MicroSave India Focus Note 21

Village Financial Systems in Northeast India

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July 2009

Villagers in Lower Assam are pioneers on the frontiers of informal finance, according to the results of recent field work conducted by the Indian Institute of Bank Management (Guwahati) in collaboration with *MicroSave*, in two local villages (Mazarpara and Khakhrisal). The villages boast 46 ASCAs (referred to locally as *xonchoi samities*) varying from 6 to 65 members (see data snapshot).

A Tale of Two Villages

	Mazarpara	*Khakhrisal*
Households	72	130
ASCAs	26	20
Memberships	524	493
Memberships/household	7.3	3.8
Bank/post accounts	6	1
Value of village system	$16,117	$13,051

With about Rs.1.45 million (US$29,168) in these villages' ASCA systems, average member balances appear small (about $35). But there are 1,017 discrete ASCA memberships distributed among the villages' 202 households – an average of 5 per household. This puts average household balances at around US$145 - a significant sum. Loan rates are typically about 3-5% a month, with some ASCAs lending to non-members at higher rates.

Of the two villages, Mazarpara is more urban and more economically active. Villagers say there are far fewer moneylenders now than in the early 1980s, when the first ASCAs started. There is a commercial bank in Chaygaon where 5 ASCAs hold liquidity or savings accounts. But individual villagers rarely use it because of its high deposit requirements and fees, combined with the villagers' low levels of literacy. Confidence in the ASCAs may be another reason: villagers state that no ASCA has failed in the history of the village.

A Financial System is Flexible ...

To accommodate more affluent households, ASCAs permit members to take shares in multiples of the base rate. Thus if the standard contribution is Rs.50 a month, an affluent household might subscribe to 3 shares at Rs.150 a month.

And to address the seasonality of rural cashflows, ASCAs in the more rural community of Khakhrisal adopt several measures:

- They start operations during surplus seasons, (55% of the sample started during the surplus months of January-April, compared to only 16% during the lean months of May-August);
- They take 'top-up' contributions, often of Rs.100 per share, during start-up;
- They permit members to defer contributions during the lean season by converting the amount into short-term loans of up to 2 months; and
- They are much stricter in collections of principal and interest at the end of the cycle (usually another surplus season) rather than the middle.

One *xonchoi* manager explained that "our financial year ends on the 1st of Magh[1] (mid-January). All of our calculations are done then. People find it easier to repay because of the surpluses in their houses".

And Meets Multiple Needs ...

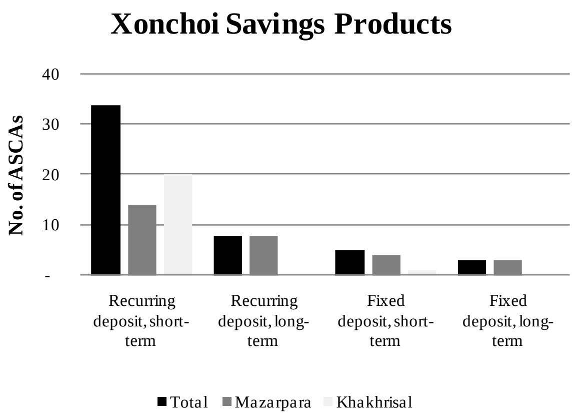
It is generally believed that the informal market, whatever its scale, cannot offer a wide scope of financial services. In Mazarpara, when there is need for a new financial service, the villagers start a new ASCA. By starting a new ASCA instead of adding the service to an existing one, they keep the risk of loss in any individual ASCA manageably small.

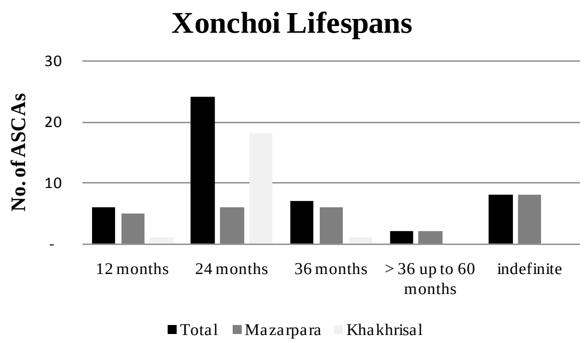
The following types of ASCAs operate in Mazarpara:

- The classic 'recurring deposit' ASCAs provide members with lump sums dedicated to a specific savings purpose, like a festival, a wedding or school fees.
- A 'retirement ASCA' with 65 members is nearing the end of its 4th 5 year cycle. It invests all savings in a recurring deposit at the nearby Post Office.
- Several 'term deposit ASCAs' were formed by members who pool cash surpluses they do not need in a one-time deposit. These ASCAs may last for 2-5 years and to avoid book-keeping complications do not accept subsequent deposits.

Average effective profits per member were 21.3% in Mazarpara and 58.3% in Khakhrisal, calculated on the basis that the groups broke and disbursed all assets the day of the survey. The wide divergence results from sharp differences between urban and rural settings and ASCA strategies.

[1] Magh is the Assamese month which begins in mid-January and ends in mid-February.





In Mazarpara ASCAs charge lower rates (typically about 3% a month) and less than 53% of their assets were invested in loans, while the balance was in bank and post office accounts. In Khakhrisal by contrast, ASCAs charge higher interest rates (typically about 5% a month) and over 99% of their assets were invested in loans the day of the survey.

Xonchoi Financial Systems Compared

	Mazarpara		**Khakhnisal**	
	Nov. 18-20, 2008		*Feb. 14-15, 2009*	
	US $	%	US $	%
Assets				
Cash in hand	3,860	24%	46	0.4%
Cash in bank	1,929	12%	-	0.0%
Term deposit in bank	1,657	10%	42	0.3%
Term deposit in post office	201	1%	-	0.0%
Loans outstanding	8,470	53%	12,964	99%
Total	**$16,118**	**100%**	**$13,051**	**100%**
Liabilities and Equity				
Savings/equity contributions	10,609	66%	9,652	74%
Retained earnings	5,509	34%	3,398	26%
Total	**$16,118**	**100%**	**$13,050**	**100%**

... and Exercises Collective Control

In Mazarpara there is an active para-profession of 6 *xonchoi* auditors, usually school teachers or educated village youth, in addition to four or five others who are sometimes called upon to undertake the job. These auditors have a vested interest in auditing the books thoroughly as most of them are also group members who own multiple shares.

Some groups assign different members to maintain assets and liability records, which are reconciled quarterly.

Rutherford has aptly described ASCA dissolution as an 'action audit', since it answers every member's silent and continuous question: "Is my money safe?"[2] But if dissolution is a highly effective form of informal audit, why are *actual* auditors needed and valued in these villages?

1. These 'frontier' ASCAs are unusually long, up to 5 years and in eight cases, indefinite. The village auditors check the books annually – effectively replacing the action audit with a more technical audit.
2. Audits are conducted immediately before dissolution, which introduces an independent check against the risk that the members may not catch an error or fraud at the end of the cycle.

In addition, there appears to be a relationship between linkage to formal sector financial services and ASCA longevity. For the small sample studied, the correlation between ASCA longevity and institutional linkage was +0.653, with confidence of greater than 99%. In other words, if an ASCA is linked to a formal institution the probability of it extending its term is much higher than otherwise. All of these linkages are savings related.

Conclusions

Globally, ASCAs generally operate within the range of 6-12 months. In the villages studied, none operated for less than 12 months. There were 8 indefinite *xonchois* ranging from 36 to 130 months old. None of these had identified a specific breaking date.

What drives the relative strength of ASCAs in these two villages? This is not yet clear and will require further research. The Mazarpara financial system has received large injections of SGSY subsidies in recent years. Poor repayments in some SHGs have made ASCAs cautious about lending – a factor that may have influenced the emergence of many savings-links with the formal sector.

What seems certain is that in these villages, everybody knows who the good ASCA leaders are, who the good members are, and who the good book-keepers are. In Mazarpara informal audit practices are such that they also know which auditors to trust. Setting up a new ASCA involves little more than identifying reliable members with a shared financial services need. The line separating this complex mix of informal shared understandings and practices from a 'permanent institution' appears thin.

[2] **Rutherford**, Stuart, "The Poor and Their Money", Oxford University Press, Delhi, 2000.