Power of Returnable Grant in Emergency for Building Financial Inclusion of Vulnerable Groups

Introduction

Over the period of years, Civil society organisations, Non-banking Financial Corporations, Banks and Government bodies have developed a range of financial instruments with the aim of improving the financial inclusion of the economically vulnerable sections. These have ranged from high-cost loans to unconditional universal cash transfers. Each approach brings its own set of inbuilt advantages, challenges and questions. One instrument that has received lower attention and has not been studied in-depth is the Returnable Grants. It is a financial instrument that provides credit with a high degree of flexibility. Recipients have no legal but only a moral obligation to repay the amount. There is no need for a collateral and provided at zero interest. Additionally, once returned, the funds are circulated in the same community with the same provisions and allows more people to access the benefit of returnable grant in a pay it forward spirit. This article looks at the implementation of a Returnable Grant project by Shram Sarathi, India's first dedicated financial services institution that offers financial services to vulnerable migrant workers and their households, and the lessons it holds for the larger financial inclusion ecosystem.

A survey of 6,600 migrant families in 2021 done by Shram Sarathi revealed two key issues emerging from the pandemic and lockdowns - Erosion of Savings and High Level of Indebtedness. Nearly 75% of the families had some form of savings prior to the lockdown in 2020 but this came down to 38% by the end of the year. These savings were further eroded when the second lockdown was announced in 2021. Families were left with no cushion to meet food, healthcare, sustenance and other basic expenses. This also led to the complete collapse of informal emergency support mechanisms (friends, neighbours, relatives, etc.) that existed in the communities. 32% families had debt beyond their repayment capacity before the pandemic and this number shot up to 52% by the end of 2020. Interest rates moved from 2-3% per month before the pandemic to 5 to 10% per month in 2021. This sharp rise was owing to the increased demand for debt and also the increased perceived risks due to the loss of livelihoods.

Study Design

As a response to this twin crisis and learning from the survey, Shram Sarathi devised a Returnable Grant programme called Sanchay (means 'small deposit' in Hindi) to provide cash relief, finance emergencies, retire expensive debts and bringing existing debts to manageable levels. The programme was implemented in 45 villages surrounding Gogunda and Bhabrana, which are 40 and 100 kilometres respectively from Udaipur. Study of the impact of returnable grants on the recipients' indebtedness, debt management and emergency management mechanisms was done which had 280 families in the treatment group and 101 families in the control group. Baseline and endline surveys were conducted with both the groups and in-depth interviews were conducted with 20 participants.

Each family in the treatment group was given a diary with coupons worth INR 15,000, in denominations of 5,000 (one), 2,000 (four) and 1,000 (two), valid for a period of 24 months. The coupons represented a pre-approved loan that could be availed during an emergency. The emergencies covered in this programme were health emergencies, issues of food security, housing / shelter emergencies (natural disasters) and ability to migrate and earn (conveyance expenses). The coupons assured the families that the funds were designated for them, and it could be redeemed as quickly as possible when the claim was made. The coupons were distributed in September 2021.

Returnable Grant Utilisation and Repayment Rates

50% households redeemed their coupons at least once during the 24 months' period. This utilisation rate reflects that the worse of the lockdowns were over by September 2021 and additionally, this was an option to be exercised only during the defined emergencies. Only 9.6% of the 280 families made more than one claim. 34% of the households claimed coupons below INR 5,000; 43% between 5,000 to 10,000 and 23% between INR 10,000 to INR 15,000. This gives us confidence that the size of the instrument was right for the emergency needs of the targeted group. In terms of the purposes for availing the returnable grant - 78% families utilised it for medical emergencies, 17% for credit improvement, 3% for Migration and 2% for other emergencies.

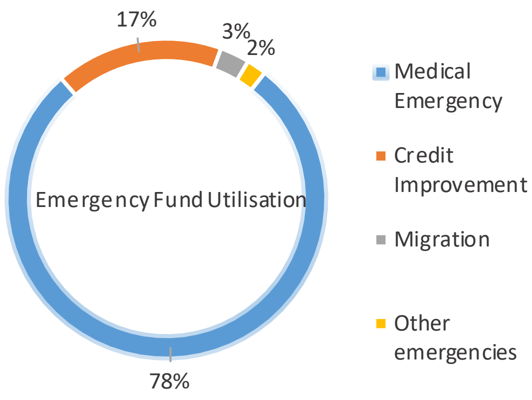

Figure 1: distribution of emergency fund utilisation

Even families covered under public insurance programmes, incur a high amount of out-of-pocket expenses in terms of travel to the city hospitals, food, accommodation for relatives and loss of income in case of daily wage earners.

93% of the households repaid either on time or before time. Even when repayment is due, our general experience has been that families are recovering from emergent financial needs but have high interest / intent to repay. As per a UBS report, default rates for unsecured loans from Indian banks was 23% in FY23[i]. 93% repayment is impressive considering the fact that there was no legal obligation for the households to pay the amount back. We believe households were driven, among other factors, by the need to maintain a good credit relationship with Shram Sarathi.

Key Findings of the Study

The average quantum of household debt for the treatment group at the endline stage (INR 42,459) had reduced by 7.5% compared to the baseline stage whereas the corresponding figure for the control group was 4%. Availability of returnable grants seems to have helped the treatment group reduce their average debt at rates almost double of the control group. The lack of interest on the returnable grant was seen as a contributing factor to reduce the overall debt quantum as households spend a proportion of their household income on debt servicing.

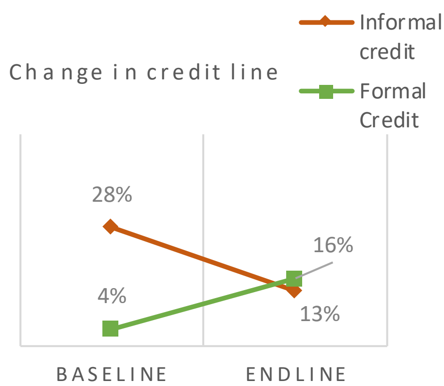

Figure 2: Change in credit line between baseline and endline of the treatment group

The treatment group's reliance on informal credit from friends, family & relatives reduced by 28% at the baseline to 13% during endline. Correspondingly, their reliance on formal credit went up from below 4% at baseline to 16% at endline.

The control group moved in the other direction with reduced dependence on formal credit and increase dependence on informal credit during the period. Informal credit often times tend to have a higher interest rate than formal credit – going up to 5 to 10% per month. The loss of livelihood and the resulting inability to repay existing loans affected the CIBIL score of many vulnerable migrant households and some of them got permanently pushed out of the formal credit system increasing their dependence on high-cost informal loans. Availability of returnable grants helped the treatment group members retire costly debts, manage emergencies and maintain viable relationship in the formal credit space.

At baseline, 3% of the treatment group and 4% of the control group answered that they would want to Reduce Debt as a means of improving the financial circumstances of the households. The survey was conducted during the pandemic and one can assume that migrant households had bigger preoccupations than reducing debt at that time. This number increased to 18% for the treatment group and 39% for the control group at the endline. The control group, without a returnable grant cushion, was experiencing the burden of debt more severely. This also shows that the treatment group had a more positive experience with debt management. This is important given the critical role that household debt plays in the financial viability and progress of poor migrant workers' households.

The study shows a number of positive outcomes for the treatment group that received the returnable grants. The returnable grant allowed the treatment group to not slide into high interest informal indebtedness. These households showed greater progress in reducing the overall quantum of their household debt, moving from informal to formal credit sources and being more comfortable with household debt and harnessing it for their financial goals.

Conclusion and Way Forward

Migrant households and other economically vulnerable groups do not have the safety net or the savings to meet emergency expenses, hence the need to borrow funds and borrow quickly enough to manage the emergency and smoothen their consumptions. The current formal credit markets, where available, are not oriented to serve the emergency needs of these groups. Commercial credit is supply driven rather than demand driven i.e. they are available only when credit providers approach households rather than when households have an emergency. This pushes the vulnerable groups towards unreasonable loans with high interest rates and unfair repayment conditions. The monthly interest rates on loans available from moneylenders can vary between 2 to 5% depending on the familiarity / unfamiliarity between the parties in the credit relationship. The monthly interest rates for loans from friends, families and completely unfamiliar moneylenders could go as high as 10%. The returnable grant works as a crucial safety net for poor households. An emergency can be better managed and tided over with the option of a returnable grant, which works as a pre-approved loan. The returnable grant enables people opportunities to employ three distinct strategies - exit informal marketplace, reduce overall credit amount from informal marketplace and better manage relationships with informal marketplaces.

Shram Sarathi processes the demand amount digitally in 24-48 hours, there is no other program in the country with this precedent. A zero-interest returnable grant with no legal (but only a moral) obligation to repay is a great catalyst for improved livelihood options for vulnerable households.

It goes without saying that organisations like Shram Sarathi cannot implement a blended finance product like returnable grants with money borrowed from the market. Returnable grants programme sits between financial capital investment and philanthropy, in spaces occupied by neither. Returnable grants are CSR and FCRA complaint and hence grant organisations, impact investors and philanthropic capital should consider it as an appropriate intervention medium[ii]. We need more engagement from philanthropy organisations to understand and support unique financial instruments that can become revolving community resources.

i https://www.business-standard.com/industry/banking/indian-banks-are-facing-a-higher-risk-of-defaults-from-unsecured-loans-ubs-123101300914_1.html

ii https://idronline.org/article/philanthropy-csr/returnable-grants-securing-the-financially-vulnerable/

Shram Sarathi is a specialized financial institution providing financial services, counselling and guidance to migration dependent workers and households. Through a range of innovative products Shram Sarathi offers credit, emergency financing, financial literacy, financial fraud protection and advisory services to migrant workers and their families.