PARADIGM PARANOIA OR MISSION DRIFT? LESSONS FROM MICROFINANCE CRISIS IN INDIA

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Globally, microfinance industry is said to be at the tipping point thanks to crisis originating from India, particularly the state of Andhra Pradesh. The crisis manifested through the suicides of the borrowers who allegedly were lured into excessive borrowing and subsequently, pushed into usurious debt-servicing by the microfinance institutions. The hard selling of the debt and questionable debt recovery practices are attributed to the drift towards profit-seeking micro-lending as against the avowed mission of serving the poor. With the help of case study of SKS, the article attempts to examine the incidence and impact of mission drift in microfinance. It , then, puts it in the broader context of the neoliberal paradigm that paranoically upholds that the markets by themselves are capable of attaining the developmental goals, including alleviation of poverty. The article highlights the tyranny of markets with the help of two more instances since SKS, viz., Sahara and Sardha. On the basis of the analysis of these failures, the authors posit that rather than being paranoid about the neoliberal paradigm that presumes that market is self-creating, self-regulating, self-stabilising, self-legitimising and hence, self-sufficient institution, it would be more advisable to take note of their limitations more so as those pertaining to the permissibility of pursuit of one's greed as genuine self-interest.

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1. Introduction

Let us clarify the concepts at the outset. According to Oxford dictionary (http://oxforddictionaries.com), paradigm means 'a pattern or a model'; paranoia means 'exaggerated self-importance'; mission means 'the vocation or calling' and drift means to 'be carried away.' Microfinance means finance in micro/ small amounts to the poor for meeting their consumption desperations arising from income uncertainties and for enabling them to undertake productive activities. Microfinance Institutions (MFIs) refer to the institutions specialising in providing microfinance. Their origin is traced to Professor Yunus' Grameen Bank. In this article, we shall be using these concepts with reference to the crisis that broke in microfinance industry in India. The paradigm in question is the belief that free,

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unregulated markets are the panacea for the world's problems, including poverty. The paradigm in the economist's jargon is referred to as the paradigm of neoliberal economics. The *mission drift* (CSFI, 2011) is the Micro Finance Institutions (MFIs) getting carried away from their mission of serving the poor by the desire to be profitable.

The question that the present article explores is whether the microfinance crisis in India is a manifestation of the mission drift of an industry or the exaggerated importance accorded to the paradigm of free and unregulated markets. The question, in research hierarchy (Cooper and Emory, 1995) is embedded in the problem of poverty in India. It is a long pending, current, and, unfortunately continuing problem of world's 2.5 billion desperately poor people living on less than $2 a day (Chen and Ravallion, 2008) as per the international poverty line.

The paper is organised in six parts. In the ensuing section, a brief account of the microfinance crisis in India is provided. An attempt is made to highlight the issues leading up to the crisis with the help of a case study of Swayam Krishi Sangathan (SKS) finance in Section II. In Section IV, the larger issues pertaining to the market paradigm are addressed. It is followed by a brief discussion of more recent instances of Sahara group and Shradha group. Section VI contains the concluding observations.

2. The Crisis

The Oxford dictionary (http://oxforddictionaries.com) defines a crisis as 'a time of intense difficulty, trouble or danger' and traces its origin to the Latin usage in medicine implying a turning point in the disease/malaise, a stage necessitating drastic actions. Crises seem to erupt suddenly, albeit these brew up slowly. These might remain latent for long, until an event or a series of events trigger its manifestation

The 2010 crisis of microfinance industry in India was triggered by the passing of legislation in the assembly of Andhra Pradesh, which is incidentally is also regarded as the cradle of microfinance industry in this country. The said legislation effectively resulted into the shutting down of all private sector MFIs operating in the state. The prequel to the state action was suicides by the borrowers of the MFIs in the wake of pressure built by them (the MFIs) on the borrowers for debt servicing. Chakrabarti and Ravi (2011) referred to the crisis as 'a moment of reckoning'. Arunachalam (2011) called it 'India's subprime'. The western private equity industry referred to it as "the most severe crisis in the 25-year history of microfinance industry in India" resulting into the denial to "millions of India's poorest

citizens' access to basic financial services" and "jeopardizing the Indian government's broader financial inclusion agenda" (Legatum Ventures, 2011). State of the Microcredit Summit Campaign Report 2012 finds that the world microfinance industry was shaken by the developments in India (Maes and Reed, 2012). Priydarshee and Ghalib (2011) observed that in view of the singular focus of private sector MFIs on maximizing their profits in an inefficiently regulated environment, it may not be possible to prevent the recurrence of similar crises in future.

The crisis of 2010 was preceded by the crisis of 2005 in the same state when the District Authority closed down 50 branches of two major MFIs following accusations of usurious interest rates and forceful loan recovery practices (Shylendra, 2006). The state government and the microfinance industry agreed to the modifications including a better code of conduct when dealing with borrowers (Sane and Thomas, 2012).

Whereas the crisis of 2005 was confined to just Krishna district of Andhra Pradesh, the crisis of 2010 rocked the nation and raised serious concerns about the efficacy of the microfinance institutions, especially those driven by profit motive, in alleviating poverty. The alleged neoliberal justification of pursuit of personal / corporate greed in the name of self-interest was perceived to be an obstacle in assuaging the poor's needs. The point is amplified with the help of the case study of SKS that was set up as a non-government (welfare) organization (NGO) but was later turned into a 'for profit' company.

3. Mission Drift at SKS

Professor Yunus' acolyte, Vikram Akula, founded his own microcredit organisation, Swayam Krishi Sangham, which stands for "self-help society" as a NGO in 1997. The company was incorporated as SKS Microfinance Private Limited under the Indian Companies Act, 1956 on September 22, 2003. In 2005, SKS Registered with RBI as a "for profit" Non Banking Finance Company. Akula began chasing private investment to achieve the massive scale required to dent global poverty.

In October 2008, Boston-based Sandstone Capital, now SKS' largest investor, made a major investment. It joined US private equity firm Sequoia Capital, on the board of directors. Akula, who had been chief executive in the company's early days, stepped down in December 2008 but stayed on as chairman. The company brought in new top executives from finance and insurance sector. Pursuant to a resolution of its shareholders passed on May 2, 2009, the Company was converted into a public limited company and the word

"private" was deleted from its name.

On December 1, 2009, SKS launched a massive sales drive. The "Incentives Galore" programme ran through February 2010, just one month before the company filed its IPO prospectus. In a month, SKS could add 400,000 borrowers and 100 branches, and train more than 1,000 new loan officers. SKS had 6.8 million borrowers in nearly 100,000 villages and had disbursed ₹15,680 crore in loans. SKS clearly was not only India's largest microlender but also the fastest growing microfinance company in the world.

In July 2010, SKS went public. Its IPO of ₹1,715 crore was oversubscribed by nearly 14 times. Its stock surged more than 10 per cent on its first day. The existing shareholders netted handsome profits at a share price that was four times greater than the book value! In celebration, the company handed out 21,000 watches to employees. It was a feast for everyone! Was it? (Saxena, 2012)

Later in the year more than 200 poor, debt-ridden residents of Andhra Pradesh killed themselves due to the pressure from the lenders. A mob of 150 people surrounded SKS' Hyderabad headquarters, protesting the suicide of a borrower's husband. In the same month, the state government passed Andhra Pradesh Microfinance Institutions (Regulation of Money Lending) Act, 2010 (the "AP Act"), effectively shutting down all profit driven microfinance institutions operating in the state. Incidentally, the state of Andhra Pradesh accounts for nearly 40 per cent of all microfinance activity in India. Hyderabad, the home of by far the largest number of microfinance giants, is virtually the capital of microfinance in India. Till a few months ago, the state wore this distinction as a badge of honour. And, now the same distinction became a burden too heavy to carry.

Around the same time hell broke loose, Akula began circulating a plan to spend ₹49 crore to train financial counsellors, who would make sure clients were not getting into too much debt and used their loans productively. But the plan was never adopted.

In fact on July 26, 2011 Akula was due to make a 55-page private presentation at the board meeting on how the pre-IPO push for growth led to a systemic breakdown and farmer's deaths and the desired reforms to restore training and lending discipline. The presentation did not feature in the minutes of the board meeting. On November 23, 2011 Akula resigned from the board of SKS.

Could the case of SKS be regarded as a stray incident of misdirected / poorly governed company that in its attempt to appear good to the stock market went overboard for enlisting

clients and disbursing loans? Or is it that the ethos of marketization inherently fraught with these possibilities? While we address to the ethos of marketization and neoliberal economics in the ensuing section, it would be useful to capture the mission and the drift there from the perspective of the industry. In India, for example it is worth examining as to why more than two-third of India's microfinance industry is concentrated in the Southern region, which incidentally does not have any desperately poor state[3]. If the objective of microfinance is poverty alleviation then their concentration should correspond to the concentration of poor. Should we label their relative absence from the poor states as an instance of mission drift or the manifestation of the fallouts of paradigm paranoia by taking a position 'for' or 'against' neoliberalism? After all, a firm or two could drift from their respective missions, could we say the same about the industry as a whole?

While speaking to Time Magazine after the famed Nobel Prize for "efforts to create economic and social development from below (www.nobelprize.org)" in 2006, Professor Yunus stated the mission of microfinance industry as "creating a poverty museum by 2030". However, CSFI (2011) captured the worldwide predicament of the industry in these words:

"A lot of people - well-meaning, thoughtful people who are in the microfinance industry - are now worried that microfinance has taken a wrong turn that it has drifted away from its original mission that had been co-opted (or even corrupted) by the pursuit of size and profitability.... This is new and...it leaves microfinance and individual MFIs at a 'tipping point'".

What implications this predicament has for the paradigm, this is what we turn our attention to.

4. Paradigm Lost?

It is but the restatement of the primer in economics that the fundamental economic problem/s may be resolved either by the invisible hand of the markets or the visible hand of the state or by a combination of these. Post World War-II, the world, in terms of economic ideology, could be easily divided into either following the ideology of free-markets ('capitalism' in common parlance) or following state planning ('socialism' in common parlance). Since 1980s, one has seen embracing of the free-market ethos in the transition

[3]According to Oxford Poverty and Human Development Initiative (OPHI, 2011) there were 421 million poor living under MPI in eight Indian states of Bihar, Chhattisgarh, Jharkhand, Madhya Pradesh, Orissa, Rajasthan, Uttar Pradesh and West Bengal. This number is higher than 410 million poor living in the 26 poorest African states. That is why these states are referred to as desperately poor states.

economies of Eastern Europe and by many developing economies in Asia and Africa. While it would be beyond the scope of the paper to discuss the circumstances in which the said shift started taking place, for the sake of simplicity we would refer to the contours of this shift collectively as 'neoliberalism.'

Though there is no point in making definitions simpler than the subject matter these pertain to, yet we define neo-liberalism as an ideology based on the advocacy of economic liberalizations, free trade, and open markets. To put it even straighter, neoliberalism is captured in the catchall, popular phrase of liberalisation, privatisation and globalisation (or LPG). Within neoliberal paradigm, the role of government is sought to be constrained or it is urged to get out of the way. It is about re-orienting the existing government institutions to promote the role of the market or creating such new institutions that will facilitate private investment (Mathur, 2013). We will be examining here under the emergence of market led, commercially inclined microfinance industry and its predicaments in the context of the neoliberal paradigm.

It may be noted that the need for credit for poor has been there for long and so have been the measures to fulfil these needs. In fact, historically, for many years, bankers and senior government officers were fond of describing the Government of India's main poverty alleviation programme, the Integrated Rural Development Programme (IRDP), as "the world's largest microfinance programme". And so it was. It involved the commercial banks in giving loans of less than ₹15,000 to poor people and, in nearly 20 years, resulted in financial assistance of around ₹250 billion to roughly 55 million families. The problem with IRDP was that its design incorporated a substantial element of subsidy (25-50) per cent of each family's project cost and this resulted in extensive malpractices and misutilisation of funds. This situation led bankers too to see the IRDP loan as a politically motivated handout and they largely failed to follow up with borrowers. The net result was that estimates of the repayment rates in IRDP ranged from 25-33 per cent only. Not surprisingly, the two decades of IRDP experience – in the 1980s and 1990s – affected the credibility of micro-borrowers in the view of bankers and, ultimately, hindered access of the usually less-literate poor to banking services.

Similarly, the entire network of primary cooperatives in the country and the regional rural banks (RRBs henceforth) both sets of institutions established to meet the needs of the rural sector in general and the poor, in particular - has proved a colossal failure. Saddled with the burden of directed credit and a restrictive interest-rate regime, the financial position of

the RRBs deteriorated quickly while the cooperatives suffered from the malaise of mismanagement, privileged leadership and corruption born of excessive state patronage and protection. While banks have been linking up with Self- Help Groups (SHG) since the onset of the SHG-bank linkage scheme in 1992, the Block Development Office (BDO), the District Rural Development Authority (DRDA) and the Panchayats have entered the arena of microcredit only after the introduction of the Swarna Jayanthi Grama Swarozgar Yojana (SGSY) scheme from April 1999. Literature on the earlier experience with the Integrated Rural Development Programme (IRDP) shows that these institutions have functioned primarily as patriarchal, corrupt, anti-poor bureaucracies (Dreze, 1990; Kabeer and Murthy, 1996; Mayoux, 1989).

If the State fails, resort to markets is perhaps the simplest explanation for the emergence and subsequent dominance of the neoliberal paradigm of economic development. In sync and perhaps spearheading what in popular parlance are referred to as "economic reforms" since 1980s, Adams (1998) points out that there has been a paradigm shift in financial policy from state-led subsidized credit to market-led financial systems development. The old paradigm was based on state-owned, sector-directed, supply-led and subsidized credit while the new paradigm, instead, emphasizes liberalization of markets as a means of financial development and thereby, economic development. Within the broad framework of this paradigm, economic researchers and management scholars began to explore the opportunities for market-based solutions to the challenges of development, particularly those pertaining to positive social impact (Battilana and Dorado, 2010; Bruton, 2010; Bruton, Khavul, and Chavez, 2011; London and Hart, 2004, 2010; Mair and Marti, 2009; Mair, Marti, and Vantresca, 2012; Ricart et al., 2004; Prahalad, 2005; Seelos and Mair, 2007).

Pablo (2007) sees an agenda in the popularisation of such participative concepts as inclusive growth, inclusive finance, sustainable development, participative development microcredit, etc. in order to mask the starker reality of growing poverty, inequality and helplessness in the neoliberal period (starting 1980s). The other linguistic innovations such as "inclusive capitalism" (Prahalad, 2005), "compassionate capitalism" (Benioff and Southwick, 2004), "virtuous capitalism" (Fikirkoca, 2007), "social capitalism" (Fast Company, 2008) and all encompassing "enlightened capitalism" may be seen in the same vein. Schwittay (2011) argues that qualifying capitalism with adjectives that endow it with humane qualities by itself is conceding that the system has some inherent problems, and, if left to its own devices, does serve those who can afford/ take advantage of its wares at the

expense of those who cannot.

We would like to posit that to and fro movement from the paradigm of the state to the paradigm of market and vice-versa represents only a part and not the whole of Hegel's dialectical formulation. It represents thesis-and-antithesis but no synthesis. In research, it is even more critical to steer clear of the isms, clichés and preconceived notions of agenda.

5. Other Recent Instances

Even if SKS fiasco were to be delinked from the larger issue of the outreach of microfinance institutions and financial inclusion generally, the frequency with which episodes of victimisation of common people in their capacities as small savers/investors etc. have occurred does compel one to sit back and reflect upon the tyranny of markets. Investors' plight due to Dotcom bubble, plantation companies, preceded by securities market scam etc. makes one wonder if all is well with the markets. And, the story continues even after SKS 2010. Two prominent instances are happenings at Sahara (2010) and Saradha (2013).

In 2010, two Sahara companies Sahara India Real Estate Corporation (SIREC) and Sahara Housing Investment Corporation Limited (SHICL) came under the scanner of the Securities and Exchange Board of India (SEBI) for the sale of bonds worth approximately ₹25, 000 crore to over 2 crore investors, who as claimed by Sahara were mostly from villages and small towns of India. Sahara christened it as private placement whereas SEBI held that it was a public issue. It may be noted that private placement is a legitimate route, but is applicable only when securities are offered to not more than 50 persons, who should be associates, friends, relatives, employees and others who are within the close circle of promoters or top management. Further, the offer must be restricted to those to whom the offer is being made. Implicit in that description is the fact that amounts of money so mobilised cannot be very large. Thus, SEBI considered it preposterous for the Sahara companies to call their massive mobilisation from over 2 crore investors, employing 10 lakh agents, as private placement and restrained those two companies from raising further funds. Sahara got stay on SEBI's order from Allahabad High Court. SEBI moved the Supreme Court. The Supreme Court ruled against Sahara, ordering that the money be handed to SEBI by February 2013, so that SEBI, in turn, can refund the money to the investors. The story does not end here. Sahara sent in 127-truck load of documents to SEBI suggesting that it has already refunded the money to the investors. But as confirmed by some independent agencies, sample of the names and addresses of Sahara investors submitted to SEBI do not

appear genuine. The point is even if such a finding were an exception, the possibility of non-existent depositors cannot be ruled out. The absence of genuine depositors raises serious concerns about the possibility of some kind of money laundering and about the claim of financial inclusion via offering debentures to small investors "mostly from villages and small towns of India". MFIs' mission drift and the drift of Sahara companies away from the self-proclaimed financial inclusion appear as mutually confirming instances of how rules of the game may be made subservient to personal interests/greed.

The happenings at Saradha, one of the largest Chit Fund companies with diverse business interests in Eastern India, represent yet another case where market-based solutions to the problem of alleged failure of state have even more deleterious impact. It may be noted that a chit fund is a corpus of fund raised from small, periodic (monthly) contributions of a group of persons. The amount so collected is lent to the member who bids the highest discount. The scheme is apparently attractive to the depositors and the borrowers alike for the amount of discount is distributed amongst the chit members and it is perceived by the borrower to be less than the interest charged by and the transaction costs associated with formal arrangements. When this local level activity is scaled up into a collective investment scheme to a commercial scale involving employment of agents, sub-agents and the resultant chain huge resources can be mobilized that in the absence of adequate governance and regulation can subject the investors lured by promise of high returns to a huge peril. This is what exactly happened in case of Saradha chit fund scam involving more than ₹30,000 crores. On April 23, 2013, SEBI directed the company to wind up its collective investment schemes and refund the money due to investors within three months from the date of the order. Enforcement Directorate registered a case under money laundering act against Shradha Realty India and the Income Tax Department had initiated an investigation into Shradha group's activities for violation of the Income Tax Act, 1961.

6. Concluding Observations

Neoliberal paradigm gained wider acceptance because of the state failure in providing services to all its citizens. However, the case of SKS and recent instances of Sahara Group and Shradha Group are indicative of the perils of market-based solutions without requisite governance. Markets tend to serve those who wield greater economic power. Thus, the problem of coordination and control over the conduct of the economic agents is not merely a matter of asymmetric information leading to adverse selection and moral hazard, but also asymmetric power that allows some to define and bend the rules to their advantage to the

peril of others. In the case of SKS, pre-IPO scaling up of lending operations represents an attempt to create and thrive upon asymmetric information; in the case of Sahara, it is manifested through deliberate information overload in the form of truck loads of incomprehensible documents; and, in the case of Shradha, it is about illusion created via distorted incentives. The common theme underlying all the three cases is the inefficiency of the market in seeing through the designs of the greedy agents and the resultant market failure. Weak institutions, be it government or regulators, greed legitimizing norms, worsen the things. Neoliberal paranoia is obviously fraught with severe limitations.

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