

## **Bloomberg Markets Magazine**

### **Suicides in India Revealing How Men Made a Mess of Microcredit**

*By Yoolim Lee and Ruth David - Dec 28, 2010*

Tanda Srinivas was lounging in the yard of his two-room house in the southern Indian village of Mondrai shortly after noon on Oct. 28 when his wife, Shobha, burst out of the door covered in flames and screaming for help. The 30-year-old mother of two boys had poured 2 liters of kerosene on herself and lit a match. The couple had argued bitterly the day before over how they would repay multiple loans, including those from microlenders who had lent small sums to dozens of villagers, says Venkateshwarlu Masram, a doctor who called for the ambulance.

Shobha, head of several groups of women borrowers, was being pressured to pay interest on her 12,000 rupee (\$265) loan. Lenders also were demanding that she cover for the other women, even though the state had restricted microfinance activities two weeks earlier, Bloomberg Markets magazine reports in its February issue. When Srinivas, 35, tried to snuff out the flames with a blanket, his polyester clothes caught fire. Within three days, both parents were dead, leaving their sons orphans.

Now, on this November morning, the boys' ailing 70-year-old grandfather and blind grandmother say they are caring for Aravind, 10, and Upender, 13, in the farming village where many men earn a living gathering palm extract to make alcoholic beverages. None of the boys' relatives can support them full time, says their 60-year-old grandmother, Saamma, breaking into tears.

## **India's Microlending Hub**

The horrific scene in Mondrai, 80 kilometers (50 miles) from the city of Warangal, has played out in dozens of ways across [Andhra Pradesh](#), India's fifth-largest state by area and the site of about a third of the country's \$5.3 billion in microfinance loans as of Sept. 30.

More than 70 people committed suicide in the state from March 1 to Nov. 19 to escape payments or end the agonies their debt had triggered, according to the Society for Elimination of Rural Poverty, a government agency that compiled the data on the microfinance-related deaths from police and press reports. Andhra Pradesh, where three-quarters of the 76 million people live in rural areas, suffered a total of 14,364 suicide cases in the first nine months of 2010, according to state police.

A growing number of microfinance-related deaths spurred the state to clamp down on collection practices in mid-October, says Reddy Subrahmanyam, principal secretary for rural development. "Every life is important," he says.

## Perverse Turn

On Nov. 8, police arrested two managers of lender Share Microfin Ltd. on allegations of abetting another suicide, this one of a 22-year-old mother. Share Microfin didn't respond to requests for comment on this story. As India struggles to provide decent education, health care and jobs to millions still locked in poverty, microlending -- the loaning of small sums to the world's neediest people to help them earn a living -- has taken a perverse turn.

Microcredit has become "Walmartized" by unrestrained selling of cheap products to the poor, says [Malcolm Harper](#), chairman of ratings company Micro-Credit Ratings International Ltd. in Gurgaon, India. "Selling debt is like selling drugs," says Harper, 75, the author of more than 20 books on microfinance and other topics. "Selling debt to illiterate women in Andhra Pradesh, you've got to be a lot more responsible."

## Opposite Effect

K. Venkat Narayana, an economics professor at Kakatiya University in Warangal, has studied how microfinance lenders persuaded groups of women to borrow. "Microfinance was supposed to empower women," he says. "Microfinance guys reversed the social and economic progress, and these women ended up becoming slaves."

India's booming microlending industry is part of a global phenomenon that began as a charitable movement but now attracts private capital seeking growth and high returns. [Banco Compartamos](#) SA, a former nonprofit that's now the largest lender to Mexico's working poor, raised about \$467 million in its 2007 initial public offering. The August IPO of SKS Microfinance Ltd., India's biggest microlender, drew further attention to the industry.

SKS began operating in 1998 as a nongovernmental organization led by [Vikram Akula](#), 42, an Indian-American with a Ph.D. in political science from the University of Chicago. The company raised 16.3 billion rupees by selling [16.8 million shares](#) at 985 rupees each. SKS [shares peaked](#) at 1,404.85 rupees on Sept. 15. As of Dec. 28, they'd fallen to 652.85 rupees.

## Andhra Pradesh Crisis

On Oct. 15, the government of Andhra Pradesh [imposed restrictions](#) that bar microlenders' collection agents from visiting borrowers and required companies to get local authorities' approval for new loans. The rules have crippled lending and repayments. Loan collection levels in the state have dropped to less than 20 percent from 98 percent previously, according to an industry group.

The upheaval in Andhra Pradesh is a long way from the vision of [Muhammad Yunus](#). The former economics professor won the Nobel Peace Prize in 2006 for his pioneering work in Bangladesh providing small sums to entrepreneurs too poor to get bank loans.

Yunus, 70, discovered more than three decades ago that when you lend money to women in poverty, they can begin to earn a living, and most of them will pay you back. Yunus started the Grameen Bank Project in 1976 to extend banking services to the poor. Since then, it has lent \$9.87 billion and recovered \$8.76 billion; 97 percent of its 8.33 million borrowers are female.

## **‘Wrong Direction’**

Yunus says he’s not against making a profit. But he denounces firms that seek windfalls and pervert the original intent of microfinance: helping the poor. The rule of thumb for a loan should be the cost of funds plus 10 percent, he says. “Commercialization is the wrong direction,” Yunus says, speaking in a telephone interview from Bangladesh’s capital of Dhaka. “An initial public offering is the triggering point for making a lot of money personally as well as for the company and shareholders.”

[David Gibbons](#), chairman of Cashpor Micro Credit, a nonprofit microlender to the poorest women in India’s Uttar Pradesh and Bihar states, says public, for-profit lenders face a conflict. “They have to decide between the interests of their customers and interests of their investors,” he says.

## **‘Can’t Be Done’**

Gibbons, 70, says he learned that lesson when he tried to raise 4 million pounds (\$6.2 million) from two wealthy London- based nonresident Indian investors in November 2006. Talks failed because of differences over expectations for returns on equity and other contract terms, he says. “That’s what made me think this just can’t be done,” he says.

Indian microlenders differ from Yunus’s Grameen Bank in key ways. To protect depositors’ money after bankruptcies among nonbanking financial companies in the early 1990s, India’s [Reserve Bank](#) in 1997 made it more difficult for them to meet the requirements needed to take deposits from the public. Only 36 microlenders are registered as nonbank financial companies, according to information supplied by the Reserve Bank.

## **‘I Feel So Sad’**

Indian microlenders themselves borrow from banks at 13 percent or more on average and extend credit to the poor. They charge interest rates that can rise to 36 percent, says [Alok Prasad](#), chief executive officer of the Microfinance Institutions Network, which represents 44 microlenders. He says all 44 firms are registered with the Reserve Bank. [SKS Microfinance](#) gets funds at about 12 percent interest and lends at 24.52 percent in Andhra Pradesh, spokesman [Atul Takle](#) says.

In Bangladesh, Grameen Bank got a banking license in 1983, which allowed it to take deposits. It charges 5 percent for education loans and 8 percent for housing loans. Beggars can borrow for free, and interest on major loans is capped at 20 percent, Yunus

says. “Microfinance has been abused and distorted,” he says. “I feel so sad because that’s not the microcredit I have created.”

Indian microfinance has roots in decades-old informal community financing. Nongovernmental organizations pioneered cooperative lending, known today as self-help groups, with seed money from the National Bank for Agriculture and Rural Development. Encouraged by these projects, the state-backed bank worked to tie borrowing groups to local bank branches in 1992.

## For-Profit Companies

Nonprofit organizations subsequently got involved as middlemen between the banks and the borrowers. By 2005, nonprofits such as [SKS](#) and Share Microfin had turned themselves into profit-making enterprises. Akula’s SKS [attracted investors](#) such as Khosla Ventures, Sun Microsystems Inc. co-founder [Vinod Khosla](#)’s venture capital firm. Capital flowed into the new industry from commercial banks, venture firms and private equity.

Sequoia Capital, in Menlo Park, California, and Bangalore- based Infosys Technologies Ltd. Chairman [N.R. Narayana Murthy](#) were among the backers. [George Soros](#)’s Quantum Fund has a 0.37 percent stake in SKS. Private-equity investors alone have put \$515 million into Indian microfinance companies since 2006, research service Venture Intelligence says.

## ‘Explosive Growth’

More than half of the 66 Indian microlenders tracked by Micro-Credit Ratings are for-profit firms. Some 260 microlenders had 26.7 million borrowers and 183.44 billion rupees of loans outstanding as of March, according to the Microfinance India State of the Sector Report 2010.

“Over the last two years, we’ve been seeing explosive growth,” says N. Srinivasan, who wrote the report. “Microfinance institutions found that it’s easy to make money. Not that making money is bad, but when you go overboard and say you require money for growth, you get into problems.” Polepaka Pula, a mother of two, says she saw microlenders rushing into her village of Pegadapalli to compete for business -- with tragic results. Her husband, Prakash, a painter who made 250 rupees on a good day, first borrowed from a group of villagers to build a house. Each participant of the so-called chit fund contributed 1,000 rupees a month and took a turn collecting the entire sum.

Microfinance officers from L&T Finance Ltd., Spandana Sphoorty Financial Ltd., Share Microfin and SKS began offering loans in the village starting in 2004, she says. The couple, already contributing to their village fund, took five more loans totaling 64,000 rupees. That saddled them with payments of 7,300 rupees a month, more than Prakash’s 5,000 rupee maximum monthly income.

## Loan Shark

When Prakash ran out of microlenders to borrow from, he went to a village loan shark, who charged 100 percent interest. With no way out and debt from multiple lenders ballooning, Prakash hanged himself in November 2009, his wife says. The small house he'd dreamed of was never completed. Only the foundation stands next to the home of his parents, a tiny structure with a roof of palm leaves. Spandana says that neither of the couple's names is in its database. The company says the media wrongly attribute harassment cases to microfinance, especially when Spandana is mentioned.

"The trigger factors for suicide are manifold, such as stressful situations at home," the company said in an e-mail response to questions about the death.

## Subprime Parallel

SKS spokesman Takle says its staff has practiced responsible lending for the past 12 years. Its [employees](#) are not paid based on the loan size or repayment percentage. "This ensures against giving out larger loans than what a borrower can repay," Takle says. A spokesman for L&T Finance declined to comment.

Overlending in Andhra Pradesh calls to mind the U.S. subprime crisis, says [Lakshmi Shyam-Sunder](#), director of corporate risk at International Finance Corp. in Washington, which invests in microlenders. "Subprime lending was initially seen as extending homeownership to poorer people, doing good," Shyam-Sunder says. As the industry expanded, making a profit became more important to some lenders, she says. "Tension arises when you work on activities with both social goals as well as commercial interests," she says, adding that it's important to strike the right balance. Companies chasing profits amid poor corporate governance are undermining the intent of microfinance, Cashpor's Gibbons says.

## 'Lending Gone Wild'

During the past five years, the number of microloans in India has soared an average of 88 percent a year and borrower accounts have climbed 62 percent annually, giving India the world's largest microfinance industry, Micro-Credit Ratings says. "This is unrestrained consumer lending gone wild," Gibbons says. "It's not about poverty reduction anymore."

[Sumir Chadha](#), managing director at [Sequoia Capital](#) India Advisors Pvt., says that without a profit motive it's hard to find anyone who will lend to the poor. "Capitalism doesn't have to be a bad thing," says Chadha, whose firm has a 14 percent stake in SKS. "If you can't profit off the poor, it means that no companies will service the poor -- and then they will be worse off than earlier."

## Chand Bee's Tale

For Chand Bee, a 50-year-old who led three borrowing groups in Andhra Pradesh, too many loans almost became her undoing. She says she ran away from home after collectors began harassing her. She took out multiple loans beginning in 2005, and she names Spandana as one of the lenders. Some of the money paid for the funeral of her

eldest son. When she fell behind on payments, she says loan officers threatened to humiliate her in front of neighbors and pressed her to sell her small grandchildren into prostitution. She left her slum in Warangal, where she lived with her deaf husband, some of her eight grown children and more than a dozen grandchildren.

After living as a beggar for a year, Chand Bee returned home in early November when family members told her that the state ordinance that went into effect on Oct. 15 had suspended some collections. A Spandana spokeswoman says none of the company's four customers in the district with the name Chand Bee has had trouble repaying.

Almost every household in the slum of 250 people -- where barefoot children play in lanes between rows of dilapidated shacks -- has taken several loans. So many microlenders ply their trade that residents refer to them by the days they collect: Monday company, Tuesday company and so on.

## **Debt Free**

Rabbani, a widow with four children, is one of the few women who are debt-free. She started a spice shop with two loans, which she repaid with her small profit. After seeing her neighbors' pains, she vowed never to seek another microloan. SKS says 17 of its clients have committed suicide, none because of loans being in arrears or harassment. "Suicide is a complex issue," Akula says.

Sitting in the second-floor conference room of SKS's seven-story headquarters in Hyderabad, where posters of smiling women running handicraft and tailor shops decorate the doors of elevators, Akula says there's nothing wrong with seeking profits.

"What does it matter to a poor woman how much an investor makes?" says Akula, dressed in his trademark knee-length kurta shirt from Fabindia, a seller of ethnic clothes made by rural craftsmen. "What matters to her is that she gets a loan on time at a reasonable rate that allows her to earn higher income."

## **Commercial Venture**

Turning SKS into a commercial venture allowed the firm to tap an unlimited pool of funds from private investors. That, in turn, let the company grow and reduce rates, Akula says. "Interest rates have come down over time," he says. "Because it works, she comes back year after year," he says of his customers.

His autobiography, "A Fistful of Rice" (Harvard Business Review Press, 2010), provides a glimpse of the expansion drive. Akula, a former McKinsey & Co. consultant, studied McDonald's Corp. and Burger King Holdings Inc. in 2005 to learn about their speedy training of unskilled workers. He devised a two-month course to train as many as 1,000 new loan officers a month. "I now had one goal for SKS; to grow, grow, grow as fast as we could," he writes. "We could practice microfinance in a way that would serve more poor people than anyone had ever thought possible." Akula says the commercial model of microfinance isn't the only way.

## **Returning to ‘Roots’**

“It’s an important complement to other forms of finance,” he says. New microfinance companies don’t spend time to build trust, Akula says. “As an industry, we need to go back to our roots,” he says. The Reserve Bank is scheduled to report on the industry in January. The finance ministry is planning new rules.

Sequoia Capital’s Chadha says he’s concerned about “regulatory uncertainty” created by the state ordinance and prefers federal regulation. Nationwide rules would prevent individual states from damaging credit discipline by waiving loans, Microfinance Institutions’ Prasad says. “It is no different than needing good regulation for stock investing or starting a manufacturing facility,” SKS investor Khosla says.

## **‘People, Not Profit’**

From Yunus’s perspective, it’s essential that the industry move away from seeking maximum profits and get back to focusing on the poor. “If not, you are not helping poor people’s lives,” he says. “You are not patient. You are not restrained. You don’t have empathy for the people. You are just using them to make money. That’s what blinds you when you are in the profit-making world. We need to see the people, not profit.”

Any such changes would be too late for Atthili Padma and Shivalingam, a young couple in Andhra Pradesh’s cotton-farming village of Chennampalli. Padma, a 22-year-old mother of two, walked out of her house on Oct. 7 with her 18-month-old son and 4-year-old daughter, according to Maruthi Prasad, a superintendent at the police station in Shankarampet.

## **Padma’s Death**

Instead of heading to her parents’ house as she often did, she walked 2 kilometers in the opposite direction. She came to an old Hindu temple where villagers worship Lord Shiva, the god of destruction. Padma continued until she stood in front of a well once used to irrigate crops, her father-in-law, Pochaiah, says. There, with no one to dissuade her, she jumped into the well with her children.

The day before she died, Padma had visited her parents after arguing with her husband over loans they couldn’t repay, according to Mangamma, the couple’s neighbor. Their marriage five years ago was arranged by their parents and the couple had become close and hadn’t fought before that day, Mangamma says. The loans totaled 20,000 rupees, Pochaiah says. Padma’s death is recorded as a microfinance-related suicide in the list by the [Society for Elimination of Rural Poverty](#).

## **‘Sad Day for Microfinance’**

Police arrested Padma’s husband, Shivalingam, on Oct. 13 for allegedly abetting Padma’s suicide. They also alleged that he’d harassed her to provide money to marry him, which is illegal in India, according to Narayana, a constable at the Shankarampet police station.

Police made two further arrests on Nov. 8: Share Microfin managers Sriram Raghavender, 27, and Polapalli Kumaraswami, 22, also for allegedly abetting the suicide, according to superintendent Prasad. The two managers and Shivalingam have been released on bail and are awaiting a court hearing, Prasad says.

Advocates and investors such as Khosla say microfinance -- when it works correctly -- is the best way to give the rural poor a shot at better lives. The tragedies in India present the worst possible outcome, says Cashpor's Gibbons, whose Nov. 15 speech opened a morning session of the annual Microfinance India Summit in New Delhi. "This is a sad day for microfinance," said Gibbons, who has promoted the movement for the past two decades. "Often people asked me, 'What are you doing here?'" he told the audience. "I've been always proud to say, 'I'm doing microfinance.' Now, when people ask, I feel embarrassed. I feel like hiding somewhere."

To contact the reporters on this story: [Yoolim Lee](mailto:yoolim@bloomberg.net) in Singapore at [yoolim@bloomberg.net](mailto:yoolim@bloomberg.net); [Ruth David](mailto:rdavid9@bloomberg.net) in Mumbai at [rdavid9@bloomberg.net](mailto:rdavid9@bloomberg.net)

To contact the editors responsible for this story: Michael Serrill at [mserrill@bloomberg.net](mailto:mserrill@bloomberg.net); Philip Lagerkranser at [lagerkranser@bloomberg.net](mailto:lagerkranser@bloomberg.net)