

STUDY ON

**ONE DECADE OF MFI CRISIS:
REVISITING THE RURAL CREDIT MARKET
IN ANDHRA PRADESH AND TELANGANA**



Centre for Research on Financial Inclusion and Microfinance (CRFIM)
Bankers Institute of Rural Development (BIRD), Lucknow
An ISO 2001:2015 Certified Institution Promoted by NABARD

Foreword

The undivided state of Andhra Pradesh was the epicentre for microfinancing in the country during the decade 2000 – 2010. It was estimated that in 2010, out of the 30 million households using microcredit in India, around one third were in Andhra Pradesh. The State was also the home to five of the country's major NBFC-MFIs. The competition among MFIs and hasty rush for business growth had caused a massive debt bubble in the state. The average debt outstanding per poor household in Andhra Pradesh was eight times higher than the national average. Further, usurious interest rates on unsecured loans and the coercive recovery practices adopted by MFIs led to panic among borrowers, leading even to suicides across the state. The Ordinance, viz, "*The Andhra Pradesh Microfinance Institutions (Regulation of Money Lending) Act, 2010*" promulgated by the State Government to contain the crisis in the sector resulted in crippling of the MFI operations in the state during 2010. The ripple effect also slowed the growth of the microfinance industry in other parts of the country. Over the years, the number of operating MFIs had reduced substantially.



The present study, "*One Decade of MFI Crisis: Revisiting Rural Credit Market in Andhra Pradesh and Telangana*" was contemplated by BIRD, Lucknow to analyse the impact of the MFI crisis on rural credit market in both the states and arrangements to meet financial needs of microFinance clients in post MFI crisis period. The study has jointly been conducted by Centre for Research on Financial Inclusion and Microfinance (CRFIM) at Bankers Institute of Rural Development (BIRD), Lucknow and LEAD at Krea University (Formerly IFMR LEAD). It was observed that the growth of SHG credit linkage programme over the decade and strengthening of other micro credit approaches, particularly the credit linked subsidy schemes served well as alternative sources of credit to the microfinance clients in the post crisis period.

I sincerely believe that findings and recommendations of the study would be useful for policy makers for further consolidation of the microfinance approaches.

I congratulate both LEAD and CRFIM teams for their effort as also thank all the stakeholders and agencies for providing their responses and inputs for the study.

Shankar A. Pande

Director, Bankers Institute of Rural Development, Lucknow

Acknowledgements

The study on *“One Decade of MFI Crisis: Revisiting Rural Credit Market in Andhra Pradesh and Telangana”* has jointly been CRFIM, BIRD, Lucknow and LEAD at Krea University (Formerly IFMR LEAD).

We are thankful to the Governing Council, BIRD, Lucknow and Micro Credit Innovations Department (MCID), NABARD Head Office, Mumbai for their guidance and support.

The study has been guided and supervised by Shri Shankar A. Pande, Director, BIRD, Lucknow without whose valuable inputs the report would not have been possible.

We are also grateful to Shri Mukesh Vats, Joint Director, BIRD, Lucknow without whose painstaking efforts, this work couldn't have been completed.

We want to place on record our sincere gratitude to Late Dr. P Satish, Executive Director, Sa-Dhan for critically reviewing the draft and giving invaluable inputs which helped to bring the report to its present form.

We acknowledge the support received from NABARD Andhra Pradesh & Telengana Regional Offices and DDMs of respective districts for facilitating the field study.

We also wish to extend our gratitude to Dr. N Jeyseelan, Sector Expert; Prof. M S Sriram, Sector Expert and Shri N Srinivasan, Former CGM, NABARD for their valuable inputs.

The study is the result of extensive field work and documentation by the LEAD team led by Ms. Sharon Buteau, Executive Director, LEAD at Krea University. We acknowledge their efforts and record our appreciation for the insights and data brought in through the report.

Last but not the least, we express our gratitude to Smt. Deepmala Ghosh, GM, WBRO & the then centre in-charge and Faculty Members of BIRD, Lucknow and Shri Tamanud Ghosh & Dr. Monika Saini, Research Officer, BIRD for formulating ToRs and evaluating the report at various stages.

Anukampa Jha

CRFIM In-charge

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List of Abbreviations

AMFIRS	Assam Micro Finance Incentive and Relief Scheme
AP	Andhra Pradesh
APMAS	Andhra Pradesh Mahila Abhivruddhi Society
AODL	Average Outstanding Debt per Indebted Household
ASA	Association of South East Asia
BRAC	Bangladesh Rehabilitation Assistance Committee
CAGR	Compound annual growth rate
DFC	Daily finance corporation
FGD	Focus Group Discussion
FLDG	First Loss Default Guarantee
GLP	Gross Loan Portfolio
IFC	International Finance Corporation
IFMR	Institute for Financial Management and Research
IICA	Indian Institute of Corporate Affairs
INR	Indian Rupee
IoI	Incidence of Indebtedness
IPO	Initial Public Offering
JLG	Joint Liability Group
MEPMA	Mission for Elimination of Poverty in Urban Areas
MFI	Micro Finance Institution
MFIN	Micro Finance Institutions Network

MIV	Microfinance Investment Vehicle
MoU	Memorandum of Understanding
MYRADA	Mysore Resettlement and Development Agency
NABARD	National Bank for Agriculture and Rural Development.
NBFC	Non-Banking Financial Assets
NGO	Non-Governmental Organization
NIRDPR	National Institute of Rural Development and Panchayati Raj
NPA	Non-Performing Asset
PAR	Portfolio at Risk
RBI	Reserve Bank of India
ROSCA	Rotating Savings and Credit Association
RRB	Regional Rural Bank
SBI	State Bank of India
SERP	Society for Elimination of Rural Poverty
SEWA	Self-Employed Women's Association
SFB	Small Finance Banks
SHARE	Society for Helping and Awakening the Rural Poor through Education
SHG	Self Help Group
SKS	Swayam Krushi Sangham
SRO	Self-Regulatory Organisations
TS	Telangana
USD	US Dollars
VLR	Vaddi Leni Runalu

Executive Summary

Andhra Pradesh emerged as the “hotbed” of microcredit in India in the decade 2001-10. The SHG-Bank Linkage Program, which started in early 1990s, received considerable support from NABARD in Andhra Pradesh and grew with active handholding by state government-led initiative, the Society for Elimination of Rural Poverty (SERP). The foundation laid by SHGs in developing a credit culture in the state was leveraged significantly by MFIs. The state was home to five of India’s largest NBFC-MFIs in the first decade. The flash point between the state-incubated SHG movement and the private MFI industry occurred with a series of media reports in late 2010 attributing suicides by borrowers to “usurious” interest rates and the “coercive” recovery practices of MFIs. As a response to these events, the state government promulgated an ordinance on October 15, 2010 (passed by the legislative assembly in December 2010) to provide for restrictions on and mandatory approvals for the conduct of business by MFIs.

The ordinance had a devastating effect on MFIs’ debt recovery operations, particularly after local politicians, riding on the populist sentiment against lenders, dissuaded borrowers from repaying MFIs. This triggered a wave of wilful defaults. The realization that MFIs would not extend another loan also served as a disincentive for borrowers to repay existing loans. Consequently, over the next year and more, MFIs started winding down operations in the state. By 2015, nearly 90% of NGO MFIs and other trust MFIs had exited the state. Small MFIs were the worst affected and had to shut shop as they did not have a footprint in other states.

Once the dust settled after the massive defaults and the shutdown of MFIs, the landscape reflected the grim effect of credit starvation. In the absence of credit from MFIs, borrowers faced difficulty in financing their regular household needs. No single source was sufficient to meet borrowers’ credit needs. SHG loan outstanding grew at 13% CAGR, but they were no match for MFIs. Studies done at that time found borrowers mentioning that borrowing from MFIs had been more convenient, and that securing loans from SHGs was time-consuming. In the vacuum created by the withdrawal of MFIs and the challenges associated with borrowings from SHGs, ‘call money lenders’ emerged as a viable but high-cost alternative. In December 2015, the State Assembly passed the Andhra Pradesh Money Lenders Act, aimed at regulating private moneylending, with licenses for all moneylenders and caps on interest rates.

Over the years however SHGs in the two states, Andhra Pradesh and Telangana, started posting better performance. SHGs became a vehicle to deliver government schemes in rural areas. Stree Nidhi was started up by SERP in 2011 as a State-backed credit co-operative federation to supplement credit flow to SHGs from the banking sector. A study conducted in 2021 established that Stree Nidhi loans helped set up new enterprises in 56% of the cases. In 2012, to incentivize prompt repayment and enhance rural enterprises’ income, the Andhra Pradesh government started a revamped ‘Vaddi Leni Runalu (VLR)’scheme to reimburse the total interest above a threshold to further strengthen rural enterprises.

A primary survey conducted by LEAD in August 2021 for the present study found the dominance in borrowing from SHGs in Andhra Pradesh and Telangana. The survey further found that in the sampled

regions, reliance on moneylenders and other informal sources had reduced. The repayment record of SHG borrowers has been shown to be good owing to the trust factor among them. The ability to repay SHG loans on time was higher (75%) than with banks, moneylenders and friends/ family. 78% of the SHG members borrowed exclusively from the SHGs and 73% of the members borrowed at least once a year from the SHG.

As of March 2022, the average loan outstanding per SHG in the country is the highest in Andhra Pradesh (about INR 5 lakh) followed by Telangana (about INR 3.5 lakh), substantially higher than in other states. Further, in a recent report by SBI on its SHG portfolio, 22 of the top 25 districts in India in terms of its SHG loan outstanding are in Andhra Pradesh (13 districts) and Telangana (9 districts).

Possibility for the re-entry of MFIs into Andhra Pradesh and Telangana

The checks and control systems developed by the MFI industry in the aftermath of the crisis have ensured that the aggressive lending and coercive recovery practices do not recur. Following up on the RBI's Malegam Committee report's suggestions for institutionalizing self-regulatory organizations (SROs) in the microfinance space, MFIN and Sa-Dhan have continued to fulfil their mandate to ensure client protection by institutionalizing a code of conduct and best practices for the industry. Both the SROs played a crucial role in defusing the Assam microfinance crisis of 2020-21. RBI's recent Master Direction 2022 reiterates its simultaneous commitment to innovation and customer protection.

While MFI and the SHG disbursements in Andhra Pradesh were at the same level in 2009-10, MFI fortunes suffered a setback in 2010-11. [Assuming a conservative 30% growth in the MFI loan portfolio in Andhra Pradesh and Telangana, in 2019-20, total loan disbursed would have reached about INR 86,000 crore, approximately 13 times the figure for 2009-10. Over the same period, SHG loan disbursements rose from about INR 6,700 crore to about INR 35,000 crore, only a five-fold jump. There is thus an as-yet-unfilled gap in the rural microfinance market in the two states.](#)

SHGs and MFIs co-exist in many states and are together charting a success story based on their respective strengths. Karnataka, Tamil Nadu and Bihar are the states with the highest MFI customer base. They account for 15%, 13% and 10%, respectively, of microfinance customers in India. They also account for 14%, 5% and 9%, respectively, of the number of SHGs with loan outstanding. In contrast, Andhra Pradesh and Telangana account for 19% and 11%, respectively, of the number of SHGs with loan outstanding, but their MFI customer base is minuscule. The RBI and NABARD continue to keep a keen eye on the evolution of the sector. SROs have a finger on the pulse of the field, through the large networks of MFIs operating across the country. There is thus merit in bringing all the stakeholders together to consider the facts on the ground objectively and discuss the incremental and calibrated steps that can be taken to allow the re-entry of MFIs in Andhra Pradesh and Telangana. The Bankers Institute of Rural Development (BIRD) can play an important role by providing a platform for dialogue between the relevant stakeholders, with independent advisory from national and international subject-matter experts.