreign banks. Large ticket loan deals are easier in the present environment of vigorous growth. Donor support too continues to flow.
- On the technology front, the use of handheld devices, varieties of smart cards and mobile phone-based collection and payment processes have been experimented. Immense effort involving several banks in smart card-based benefits payments to bank accounts under the National Rural Employment Guarantee Scheme (NREGS) is being experimented. A mobile-based transaction process has been fairly effective and seems to have potential for main stream application, once the surrounding regulatory issues are resolved. Telecom Companies like Vodafone, Airtel and Tata Telecom have been in the news promising financial services on their networks.
- The Government has brought about a simplified life insurance scheme covering vulnerable sections of people with a low, subsidized premium. Life Insurance Corporation of India (LIC), one of the largest insurance companies in the world, has launched a "Janashree Bima Yojana" scheme to cover all women SHGs that are credit-linked to the banks. LIC has already written about 40 million policies under the scheme.

- It will be seen that MFIs are broadly divisible into two categories. The first set consist of institutions registered under diverse legislative frameworks and not regulated by RBI. The share of these institutions in credit (40 percent) relative to their numbers (98 percent) is not significant at the disaggregated (MFI) level. On the other hand, as few as five (5) MFIs for which data is available and which are registered as NBFCs and regulated by RBI purvey 60 percent of ground level credit by MFIs. In short, India has a large number of MFIs with diverse legal forms, varying significantly in size, outreach and credit delivery methodologies.

Overall, the year has not only been one of vigorous growth, increased interest and awareness levels on the part of institutions, initial attempts at improving the finances and governance, but also of an increased risk potential that seems to come under greater scrutiny. Certainly, more clients are served today than before. The growth in outreach points to the potential that exists. But are these clients being served well? The impression is that widening is targeted at the cost of deepening. The 'touch and move on' method of expansion of services could not only result in sub-optimal services to the clients, but also reduce profitability of MFIs. The slow growth of average loans in case of SHGs reveals a lack of enthusiasm for increasing loan volumes by banks. The reduced number of new groups linked to banking system indicates a loss of appetite for SHG clients. The slowing down, however, might help in consolidation and deepening. The congruence of policy intent, business interests, enterprise opportunity, technological edge and a virgin market make up for an exciting amalgam in the financial inclusion sphere. The inclusion objective is tough, but doable as long as all the stakeholders keep the poor people first in their list of priorities.

12. Overview of MFO Sector

An inventory of 786 MFOs in 13 states carried out under NABARD-GTZ Rural Finance Program has brought out the following key revelations:

- **High geographic concentration** – 75 percent of MFOs in two states, Andhra Pradesh 61 percent and Tamil Nadu 13 percent;
- **Highly atomized and decentralized** – 95 percent of MFOs operate in not more than one state and 68 percent operate in only one district.
- **Young age** – majority of MFOs (58 percent) are rather young and have been established in the past five years.
- **Extreme polarization in numbers and loan amount** – only 4 percent of MFOs (companies) account for 67 percent of the total loans outstanding and the majority of microfinance clients.

13. Maturing Microfinance – Emerging Challenges

Despite the massive efforts of all stakeholders to make the Indian SHG movement the largest in the world, the World Bank estimates that the Indian microfinance activity currently reaches only four (4) percent of the poor. The village-level "money-lender" is still supreme, holding average outstanding loans at a level which is far higher than that under SHGs'. A national government survey a few years ago had found that 22 percent of all cultivator households accessed credit from informal sources and only 27 percent from formal sources. It clearly appears that, in spite of the rapid growth in the past, the supply of institutional credit is well below the demand.

There are several emerging issues and challenges facing the microfinance sector in India that would need to be addressed suitably for sound consolidation and growth of this sector in the times to come. These issues are discussed in the following paragraphs.

Microfinance has gone beyond the take-off stage and has shown vigorous growth in many parts of the country. Over the last few years, both the models of delivery have posted very good growth rates. However, the expansion with some exceptions lacks depth. Growth is confined to credit, with very little insurance and even, less savings coverage offered. Even in credit, increase in client numbers accompanied by increase in geographical coverage did not lead to deeper engagement with clients in terms of larger loans and diversified products. The shallow engagement with the clients on account of the 'touch and move on' business models rendered the operational costs high. The operational costs could have declined more rapidly if 'higher per client' business had been targeted. Consolidating the existing client base and fulfilling their financial services needs more comprehensively hold the key to lower costs, higher returns and client loyalty. The intense competition in the sector warrants better client retention strategies in terms of costs and products.

Commercial funds are available to a much larger extent than ever in the past. But funds do not flow freely everywhere. The larger MFIs, professionally run medium-sized ones and some of the smaller MFIs find it easier to access funds. SHGs do find it easy to get the first linkage in several states and even after linkage, the size of loans remains small. Equity funds have started flowing from large and small equity investors and also institutions like SIDBI and NABARD. The capital requirements of existing companies are set to escalate with the resetting of the regulatory capital norms. The non-company MFIs require more capital funds in view of the very high leverage ratios. Considerable work has to be carried out by NBFCs to become equity-friendly and create a positive investment environment. It is difficult to predict the form and avenue of capital funds flows to the non-company MFIs. Quasi-equity and long-term loans might substitute for equity, but such investments may not figure high on the list of preferences of investors.

Mission Drift is more often mentioned in discussions. The admiration for the pace of growth is accompanied by unease at the manner and content of expansion. The yearning for organizational transformation in many cases does not seem to be a well thought-out strategy of up-scaling operations, but seems an image-makeover exercise. Community-owned and managed forms seem to be out of fashion. Most transformations involving MFIs tend to result in erosion of public goods. The donors, funders and industry leaders need to have a serious rethink of the pattern of growth, which is tending to become one-dimensional toward private profits. Community-owned financial institutions designed as 'for profits' would probably target double bottom lines better than privately owned forms.

The initial experiments with cell phone solutions promise a lot. They have the capacity to up-scale rapidly, as both the infrastructure and software are not constraints. Cellular finance might emerge as an alternative to brick and mortar MFIs with significant competition for the medium and small MFIs. Technology and platform providers might take to finance rather than providing a space for MFIs to operate on their technology and infrastructure. In the Business Correspondent/Business Facilitator (BC/BF) sphere, such developments have already taken place where technology providers have set up entities to function as correspondents with multiple banks. *Vodafone* and *Airtel* have announced their intentions of entering the financial sector space. Such large players have the muscle required to roll out services across the country. Cell phone companies' familiarity with client acquisition in new markets and compliance with Know Your Customer (KYC) norms should place them at an advantage over other competitors.

Although the BC/BF scheme is slow in taking off, there are signs of faster growth. The initial learning period seems to have been a long one in which the banks have done their preparatory work. The regulatory norms on location of banking correspondents have come as a dampener. The BC arrangement has the potential to provide stiff competition to MFIs. BCs, operating as agents of mainline banks, are in a position to offer a variety of services including the critical savings services. This provides them an edge over the MFIs. Banks are investing in technology to strengthen the BCs' capacity to provide efficient services to the clients and seamlessly work with the bank's own accounting and information systems. This

might prove to be a critical difference in the market place where technology adoption among MFIs is not very high. When the competition intensifies, some of the larger MFIs may appoint BCs to survive.

The MFIs, in order to be ahead of the game and offer a viable alternative to clients, should add other features to their present basket of services. The entry of large corporate players is likely to intensify the competitive pressures. Apart from technical and human capacities, deep pockets might be needed to counter serious competition from large players.

Regulation is an aspect that would continue to be watched by the sector. While the NBFCs are being brought under increasing regulatory rigor, the NGO/MFIs are not subject to much regulation. The weak regulation attempted through passing the Microfinance Bill into a statute is not likely to protect the large number of clients that borrow from the NGO/MFIs. Regulatory stance must move from the position that only depositors' interests need to be protected. The small borrowers are equally active in the local economies, and they invest their future compared to savers who sacrifice only their past with the financial institutions. The millions of microlivelihoods that critically depend on continued availability of credit need to be protected. This would call for a significant change in the regulatory stance. The Central Bank of the country must design means for effectively regulating the credit activity that takes place in the vulnerable sections of the economy although they may not be systemically significant.

Avenues for savings need expansion. Saving has been an aspect of microfinance service that has, by and large, been left to the working of SHGs to do. The MFIs neither actively pursue this nor those who pursue do so in a manner designed to produce best results. The regulatory clearances required to mobilize savings mostly preclude MFIs. The regulator has to take a view as to whether institutions set up at a great expense with adequate infrastructure and manpower should work to only one-half of their potential. The issues relating to depositor's safety needs are to be addressed separately through a mechanism of deposit insurance.

Microinsurance, despite the potential, has a long way to traverse. The present market is more dependent on government initiatives. The insurer and MFI/NGO-led initiatives are far too small to be significant in the context of the size of the market. Life and health insurance products are receiving attention; while on other risks, there has not been much action. Even where the government has come out with good products, distribution to the potential clients has been difficult for want of partners across the country. The area of immediate action in insurance seems to be in recruitment of partners for distribution of insurance and marketing campaigns. MFIs stand to gain in the distribution of insurance.

Clients, despite becoming large in numbers, are still in the fringes of the sector. Supply being severely limited when compared to demand, the market is dominated by the sellers. As the clients are from vulnerable sections, the presumption is that they are unequal in dealing with any financial institution and would be subject to exploitation. Client protection in such markets is the responsibility of the State. Before the issue becomes a core concern of the State, the sector has to voluntarily introduce safeguards that improve client protection. Grievance redressal mechanisms within each institution and across the sector are necessary. The code of conduct should be strengthened and mechanisms of compliance, put in place.

Shortage of human resources is undoubtedly the major problem that would impact the sector during the next two years. While few efforts have been taken to create academic courses at universities and management institutes, training courses for personnel to improve their industry readiness is not available in general. The institutions have to organize in-house training for the new recruits as well as existing staff. Industry-level investments in training, including infrastructure, must be enhanced.

Microfinance has to develop a greater sensitivity to the needs of the poor clients. The small loans should give way to livelihood support loans of a larger size and longer duration. Only when livelihoods and incomes are targeted can the microfinance sector claim that its mission is achieved.

To enhance the outreach of the microfinance services to the needy, the legal, regulatory, organizational, systemic and the attitudinal problems need to be addressed and the desired changes brought about to make them more effective. With a majority of the customers being illiterate, needing consumption loans and a majority of the lenders requiring high documentation and collateral security, the products are not reaching the rural poor.

Although the interest rate offered to the borrowers is regulated, the transaction costs in terms of the number of trips to be made, the documents to be furnished and the possibilities of illegal charges to be paid result in increasing the cost of borrowing. This makes the exercise less attractive to the borrowers.

14. Scaling up of Microfinance Program in India

The role of NABARD in the growth of microfinance model has been multidimensional, focusing on policy formulation, financial innovations, technological interventions and institutional strengthening. The following are the specific initiatives by NABARD towards scaling up the microfinance program:

14.1 Rajiv Gandhi Mahila Vikas Pariyojana

The project has been primarily designed by NABARD. The Rajiv Gandhi Mahila Vikas Pariyojana (RGMVP) is a special initiative for promotion, credit linkage and formation of SHG federations in select districts of the State of Uttar Pradesh. The project aims to replicate the SHG institutional model implemented under the UNDP-South Asian Poverty Alleviation Program (SAPAP) in Andhra Pradesh in collaboration with the Society for Elimination of Rural Poverty (SERP), Government of Andhra Pradesh.

The project envisages promoting and credit linking 22,000 SHGs, 1,100 cluster level associations (CLA) and 44 block level associations (BLA) in collaboration with participating banks and implementing NGOs within the implementation period of eight (8) years (2007-2014). The strategy involves using professional and trained resource persons to provide continuous handholding, training, extending support to SHGs and their federations at cluster and block levels. Demonstration effect of the external community resource persons on the rural population is an important part of the project.

14.2 Pilot Project for promotion of Microenterprises

The pilot project for promotion of microenterprises among members of mature SHG is based on the 3M approach (microcredit, micromarket and microplanning). It is being implemented by 14 NGOs acting as microenterprise promotion agency in nine districts in as many States in India. Under the project, 11,000 SHG members have been identified to take up microenterprise through credit support. Cumulatively, 6,107 microenterprises were established by 31 March 2009.

14.3 Support to Microfinance Institutions

Recognizing the role of MFI in supplementing the efforts of the formal banking network in providing credit support to unreached clients for inclusive growth, NABARD supports them through grant and loan-based assistance from the Microfinance Development and Equity Fund (MFDEF). The MFDEF, with a corpus of USD40 million, contributed by different partners and maintained by NABARD, is used for

promoting microfinance through up-scaling the SHG-bank linkage program, extending Revolving Fund Assistance (RFA) and capital support to MFIs and supporting various promotional initiatives/activities. The Advisory Board of MFDEF, consisting of representatives from RBI, commercial banks, professionals with domain knowledge and NABARD provide guidance in formulation and refinement of policy initiatives. Some of the major supports provided by NABARD to MFIs are as follows:

- **Revolving Fund Assistance** – NABARD has been selectively supporting MFI for on-lending to the unreached poor and also experimenting with various microfinance models to innovate alternative, sustainable and replicable credit delivery systems.
- **Support for Rating of MFIs** – NABARD now provides grant assistance to MFIs directly to enable them to avail the services of the accredited rating agencies for their rating. Under the scheme, NABARD meets the cost of rating to the full extent of the professional fees, subject to a maximum of Rs3.00 lakh. The assistance is available only for the first rating of the MFI. Only MFIs with a minimum loan outstanding of Rs50.00 lakh, seeking capital/equity support and/or RFA from MFDEF and not possessing a current rating/grading report from any rating agency are eligible.
- **Capital Equity Support** – The scheme seeks to enable MFI to leverage capital/equity for accessing commercial and other funds from banks for providing financial services at an affordable cost to the poor and achieve sustainability in credit operations over three to five years. NABARD also provides for capital support to start-up MFI with potential to scale-up their activities but lacking in capital, infrastructural facilities and managerial skills. Microfinance organizations (MFOs) and MFI-NBFC, identified as 'start-ups' on the basis of area of operation, client outreach, lending model, borrowing history, etc., are eligible for support under this scheme. The financial support from NABARD is in the form of unsecured, sub-ordinate debt and the quantum of support is commensurate with the business plan of the MFO/MFI-NBFC but shall not exceed Rs50.00 lakh. The assistance, repayable in seven (7) years (with two (2) years' moratorium) but with no option for pre-payment, carries an interest rate of 3.5 percent p.a. for MFO and the prevailing bank rate for the MFI-NBFC.
- **Support to SHG Federations** – Recognizing the emerging role of the SHG Federations in nurturing of SHG, enhancing the bargaining powers of group members and promoting livelihood NABARD introduced a flexible scheme to support such federations on a model neutral basis during 2007-08. The broad norms identified for supporting SHG federations stipulate that the federations should be need-based, member owned/driven, democratically managed with members at liberty to join/become self-managed over three years, etc. Support to federations is extended by way of grant for training, capacity building, exposure visits of SHG members, etc., and also under all existing promotional schemes of NABARD.

15. Policy Environment and Regulation

India seems to be a very peculiar case when it comes to microfinance regulation and supervision. It is not only its sheer size that makes it very different from all others countries; involvement of formal public sector banks is also much stronger than anywhere else. India today has a huge and very extensive banking infrastructure as may be seen from below (Position as on 30.06.2009):

Bank	Number	Total Branch Network	Rural Branch Network
Scheduled Commercial Banks	85	65,225	20,058
Regional Rural Banks	86	15,144	15,144
Cooperative Banks – Long term	20	1,581	1,561
Cooperative Banks – Short term	31	107,503	107,503
Total	**222**	**189,480**	**144,266 (76.14%)**

Regulation has been an intensely debated aspect of the microfinance sector's functioning. The divisions within the sector as to what needs regulation, which should regulate and how it shall be done are yet unresolved. Given the other developments that have taken precedence over the problems of the microfinance sector, it remains to be seen whether the bill will become a statute during the current year. Although the debate on regulation seems determined to continue, the microfinance sector is not in a regulatory vacuum. Significant part of the clientele of microfinance is with institutions that are under direct or indirect regulation.

The self-help groups linked to banks are, in Reserve Bank of India's (RBI) viewpoint, under the indirect regulation of RBI as the norms for engagement with SHGs as clients have been stipulated by RBI. Further, the banks are regulated by RBI under the Banking Regulation Act. Regarding microfinance institutions (MFIs), of the reported clientele of 14.1 million, 9.56 million are subject to the direct supervision of RBI as non-banking financial companies (NBFCs) (both for-profit and non-profit). About 4.53 million clients served by trusts, societies and cooperatives are outside regulatory coverage.

The need for an appropriate policy and regulatory framework for microfinance has been engaging the attention of policy makers for a long time. In 1998, a 'High-Power Task Force on Supportive Policy and Regulatory Framework for Microfinance' was set up by NABARD at the instance of Reserve Bank of India. Key stakeholders such as GOI, RBI, NABARD, banks and NGOs were represented in the Task Force. The objective of the Task Force, *inter alia*, was to suggest a regulatory framework that would create an enabling environment for MFIs to improve their operations. It recommended the regulation of MFIs whether deposit facilities were offered by them or not and the amount of savings mobilized could determine the extent of regulation. From a long-term perspective, the Task Force favored the setting up of a system of self-regulatory organizations.

As self-regulatory mechanisms take time to evolve, and as an intervening arrangement, a regulatory framework for MFIs was recommended with the following broad features:

- **For NGO-MFIs** – The Task Force proposed that the regulation and supervision of **NGO-MFIs** could involve the following:
  - **Registration of NGO-MFIs** – The first step for regulation proposed is a mandatory registration with a competent authority. While registration under Societies Registration Act, Indian Trusts Act or any other Act, provides legal status, this registration does not

empower them to undertake microfinance services. This is considered necessary as NGOs engaged in microfinance activities are operating without any license from the financial authority.

- **Receipt of Periodic Information** – NGO-MFIs should be required to furnish the operational/financial information to an authority designated for the purpose.
- **Proposed Regulation** – The framework proposed for regulation of NGO-MFIs is as under:
  - **MFIs purveying credit only**: There need not be any regulation for the MFIs purveying **credit only** and not involved in mobilizing savings in any manner. Once the initial registration is done, the agencies may furnish only periodic statements providing details of their financial operations.
  - **MFIs purveying credit and mobilizing savings from the clients and loanees**: The Task Force was of the view that those NGO-MFIs mobilizing savings not exceeding Rs2.00 lakh at any point of time, might be excluded from the regulatory norms. They may, however, obtain registration and submit periodic information to the competent authority.
  - **MFIs purveying credit and mobilizing savings from the clients/loanees (above cut-off limit)**: For those MFIs mobilizing savings above Rs2.00 lakh and below Rs25.00 lakh, the regulation may comprise a minimum reserve of **10** percent of savings mobilized. In respect of MFIs having savings above Rs25.00 lakh, reserve requirement may be **15** percent of the savings. In addition, these MFIs should be subjected to compliance with prudential norms regarding income recognition, asset classification and provisioning.
  - **Supervision of MFIs**: The Task Force recommended that NGO-MFIs should also be subjected to supervision right from the beginning like any other agency in the financial sector. However, the norms and the parameters could not be as stringent as in the case of banks and financial institutions and a system of off-site supervision would be adequate for such institutions.
- **For NBFCs** – The Task Force observed that NBFCs engaged in microfinance are subjected to the same regulations as applicable to other NBFCs. It was proposed that the net owned funds requirement for NBFCs engaged in microfinance should be reduced to the level of Rs25.00 lakh.

The regulatory effort in bringing a new bill thus addresses a small number of clients. In fact, the effort should be on unifying, improving and consolidating the present regulatory framework and apply it across all MFIs without any form-related distinctions on prudential norms. The non-banking financial companies engaged in microfinance are regulated by the Reserve Bank of India (RBI). In the case of not-for-profit companies, there is more of benevolent oversight that exempts them from any kind of regulatory exercise, except that of filing information in the appropriate returns. In the case of other non-banking financial companies in microfinance, the RBI treats them on par with other NBFCs. The sector norms relating to capital adequacy, prudential requirements, issues relating to governance, borrowing and lending norms, apply evenly on these NBFCs. Some of the problems arising from regulation that these NBFCs are facing have been raised in various platforms by the industry practitioners. One of these relates to the difficulties in accessing commercial borrowing in foreign currency. The other relates to the high level of capital that has now been stipulated for NBFCs.

16. Microfinancial Sector (Development and Regulation) Bill, 2009

The Microfinancial Sector (Development and Regulation) Bill was introduced in the Parliament in 2006 and has undergone several changes from time to time and is still under consideration of the House. The salient features of the draft Microfinance Bill, as at the beginning of 2010, are as follows:

- Enactment of the bill will give NABARD explicit powers to regulate the microfinance institutions which will, in turn, ensure greater transparency, effective management and better governance. This will facilitate the flow of microfinance services in a more efficient way to the un-banked population.
- The term "**microfinance services**" means and includes "provision of financial assistance to the eligible clients, either directly or through group mechanism, for small and tiny enterprise, agriculture, allied activities including consumption, up to an amount not exceeding Rs50,000 in aggregate and up to Rs150,000 for housing purpose or such other amounts for the above purpose or such other purposes as specified by the NABARD from time to time".
- M**icrofinance Organization** is defined as "an organization, other than a group, established for the purpose of carrying on the business of providing microfinance services to eligible clients and includes the following:
  - A society registered under the Societies Registration Act, 1860 and any other State enactment governing such societies;
  - A trust created under the Indian Trust Act, 1882 or public trust registered under any State enactment governing trust for public, religious or charitable purposes;
  - A co-operative society or mutual benefit society or mutually-aided society registered under any State enactment relating to such societies or any multi-state co-operative society registered under the Multi-State Co-operative Societies Act, 2002 but does ***not*** include:
    - A co-operative bank as defined in clause (cci) of Section 5 of the Banking Regulation Act, 1949; or
    - A co-operative society engaged in agricultural operations or industrial activity or purchase or sale of any goods and services; Society registered under the Societies Registration Act, 1860 or a Trust created under the Indian Trust Act, 1880 or Public Trust registered under any State enactment or a Co-operative Society engaged in Microfinance service, excluding a Co-operative Bank as defined under the Banking Regulation Act, 1949".
- It differentiates between organizations accepting "thrift" and those not accepting "thrift". The term thrift is defined as "any money collected by a group or a microfinance organization from its members, not exceeding such amounts and subject to such terms and conditions as may be prescribed". Thrift-receiving organizations will be kept under sharp focus. No microfinance organization would be able to accept thrift unless it obtains a certificate of registration from the NABARD, subject to fulfillment of certain conditions.
- Every microfinance organization registered with NABARD under this Act shall create a reserve fund and transfer therein a sum, not less than 15 percent of its net profit or surplus realized out of thrift services and microfinance services every year as disclosed in the profit and loss account or income and expenditure account before any dividend is declared or surplus is utilized for any other purpose.
- It provides for the creation of a Microfinance Development Council for advising NABARD on formulation of policies.

- It provides for facilitating constitution of a Microfinance Development and Equity Fund to provide loans, refinance, grant and seed capital to MFOs. The fund will be managed by NABARD and will consist, as fund sources, of all Government grants received and fees payable under this Act, all sums that may be raised by NABARD from donors, Governments, other entities, and public for the purpose of this Act, any interest or other income received out of investments made from the Fund and the balance outstanding in the Microfinance Development and Equity Fund maintained by NABARD before the commencement of this Act.
- It will provide a redressal mechanism through a Scheme of a Microfinance Ombudsman.
- It will provide penalties for violation on the provisions of the Act.
- It will authorize the Central Government to make rules and authorize NABARD to formulate regulations with the previous approval of the Central Government.

17. Microfinance Bill – Overall assessment

The proposed bill is the second-best compromise. It seeks to legitimize and legalize the existing practices (thrift) while there is no long-term vision of an inclusive financial sector where microfinance will be fully integrated. There have been extreme views on the current state of regulation and the proposed future framework. An unbiased reading of the situation appears to be that a deliberately weak regulatory effort has been designed to let the microfinance sector have the flexibility to grow. Once the growth is achieved and the institutions become significant in size and outreach, they would be subjected to regulation. This is already seen in the gradual tightening of prudential norms on NBFC-MFIs. A comprehensive, regulatory effort on a small part of the financial sector without commensurate benefits does not seem justified.

The microfinance bill that has been in the public domain for long does not seem to be reaching a conclusive stage. After several announced deadlines, the bill seems to have entered a comatose phase. The divisions within the sector as to what needs regulation, who should regulate and how it shall be done are yet unresolved. As there is no consensus emerging from the sector on the regulatory aspects, the standing committee on finance have not been able to reach a conclusion. The available information on the discussions indicates that an interest cap is being debated, which if introduced may not serve the sector well. Given the other developments that have taken precedence over the problems of the microfinance sector, it remains to be seen whether the bill will become a statute anytime soon.

18. Issues and Challenges on the Horizon

As the nation debates the bill in the Parliament and outside, there are several other issues that are not covered in the proposed bill and these issues would need to be properly dealt with a sound regulatory framework in place in India in the future:

18.1 Prudential Norms

As the microfinance bill has not yet been passed into a statute, a regulatory void, though small, continues to exist. The non-governmental organization (NGO) MFIs and other non-company entities are by and large ignored or, at best, left to the State governments' desire to regulate. The lack of regulation of these entities also implies a certain lack of information on the volume and the nature of their activities which makes it difficult to judge when they become systemically important. There are reported incidences of frauds and misappropriations in some of these institutions. These are not taken seriously and are ignored as an unavoidable part of a growing sector. However, unless frauds are seriously viewed at the MFI and higher levels, the clients' interests may be compromised. The absence of regulation of non-company MFIs

also results in uneven regulation and provides for the new start-up institutions to settle for the minimum tolerable standards. Some of these have acquired a large number of clients that have assets equivalent to the systemically important NBFCs as defined by RBI. Mission drift is a small threat when compared with the transfer of assets and liabilities that take place between NGOs and MFIs within the same group and movement of costs and profits across different books of accounts. As these happen in the regulatory void, remedial action, if at all feasible, is slow and protected.

18.2 Remittances

Remittances are an area of interest to the vulnerable section of people and, as a consequence, to MFIs/NGOs. Given the high level of migration in search of livelihoods, remittance of money from the point at which the migrants earn to the point at which it is spent by their families is a critical requirement. Today, the available remittance facilities are unsatisfactory, costly and are also difficult to access. With core banking solutions being put in place by the banking system and decent branch network in several parts of the country, one would assume that it would be easy to transfer money across the country. But the last-mile problems in opening accounts by migrants, either in the original habitat or in the place where they have migrated to, the existing process of withdrawing money out of bank accounts in the rural branches and the reluctance of banks to entertain small money transfers, have all reduced the functionality of bank's remittance services. Even with the financial inclusion initiatives, the migrants may find it difficult to comply with 'know your customer' (KYC) requirements to open accounts. Some NGOs have tried to bridge this gap between the clients and the banking system. Institutions like Adhikar, based in Orissa, have set up remittance facility enabling the clients to use the NGO's bank account for remitting their funds to the families back home. Money is paid into the NGO's bank account by the migrant near his work place. The NGO transfers the money to its account at the paying center; cash is withdrawn by the NGO's staff and delivered by hand at the residence of the recipient. However, regulatory implications of such movement of funds are unclear.

18.3 MIS – Need for Continuing Improvement

The information base on the MFIs operations and performance needs to be strengthened. Regardless of whether the MFIs are brought under regulation or not, there is a strong case for setting up of a reporting system covering all institutions engaged in microfinance.

18.4 Microinsurance and IRDA

Microinsurance delivery in India is fraught with challenges. A major hurdle is the acceptance of microinsurance among the rural poor who not only have low levels of awareness about possible risks to their lives but also lack trust in most financial schemes structured for the long term with no immediate benefits. Non-availability of authentic admissible documentation during enrollment and claims processing and a lack of facilities for premium remittance further add to the complexity in insurance administration in the remote and far-flung pockets of India. Despite the numerous challenges, insurance companies have in the recent past made significant inroads to take insurance to the masses at the bottom of the pyramid. Insurance Regulatory and Development Authority (IRDA) has defined the social sector in terms of classification of people and their *vulnerability*. In the case of the rural sector, the definition is based on census classification on the size of population in a given location. IRDA has introduced the concept of priority sector in insurance through its social and rural sector obligation for insurers. It has actively pursued compliance with the obligations and periodically reset the level of obligation.

18.5 BC/BF Norms

In 2006, the Reserve Bank of India had issued new guidelines allowing banks in India to employ two categories of intermediaries – business correspondents (BCs) and business facilitators (BFs) – to expand their outreach. Banks may pay a reasonable fee/commission to BCs/FCs. However, BCs/FCs are not permitted to obtain any fee from the clients. The scope of activities of BC/BF and various issues associated with them are as follows:

- **Business Correspondents** – BCs are the organizations or individuals that organize and offer one or more points of transaction outside of bank branches. The BCs organize and manage a network of such transaction points in partnership with a bank. The scope of activities for BCs would cover (i) disbursal of small-value credit; (ii) recovery of principal/collection of interest; (iii) collection of small-value deposits; (iv) sale of microinsurance and mutual fund products; (v) receipt and delivery of small-value remittances and payments; and (vi) all other activities that a business facilitator would be required to carry out.
- **Business Facilitators** – BFs are the intermediaries such as NGOs, farmers' clubs, cooperatives, community-based organizations, IT-enabled rural outlet of corporate entities, post offices, insurance agents, village panchayats, agri-clinics and agri-business centers, etc. that can provide facilitation services to a bank. Such services may include (i) identification of borrowers and fitment of activities, (ii) collection and preliminary processing of loan application, (iii) creating awareness about the bank's financial and service products, (iv) processing and submission of applications to the bank, (v) promotion and nurturing of SHGs/JLGs, (vi) post-sanction monitoring, and (vii) follow-up for recovery.

The new guidelines have arrived at the same moment when a vast array of new technologies is available, offering new and inexpensive ways for transactions to be managed from remotely located offices. The combination of these new technologies with the new guidelines has inspired a number of efforts in India to experiment with the BC/BF model. These efforts use a variety of new technologies, for example, POS Devices and Mobile Phones, to secure and process transactions. New organizations are being formed to offer BC services. Some of the efforts also include responding to Government policy to open 'No Frills Accounts' and to process Government payments (G2P) such as the National Rural Employment Guarantee Scheme, Pensions and other social payments Quite a few banks have set up their BCs and appointed a number of BFs in many States.

There are certain teething problems. Some of the major operational issues, especially with regard to BCs are cash handling, irregular accounting, gullible client profile, fraud and misappropriation, inactive "no frill" accounts, non-viability of the model for the BCs themselves, interest capping, rigidity of distance criteria (15 kms), difficulties in ensuring cash settlement within the mandatory 24 hours, etc.

In the initial stages, the focus seems to be on inclusion. The experiments are by and large not treating the BC-led inclusion as a commercial prospect. The regulatory stance is to learn from ongoing implementation and incrementally remove hindrances. This stance while not entirely proactive is sufficiently supportive. While the technology service providers have taken a keener interest to prove the practicability of the model, they necessarily focus on technology aspects rather than the customer aspects. The key to success of BCs lies in banks making client acquisition and business expansion a business proposition and not treating it as a corporate social responsibility activity.

19. Conclusion

As a financial services delivery model, the self-help group approach is unique. It has clearly emerged as a superior model compared to the Grameen Bank or MFI models. By emphasizing savings before credit, it takes care of both the legs of basic financial services. People's participation is fully ensured with autonomy for the groups of the poor in credit decisions. Linkage to bank branches enables the groups to access loans and also keep their savings safely. The groups have been able to build a corpus through their financial intermediation (arising from the margins between costs of resources and lending rates). The members while paying high interest rates (still lower than money lenders' rates) do not lose the same, as it helps the corpus of funds to grow. The banks are far more comfortable in financing the poor through this mode as they find the risk and transaction costs to be low. This would guarantee their sustained interest in the program. The sustainability of the program from the point of view of availability of resources is clearly established.

The Indian experience has demonstrated that microfinance can be a participatory exercise and the banking system can deliver it sustainably. Instead of creating new institutions to deliver microfinance, it has enabled linkage of groups of the poor with the existing banking infrastructure. Though there are emerging issues that need to be addressed to make it sustainable in the long run, it shows that by involving voluntary organizations in social mobilization and creating an enabling and flexible policy environment, autonomy and the space for innovations, microfinance can achieve a vast scale and can become a national movement.

The major constraints identified regarding microfinance in India are greater and more diverse sources of funding, a meaningful set of poverty impact indicators in order to make meaningful statements about social impact and lack of an enabling policy environment for microfinance. The idea of NGOs and financial institutions (NBFCs) coalescing into one entity may appear to some to be detrimental to the core intention of a MFIs, i.e., alleviating poverty. But the changing face of microfinance in India appears to be positive in terms of the ability of microfinance to attract more funds and, therefore, increase its outreach.

Annex 2

NATIONAL MICROFINANCE DEVELOPMENT FORUM

Ulaanbaatar, Mongolia
16 March 2010

AGENDA

Organizers:
XacBank, and IFAD Rural Poverty Alleviation Project in Mongolia

Special sponsorship by:
Asia-Pacific Rural and Agricultural Credit Association (APRACA) FinPower Program

09:00-09:30	Registration
09:30-10:30	Opening Ceremony ***First speaker:*** Opening Remarks by Mr. Bold, CEO, XacBank ***Second speaker:*** Speech by Mr. Benedicto S. Bayaua, Secretary General, Group Photo
10:30-11:00	Presentation by Ms. Oyunchimeg, Director of Microfinance Department, Financial Regulatory Committee on the Status of Rural and Microfinance Policy Environment and Regulatory Framework in Mongolia
11:00-11:20	Coffee break
11:20-12:30	Presentation by Mr. Praful Dholakia, APRACA-FinPower Consultant from NABARD, India
12:30-13:00	Presentation by Ms. Nergui, Consultant, Achid Finance on Microfinance Development: Role of Rural Finance Companies' (RFCs) – as a local community microfinance institution
13:00-14:00	Lunch
14:00-14:15	Ms. Onon, Together Against Poverty – Organic Mongolia Program
14:15-15:30	Open Forum
15:30-16:00	Break
16:00-17:00	Conclusions and Recommendations

Annex 3

LIST OF PARTICIPANTS
National Microfinance Development Forum

Bank of Mongolia

1. B Suhbaatar
2. Ch. Chinzorig
3. Soyolmaa Erdenetsogt

Financial Regulatory Commission

4. Oyunchimeg, Director, Microfinance Department

Ministry of Finance, GoM

5. G. Bolormaa, Official
6. S. Tserendash, Official

Ministry of Food & Agriculture, GoM

7. B. Tsogbadrah, Official
8. Ch. Altanshagai, Official

Ministry of Justice, GoM

9. Sh. Tserentsoodol, Official

Govt. Implementing Agency – SME

10. J. Delgerjargal, Official
11. L. Batsukh, Official

WB/MDF

12. A. Amarsanaa, Accountant
13. Z. Orgilmaa, Non Financial Service Officer
14. A. Tsolmontuya, Secretary Asst.

RPRP, IFAD, Mongolia

15. D. Dalantainyam, Director
16. S. Gunuyanga, Staff
17. B. Ariunaa, Staff
18. J. Boldkhuyag, Accountant

WB/IBLIP

19. TS. Delgertsetseg, Legal Coordinator

Mongolian Women's Federation

20. J. Erdenechimeg, President

Mercy Corps, Mongolia

21. Dominic Graham, Country Director
22. D. Unenbat, Program Officer

Development Solutions, Mongolia

23. B. Serjmaa, Executive Director
24. B. Altanbagana, Vice Executive Director
25. E. Bat-Orshis, Director, Policy & Planning
26. L. Dansranbavuu, Director, UB – IU
27. B. Munhbaatar, Financial Service Manager
28. M. Ganchimeg, Manager, UB BD Centre

ADRA, Mongolia

29. D. Khishgee, Project Manager, SPRADP
30. Gerarad Erardganaba, Prog. Coordinator
31. Kh. Dorjsuren, Project Officer
32. N. Uranchimeg, Official, MED
33. S. Altantuya, Official, MED

Organic Mongolia

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35. Sh. Goohuu, President
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Mongolian Employers' Federation

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Ariunden SCC

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48. E. Purevlham

Anhdagch Anduud SCC – Huvsgul

49. P. Odgerel

Zoos Hurd SCC – Hentii

50. B. Narantsetseg

Farmer/Bank client

51. O. Badarch
52. M. Sarantuya

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53. M. Bold, CEO
54. L. Soronzonbold, 1st Deputy CEO
55. S. Munhbold, Official
56. Ch. Oyuntsetseg, Official
57. Z. Uyanga, Official
58. O. Undraa, Official
59. O. Munhmandah, Official

Khan Bank, Mongolia

60. N. Ospurev, Official, Head, Rural Credit Dept.

NABARD/NABCONS, India

61. Praful Dholakia, Asst. General Manager/Consultant

Mongolia

62. Ch. Ariunaa, Interpreter

APRACA

63. Benedicto S. Bayaua, Secretary General
64. Unchana Steane, Accountant

Annex 4

LIST OF KEY DIALOGUE PARTNERS

Sr. No.	Name & Designation	Institution
1.	Dr. Lkhanaasuren Purevdorj, Governor	Bank of Mongolia
2.	Mr. B. Lkhagvasuren, Director	Bank of Mongolia
3.	Mr. D. Boldbaatar, Director	Bank of Mongolia
4.	Ms. Soyolmaa Erdenetsogt, Economist	Bank of Mongolia
5.	Mr. Chuluuntseren Otgocguluu, Employment Policy Advisor to the President of Mongolia	Government of Mongolia
6.	Ms. Oyunchimeg, Director, Microfinance Department	Financial Regulatory Commission
7.	Mr. Sorinzonbold Lhagvasuren, 1st Deputy CEO	XacBank
8.	A. Serik, Senior Officer, Rural Credit Department	Khan Bank, HO, Ulaanbaatar
9.	Mr. Oyuntsetseg Chuluunbat, Director of Microfinance Banking Department (Retail)	XacBank
10.	Mr. D. Dalantainyam, Director	RPRP Project, IFAD
11.	Mr. Timothy Hooper, Executive Director	Vision Fund
12.	Ms. Bayarsaikhan Dembereldash, Executive Director	Microfinance Development Fund (MDF)
13.	Ms. Doljinmaa Dorjpurev, CEO	ValueQ of Achid Finance Group
14.	Ms. Oyunchimeg Togoodorj, ED	Mongolian National Cooperative Association
15.	Ms. Uranchimeg Navaansambuu, Program Coordinator (MEDP)	ADRA
16.	Ms. Nergui, Consultant	Achid Finance
17.	Ms. Onon Deriilaamyatav, Executive Director	Together Against Poverty Foundation/ Organic Mongolia
18.	Mr. S. Munhbold, Director of Retail Banking Division	XacBank
19.	Mrs. Narantsetseg, Manager	SCC, *Zoos Hurd, Henty* province of *Omnodelger* soum
20.	Mr. Timothy Hooper, Executive Director	Vision Fund, Mongolia
21.	Ms. Tseveg Otgontsetseg, Manager, Internal Control and Assessment Department	Vision Fund, Mongolia

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