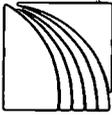


CREDIT CONNECTIONS

Meeting the Infrastructure Needs of the Informal Sector through Microfinance in Urban India

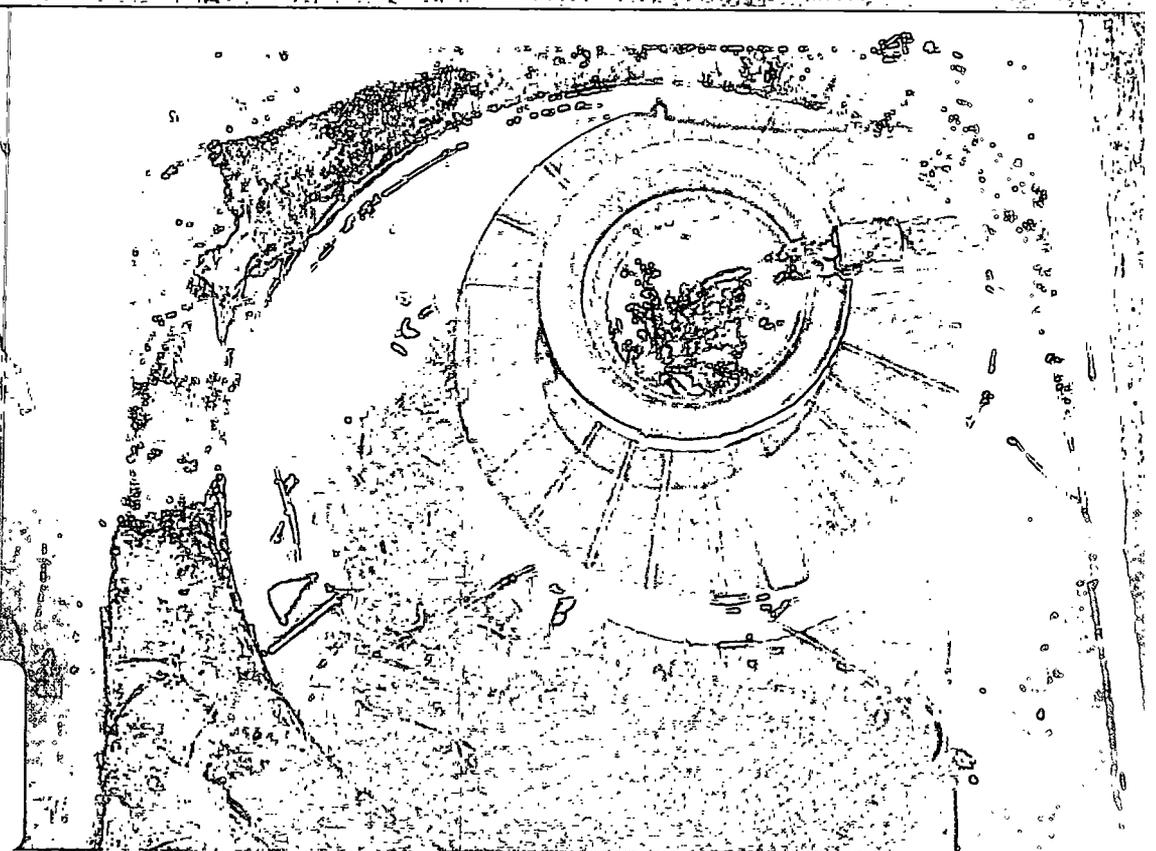
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UNDP-
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Water and
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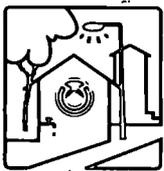
South Asia Region

Dedicated to all the countless women who are engaged in a daily battle to improve their quality of life, and to those microfinance institutions that are helping them, through access to a basic human right – the right to credit.



FILE COPY

Gujarat Mahila
Housing SEWA Trust



Introduction

This research initiative comprises a series of four national-level Field Notes, an Action Research component and a Discussion Paper on issues arising out of the research. It focuses on microfinance institutions operating in urban India and especially studies the way they are

facilitating the provision of water and sanitation services (along with other infrastructure upgradation) to poor women consumers in the informal sector.

Mahila Housing SEWA Trust, Ahmedabad, undertook the initiative on behalf of the UNDP-World Bank Water and Sanitation Program – South Asia. The research project was fully sponsored by the Water and Sanitation Program – South Asia.

DFID

Department for
International
Development

Objectives

- To identify, analyze and document the credit-related activities of four microfinance institutions based in urban India and involved in providing small-scale credit for infrastructure (particularly water supply and sanitation) to poor women consumers working in the informal sector.
- To develop a comprehensive loan and repayment system for housing and infrastructure credit to poor women consumers in the informal sector, through an Action Research component.
- To highlight and discuss the main issues and lessons arising from the four field-level case studies and Action Research relating to:
 - (a) the sector as a whole; and
 - (b) the specific situation within India, including the need for new thinking and policy to promote the sector.

Methodology

The research was undertaken using a multi-pronged approach, including:

- desk-based study of secondary literature at the office of the UNDP-World Bank Water and Sanitation Program, New Delhi;
- formal discussions with officials of the Andhra Pradesh State Housing Board, Ahmedabad Municipal Corporation and Mumbai Slum Clearance Board;
- discussions with bilateral and donor agencies involved in the water supply and sanitation sector in India and various microfinance institutions based throughout urban India;
- three- to four-day field visits to each of the four institutions studied; structured questionnaires for both

microfinance institution personnel and clients of the microfinance institution were completed, along with notes of detailed, informal-level discussions with the concerned parties;

- extended visits to SEWA Bank, Ahmedabad, to coordinate Phase I of the Action Research, which included a market survey of poor women in the informal sector; and
- field-level photographs taken at each site visit to compile pictorial evidence for the study.

Basis for Sample Selection

While there is a large and growing number of organizations working in the microfinance field in India, there are relatively few with a long track record of dealing with infrastructure financing. Of these, the study looked at a sample of four.

To provide the study with a robust and reliable picture of infrastructure credit provision, the selection of the four sample microfinance institutions to be documented was based on the following criteria:

- Good track record (over five years specialized experience in microfinance).
- Good outreach (over 4,000 clients; direct loans to women in the informal sector).
- High field-level loan recovery rate (over 90 percent).
- Experienced in disbursing loans for infrastructure/shelter upgradation, particularly for water supply and sanitation purposes.
- Experienced in disbursing small-scale loans to both individual members and collective member groups.
- Experienced in organizing and building the capacities of its members as well as facilitating collective

infrastructure upgradation projects.

- Ideological belief in the capacity of poor women to solve their own problems and the need for maximum community participation and ownership.

The final selection resulted in four case studies describing three very different organizational models: evolving Community-based Financial Institutions; mainstream Community-based Financial Institutions; and the traditional Non-governmental Organization model. The fourth 'type' of microfinance institution found in India is commonly referred to as the Banker's Model and operates on the Grameen Bank guidelines. These organizations are mainly operational in rural areas and, therefore, are outside the remit of this study. Details on the types of microfinance institutions prevalent in India are contained later in this document.

This research found that the 'type' of microfinance institution is not a determining factor for whether it disburses loans for water supply and sanitation purposes or not. Regardless of their lending methodology, prominent microfinance institutions with a good track record are beginning to provide microfinance for infrastructure, in response to increasing demand from their clients.

Output

Overall, the study has produced the following outputs:

1. Series of Field Notes on four urban microfinance institutions, focusing on their infrastructure-related credit activities.
2. Issues Paper to introduce the research initiative and highlight the

main issues emerging from the field work (this document).

3. Short video accompanying the SEWA Bank Field Note, containing interviews with clients and SEWA Bank personnel.

4. An Action Research document comprising:

- market survey study on 'Housing Finance Needs of Women in the Informal Sector in Ahmedabad City';
- development of a prototype infrastructure and housing loan department for financial institutions disbursing credit through individual loans to poor women in the informal sector in urban India; and
- copies of relevant application forms to be used at each stage of the proposed housing and infrastructure loan disbursement and recovery system.

A summary of the key indicators of the four microfinance institutions studied for the purposes of this initiative are detailed on page 4.

Issues Arising

This section of the report presents the key lessons and issues identified during the research.

A. Sector-specific Issues

1. Microfinance is an enabling tool for improved water and sanitation services

There is general consensus on the fact that improved water supply and sanitation is imperative for prevention of disease. According to the World Bank, "The two areas requiring the most attention include:

- (i) one-third of the world's population that has inadequate sanitation, and
- (ii) one billion people without safe water.

The final selection of microfinance institutions resulted in four case studies describing three very different organizational models: evolving Community-based Financial Institutions; mainstream Community-based Financial Institutions; and the traditional Non-governmental Organization model.



Highlights of Four Successful Microfinance Institutions Disbursing Infrastructure Loans to the Urban Poor¹

Indicator	Baroda Citizens Council	महिला मजदुरा (Byculla, Mumbai)	SEWA Bank	Sri Padmavathy Mahila Abyudaya Sangam
1. Type of microfinance institution	Traditional NGO ²	Evolving CBFI	Mainstream CBFI ³	Evolving CBFI
2. Member outreach	7,311	536	125,000	5,700
3. Start date of HI ⁴ loans	1989	1993	1976	1992
4. Maximum HI loan amount (Rs)	7,500	5,000	25,000	40,000
5. Sources of re-finance	Members' own savings	Members' own savings & RMK ⁵	Members' own savings, HUDCO ⁶ & HDFC ⁷	Members' own savings, HUDCO, SIDBI ⁸ & HDFC
6. Interest rate of HI loans: to microfinance institution	6% (savings)	8% (RMK) 12% (savings)	8% (savings) 9% (HUDCO) 10% (HDFC)	10% (HUDCO & HDFC) 11% (SIDBI)
7. Interest rate of HI loans: to clients	12%	24%	13%	15-24%
8. Interest rate of non-HI loans: ⁹ to clients	12%	24%	17%	18-24%
9. Maximum HI loan repayment period	2 years	Flexible	5 years	Flexible
10. Non-HI loan repayment period	2 years	Flexible	3 years	Flexible
11. Average loan repayment rate ¹⁰	95%	100%	94%	100%
12. Collateral required for HI loan ¹¹	Two guarantors from the community	None	Two guarantors; one with a formal payslip	Joint liability guarantee form signed by all the members of a SHG ¹²

¹ At the time of preparation of this report, \$1=Rs 42.

² NGO: Non-governmental Organization.

³ CBFI: Community-based Financial Institution (See later sections of this document).

⁴ HI Loans: Housing and Infrastructure Loans.

⁵ RMK: Rashtriya Mahila Kosh (public sector re-finance institution).

⁶ HUDCO: Housing and Urban Development Corporation (public sector mainstream housing finance institution).

⁷ HDFC: Housing Development Finance Corporation (private sector mainstream housing finance institution).

⁸ SIDBI: Small Industries Development Bank of India (public sector re-finance institution).

⁹ Non-HI loans: Refers to loans for purposes other than shelter-related needs, including income generation, skills training, consumption purposes etc.

¹⁰ Loan Repayment Rate: Defined as percentage of loan repayments made within 30 days of the actual repayment due date.

¹¹ Please note that none of the four microfinance institutions surveyed require legal land ownership documents to be submitted, in order to access housing and infrastructure loans.

¹² SHG: Self-help group.



Organization, says that “Health must be a conditionality for economic development.” She states, “Health is wealth, but wealth does not necessarily lead to health.” The World Health Organization advocates that the link between health and development be made in microcredit.

Stephen Latham’s paper entitled ‘Microcredit and Water Supply and Sanitation: An Exploration of a Strategic Partnership in Benefit of Peri-urban Communities in Tegucigalpa, Honduras’ describes how a coordinated effort between microcredit institutions and the water supply and sanitation sector to provide safe water supply and sanitation is resulting in “healthier and wealthier

Unsafe water supply and sanitation results in 900 million cases of diarrhoeal disease every year that cause the deaths of more than three million children. By simply making adequate water supply and sanitation available, two million of these deaths could be prevented.”¹³

The World Bank also estimates that India loses a substantial \$80 billion annually on account of sickness and death from pollution (including deteriorating water quality due to poor sanitation, poor solid waste management and lack of clean drinking water) and economic costs attributed to resource degradation.

Dr El Bendari Hammad, former Executive Administrator for Health Policy and Development, World Health

communities – thus ensuring a more sustainable, equitable and holistic form of development”.

Despite the above findings on the positive correlation between improved infrastructure and improved health indicators along with enhanced income levels, widespread funding for infrastructure through microcredit is still an underdeveloped sector.

In India, provision of infrastructure including drinking water and sanitation services has long been viewed as a State responsibility, to be funded through State resources. However, with the recent political shift towards decentralization to local governance, the climate is becoming increasingly favorable to community participation in water supply and sanitation provision.

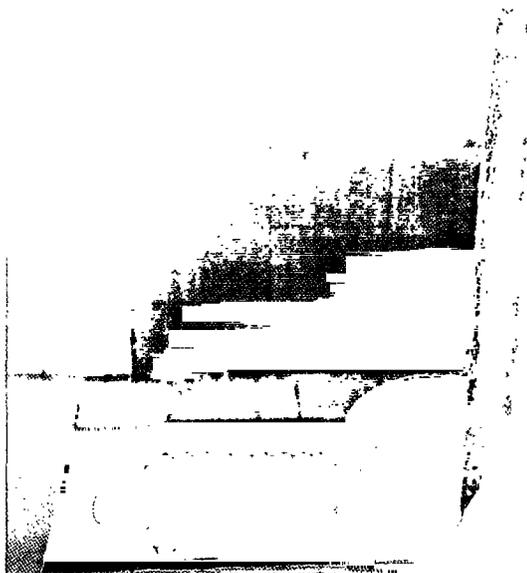
¹³ Source: *World Development Report 1992: Development and Environment*, the World Bank, 1992.

Timely and efficient supply of microcredit has already made a substantial contribution in providing loans to individual households for building (own use) toilets, digging borewells, installing handpumps or getting electricity connections.

The potential role for suppliers of microcredit in such projects is clear.

At the same time, the timely and efficient supply of microcredit has already made a substantial contribution in providing loans to individual households for building (own use) toilets, digging borewells, installing hand pumps or getting electricity connections. Loans for such upgradation or installation purposes are disbursed in the form of housing and infrastructure loans through grassroots microfinance institutions.

Microfinance is a growing sector with great potential for delivering housing and infrastructure finance to the poor. India has an existing number of well-established, credible microfinance institutions working with poor, informal sector communities, which have already disbursed substantial funds for individual water supply and sanitation and other infrastructure loans. Interestingly, microfinance institutions are also increasingly emerging in new partnerships involving municipalities, poor communities and various other partners such as non-governmental organizations and donor agencies, involved in slum upgradation projects.



In addition to describing each of their credit-related activities and achievements, the series of Field Notes enclosed clearly demonstrates how four prominent Indian microfinance institutions are facilitating improved water and sanitation services to poor communities in order to improve the health of their members, as well as providing increased opportunities for income generating activities.

The demand for improved services in urban India is huge. More importantly, poor communities are increasingly demonstrating their capability to pay for and manage their own shelter-related needs. The key emerging issues described in this document highlight the positive achievements from the field and identify areas where further support is required.

2. Access to technical advisory support is vital for the success of credit provision for infrastructure

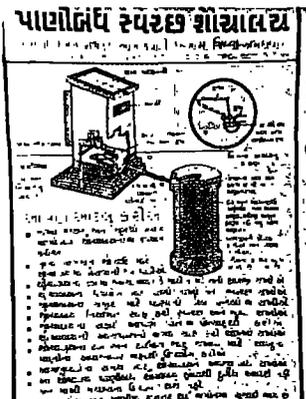
Each of the four sample microfinance institutions were found to provide loans along with support services for collective infrastructure projects.



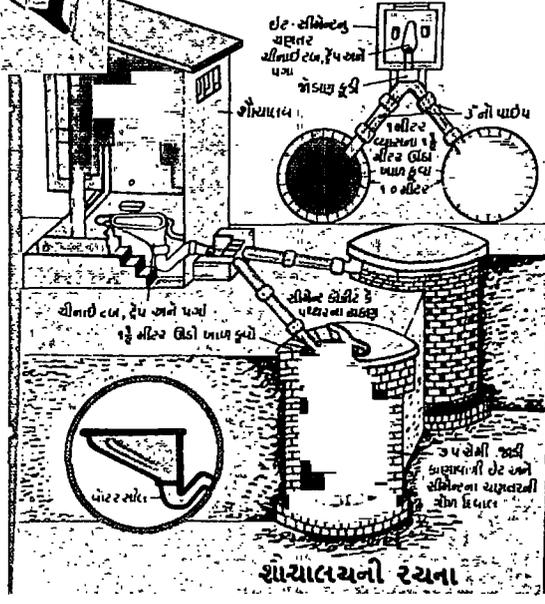
In the case of Mahila Milan, Mumbai, credit was linked to the provision of complete infrastructure for a relocated community. Technical and 'Bridge Fund' support was provided by the Society for Promotion of Area Resource Centers.

In the case of Ahmedabad, financial

સામૂહિક ગટર યોજના



II પ્રસારનું પાણીનું શોચાલય



and credit services for the Parivartan project are provided by SEWA Bank, while technical support and community motivation is provided by Mahila Housing SEWA Trust

In Vadodara¹⁴, STHAPATI Credit Ltd provided loans for the upgradation of Ramdevnagar slum, while field workers from Baroda Citizens Council provided engineering and supervisory inputs

Finally, in the case of Sri Padmavathy Mahila Abyudaya Sangam in Tirupati, the women community leaders themselves initiated slum upgradation works by accessing a government contributory scheme along with loans from their savings and credit self-help groups or Sangams.

Thus, in each of these collective infrastructure projects, access to credit was vital but access to technical and supervisory support was also critical. While all of these examples prove that the poor are willing to pay and have paid for services (between 30-50 percent of capital costs), they also require technical assistance and a liaison agency to interact with the various involved parties.

However, there is no requirement for technical agencies to invest in

increased staffing costs by recruiting highly qualified engineers or technical experts. The greatest need of poor communities involved in procuring improved infrastructure, including water supply and sanitation, is for institutional support to provide a linkage with the urban local body. Additional support in terms of an easily accessible, low-cost resource center to help with efficient procurement of raw materials, cost estimations and supervisory help while physical upgradation is underway is also important, particularly where the urban local body expects communities to contribute towards construction and management of local facilities.

The greatest need of poor communities involved in procuring improved infrastructure, including water supply and sanitation, is for institutional support to provide a linkage with the urban local body.

¹⁴ Vadodara was formerly known as Baroda.

One common misconception is that once a poor community is relocated or provided with on-site infrastructure, it is prone to sell and move.

3. Lack of land tenure; lack of traditional collateral – in the sector

The linked issues of collateral and legal land tenure are contentious ones, especially when they are viewed with regard to the sanction of shelter-related credit.

The reality is that the majority of the urban poor are settled in slums based on public or privately owned land and lack legal land tenure. Hence, they are unable to provide any form of traditional collateral for loans (such as land ownership documents or utility bills). Even in cases where certain utilities have been accessed, such as electricity, most of these connections are illegal.

The majority clientele of urban microfinance institutions are slum dwellers without legal land ownership documents; to insist on these for loan security is, therefore, impractical. Some microfinance institutions use 'peer pressure' or 'social collateral' through the self-help group model to ensure loan repayments, although this model is more prevalent in rural India. Others rely on close contact with the community for 'security', while community owner-managed financial institutions – such as Mahila Milan – themselves decide which loans are to be sanctioned. All of these approaches appear to work well and result in good levels of loan repayment.

The main problem arises when the microcredit activity expands and re-finance is required from mainstream financial institutions to meet increased demand for loans. Until recently, these institutions mostly insisted on traditional forms of collateral or large-scale bank guarantees prior to sanction

of loans to microfinance institutions. These made accessing bulk funds near impossible, very time-consuming and fraught with a variety of bottlenecks. However, recently the Government of India along with the Reserve Bank of India has begun to recognize the potential of microcredit in reaching its target group of the poor in an efficient way. Thus, alternative security measures such as a percentage of the total loan in the form of a cash deposit with the mainstream financing institution (up to 20 percent) are gradually being introduced to make the loaning process easier.

Returning to the local level, in the case of on-site slum upgrading projects such as in Vadodara and Ahmedabad, one requisite has been an assurance by the municipal authorities that the upgraded slums will not be relocated for a minimum of 10 years. This 'near legal' tenure status has proved a powerful incentive for poor communities to 'buy-in' to the upgradation projects and pay their own contributions.

Finally, one common misconception is that once a poor community is relocated or provided with on-site infrastructure, it is prone to sell and move. On the contrary, all of the communities studied for this project confirmed that this is a rare phenomenon. Interviews with slum residents who have benefited from Ahmedabad Parivartan (Sanjay Nagar and Sinheshwari Nagar) and Vadodara (Ramdevnagar)¹⁵ confirmed that they had no intention of moving as they felt ownership in the upgradation process; they had not only paid for it but had also been an integral part of all

¹⁵ Please refer to the accompanying individual Field Notes.

decisions that were made and were fully involved in the supervision of the physical works. They also expressed relief that they were finally able to have access to better services maintained by their own Residents Associations. In fact, in Sanjay Nagar, the community had devised its own check to ensure that people were not tempted to sell and move by making it mandatory for anybody who wanted to sell, to explain their reasons to the Residents Association and get each of their signatures before the sale could proceed. Even two years after the upgradation was completed, only two families had moved away from Sanjay Nagar.

4. Community and municipal partnership is the key to sustainability

In all the infrastructure projects documented in the case studies, there was a deep feeling of community ownership, usually brought about through the community mobilizing efforts of the non-governmental or technical partner organization. In most cases, while the loans to finance service provision may ultimately be individual, community action as a collective group is essential to bring about actual improvements in infrastructure.

Moreover, in most cases where communities have been provided with infrastructure upgradation, 100 percent



Besides community action, strong linkages with local authorities are also critical for successful infrastructure projects.

of the maintenance responsibilities are being handled by the community. For this purpose, the communities have organized themselves into formal organizations or groups responsible for collection of a maintenance fund and implementation of maintenance works. For the city government, this is a huge saving in the long run, which is not to be underestimated. When questioned, community members stated that since they had paid for the services and been involved in their provision, they felt that they genuinely owned them and thus had a duty to look after them.

Besides community action, strong linkages with local authorities are also critical for successful infrastructure projects. All the four Field Notes clearly highlight the importance of partnerships with the urban local body, as they are the ultimate providers of infrastructure services. This dependence upon the local authorities for off-site connections up to the city mains is a major factor distinguishing the urban situation from that of the rural areas in India.

5. Regular savings and effective field workers are vital for financial sustainability

The field-level research of four prominent microfinance institutions undertaken for this study clearly highlights the necessity for regular savings to ensure high loan repayment rates. All the institutions studied insist on regular savings over a sustained period (ranging up to one year), before a loan may be applied for. Even while a loan is being repaid, ongoing savings are encouraged.

All the microfinance institutions interviewed stated that in their experience, a regular savings habit

usually meant a creditworthy client. With the absence of usual collateral, microfinance institutions rely heavily on good savings habits coupled with monthly household income levels, outstanding dues and asset ownership, among other factors, in determining the extent of loans to be sanctioned.

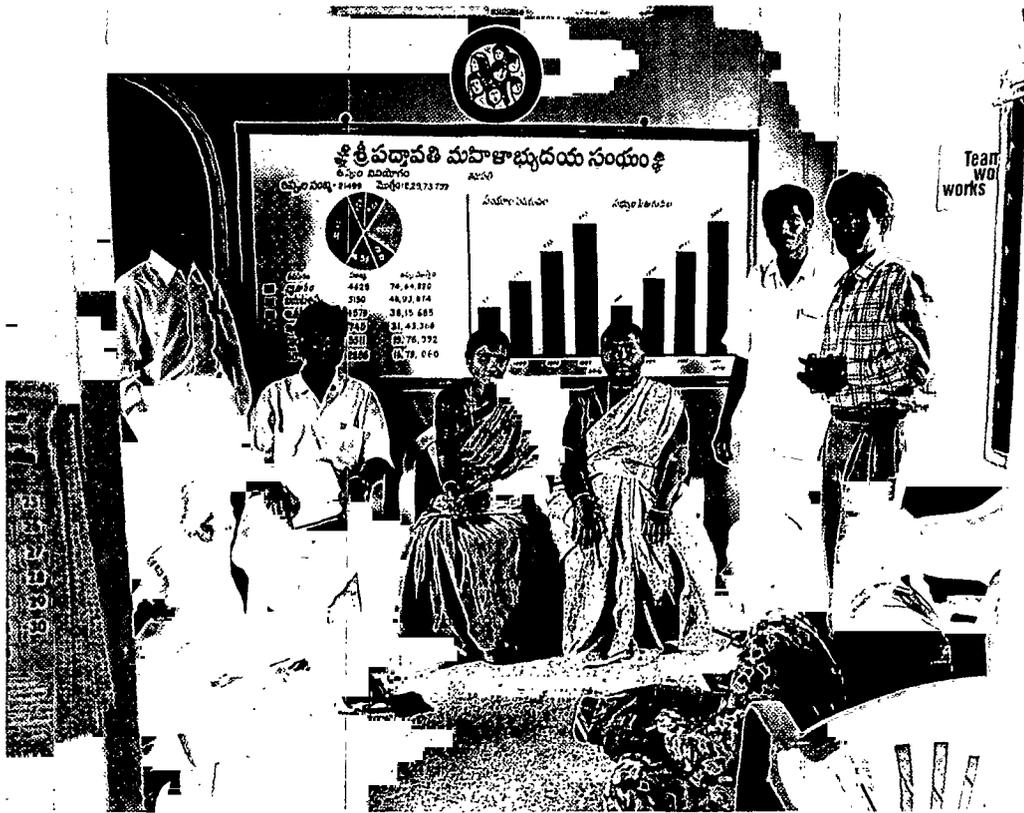
Equally important for ensuring financial success is the role of the field worker within a microfinance institution. This is especially true of those institutions that disburse loans on an individual case-by-case basis, such as SEWA Bank and Mahila Milan. Close interaction and familiarity between the field worker and her clients ensures that she is fully aware of the financial situation of her clients. This in turn ensures that appropriate decisions are taken regarding loan sanction, resulting in high repayment rates.

6. Variety of delivery and implementation mechanisms

While all of the institutions shared important similarities, especially in terms of a high level of community involvement and provision of technical support along with credit support, some differences were also found.

The main difference between the various collective projects documented was in implementation. Some communities left the physical work to municipal engineers while others hired the cheapest contractor. The former usually took longer as municipal corporation workers were not accountable to community groups, while the latter took less time as long as they were well supervised by members of the community and technical persons. However, in the latter case, external factors such as delay in procuring a 'No Objection

All the microfinance institutions interviewed stated that in their experience, a regular savings habit usually meant a creditworthy client.



Certificate' from the Municipal Corporation for upgradation work, contributed to delays. Ultimately, both approaches led to successful infrastructure provision, and the preferred approach probably needs to be worked out on a city-specific basis. Whatever arrangements are made, one key question is always the ability of the urban local body to sustain its involvement with community initiatives.

In the case of 'Parivartan' in Ahmedabad, the Ahmedabad Municipal Corporation has formally adopted the ongoing project and set up a 'slum networking cell' within the Corporation to oversee project implementation and expansion. Eighteen slums are currently being targeted by Parivartan. On the other hand, the upgradation of Ramdevnagar slum in Vadodara was a pilot project initiated by the Baroda Citizens Council and community members. The concept of on-site overall upgradation is yet to

be formally adopted by the Vadodara Municipal Corporation. The replicability of this pilot project is not assured.

B. India-specific Issues
1. Microfinance institution models in urban India

In the past five years, there has been a marked growth in the number and outreach of microfinance institutions disbursing infrastructure loans to the urban poor in India. This is largely due to an institutional shift to recognize, support and facilitate these credit organizations working at the field level to enable poor communities to access improved infrastructure. Most successful microfinance institutions such as SEWA Bank, Ahmedabad, have average loan repayment rates ranging from 90 to 100 percent – a powerful statistic to reinforce their sustainability. Conservative estimates indicate the following:

- There are currently about 50

- **Banker's Model**, e.g. SHARE, Hyderabad; ASA, Trichy: Developed from the Grameen Bank operational guidelines; dependent on appropriate group formation and peer pressure or 'social collateral' to ensure high loan repayments. Solely a financial institution, playing the same role as any commercial bank, with one major difference: all its clients are women subsisting below the poverty line. This model is purely that of an alternative credit institution; it does not wish to dilute its primary mandate of providing microfinance to the poor through the provision of additional social 'development' services.

- **Traditional Non-governmental Organization Model**, e.g. SIDA, Koovapally, Kerala; Baroda Citizens Council, Vadodara: Plays the role of a financial intermediary, supplying small-scale loans to the poor, accessed in bulk from mainstream financial institutions. These may be disbursed in the form of individual loans or through group loans. Their objective is to bring about 'overall development' of the target community. Thus, they undertake a host of other developmental activities in the areas of health, education etc. SIDA has a building center and has constructed 2,350 sanitary latrines accessing a combination of government subsidies and owner contributions. It has also facilitated drinking water facilities to 300 families by channeling government funds and involving community participation.

- **Evolving Community-based Financial Institutions**, e.g. SPMS, Tirupati, Tamil Nadu; Mahila Milan, Mumbai: 'People-led' organizations that only play the role of a financial intermediary. All decision or policy making is fully member controlled – ownership rests with the community. Paid professional staff undertake day-to-day maintenance functions. High priority is given to training to build community capacities.

- **Mainstream Community-based Financial Institutions**, e.g. SEWA Bank, Ahmedabad: Essentially 'people-led' financial organizations, which are community-owned and community-governed. Policy decisions are made by a Board of governors elected by the community, but implementation is undertaken by a body of professionally trained staff, a high proportion of whom are grassroots field workers. Despite catering solely to the credit needs of the poor – usually through individual loaning – these institutions have attained the status of a mainstream commercial bank due to their excellent track record, substantial outreach and favorable financial indicators.

microfinance institutions disbursing housing and infrastructure loans to the economically weaker sections throughout India.

- There are over 150 additional microfinance institutions, currently supplying income generation and a small proportion of consumption loans to the poor. A large number of these institutions are poised to begin on-lending housing and infrastructure loans to their clients.

Research at the field level indicates four main models of microfinance

institutions involved in disbursing credit to the urban poor in India. Their broad characteristics in terms of lending methodology, organizational structure and basic ideology are summarized on this page¹⁶.

2. Lack of accurate loan categorization by microfinance institutions – sector volume difficult to quantify

Traditionally, in India, provision of infrastructure has been viewed as the responsibility of the government alone.

Research at the field level indicates four main models of microfinance institutions disbursing small-scale credit to the urban poor in India.

¹⁶ This typology is a basic introduction to the microfinance models currently prevalent in India; a substantial amount of research has recently been undertaken on issues relating to the microfinance sector, including its legal status, capacity-building needs, performance norms, credit rating etc. More information may be obtained from Sadhan, 2163, DII Vasant Kunj, New Delhi 110 070.

It is only recently, with changing needs and changing attitudes, that poor communities are beginning to view the installation of services as an area in which they can actively participate. As far as they are concerned, this is a newly emerging sector.

In response to this emerging demand from clients, small-scale loans for infrastructure and slum upgradation are a fairly new loan 'category' introduced by urban microfinance institutions in India. Of the four microfinance institutions selected for this study, all were found to include infrastructure loans within the overall category entitled 'housing upgradation/repair'. Unfortunately, loans for a wide variety of purposes, including converting a house from *kuchcha*¹⁷ to *pucca*¹⁸, plastering walls, adding an extension or converting a mud floor to a concrete one are also included in this categorization.

On-site infrastructure generally refers to individual tap connections, toilets, drainage, sewerage and electricity connections as these are all integral to a house. Thus, it is reasonable for microfinance institutions to include loans for infrastructure within the overall housing upgradation category. Unfortunately, this 'generalized' categorization does not allow an accurate estimation of the volume of loans currently being disbursed for infrastructure through microfinance.

A preliminary review of SEWA Bank's housing and infrastructure loan portfolio suggests that up to 15 percent of the total loans disbursed by SEWA Bank are for infrastructure-related

needs. In order to get a better idea of the size of this sector, a detailed review of loans within the 'housing repair and upgradation' category of each microfinance institution would have to be undertaken. All the loans would need to be analyzed on a sample basis for the previous three to five years. A detailed analysis of this kind would yield a more accurate estimate of the total volume of 'infrastructure' loans currently being disbursed by microfinance institutions to poor consumers in urban India.

3. Institutional funding for infrastructure – sources, blockages and recommendations

Field-level interviews have clearly demonstrated that demand for infrastructure-related credit is very high among women in the informal sector. While the implementation of large-scale infrastructure projects for the purpose of building main arterial roads, bridges and electricity plants have been regularly undertaken, it is important to recognize that the provision of improved drinking water or drainage facilities in urban slums are equally important infrastructure requirements. Existing formal institutional funding mechanisms usually do not allow poor communities to be involved in accessing improved services. With increasing demand at the grassroots for better services, small-scale loans accessed from microfinance institutions are an effective facilitating tool. However, microfinance institutions face a variety of institutional problems in accessing adequate funds for on-lending to poor communities.

On-site infrastructure generally refers to individual tap connections, toilets, drainage, sewerage and electricity connections as these are all integral to a house.

¹⁷ *Kuchcha*: Mud walls and floor with thatch or tiled roof.

¹⁸ *Pucca*: Bricks and concrete; sometimes with asbestos roof.

Despite repeated representations by grassroots organizations demonstrating that housing and infrastructure loans are productive loans for women in the informal sector and that the composite credit needs of the poor should not be artificially segregated, this divide continues at the institutional level.

“There is more and more demand on the ground from women for housing and infrastructure finance. By our estimates, women in the informal sector can absorb and repay Rs 200,000 million right now, today, in India.”

**Renana Jhabvala,
Executive Trustee,
Mahila Housing
SEWA Trust**

The first source of funds for on-lending available to microfinance institutions is the credit fund built up from members' own savings. Usually, this is fairly substantial and adequate to supply small-scale credit needs. In time, however, this fund becomes inadequate to meet the high demand for credit from members. This is especially true for infrastructure upgradation loans, which are often of a higher quantity and have longer repayment periods.

“There is more and more demand on the ground from women, for housing and infrastructure finance. By our estimates, women in the informal sector can absorb and repay Rs 200,000 million right now, today, in India. Microfinance institutions have been providing housing and infrastructure finance to women in the informal sector, but they need to keep increasing their loan volumes.”

This recent statement by Renana Jhabvala, Executive Trustee, Mahila Housing SEWA Trust, quantifies the huge field-level demand for housing and infrastructure credit. Unfortunately, the supply of credit to this sector is a fraction of the total demand. In order to provide bulk infrastructure loans to the poor, most microfinance institutions, including the four studied for the purposes of this report, are dependent upon two main institutional sources for accessing loans in large quantities. These are the two national housing finance institutions – namely, the Housing and Urban Development Corporation Ltd and the Housing Development Finance Corporation Ltd. Other government sources of bulk

funds for microfinance institutions, such as Small Industries Development Bank of India and Rashtriya Mahila Kosh cannot be accessed for any housing or infrastructure loans as their mandate clearly states that loans may only be used for income generation or productive purposes. Despite repeated representations by grassroots organizations demonstrating that housing and infrastructure loans are productive loans for women in the informal sector and that the composite credit needs of the poor should not be artificially segregated, this divide continues at the institutional level. This artificial distinction discriminates heavily against home-based workers¹⁹, for whom water and electricity are often important factors of production.

In addition, there are multiple procedural problems in accessing timely and adequate bulk credit from mainstream re-finance institutions. These include problems with furnishing adequate security collateral; a highly bureaucratic loan procedure leading to indeterminate delays; lack of flexibility in the loan system despite the nature of the clientele; interest rate caps which are too low to meet the expenses of the microfinance institution; and a general lack of exposure to this special client sector and its particular needs.

In recent years there has been an active effort by microfinance institutions disbursing housing and infrastructure loans to poor women in the informal sector to sensitize mainstream housing finance institution officials to the procedural problems they face in accessing adequate re-finance from them. A national-level task force has

¹⁹ Approximately 20-30 million of the Indian labor force are home-based workers, of which over 80 percent are women (Source: Renana Jhabvala, SEWA).

been set up with the mandate to remove these hurdles²⁰. In the meantime, the grassroots microfinance institutions continue to face difficulties in accessing adequate bulk loan funds to meet the infrastructure credit needs of their clients.

C. India: Specific Future Needs

1. Need for a national Loan Bridge Fund²¹/Loan Guarantee Fund

Many of the microfinance institutions that were interviewed felt that a national-level 'Bridge Fund' would be very useful in overcoming the current delays in accessing bulk funds from mainstream housing finance institutions for on-lending infrastructure and housing loans to their members.

Especially in the case of infrastructure, delays in the middle of

projects or beyond the monsoons can yield much hardship to slum residents and delay completion. Thus, while the formal loan application to mainstream re-finance institutions is being sanctioned and released (typically 12 to 18 months), access to a 'Bridge Fund' may be an interim solution. As Sheela Patel of the Society for Promotion of Area Resource Centers, Mumbai, says, "A Bridge Fund to tide communities over those long, unglamorous 'middles' of (infrastructure) projects is sorely needed."

Even in the case of accessing government subsidies, a Loan Bridge Fund is needed. For example, the experience of Mahila Housing SEWA Trust has been that on average it takes six to eight months to receive the subsidy for toilets available to the urban poor from the Government of

“A Bridge Fund to tide communities over those long, unglamorous 'middles' of (infrastructure) projects is sorely needed.”

**Sheela Patel,
Society for Promotion
of Area Resource
Centers, Mumbai**



²⁰ For more information on the Task Force, contact Mahila Housing SEWA Trust, Ahmedabad.

²¹ This Bridge Fund would be a centralized, easy source of interim, short-term funds to tide community groups and microfinance institutions through cash flow crises.

66 Microfinance has tremendous potential as an instrument for poverty reduction, but complementary efforts such as teaching women to read and write and training are necessary to help those who lack the skills to make credit work for them.

Shahid Khandkar,
Senior Economist,
Poverty Reduction and
Economic Management
Network

Gujarat. The subsidy is granted on a reimbursement basis after the beneficiary has completed building the toilet as per the government's design specifications and following a satisfactory inspection visit. For this, she is required to make upfront payments. Often, SEWA Bank provides intermediary loan funds to these women, to allow them to build their 'subsidized' toilets. In reality, most of the loans (usually between Rs 3,000 to Rs 3,500) are repaid in full, before the subsidy is finally handed over to the 'beneficiary'. This common occurrence reinforces the need for a national-level, easily accessible Loan Bridge Fund.

A more ambitious idea, to float a housing and infrastructure loan guarantee fund²² at the national level, has also been suggested by the microfinance institutions. This would provide a credit guarantee for loans to microfinance institutions. It would remove the issue of 'adequate security' and give mainstream financing institutions more confidence in sanctioning loans to non-formal financing institutions. The Housing and Urban Development Corporation Ltd has recently set up an internal Loan Guarantee Fund, in order to give its regional offices a greater degree of confidence and flexibility in sanctioning loans to prominent microfinance institutions. However, success in implementation is yet to be determined.

2. Need for capacity-building – communities, microfinance institutions, municipalities and housing finance institutions

A recent World Bank study by Shahid Khandker, Senior Economist, Poverty Reduction and Economic Management Network, has found that:

"Microfinance has tremendous potential as an instrument for poverty reduction, but complementary efforts such as teaching women to read and write and training are necessary to help those who lack the skills to make credit work for them²³."

The microfinance institutions studied for this initiative echo the same findings. Especially in the area of infrastructure upgradation, where interaction with municipal and other government officials is required, capacity-building, exposure and negotiation skills training for community leaders are very important. Equally important is technical training for building toilets, sinking borewells, carrying out accurate cost estimations and the maintenance of the facilities.

Given that infrastructure-related microfinance is a relatively new, emerging sector, most microfinance institutions in India are yet to develop specialized systems for loan sanction and repayment. Shelter-related loans have specific characteristics distinguishing them from other loan types. They are usually of higher volumes with longer repayment periods and require careful utilization

²² The modalities of the proposed National Loan Guarantee Fund will need to be researched. The essential aim is to build a fund with contributions from housing finance, microfinance, bilateral and other interested institutions. Eventually, each microfinance institution would own a share in the fund, which it could draw upon in case of delayed repayments from clients. Such a fund would resolve the contentious issue of adequate 'collateral' when accessing re-finance from formal financial institutions.

²³ Source: Khandker, S., *Fighting Poverty with Microcredit: Experience in Bangladesh*, the World Bank, 1999.

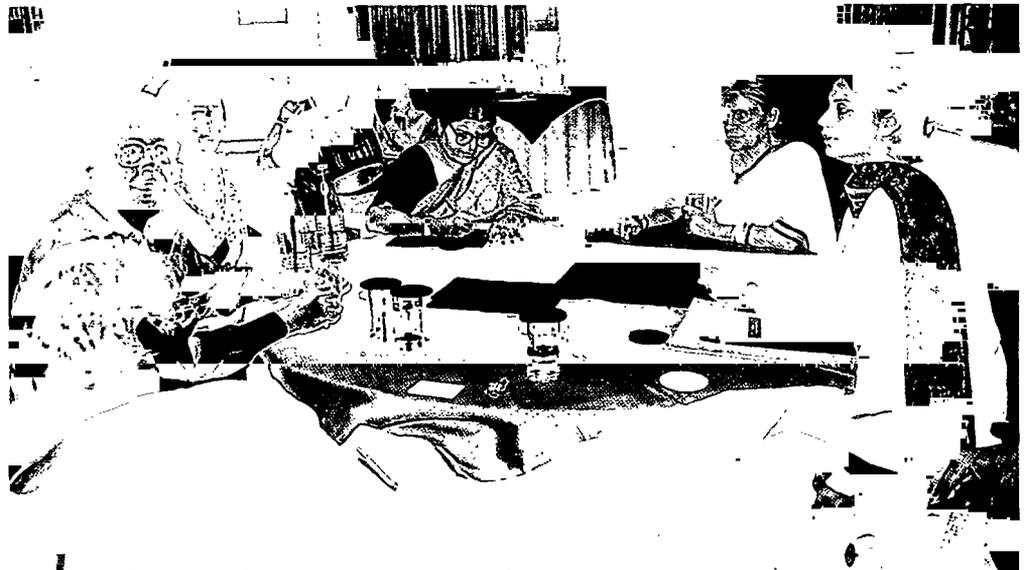


monitoring. At the same time, the field-level demand for such loans is very high. This necessitates the development of a specialized loaning and monitoring system for such loans. The Action Research component of this initiative attempts to fill this need by detailing a prototype housing and infrastructure loan department that may be adopted by microfinance institutions catering to the shelter-related needs of individual, poor women in the urban, informal sector.

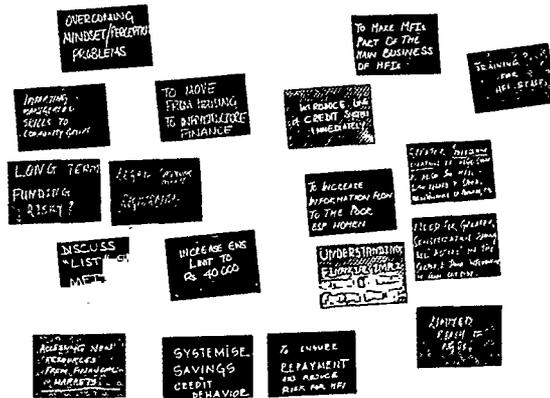
In the absence of careful monitoring systems, loan repayment rates may suffer. STHAPATI Credit Ltd in Vadodara is an example where the speedy growth of the microfinance operation as a whole overtook the development of the requisite systems, caused largely by the high field-level demand for loans. As a

result, the percentage of delayed loan repayments (later than three months after the loan repayment due date) increased to 35 percent. Fortunately, due to the close interaction between the microfinance field workers and the loanee community, this delay did not translate into large-scale loan write-offs. The institution has recently been investing substantial resources and time to improve its loaning systems, so as to keep up with the ever increasing demand for greater loan numbers and volumes, especially for shelter-related purposes.

In addition, capacity-building for microfinance personnel, so that they may train community leaders in technical and maintenance functions and facilitate collective infrastructure upgradation projects by providing a



CAPACITY BUILDING



A particular lesson that emerges for institutions looking at channeling money (loans and grants) through mainstream housing finance institutions to microfinance institutions, is to consider how to most effectively channel the technical assistance required for capacity-building, to community groups and microfinance institutions.

liaison with government officials, is also vital. Municipal officials also require training and exposure to help them realize the potential for poor communities to manage infrastructure projects and to facilitate their working in partnership with communities. This will enable the scaling up of infrastructure related projects and, therefore, the infrastructure loans sector.

Finally, capacity-building for mainstream housing finance institution personnel, especially at the regional office level, regarding the activities and criteria for identifying and assessing the creditworthiness of microfinance institutions is also required in order to facilitate increased re-finance being

made available to the microfinance sector.

A particular lesson that emerges for institutions looking at channeling money (loans and grants) through mainstream housing finance institutions to microfinance institutions, is to consider how to most effectively channel the technical assistance required for capacity-building, to community groups and microfinance institutions.

3) Exploring scaling up

In order to scale up both infrastructure provision and infrastructure credit to poor communities, there is a need to understand and detail the roles and responsibilities of different stakeholders, clarify the different roles required and match appropriate actors with these. In addition, producing joint guidelines with the local authorities, containing a clear and simple set of rules vis-à-vis access to and level of subsidies and detailing the norms and requirements for service connections to slum communities, would also contribute in eventually up-scaling slum development efforts.

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