SHG Banking in India:  
the developing world’s largest and fastest-growing microfinance program  

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SHG banking, or linking banks and self-help groups, in India is the largest and fastest-growing microfinance program in the developing world. Implemented since 1996 on a national scale, it has reached 1.43 million groups with 21 million members, covering over 100 million people from the lowest strata of the rural population (as of March 2005). It is a flexible approach adapted to local conditions by the participating agencies as autonomous business partners. The enormous growth in outreach has been made possible by drawing on a wide array of institutional resources - India’s social capital. This includes the National Bank for Agriculture and Rural Development (Nabard) as the prime mover and refinancing agency; some 36,000 bank branches and primary cooperatives providing deposit services and credit; some 3,100 governmental and non-governmental agencies with experience in group development as facilitators of previously existing or newly established SHGs; the National Reserve Bank of India which has adjusted the policy framework for banking relations with informal groups; and the political leadership at various state and union levels, prominently providing legitimacy in the annual union budget speech as an unequivocal expression of the political will.¹

At the same time the program has drawn on India’s human capital: on the one hand the competence and enthusiasm of the staff in all participating agencies, many of which select their staff through competitive exams; and on the other hand the willingness and ability of people from the lowest classes (scheduled castes) to form a group, meet regularly, pool their miniscule savings, lend to members, and establish a documented track record of financial intermediation within the group. On that basis, the groups are then permitted as informal entities to open savings accounts and obtain bank loans, which they onlend to their members on terms and conditions autonomously decided by each group. In India, as in some neighbouring countries, small groups with financial activities attract predominantly women, even if no such bias is built into the program design: 90% of the group members are women, through self-selection.

Neither social nor human capital would suffice were it not for the financial capital created by the program: steadily increasing internal resources of the groups, generated through savings and profits from interest income; and high profitability of SHG banking as a financial product of the banks (higher than any other rural financial product), due to high repayment rates and low transaction costs of both banks² and SHGs³. SHG banking is viable for SHGs and banks.

Representative national studies are absent; but there is strong indicative evidence that impact is deeply felt by the women, the majority of them illiterate: they save, borrow, invest and repay; manage their own SHG affairs, albeit with assistance in bookkeeping; enter banks for financial transactions; contribute to the household economy and improve their standing in the family; send their children to school (almost all reportedly do, previously only few did); and for the first time in their life take a positive view of the future.⁴

Impact at the institutional level includes the formation of SHG federations and associations, some of them registered as Mutually Aided Cooperative Societies (MACS), a new legal status for financial cooperatives free from government dominance – “based on thrift, self-help and mutual aid and owned, managed and controlled by members for their economic and social betterment”⁵. Impact at the policy level includes central bank authorization of financial transactions by banks with informal groups of the lowest economic standing.
All this is just a beginning. **Enormous challenges** remain: reaching out to the remaining 150 million rural poor in India; expanding into states where coverage is still minimal; assuring adequate financial accounting, reporting and control at SHG level as an indispensable basis of financial deepening; finding profitable microenterprise investment opportunities; and making access to financial services sustainable in the long run.

**Sustainability** of SHG banking in the long run is an unresolved issue. Given the flexibility of SHG banking in India, there may be different routes to the sustainability of access to formal financial services. One is direct access of individuals to bank services, based on the growth of their microenterprise activities and the track record provided by their SHGs; for a transitional period, small-size loans from group funds and opportunities for graduation to larger-size individual bank loans may exist side by side. Another option, presently developing in Andhra Pradesh and neighbouring states on a growing scale, is the formation of federations\(^i\), some with and others without financial intermediation functions, indirectly giving legitimacy to the member-SHGs. A third option presently under discussion may lie in the full integration of credit NGOs and MFIs, with their SHG clientele, into the formal financial sector. The least promising option of sustainability in the long run is the continued existence of informal groups (limited by law to 20 members) with full access to bank services – unless the lawmaker, impressed by their social cohesion and determination to stay together, decides on a new legal status for such groups.


M. Harper, Promotion of Self Help Groups under the SHG Bank Linkage Programme in India–An Assessment. Nabard 2002


\(^iv\) W. Hannover, Summary of Major Results from Existing Studies on the Impact of the Microfinance Linkage Banking Program in India on the Millennium Development Goals.. GTZ, Eschborn, Jan. 2005.


\(^v\) Andhra Pradesh, Mutually Aided Cooperative Societies (MACS) Act, 1995. From Andhra Pradesh, the act has been spreading to other states.