EXPANDING THE FRONTIER OF MICROFINANCE SERVICES THROUGH SOCIAL MOBILISATION IN NEPAL

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1. INTRODUCTION

Nepal is one of the 49 least developed countries (LDCs) of the world. Poverty is still widespread and poverty incidence fluctuates between 31% and 42% during 1977 and 2003. Population below poverty line is estimated at 30.8% in 2003/04. Despite several measures initiated to address poverty problems, number of people below poverty line increased from about 4.9 millions in 1977 to about 7.5 millions in 2003. Agriculture dominates the Nepalese economy with around 39% share in GDP in 2005. Over 85% of the Nepalese population live in rural areas and nearly 80% of the employment come from agriculture and related activities.

Poverty is a complex phenomenon in Nepal due to varied reasons. First, the proportion of the poor in rural areas is almost twice as high as in urban areas. Second, there is a high regional variation in the incidence of poverty with the mountain regions having the highest concentration of the poor. Finally, poverty is also high among lower castes and disadvantaged social groups. In general poor have are characterized by limited access to paid employment, which is a key asset for the poor and underemployment and unemployment problems must be addressed by any poverty reduction interventions. Poverty reduction has been an explicit goal of planning in Nepal since the mid 1980s and various plans implemented in the past including the on-going interim plan (2008-2010) states poverty reduction as its sole objective.

Nepal's Gross Domestic Savings is only about 12.4% of its GDP and the level of rural HH savings is even much lower at 7% in 2004/05. Low level of HH income led to low level of savings, and a limited extent of self-financing on farm, off-farm and non-farm income and employment generating activities. Considering the need to ensure adequate access to financial services to promote growth and reduce widespread poverty, the Government of Nepal (GON) has implemented several targeted credit and microfinance programmes since mid 1970s with the ultimate goal of poverty reduction through an increase access of rural poor to subsidized credit and other microfinance services. The sector gained momentum after the restoration of democracy in 1990.

Nepal's microfinance sector is governed by the Bank and Financial Institutions Act 2006, Cooperative Act 1991 and Act for NGOs involved in Financial Intermediation 1999. Within the prevailing legal and regulatory framework, Microfinance Institutions (MFIs) in Nepal are: (i) commercial oriented MFIs such as Regional Grameen Bikas Bank (RGBBs), Microfinance Development Bank (MDB), and Financial Intermediary NGOs (FI-NGOs); (ii) community based MFIs such as Savings and Credit Cooperatives (SCCs), Small Farmers' Cooperative Limited (SFCLs) and (iii) apex institution namely Rural Microfinance Development Centre (RMDC), Sana Kisan Bikas Bank (SKBB) Ltd. and Rural Self Reliance Fund (RSRF) providing wholesale loan to MFIs[2].

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[2]As of mid July 2007, there are five RGBBs, four MDBs, 48 FI-NGOs, over 3200 SCCs, over 220 SFCLs and three apex institutions (RMDC, SKBB and RSRF formally active in Nepalese microfinance sector.

Despite significant growth in both the number of MFIs and microfinance programmes, their cumulative impacts are yet to be significant. They have faced major challenges to extend their services in inaccessible hills and mountains. Their outreach, which is slightly more than 850,000 in 2007, is about 37% of the potential market and is concentrated in accessible areas and virtually no or limited access in remote areas[3]. Expansion of outreach has been impeded among other due to complicated geo-political environments, weak technical capacity of the MFIs in key areas such as accounting and auditing; strategic planning; financial analysis and human resource management; lack of commercial orientation and a slow professionalism, and distortions arising from directed lending program and limited to a small relatively less poor segment of rural population and concentrated in plains and accessible hill districts. There are still sizable numbers of poorer segments mainly living in remote areas still relying with informal sources to meet their financial need/demand.

While commercial oriented MFIs are quite successful to penetrate their services in urban and densely populated peri-urban areas, the community based MFIs have comparatively better penetration in relatively inaccessible areas. On the other hand, thousands of Savings and Credit Groups (SCGs[4]) promoted under social mobilization programme by government and non-government sectors exist throughout Nepal irrespective of remoteness, but are yet to be fully used up to the potential level. Attempts to use the potentials of SCGs promoted under social mobilization initiatives has been almost forgotten in Nepalese financial market. In cognizance to above, this paper aims at assessing the prospects of social mobilization on expanding the frontier of microfinance in Nepal. The information used in this paper are obtained through review of available progress reports, relevant papers and literatures on social mobilization as well as key findings of study conducted by the author on expanding the frontier of microfinance services in Nepal and his over two decades of experiences on community based banking.

The paper is organized into six sections. After this introductory section, conceptual discussions on social intermediation; need for financial services for the poor and relationship between microfinance and poverty reduction has been discussed in section two. Section three outlines salient features of microfinance service delivery in Nepal while section four discusses on social mobilization and SCGs in Nepal. Potentials of savings and credit groups are discussed in section five while section six provides conclusions and recommendations of this paper.

2. CONCEPTUAL FRAMEWORK

2.1 Social Intermediation

For individuals whose social and economic disadvantages place them "beyond the frontier" of formal finance through by social intermediation, successful financial intermediation is often accompanied by social intermediation. It prepares marginalised groups or individuals to enter into solid business relationship with MFIs. Evidence has shown that it is easier to establish sustainable financial intermediation systems with the poor in societies that

[3]In this paper, remote areas and inaccessible hills and mountains are treated as are synonymous.

[4]A SCG is a voluntary association of persons with common interest, formed democratically without any political applications to improve economic and social status of the members in terms of their needs and interests. While the SCG activities are multi purpose, they quite often have a special focus on S&C management. Although unregistered, they function within the framework of an informal set of by-laws framed by members themselves. Number of members in SCG ranges between 15 and 40 people, either men only or women only or mixed.

encourage cooperative efforts through savings and credit groups, user groups or in other words, societies with high levels of social capital. Perhaps more than any other economic transaction, financial intermediation depends on social capital, because it depends on trust between the borrowers and the lender. Where neither traditional systems nor modern institutions provide a basis for trust, financial intermediation systems are difficult to establish.

Social intermediation refers to the process of building human and social capital required by sustainable financial intermediation with the poor. Social mobilisation is not always provided by MFIs nor it always result on group formation. In general such services for individuals are provided by the MFI itself or by other organizations attempting to link low income clients with the formal financial sector. Evidence has shown that it is easier to establish sustainable financial intermediation systems with the poor in societies with high levels of social capital. In contrast to any economic transaction, financial intermediation depends on social capital i.e. on trust between borrowers and lender and financial intermediation systems are difficult to establish in areas where neither traditional systems nor modern institutions provide a basis for trust. In this sense, social intermediation shall be understood as the process of building human and social capital required for sustainable financial intermediation with the poor.

In general, MFIs provide social intermediation[5] through groups to respond growing concern that poor in remote, sparsely populated areas with low social capital are not ready for sustainable financial intermediation without first receiving some capacity-building assistance on group cohesiveness and increase on self management capacity on savings mobilisation, participatory management, accounting, basic financial management and record-keeping to enable them lower the costs of financial intermediation by reducing default through peer pressure – and consequently to lower the transaction costs that MSPs incur in dealing with many small borrowers and savers.

2.2 Need for Financial Services to the Poor

In general, poverty is not a personal problem due to laziness or lack of intelligence, but in many cases it is a structural one i.e. due to lack of capital. In general poor lacks propensity to save or invest to their betterment. A majority of the poor rely on informal sector including moneylenders to meet their capital needs and pay exorbitant interest rates. As a consequence, despite their hardships and commitments, they are unable to raise themselves above subsistence level. They desperately need to link their work with capital to enable them accrue an economic cushion and earn a ready income. Poverty covers people in a thick crust and makes the poor appear stupid and without initiatives. Ensuring the access to financial services is identified to be one of the effective interventions to link the hardship of the poor with capital. Such access has prospects to bring poor back to normal life. Even those who lack conceptual thought or ability to think of yesterday or tomorrow are in fact quite intelligent and expert at the art of their survivals. Access to microfinance services is the key that unlocks their humanity.

2.3 Microfinance and Poverty Reduction

Microfinance service for the poor is one of the interventions to reduce poverty and relate to a wide range of flexible and appropriate financial services (savings, credit, insurance, leasing,

[5]Group social intermediation refers to efforts of building institutional capacity of groups and invests in human resources of their members, so that they can begin to function more on their own with less help from outside.

money transfer, remittance, etc.) provided by MFIs to address preferences and needs of the poor. In principal, microfinance services correspond to the chronic (*non-destitute*) poor and to the *transitory poor* in different ways. The lack of access to credit is readily understandable in terms of absence of collateral that poor can offer, in addition to various complexities and high costs involved in dealing with small, often illiterate borrowers. The poor have either to rely on loans from moneylenders at high interest rates or friends and families whose supplies of funds are limited. MFIs attempt to overcome these barriers through innovative measures such as group lending and regular savings schemes, as well as the establishment of close links between poor clients and their staff. The range of possible relationships and the mechanisms employed vary widely.

The case of microfinance as a mechanism for poverty reduction is very simple. If access to credit can be improved, it is argued, the poor can participate in productive activities that will allow income growth, provided there are no other binding constraints. This enables poor to mitigate risk, plan for future and make choices that translate to increase food consumption, invest in education, health housing, water and sanitation. This is a route out of poverty for *non-destitute chronic poor*. For *transitory poor*, who are vulnerable to fluctuations in income that bring them close to or below the poverty line, microfinance provides the possibility of credit at times of need. In some schemes the opportunity of regular savings by a household itself can be drawn on. The avoidance of sharp declines in family expenditures by drawing on such credit or savings allows '*consumption smoothing*'. In practice, such a distinction between needs of *chronic* and *transitory* poor for credit for '*promotional*' (i.e. income creating) and '*protectional*' (i.e. consumption smoothening) purposes, respectively, is over-simplified since the *chronic* poor will also have short-term needs that have to be met, whether it is due to income shortfalls or unexpected expenditures like medicinal bills or social events like weddings or funerals. One of the most interesting generalizations to emerge from microfinance and poverty literature is that the poorest of the *chronic poor* (the *hard core poor*) will borrow essentially for protectional purposes given both the low and irregular nature of their income. This group, it is suggested, will be too risk-averse to borrow for promotional measures (i.e. for investment in future) and will therefore be a very limited beneficiary of microfinance schemes.

Thus, experiences on implementing microfinance programme around the universe indicate that microfinance is not for everyone. The sick, mentally ill, destitute are not good candidates for MFIs, but they should rather receive direct assistance. Microfinance can be effective also for the poorest because there is no proof of either an inverse relationship between a client's level of poverty and their entrepreneurial skills or minor inclination to save among the poorest. Further, it is not true that only people with an existing entrepreneurial activity can benefit from microfinance. As a matter of fact, MFIs enable the poorest to improve their socio-economic conditions only if an appropriate programme design and targeting are implemented and the impact of microfinance can increase when it is provided together with other social services such as education and health.

3. SALIENT FEATURES OF MICROFINANCE SERVICE DELIVERY IN NEPAL

In Nepal, microfinance has become accepted over the last 30 years as an effective and sustainable strategy for poverty reduction and development. As a consequence microfinance institutions/programmes are mushroomed and some of them are in a gradual process to become large sustainable financial institutions for the poor. These developments are the outcomes of Nepalese context and realities of lack of access to formal financial services in

rural areas, inability of informal sector to provide sustainable financial services to the poor and efforts to integrate microfinance into an economic and development process. These institutions were emerged with the support of government, non-government and donor organizations and their services facilitated autonomy, enhanced integration and improved socio-economic status of poor including women.

There exist instances that establishment of commercial, profit-making microfinance models led to competition and to a large and diversified services translating into reaching more people. However, this profitability rationale has led to an increase in the number of sustainable MFIs working in accessible areas in order to limit their operational expenses. Remote areas in particular have been neglected for plains and accessible hills where operational expenses are lower. This is especially true as a high concentration of competition in accessible areas has led to a gradual observation that diversity of microfinance services in a very competitive markets yields both positive (choices of services providers, low interest rates, proximity, etc.) and negative (higher risk, overindebtedness, occasional unfair competition, profit search geared towards more profitable clients, etc.) effects. It is thus apparent that development of microfinance sector should not be accompanied by an increase in default cases and overindebtedness, which could yield results that are contrary to initial goal of microfinance towards checking financial exclusion while expending the services. Notwithstanding commendable progress achieved by microfinance service providers in extending their services in rural areas, a large majority of rural population, particularly those poor living in remote areas are still outside the ambit of their services and depend on private sources/money lenders to meet their most basic human needs.

The above argument implies that there is a need to find alternatives to help these sections of population to gain access to formal credit. Recent experience shows that putting together small group of people living in same settlements with similar interests and other homogenous factors as SCGs enables them to augment their meager resources and help them to sort out their own priorities according to their felt needs and problems. Large numbers of SCGs almost uniformly distributed across ecological belts and development regions including remote areas are not used to a full potential on the absence of mechanism.

4. SOCIAL MOBILIZATION AND SAVINGS AND CREDIT GROUPS IN NEPAL

4.1 Social Mobilization

Social mobilization has been a very popular methodology to organize people both government and non-government organization (GOs/NGOs) working for rural development. During last two decades of development, both GOs/NGOs used social mobilization as one of the important instruments to organize and empower people. Social mobilization focuses on building community organisations (COs) to directly articulate people's needs and priorities, rather than concentrating only on income generation activities. Once sensitized, communities build their own organisations and develop their own leaders. Savings collection and mobilization for credit operation is one of the key activities undertaken by the COs in their operations. There are instances where savings collection started with small has resulted into sizable accumulation and eventually emerging as village bank in rural areas. In general, they start small and gradually grow to a level where they can exert influence over local government, local service delivery institutions and private sectors. Thus it increases people's access to knowledge, skills and technologies. Due to its growing popularity to organize the people, especially among poor communities, social mobilization has been extended in most

of the rural areas of Nepal. In cognizance to this, GON has used this method as an instrument for poverty reduction and has clearly spelled out social mobilization as a tool to address poverty problems in already completed Ninth (1997-2002) and Tenth (2003-2007) Plans and it is also an integral component in the ongoing interim plan (2008-2010).

At present, social mobilization activities exist in all the 75 districts of Nepal. Such activities have been implemented even in remote districts such as Humla and Mugu through government projects and INGOs. Various rural development programme implemented by GOs and I/NGOs' have played a vital role in social mobilization and are acting as a driving force in the field of poverty alleviation through social mobilization. A general issue however is the lack of a national system to record their efforts and impacts on poverty reduction. In view of the endemic and deep rooted poverty situation, there is a need to further expand these social mobilization efforts and enhance their effectiveness. Despite wide scale popularities and coverage, there remain many challenges to fully extending social mobilization activities in Nepal. Barriers to their expansion and improvement are: inability to reach in those section of the society who are most in need; cost-effectiveness; proper savings mobilization for income generating and enterprise activities; coordination among and across agencies involved in social mobilization; paradigm shift from input delivery focus to output, effect and impact; and strengthening monitoring and evaluation issues. Above all, adequate use of COs (also SCGs) upto the potential level is the major challenges behind on-going social mobilization initiatives in Nepal.

4.2 Savings and Credit Groups

In Nepal, history of group approach to poverty reduction dates back to mid 1970s wherein about 9-25 people below poverty line and living in a settlement are organized into groups (male only, female only or mixed) under the technical backstopping support of the government promoted programmes such as Small Farmer Development Programme (SFDP) and Intensive Banking Programme (IBP) to work together for addressing their common problems. Other programmes such as Production Credit for Rural Women (PCRW), Banking with the Poor (BWTP), Micro-credit Project for Women (MCPW), etc. also attempted to address poverty problem using group approach. Encourages by the positive experiences and success on implementing these programme under group approach led to its expansion among different GOs/NGOs in the recent years with the idea that people living in a settlement shares an environment and common needs together and they are bound to take up activities jointly which are meant for the welfare of whole group.

Thousands of SCGs share among them basic feature of savings collection and loan operation as one of their key activities and could be termed as a SCGs. They are wide spread throughout Nepal and World Bank has estimated their number to exceed 400,000[6]. At present there are hardly any settlements or villages in Nepal without SCGs. There are cases where member of the households have participated in more than one groups promoted by different organizations. The number of SCGs formed by different GOs/NGOs through their 10 major programmes has been estimated to be at least 95,574 with 1465506 members. Most of them are promoted under social mobilization process and possess potential promoting income generating activities and asset creation, and implementing activities for social and economic development thereby contributing towards for poverty reduction. Most of the SCGs are

[6]World Bank Nepal, "Unequal Citizens – Gender, Caste and Ethnic Exclusion in Nepal, 2006", Kathmandu, Nepal

engaged in informal banking operations i.e. savings and credit activities and there is death of mechanism to encourage efforts of SCGs that are already functioning with good financial discipline to scale up the provision of complete microfinance packages.

Table 1: Savings and Credit Group, Members and Savings Mobilization in Nepal

S.N.	Name of the Programme	Supporting agency	Districts (No)	Groups (No)	Members (No)	Savings Mobilization (Rs.)	Remarks
1	Decentralized Local Governance Support Programme	UNDP	66	21730	530108	657000000	Dec. 2006
2	Rural Urban Partnership Programme	UNDP	20	5273	220299	113923000	Dec. 2006
3	Microenterprise Development Programme	UNDP	20	2448	19636	10996909	Dec. 2006
4	Rural Energy Development Programme	UNDP	25	5061	116077	66827514	Dec. 2006
5	Tourism for Rural Poverty Alleviation Programme	UNDP	6	781	15565	10216275	Dec. 2006
6	Participatory Conservation Programme	UNDP	22	3631	123322	101953634	Dec. 2006
7	Mainstreaming Gender Equity Programme	UNDP	16	305	8949	1074750	Dec. 2006
8	Western Upland Poverty Alleviation Programme	IFAD	8	595	14681	6263500	Oct. 2003
9	Bishwor with the Programme Poor	GON	75	6823	100520	70000000	-
10	Women Development Programme	GON	75	48927	316349	421974892	July 2006
		Total	75	95574	1465506	1460230474	

Source: NRB, Report of the Task on Policy Study to Link SCGs with Financial Service Providers

The members of the SCG save every week or fortnight or month on regular basis and use the savings thus collected for making small interest bearing loans to their members. Interest charged by most SCGs on such loans ranges between 24% and 36%, which is higher than the interest charges by most microfinance service providers. Quality of loan portfolio managed by most SCGs is better than the portfolio quality of microfinance service providers, which exceed more than 90%. Cumulative savings mobilized by these programme is Rs. 1460230474. There are large numbers of SCGs demonstrating their competency to act as efficient financial intermediary; to set efficient lending terms and conditions; to maintain proper book of accounts and financial management systems; to build financial discipline and credit history for themselves. These SCGs have also learned to handle resources of a size that is much beyond their individual capacities. Most SCGs have appreciated their capacity to properly handle more financial resources to address their poverty problems.

These SCGs are invaluable resources for poverty reduction endeavors and they should be used to ensure that poor would live with dignity, sufficiency and responsibility; and to

recognize that poor are bankable and they themselves are likely to have better appreciation of their socio economic situations than larger official and private institutions.

5. POTENTIALS OF SAVINGS AND CREDIT GROUPS

5.1 Operation of Savings and Credit Groups

Operations of SCGs are very simple which is based on mutual trust and confidence of group members. As a democratic body, all members have equal opportunity to speak and express their opinions. Any decisions to be taken are to be made unanimously after through discussion among them. Financial transaction such as the purpose of loans provided is need based, prioritization among different purposes and members' collective decisions. The interest rate or service charge charged varies widely among different groups and for different purposes within same group. Even though in some SCGs interest rate charged is higher than formal credit systems, borrowers are willing to pay higher interest rate as this is still far less than the interest rate charged by local money lenders. At the same time, members can access services in time and benefit of the higher interest rate goes to the group itself. The terms and lending norms, such as cost, repayment, interest rates, etc., are often different from lending procedure followed by formal credit institutions.

Members of the SCGs have received microfinance services at a varying degree, either through the internal capital or linkages to external credit capital created under Local Funds of these programmes. Ensuring the access to sustainable microfinance services to these people is an arduous task in view of the fact that the operation of existing microfinance service providers[7] is concentrated in Tarai and accessible hills with limited or no services in inaccessible hills and mountains and SCG linkages scheme is yet to be formalized / institutionalized among them. This implies that adopting mix of strategies rather than single uniform strategy is a necessity rather then luxury to ensure access to sustainable microfinance services to SCG members promoted by different programmes in Nepal.

5.2 Comparative Advantages of SCGs against MFIs

Potentials of the SCGs on expanding the frontier of microfinance services has been identified through an assessment of the comparative advantages (if any) that SCGs have against MFI on the provision of microfinance services in remote areas. This has been done through a comparative assessment of their cost structure, efficiency and productivity and portfolio quality as discussed hereunder[8].

5.2.1. Cost Structure

Cost structure of the existing MFI has been assessed to better understand their capability to continue serving people tomorrow as well as today. Cost structure of these MFIs across geographical regions is analyzed using ratios such as return on average performing assets (APA), total operating expenses and operating self-sufficiency.

[7] They are MDB, FI-NGO, SCCs and SFCLs.

[8] Discussions in this section is based on information gathered through the survey of MFIs including 48 SCGs, 14 SCCs, 7 SFCLs, 4 MDBs and 3 FI-NGOs - from 16 districts representing mountains, inaccessible hills, accessible hills and Tarai using criteria such as age of operation, products, services, operational policies, pricing, leadership and management capabilities to ensure homogeneity and make appropriate comparision. For details see Dhakal (2007).

Table 2: Return on Average Performing Assets (%) across MFI Type

S.N.	Areas	SCGs	SCCs	SFCLs	MDBs	FI-NGOs
1	Mountains	17.5	16.2	-	-	-
2	Inaccessible hills	17.7	17.1	12.1	13.2	13.4
3	Accessible hills	17.2	16.6	13.8	15.1	15.3
4	Tarai	17.9	16.9	14.7	16.3	16.1
	Total	17.6	16.6	16.4	15.2	14.9
	Effective interest rate (%)	18.0	18.0	18.0	18.0	18.0

Source: Dhakal (2007)

Return on APA signifies the financial productivity and it is almost identical in SCGs and SCCs, close to effective interest rate and with minor variation on financial productivity across geographical regions while there is significant difference between effective interest rate and return on APA in case of SFCLs, MDBs and FI-NGOs. Financial productivity is relatively low in SFCLs, followed by MDBs, FI-NGOs, SCCs and SCGs. Across ecological belts there is inverse relationship between return on APA and remoteness. As expected, financial productivity of SFCLs, MDBs and FI-NGOs is lower in inaccessible hills, followed by accessible hills and relatively higher in Tarai. Financial productivity is highest in SCGs and lowest in FI-NGOs.

Table 3: Total Operating Expenses/Average Performing Asset Ratio (%) across MFI Type

S.N.	Areas	SCGs	SCCs	SFCLs	MDBs	FI-NGOs
1	Mountains	7.2	19.4	-	-	-
2	Inaccessible hills	5.4	16.2	17.3	17.2	15.7
3	Accessible hills	6.2	12.6	14.3	15.8	13.9
4	Tarai	4.6	11.5	11.6	14.6	12.9
	Total	5.9	16.4	15.4	15.6	14.2

Source: Dhakal (2007)

Total operating expenses (sum of financial cost, loan loss provision and administrative cost) to APA ratio is very low in case of SCGs (5 and 7%), while it ranges between 11 and 19% among SDU of other MFIs. In all these cases, there is a direct relationship between operating expenses ratio and geographical remoteness with high ratio in remote areas than in accessible areas. Variation on ratios is quite high in case of SCCs and SFCLs across geographical remoteness while it is relatively narrow among FI-NGOs and MDBs.

Table 4: Operating Self Sufficiency Ratio (%) across MFI Type

S.N.	Areas	SCGs	SCCs	SFCLs	MDBs	FI-NGOs
1	Mountains	243.1	83.5	-	-	-
2	Inaccessible hills	327.8	105.6	69.9	76.7	77.1
3	Accessible hills	277.4	131.7	96.5	95.6	97.8
4	Tarai	389.1	147.0	126.7	111.6	110.9
	Total	300.4	101.4	106.7	97.9	105.4

Source: Dhakal (2007)

As expected operating self-sufficiency (OSS) is highest (300%) in case of SCGs and lowest (98%) in case of MDBs. In general, all the MFIs in Tarai and SCGs and SCCs in remaining three geographical regions have OSS more than 100% indicating that they have earned enough revenue to cover their total operating cost. There are SCCs in mountains, SFCLs,

MDBs and FI-NGOs in hills (both accessible and inaccessible) not able to cover their operating costs and yet to be self-sufficient.

Analysis of the cost structure of the MFIs indicates limitations of the SFCLs, MDBs and FI-NGOs to expand their services in remote areas. The findings imply that SCCs is a sustainable model to ensure access to microfinance services in all four geographical areas except mountains while SCGs as an isolated entity is feasible in all the four geographical regions. Innovation to reduce operating cost is one of the pre-requisite to expand microfinance services through SCCs in mountains and other modalities (MDBs, SFCLs and FI-NGOs) in high hills and mountains.

5.2.2. Efficiency and Productivity

Most of the MFIs are quite efficient and benefit from low salary levels, high staff productivity and an integrated approach to credit delivery, all of which has contributed to maintain cost structures at current low level. In the MFI covered under this research, on an average one staff serve 131 loan clients. Across MFIs, FI-NGOs are the most productive than other MFIs. Their local existence and unique delivery system distinguishes them from MDBs. In both MDBs and FI-NGOs, jobs are tied to staff performance; hence there is drive to attain higher productivity. Design consideration, legal framework and management factor limits borrowers to staff ratio of SCCs and SFCLs towards lower bound that warrants improvement through enhanced professionalism.

Table 5: Borrowers/Staff ratio (No) across MFI Type

S.N.	Areas	SCGs	SCCs	SFCLs	MDBs	FI-NGOs
1	Mountains	-	72	-	-	-
2	Inaccessible hills	-	86	200	132	159
3	Accessible hills	-	118	117	140	192
4	Tarai	-	171	130	169	247
	Total		97	159	153	199

Source: Dhakal (2007)

In addition to being productive, the MFIs covered by this research are efficient and minimize cost of service delivery. It cost the sample SDU just NRs. 642 (i.e. 9 dollar) to maintain one client. Across MFIs, cost per borrowers is highest among SDU of MDBs and lowest in SFCLs. FI-NGOs and SCCs are in between. SCCs/SFCLs are able to achieve higher efficiency as a result of its lower operating costs and larger loan sizes.

Table 6: Cost per Borrowers (Rs.) across MFI Type

S.N.	Areas	SCGs	SCCs	SFCLs	MDBs	FI-NGOs
1	Mountains	-	518	-	-	-
2	Inaccessible hills	-	497	203	1953	1344
3	Accessible hills	-	448	217	1652	931
4	Tarai	-	406	280	1281	686
	Total		486	293	1542	987

Source: Dhakal (2007)

The findings of this research indicates that key microfinance actors are located at the frontier of microfinance services and strategy to strengthening existing MFIs and using thousands of SCGs to a full potential is most fundamental to expand microfinance services in remote areas.

5.2.3. Portfolio Quality

With portfolio at risk (PAR) over 30 days of 10.6%, the MFIs covered by this research reports almost one tenth of the portfolio as delinquent which is quite high. PAR is more (25.6%) in case of SFCLs, followed by SCCs (13.2%) and FI-NGOs (11.5%). With an average 3.6% PAR, MDBs are performing fairly well. As with productivity, organizational culture (zero tolerance on overdue) is also the key determinant of portfolio quality.

Table 7: Portfolio at Risk (%) across MFI Type

S.N.	Areas	SCGs	SCCs	SFCLs	MDBs	FI-NGOs
1	Mountains	12.4	12.6	-	-	-
2	Inaccessible hills	8.6	17.2	33.4	5.6	13.6
3	Accessible hills	5.1	11.4	17.2	4.1	12.1
4	Tarai	6.7	8.7	21.4	2.3	8.7
	Total	8.2	13.2	25.6	3.6	11.5

Source: Dhakal (2007)

Writing off delinquent loans currently remains a taboo practice among Nepalese MFIs. As a result, loan loss rates reported by these units are likely to understate actual portfolio loss. Most of the microfinance managers lack clear understanding on true sprit of write-offs as they fear that once a loan is written-off, it can no longer be recovered in future.

5.3 Strategy for Expanding Microfinance Services through Savings and Credit Groups

The strategy to ensure access to sustainable microfinance services to existing SCGs ranges from federations of SCGs into Savings and Credit Cooperatives (SCCs) to SCGs' linkages with existing SCG nearby their vicinity and/or microfinance services providers with prudent technical support provided by promoting agency. Thus there could be three different strategies for expanding the frontier of microfinance services through SCGs.

Strategy 1: Savings and Credit Group Banking
This strategy promotes financial transactions between MFIs and SCGs. SCG-Banking through SCGs and existing decentralized formal banking network including several organizations in formal and non-formal sectors as banking partners allow for large-scale outreach of microfinance services to the poor. These banking services (depositing savings, taking loans) made available at low cost are easily accessible and flexible enough to meet poor people's needs.

SCG Banking is a scheme that helps to promote financial transactions between formal rural banking systems[9] with informal SCGs as clients. As a savings mobilization initiative, SCG members are encouraged to save on regular basis and their capacity is enhanced to use pooled resource on making small interest bearing loans to their members. This process helps them imbibe essentials of financial intermediation including prioritization of needs, setting lending terms and conditions, book keeping, accounting and financial management. This gradually builds financial discipline and credit history for themselves, as the money involved in the lending operations is their own hard earned money so called "warm (hot) money", saved over

[9]Rural banking systems comprises of public and private sector commercial banks, development banks and MDBs as well as SCCs and FI-NGOs.

time with great difficulty. They also learn to handle resources of a size that is much beyond their individual capacities. In course of operation, the SCG members begin to appreciate that resources are limited and have a cost.

In SCG Banking scheme, SCGs act as a financial intermediaries owned by the poor. Once SCGs demonstrate mature financial behavior, banks are encouraged to make loans to SCG in certain multiples of their accumulated savings. The bank loans are given without any collateral and at market interest rates. Only SCGs demonstrating proven credit history and set standards will be eligible for borrowing and banks find it easier to lend these SCGs as their members have developed a credit history.

In the operational term, "cold (outside) money" borrowed from the banks is added to SCGs' own "warm (hot) money" and used as a loanable fund to extend interest bearing loans. In most cases mixing of "cold and hot money" enforce credit discipline among SCG members. Bank loan provides additional liquidity to SCG on meeting the financial needs of the members on production, investment or consumption activities. The members have experienced the benefits of credit discipline by being able to save and borrow regularly without many hassles. The SCGs continue to decide terms of loans to their own members. The peer pressure ensures timely repayments and replaces the "collateral" for bank loans. In most countries including India, the SCG banking scheme is quite effective to extend outreach of microfinance services in areas where formal sector is reluctant to operate.

This strategy consist of four elements: First, identify SCGs, devise mechanism to record their existence and enhance their capacity on self regulation and support to build-up capital by regular savings. Second, undertake in-depth study on different models of promoting SCG linkages[10]. Third, legal provision to microfinance service providers to extend a line of credit directly to mature SCGs (not through an intermediary) without determining the purpose for which the members could use the loans or any other norms like restricting loan size to tangible assets or determining unit costs for loans coverage. The SCGs could lend for any purpose including meeting various emergency expenses, consumption requirements and productive investment, without any prescribed ceiling on interest rate. Finally, consultations with potential microfinance service providers to involve as partner to extent microfinance services to identified SCGs. Major thrust of this strategy lies at initiating linkage processes, in two dimensions. First, institutional linkages between SCGs and microfinance service providers either indirectly by involving NGOs and other Self-Help Promoting Institutions as financial intermediaries or direct. Second, financial linkages between savings and credit in fixed ratios or in dynamic ratios of savings: credit which increases in repeat credit cycles. The pre-requisites underpinning this strategy includes the (i) amendment of micro-finance policy and related acts/rules to enable existing MFIs/DBs/CBs provide wholesale loans to SCGs; and (ii) upgrading the capacity of the SCGs to be creditworthy with microfinance service providers to receive wholesale loans.

Strategy 2: Linkages of Savings and Credit Groups with Savings and Credit Cooperatives
There are districts or areas within a district where sub-strategy 1 can't be applied due to access and lack of basic infrastructures. However, by virtue of cooperative movements started with the enactment of Cooperative Act 1991, there are VDCs / areas with self-emerged

[10]They are (i) SCGs formed and financed by banks, (ii) SCGs formed by NGOs/formal agencies and financed by banks and (iii) SCGs financed by banks using NGOs and other agencies as financial intermediaries.

and/or agency pursued SCCs in which most SCGs members are also shareholders. The case of one member depositing savings in 2-3 informal or formal places[11] is quite common in most areas. In those areas, strategies to be pursued will be ensuring linkages of SCG members with existing SCCs[12]. Re-alignment exercise should recognize these SCCs as its partner and assist them to enhance their capacity on aspects such as promotion and management, loan operation, accounting/book keeping, financial management and linkages with apex[13] institutions. This strategy requires close scrutiny and assessment of SCCs that exist within a VDC/Municipality where SCGs exist. Further, the strategy is to enhance the capacity of SCCs that co-exist in areas where SCCs exist using the packages of services that ensures upgrading of them to a level where apex institutions will find them credit worthy to provide wholesale loans.

Strategy 3: Promotion of Savings and Credit Cooperatives
There are districts or VDCs within a district where existing microfinance services providers are reluctant to extend their services and/or SCCs do not exist, but there exist proven local capacity (education level and leadership) to promote SCCs. In such areas strategy will be to support the promotion of SCCs. In those areas, SCGs will be assisted to promote SCCs either through (i) federation of the COs within a VDC or (ii) using on lead CO to register the SCC with responsibility to increase shareholders over time and keeping the status of the COs intact. This strategy demands complete packaging of services to support emergence and growth of SCCs as well as enhance their capacity on aspects such as promotion and management, loan operation, accounting/book keeping, financial management and linkages with apex institutions[14]. Support packages should be flexible that assists their graduation to a level where they will be creditworthy to the apex body for wholesale loans.

6. CONCLUSIONS AND RECOMMENDATIONS

This paper has analyzed potentials to expand frontier of microfinance services through social mobilization and concluded that thousands of COs/SCGs formed under social mobilization interventions throughout Nepal under GOs/NGOs programmes are not adequately used upto their potential and highlighted a need to have fresh look to properly use them to accelerate poverty reduction initiatives in different parts of Nepal. COs/SCGs have diverse geographical existence and they possess prospects of being used for diverse purposes for local economic development ranging from social development, legal awareness, economic development and enterprise development. As far as provision of microfinance services is concerned, the paper concluded that COs/SCGs have comparative advantages in terms of cost structure, efficiency and productivity and portfolio quality compared to other commercial oriented and community based MFIs.

Considering the potentialities that COs/SCGs have on expanding the frontier of microfinance services the study has recommended to follow a mix of strategies ranging from federations of SCGs into SCCs to SCGs' linkages with existing SCG nearby their vicinity and/or MFIs with prudent technical support provided by promoting agency. Considering the geo-political diversity, any effort to consider a blanket model towards proper use of these SCG will

[11]These organizations are SCGs, SCCs, producer's groups, forest users' groups or women's group.
[12]There are five SCCs in Dhungkharka, three in Dulari, one in Jyamirgadi, one in Ramche and 11 in Jiri VDCs Kavre district, Morang, Jhapa, Sindhupalchok and Dolakha districts.
[13]The apex institutions providing wholesale loans to SCCs are RSRF, RMDC, Cooperative Banks and SKDB.
[14]Ibid

undermine their potentials greatly and warrants a strategic decision on making appropriate choices out of the menu of feasible alternatives.

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