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LINKING FORMAL AND INFORMAL FINANCIAL INSTITUTIONS: AN ACTION PROGRAM IN ASIA AND THE PACIFIC - WITH A CASE STUDY OF INDONESIA -

by

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October 1989

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ABSTRACT and SUMMARY

LINKING FORMAL AND INFORMAL FINANCIAL INSTITUTIONS: AN ACTION PROGRAM IN ASIA AND THE PACIFIC - WITH A CASE STUDY OF INDONESIA -

Prof. Dr. Hans Dieter Seibel
and Dr. Uben Parhusip

In the past, programmed credit, subsidies and neglect of savings mobilization have undermined rural finance. This has rendered financial institutions unviable and development unsustainable. In recent years, the number of countries has been growing in which banks mobilize savings and practice commercial banking. But due to excessive transaction costs for both banks and customers, they rarely reach down to the grassroots level. The rural poor therefore have to rely on informal financial institutions, which are viable, selfsustained and adjusted to local conditions. Yet their resources are insufficient for the local microentrepreneurs; they are too weak to reverse the trend of the rural-urban capital flow; and they alone cannot financially support a dynamic development process.

During the early 1980s, a novel approach entered into the debate: linking informal and formal financial institutions. In 1986, APRACA took the step from debate to action. Being an association of central banks and major financial institutions in Asia and the Pacific, it took the lead role on the international level, while its members initiated action on the national level. In the new approach, financial self-help groups act as intermediaries between microentrepreneurs and banks. This reduces transaction costs substantially, for the benefit of both: microentrepreneurs gain access to banks, while banks extend their services to low income groups. The strength of the APRACA initiative lies in the fact that the bottom-up movement of local self-help groups is met by the top-down approach of an association of leading banks.

Subsequently, member countries began to survey self-help groups, elaborated linkage models and prepared projects. Indonesia was the first to implement a pilot project. Bank Indonesia, Bank Rakyat Indonesia and the PVO Bina Swadaya formed a national task force, carried out studies and initiated processes of dialogue and participation among the potential partners, who in turn negotiated institutional linkages and financial terms among themselves. In a favorable policy climate, a project was designed which incorporates the major factors of sustainability, such as reliance on institutional capacity, cooperation between governmental and private voluntary bodies, preexisting grassroots organizations, domestic resource mobilization, market forces, scheme flexibility and sociocultural adjustment. It gives a push to self-supporting market processes between banks and SHGs of microentrepreneurs. In 1989, 30 bankers, 30 PVO staff and 815 SHG staff were trained. From May to September, a first set of some 20 bank units, 10 PVOs and 100 SHGs entered into their initial financial transactions.

Jakarta & Yogyakarta,
4 October 1989

1. LEAD AGENCY ROLES IN THE DEVELOPMENT OF RURAL FINANCE IN ASIA AND THE PACIFIC

1.1 PROBLEMS IN RURAL FINANCE

In most developing countries, policies of rural financial development have been based on **three fallacies** concerning their target groups: Rural microentrepreneurs are unable to organize themselves; they are too poor to save; and they need cheap credit for their income-generating activites or small enterprises.

Three financial policies resulted from these assumptions: credit-oriented development banks and special programs were set up which ignored savings mobilization; credit was subsidized; generous credit guarantee schemes were set up to cover anticipated losses.

The resulting consequences of these policies did not contribute to the self-sustained growth of rural finance, nor did they sufficiently benefit the rural poor:

(1) Subsidized credit meant that the scope of credit remained severely restricted. There was no built-in growth factor which would have resulted from internal resource mobilization. The amount of credit was directly tied to the amount of subsidies available. Small numbers of relatively large loans went to medium and large enterprises. The masses had no, or little, access to institutional finance.

(2) Banks were not motivated to give their customers a thorough screening and to recover their losses, while borrowers felt little motivation to repay their loans. This resulted in high default rates and in continuous program decapitalization.

(3) Subsidies led to misallocation of production factors.

Around 1980, a **reorientation** set in among rural financial policy makers: mounting international debts, increasing shortages of internal and external credit supplies and a growing dissatisfaction with state nurtured and seemingly ineffective credit programs led to a rethinking, centering around such concepts as self-help, self-reliance, self-sustained growth and institutional viability. In terms of financial systems, this meant in particular an emphasis on savings mobilization as a prime mechanism of internal resource generation. As of then, development assistance was to promote, not to replace, self-help and personal effort.

It was then found that microentrepreneurs in developing countries may be poor; but they are able to save, and they are capable of forming their own self-help organizations. Yet, they usually face a number of **problems:**

(1) Institutional finance is inaccessible to the large majority of microenterprises.

(2) Concessionary financial programs for microenterprises have largely failed. Economically they are not viable; in terms of impact, they reach but a minute proportion of their target group.

(3) There is a wealth of human, organizational and institutional resources. But as long as they are not mobilized and appropriately linked, their potential may remain untapped. Such resources include microenterprises, informal, semiformal and formal financial institutions, private voluntary organizations and governmental agencies and programs.

(4) Conventional approaches to rural microenterprise finance face high transaction costs for both lenders and borrowers. At low interest rates they are unviable for banks; at market rates, they may be unviable for most of the potential borrowers.

(5) Credit programs without a savings component ignore savings as a means of internal resource mobilization; at the same time, they ignore savings habits as a psychological basis for investment and repayment behaviors.

(6) Confined to their own resources and membership and barred from access to banks, most self-help groups of microentrepreneurs have been unable to fully mobilize their potential. Operating outside the formal sector, they have tended to keep a near-stationary economy going and to contribute more to its stabilization than to rapid development.

A core problem of rural finance is that the existing institutional resources are not adequately utilized and that the financial services of the formal sector are therefore not available to the poorer sections of the rural population. **APRACA** and its member institutions are among those who decided that action was to be taken.

1.2 THE APRACA PROGRAM

APRACA (Asian and Pacific Regional Agricultural Credit Association), an association of central banks, rural development banks and rural commercial banks, is one of four Regional Agricultural Credit Associations (RACA) originally promoted by the United Nations Food and Agriculture Organisation (FAO). Established in 1977 with an emphasis on agricultural credit, it subsequently broadened its scope towards rural finance. At a workshop held in May 1986 in Nanjing, China, the member countries adopted a novel program of access to formal financial institutions for the poorer sections of the population. The innovative focus of this program is on:

a financial intermediation system built around self-help groups as grassroots intermediaries between banks and rural microentrepreneurs.

Subsequently several APRACA members carried out surveys in their respective countries. They found that there are **many organizational and institutional resources** with great potential for microenterprise finance and rural development. What stands in the way of the full utilization of these resources is financial market segmentation. There are formal financial markets for the upper 5 to 20 percent of the population. These markets fall under the control of state credit and related financial laws and are supervised by the central bank. They comprise central, commercial, development, savings and secondary banks as well as non-banking institutions. In addition, there is a small but growing semiformal financial market, which comprises governmental and private voluntary organizations, so-called Self-Help Promoting Institutions (SHPI), with their own savings and credit programs. They do not fall under the state's credit law but operate with the approval of the state and its organs. Informal financial markets comprise financial self-help groups, other self-help groups with secondary financial functions and individual financial agents, such as moneylenders, deposit collectors and trade, crop or land related financial arrangements. From a policy viewpoint, financial self-help groups are of particular importance. They are found in most Asian countries and in most culture areas or ethnic groups within them. Their main financial functions usually are accumulation and depositing of savings, granting of loans and, to some extent, rendering of insurance services. They may be found in urban and rural areas, among traders and market-women, farmers and fishermen, craftsmen and small industrialists, wage and salary earners, and among bank employees. Though part of the informal financial sector and lacking legal status, most associations do possess organizational structure. Typically, they are headed by a staff of elected executives; they have written rules and regulations; they keep membership lists and they practice some form of book-keeping. Local social control mechanisms effectively prevent defaulting or fraud, which plague so many formal credit programs.

For more effective financial coverage of the poorer sections of the population, **three different approaches** have been discerned in the APRACA discussions on rural finance:

- **upgrading** financial self-help groups of microenterpreneurs;
- **linking** existing self-help groups and banks;
- adapation of banks to their environment ("**downgrading**").

The participants decided on the **linkage program** as a focal approach which may eventually comprise both upgrading and institutional adaptation measures.

While the member countries are likely to recommend particular models of linkages which reflect the sociocultural and economic situation, the main emphasis is on the initiation of **processes of interaction and dialogue**. These are to result in appropriate national and local activities to promote financial services for microenterprises.

In many countries, discussions have been held, and research has been carried out, on self-help groups and their importance for the development of rural finance. Yet, these discussions held on, or below, national levels have not resulted in national policies. It was only when the discussion moved to the **international level of APRACA** that it gained a new momentum.

Two types of **lead agencies** evolved:

- On the international level: APRACA as an association of central banks and national financial institutions with a rural mandate;

- On the national level: central banks, and some major rural financial institutions, as national policy makers.

Policies were discussed, and procedures worked out, of initiating the process of linking banks and self-help groups within the member countries. This provided the basis for **baseline research and policy discussions on the national level**, the results of which were fed back to the international level. Since 1986, there has been a continuous process of **communication** shifting back and forth between the international level and the respective national levels of the member countries. This dialogue provides the basis for a learning process which allows every country to benefit from the experience of the others. In addition to a variety of conferences, meetings and workshops, two instruments of communication and mutual learning deserve particular attention: one is an **international training program**, another one a new journal, **ASIA PACIFIC RURAL FINANCE**, published by APRACA (Maliwan Mansion, Phra Atit Road, Bangkok 10200).

1.3 GUIDING PRINCIPLES

APRACA members discussed essentials of a sound policy for financial market development. No unequivocal consensus was attained, but several **guiding principles** emerged from the discussion:

(1) Working through existing formal and informal institutions

Existing formal and informal institutions are encouraged to cooperate. In particular, this comprises informal financial self-help groups (SHG), banks and PVOs or other Self-Help Promoting Institutions (SHPI). Program activities will not be geared at the establishment of new institutions; instead, there shall be an emphasis on upgrading existing institutional resources.

(2) Promoting savings mobilization

Financial institutions shall be encouraged to mobilize rural savings in order to strengthen their internal resource base. There are two prerequisites for effective savings mobilization:

- For savers, who demand deposit facilities, savings shall not yield negative real returns (relative to the rate of inflation)

- For financial institutions, which supply deposit facilities, savings mobilization must not be "undermined" by cheap (i.e., subsidized) credit (D. Adams et al.) from the central banks or from donors. Thus, the interest rate on liquidity credits shall equal the cost of mobilizing rural savings.

(3) Promoting credit delivery at market rates

Financial institutions should be encouraged to apply market rates of interest in order to achieve a balance of the supply of, and demand for, credit in rural areas. Financial policy makers should be advised to create the conditions and regulatory framework for the application of market rates.

(4) Linking savings and credit

Credit shall be linked to savings: no credit without savings, no savings without credit! Participating institutions may agree upon a savings-to-credit ratio, reflecting the credit worthiness of the borrower.

(5) Substituting group liability for conventional collateral

It is suggested that no other physical collateral will be requested over and above the savings deposited. For the remaining balance, the SHG will act as a joint liability group.

(6) Ensuring institutional viability

As a basis for their institutional viability, all financial intermediaries involved - SHGs, PVOs and banks - shall cover their costs of intermediation through an adequate interest margin. Over and above costs of funds, intermediation costs include transaction costs, reserves for bad debts and costs of extension services.

(6) Covering the risk from the margin

The risk of defaults shall be borne by the financial intermediaries themselves. External credit guarantees, though sometimes necessary for banks as an inducement to participate in an experimental phase, are seen as contrary to program sustainability and selfreliance.

The first APRACA countries to design pilot projects were Indonesia, Nepal, Philippines and Thailand. In Indonesia, the pilot project started in 1988; Nepal, Philippines and Thailand are expected to follow in 1989/90.

2. LINKING FORMAL AND INFORMAL FINANCIAL INSTITUTIONS: A PILOT PROJECT IN INDONESIA

2.1. BACKGROUND

The Republic of Indonesia surpasses most other developing countries in terms of population size (175 millions in 1988), geographical extension and ethnic or cultural diversity. The number of enterprises exceeds 30 million; more than 90 percent are microenterprises, mostly in the informal sector.

Until 1983, financial markets were tightly regulated. Since then, they have been gradually deregulated. Exchange rates are allowed to fluctuate according to the market. This has led to substantially higher levels of domestic savings mobilization. Interest rate restrictions have been removed; minimum reserve requirements have been lowered to 2 percent; the ban on establishing new banks has been lifted. Indonesia has now the highest interest rates in the region (e.g., time deposit rates from 16 to 24 percent), which has reduced capital flight.

For twenty years, the Government of Indonesia has experimented with financial schemes for small enterprises. Most of its credit programs were subsidized and had no savings component. Banks served mainly as channels for the distribution of government funds. They had little, if any, motivation to mobilize savings, to actively search for borrowers and, equipped with generous credit guarantee schemes, to scrutinize loan applications and enforce repayment. As a result, loan repayment performance was usually poor. Access of the masses of the population in rural areas, and even more so in the urban informal sector, remained severely restricted--with a negative impact on productive investments and income generating activities.

In the new era of financial market deregulation, disenchantment with subsidized programs, with their poor performance and their questionable effectiveness, has been growing, both in government and bank circles. They are now being gradually dismantled in Indonesia. The new **policy** environment encourages banks to embark on vigorous campaigns of **domestic savings mobilization**, to expand **credit delivery at market rates** and to experiment with **innovative approaches** to rural and urban finance.

The present financial market situation in Indonesia bears the marks of both old and new, regulated and free market policies. Financial markets are segmented into formal, informal and semiformal financial markets. Banks are the core institutions of the **formal financial sector**. This sector also includes a number of small second-tier institutions, which are defined as non-banks, such as BKK in central Java, LPD in Bali,LPN in West Sumatra and others, which are supervised by primary banks (in this case regional banks, BPD), as well as registered cooperatives (KUD and others), which fall under the cooperative law. There are numerous **informal financial institutions (IFI)** which operate without legal status and outside state control: money lenders, financial self-help groups (rotating and nonrotating savings and credit associations, unregistered credit unions) and numerous other groups with secondary financial functions. In terms of origin, they may be indigenous, state- or PVO-initiated, with considerable overlaps between these three categories. **Semiformal financial institutions** include PVOs as well as GOs, which act as intermediaries between domestic or foreign donors and informal self-help groups or final individual borrowers. They are extralegal in their financial activities, but so far have obviously enjoyed the tacit tolerance of the state. In addition, one may include officially recognized but unregistered precooperatives in this sector.

There is a wide network of **institutional resources in Indonesia.** There are more than 15,000 bank and nonbank institutions offering financial services. There are a great many self-help groups (SHGs). Their number probably surpasses the one-million mark. They have generated their own funds from various sources and, as IFI, have built up their own savings and credit business. There is a small number of Self-Help Promoting Institutions (SHPI) which, acting as semiformal financial institutions, have made substantial contributions to the development of a selected number of self-help groups in such fields as group formation, personal development, skill training, income-generating activities and finance.

Both informal and semiformal financial institutions share a number of **shortcomings:**

- They are not linked to the banking sector, except, in some cases, with regard to fund depositing or transfer.
- They have no access to the refinancing facilities of the central bank; at best they depend, to a moderate extent, on external donors.
- They are restricted in their savings and credit activities due to shortages of funds.
- They have no access to bank training facilities; consequently they lack financial skill and banking experience.

2.2. OBJECTIVES OF THE LINKAGE PROJECT

Despite substantial contributions made by the extention of the rural banking network and by special credit programs, rural finance has remained inadequate in providing for the growing needs of small enterprises and farmers, particularly among the poorer section of the population. Bureaucratic red-tape, lack of collateral and legal requirements have effectively barred the poorer sections of the rural population from banking services. In addition, there is one **obstacle** which may surpass all others in economic importance: **excessively high transaction costs for both banks and their clients.** Private money lenders have moved in to fill the void, charging interest rates which cover these transaction costs. At these rates, however, most microenterpreneurs find it difficult to use credit for the financing of their business, except in some fast turn-over trading activities.

Indonesia, together with other APRACA member countries, decided to carry out programs **to improve the system of rural finance available to the poorer sections of the rural population.**
The initiative was taken by Bank Indonesia (BI)--the central bank--, together with Bank Rakyat Indonesia (BRI)--the largest commercial bank with a rural mandate--and Bina Swadaya--a prominent PVO. After extensive consultations with APRACA, FAO and GTZ, they jointly formed a national task force, commissioned a study of self-help groups to Gadjah Mada University (Prof. Mubyarto et al.) and worked out a linkage program. This was followed by intensive national consultations with numerous organizations.

In a **pilot project**, a novel approach to the development of rural finance was to be tested,

> **linking existing financial self-help groups as grassroots intermediaries to banks for both savings mobilization and credit delivery,**

thus **minimizing transaction costs** for both banks and final borrowers. The **project purpose** is that,

> **Viable financial services are made available to self-help groups of microentrepreneurs and small farmers.**

2.3 PROJECT OUTPUTS

In order to attain the project purpose, the following **outputs** are to be achieved by the project:

(1) Project organization is set up and works effectively.
(2) Processes of dialogue among participating and related institutions are established.
(3) Institutional linkage models are worked out by the National Task Force.
(4) Financial schemes are worked out by the National Task Force.
(5) Institutional linkage models and financial schemes are adjusted and agreed upon by participating institutions.
(6) Linkages are implemented on the local level.
(7) A training program is established and implemented.
(8) Institutional development of participating institutions is initiated.
(9) Monitoring and evaluation services are provided and are used as a management information system.
(10) Research services are provided.
(11) Preparation for project follow-up is concluded.
(12) Project materials are published.

2.4 DIMENSICNS OF LINKAGES

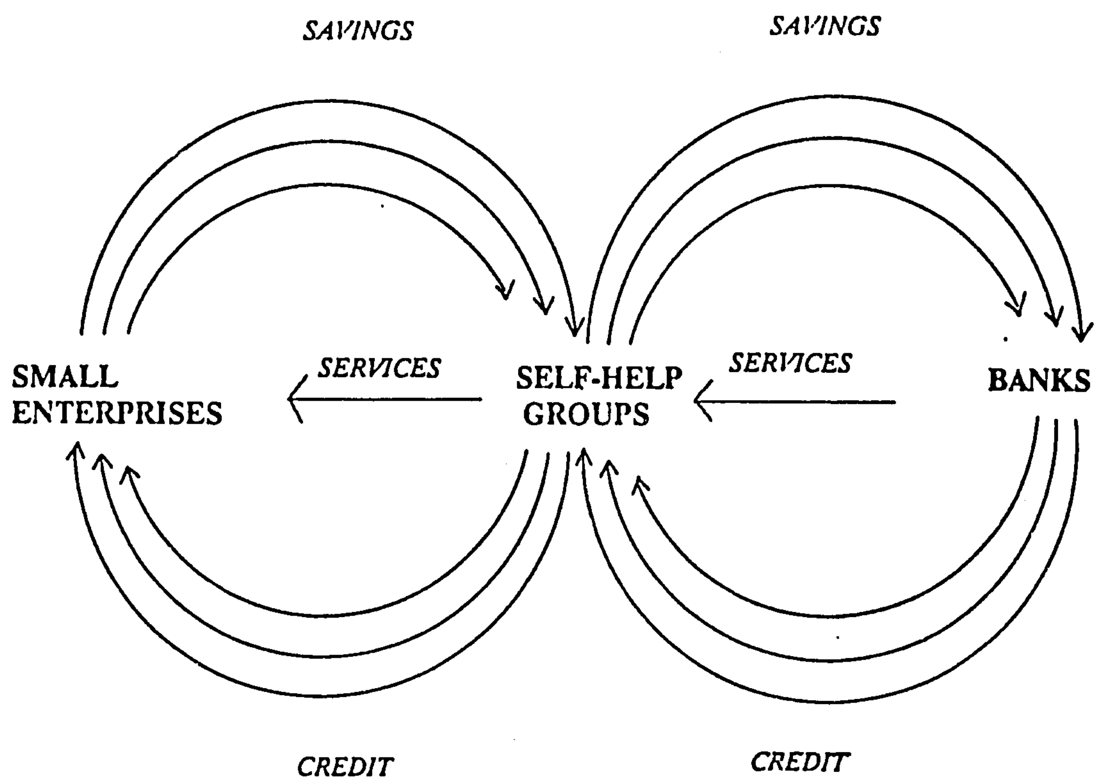
To implement the objective, the project is designed to **participatively initiate linkage processes,** rather than prescribe specific models. Any specific schemes are to be the outcome of participative processes among the respective participants. There are **two principal linkage dimensions:**

- **Institutional linkages between SHGs and banks.** They may either be **indirect,** involving SHPIs/PVOs as financial intermediaries or as consultants, or **direct.** In addition, banks **may link up with the central bank for refinance.** This is a novely in Indonesia, and it is of particular interest to small rural banks which are short of funds and far from sources of refinance.

- **Financial linkages between savings and credit.** In fixed ratios, the amount of credit is contingent upon the amount of savings. In dynamic ratios, the amount of credit increases with the number of successful repayment cycles--to ensure a gradual growth of the balance between credit and the borrowers' capacity to save, invest and repay.

On principle, these linkages are to be **self-sustained.** Therefore interest rates on savings and credit are market rates, and an adequate interest margin provides the basis for the institutional viability of each intermediary: bank, SHPI/PVO and SHG.

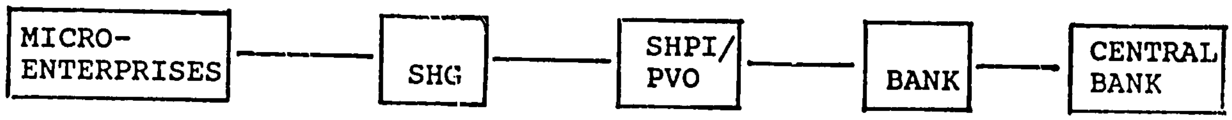
Exhibit 2.1: Institutional and financial linkages



Institutional linkages between banks and SHGs may proceed in an **evolutionary sequence**of three steps, from indirect linkages to direct linkages, with the ultimate step of making the individual microentrepreneur bankable and giving him direct access:

Exhibit 2.2: Evolutionary stages of institutional linkages

Stage I: Indirect linkage model



Stage II: Direct linkage model

Stage III: Direct access model

Between these stages, there may be intermediate steps, with SHPI or SHG, respectively, in a consultative role. In addition, SHPI and various other agencies may supply supplementary technical and extension services.

2.5 Financial Scheme

Interest rates are worked out locally by the participating institutions. The project issues guidelines and recommendations which the participants are free to modify according to local conditions. Some major **recommendations** are:

- SHGs use part of their funds for internal lending, another part for depositing in a bank as a basis of refinance from the bank
- Savings first: no credit without savings
- Savings as partial collateral
- Bank loans are group credit, to be onlent to members
- Interest rates on savings and credit are market rates, taking into consideration reductions in bank transaction costs due to intermediary services of thirds
- Joint liability as a substitute for physical collateral (on the balance not covered by the savings deposited)
- Ratio between savings and credit contingent upon credit worthi-

ness, primarily of the group and secondarily of the microenterprises, increasing over time with good repayment performance
- Credit decisions for onlending to members by the group
- Short-term credit up to 18 months
- All intermediaries (central bank, banks, SHPI/PVOs, SHGs) are alloted an interest margin to cover their costs
- Instead of penalties for arrears, banks may impose an extra incentive charge to be refunded in case of timely repayment
- SHGs may levy an extra charge on the interest rate for internal fund generation (= self-imposed forced savings)
- Central bank refinance at an interest rate equal to the costs of mobilizing savings

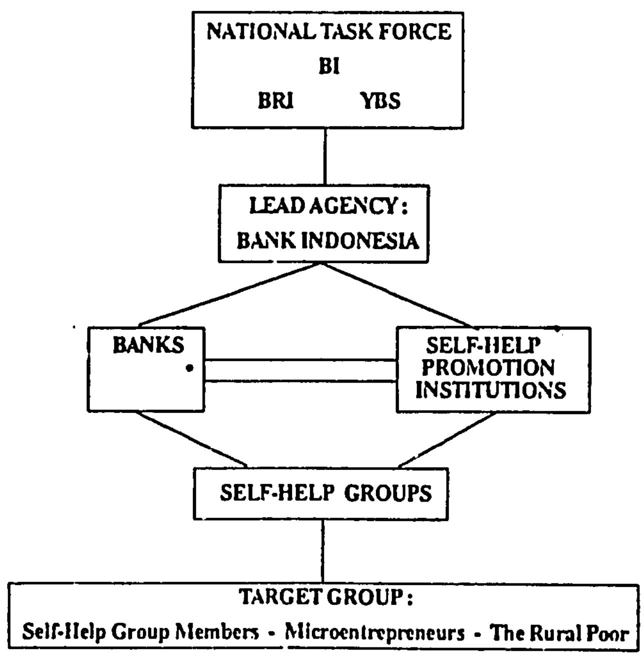
The main **components of the interest rate** are:

- Cost of funds
- Gross margin to bank (incl. transaction costs, reserve for bad debts, profit)
- Gross margin to SHPI/PVO (for financial intermediation and/or supporting services)
- Gross margin/incentive payment to SHG

2.6 PROJECT ORGANIZATION

Bank Indonesia, the central bank, is the project holder and lead agency. Together with BRI and Bina Swadaya, it forms a National Task Force, which has initiated the project, functions as a policy making body for the project and supervises its implementation. Bank Indonesia works directly with two types of participating institutions, banks and SHPI/PVOs, and promotes linkages between banks and SHGs. These linkages may be either direct, or they may be indirect through SHPI/PVOs as intermediaries. At the grassroots level, self-help groups act as intermediaries between their members and banks or SHPI/PVOs, respectively. (Exhibit 2.3)

EXHIBIT 2.3:
Project design



At national level, there are two different functional units:
- a policy making unit in Jakarta; and
- a project implementation and coordination unit in Yogyakarta.

On the national policy making level in Jakarta, a National Task Force (NTF) and a Technical Team (TT) as its instrumental arm have been established. They comprise members from BI, BRI and BS. The general manager of the Department of Cooperative and Small Credit, BI, is the head of the NTF and the general manager of the project. He reports directly to the Board of Directors of BI, which is the ultimate policy making body and has overall responsibility for the project.

A national **project implementation and coordination center** has been set up in Yogyakarta, where the project has been established as an organizational unit of BI (PPHBK). This places the project into the organizational structure of Bank Indonesia and provides the structural basis for its sustainability.

Project implementation is managed by a National Coordinator and his deputy in Yogyakarta. They are assisted by four professional coordinators: a bank, PVO, Training and Monitoring & Research Coordinator. There is an advisory team, comprising Indonesian and German experts.

Technical assistance is given by the Federal Republic of Germany through its technical cooperation agency GTZ.

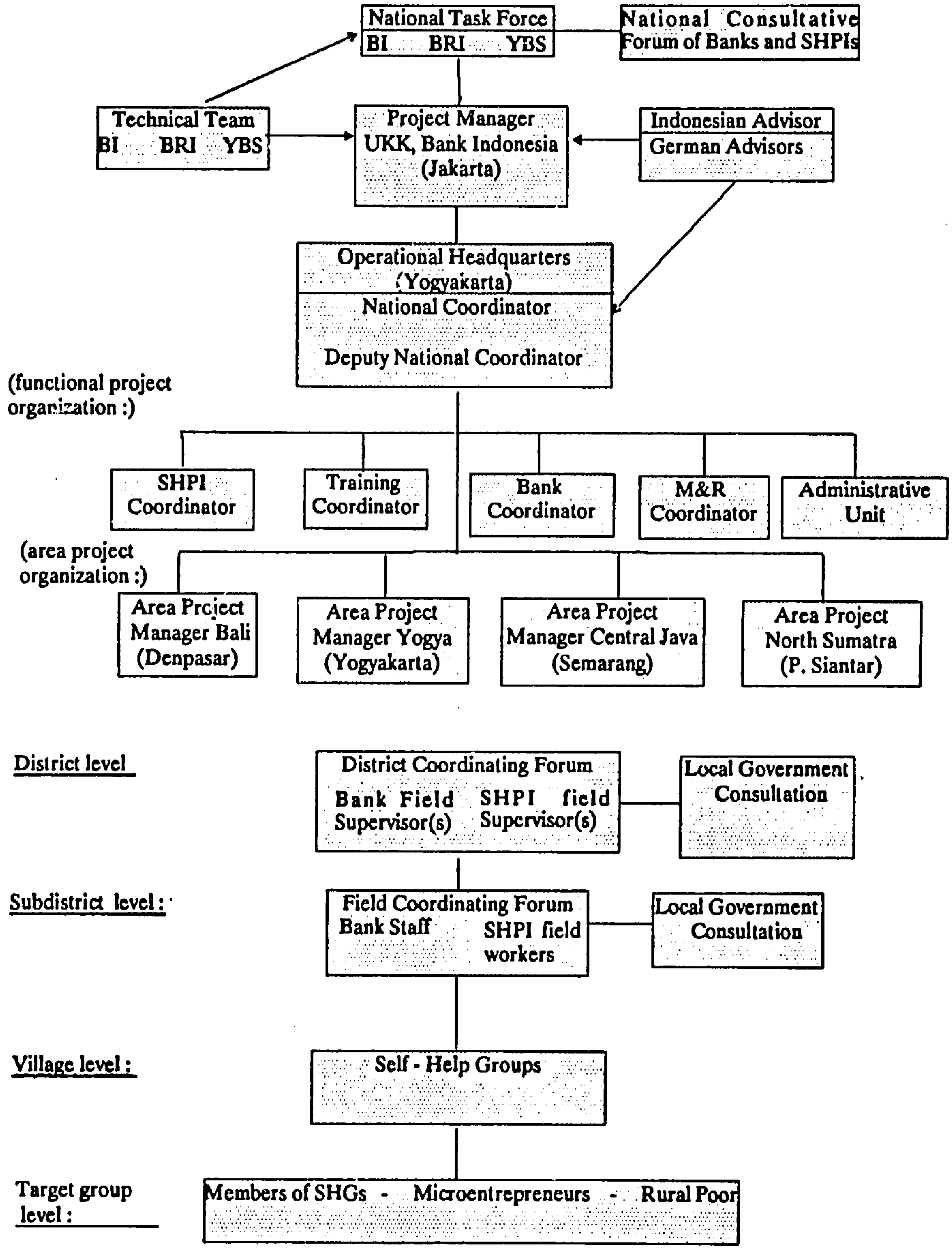
The project comprises **four areas**, D. I. Yogyakarta, Central Java, North Sumatra and Bali, with a total of thirteen districts (kabupaten) (MAP 1). They are managed by Regional Project Managers (RPM) in the respective Bank Indonesia branches and PVO & Training coordinators.

Within each district (kabupaten), there may be one or several participating SHPI/PVOs and one or several participating banks or bank branches, plus additional village or subdistrict bank units. Each participating SHPI/PVO appoints a supervisor. He supervises field workers who in turn work with SHGs. Similarly, each partiticipating bank appoints a supervisor in charge of project activities.

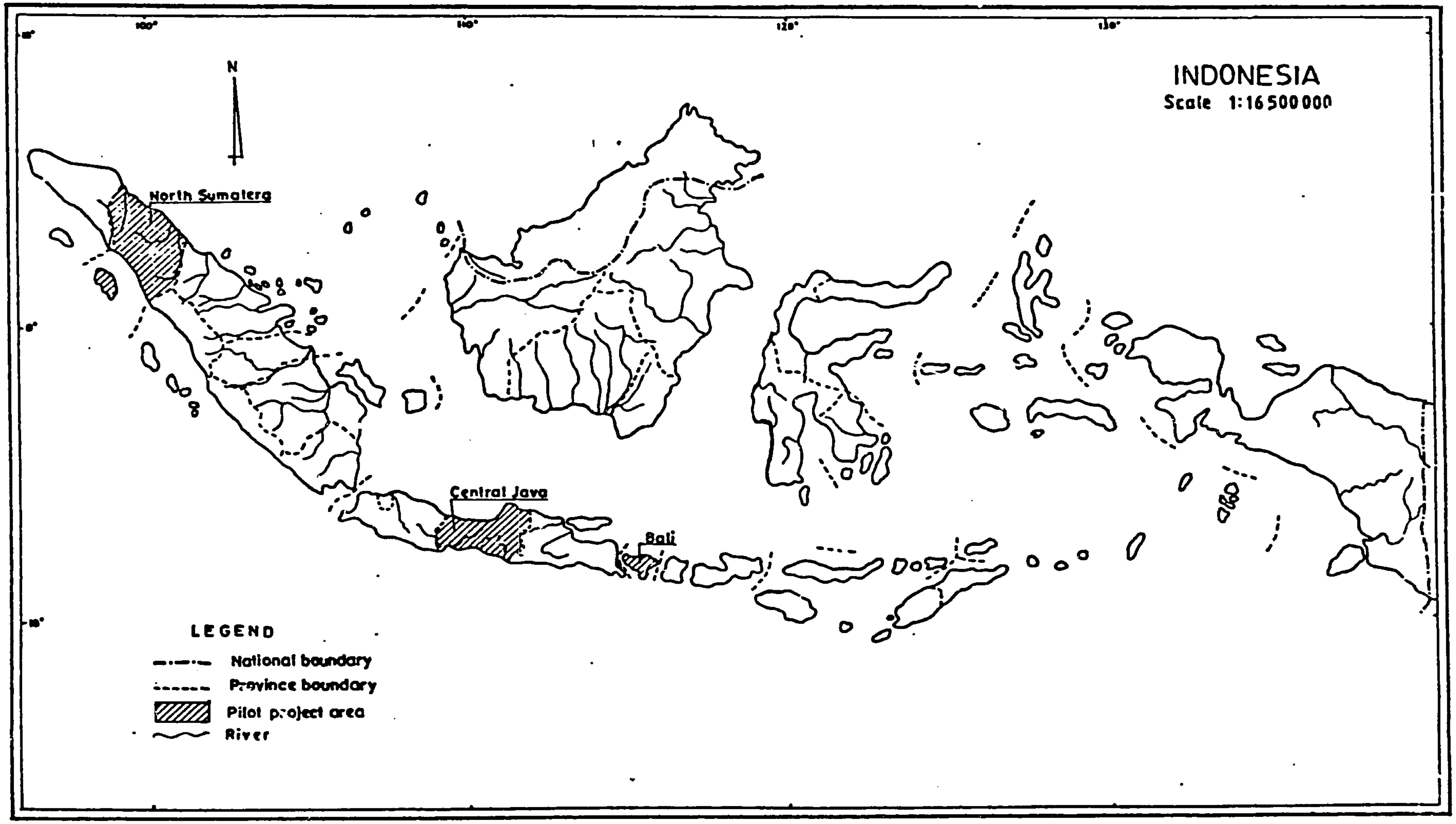
At district level, the SHPI/PVO supervisor(s) and the bank supervisor(s) work closely together and jointly form a district forum. It is the task of the forum to coordinate implementation activities at the field level. Chairmanship is determined by mutual consent.

Both in structural and functional respects, the project is founded on the **autonomy of existing groups** and institutions. The project strengthens participating institutions in functional respects by contributing to their institutional development and to the professionalism of their staff.

EXHIBIT 2.4: Project organization



MAP 1: Pilot project areas in Indonesia



2.7 PROJECT IMPLEMENTATION AND PROGRESS

During a first project phase, it is expected that approximately 420 SHGs may participate in the project: 250 in Java, 150 in Bali and 20 in Nordsumatera.

There are 13 participating banks with a total of more than 50 bank units involved, among them BRI with 4 regional offices, 13 branches and appr. 30 village units; 3 regional banks, Bank Pemerintah Daerah (BPD) in Yogyakarta, Semarang and Denpasar, each with several branches; 9 unit banks, among them village (bank desa) and market banks (bank pasar).

There are 12 SHPI/PVO involved in the project who altogether work with approximately 1500 SHG.

Under the project, the first financial transaction between a SHG and a bank took place in May, 1989. The linkage process is expected to gain momentum by the end of 1989, after an initial experimentation phase of approximately six months.

2.8 FACTORS OF SUSTAINABILITY

Sustainability can only be tested after completion of a project. Yet, no project can have a chance of sustained impact if the relevant **factors of sustainability** are not **built into** the project.

(1) Institutional capacity
The project is founded on the autonomy of existing organizations. In Bank Indonesia, it has a highly professionalized project holder with an immaculate reputation and a legitimate responsibility for the development of the financial system. The project is part of the line structure of Bank Indonesia and the participating banks. For its success, it does not depend on charismatic leaders. Routine personnel rotation is used as a means of providing training on the job to future project managers.

The project does not work through public administration bureaucracies. Its partners are institutions which work in the private economy. In banks, PVOs and SHGs, it builds on existing personnel and activities; it does not provide incentives to lure institutions into donor programs. Through its institutional development and associated human resource development components, it contributes to the planning and financial management capacity of participating institutions.

(2) Motivation
To all participating institutions--banks, PVOs, SHGs--, the linkages are expected to be profitable. This provides the basic motive for sustainability. They all have carefully examined, and proven over time, that they are able and willing to allocate personnel and financial resources to the project activities.