Employment Generating Programmes in the Urban Context of India

The Nehru Rozgar Yojana

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1 Introduction

Unemployment and underemployment in association with low and irregular incomes are major causes of urban poverty in India. Studies on the Indian labour market show that the urban formal sector has been unable to absorb the expanding labour force resulting in the proliferation of the informal sector where most of the urban poor seek to ensure their livelihood (ILO 1996). A further sign of continuously deteriorating labour market conditions is the increase in casual employment (Amis 1995: 487; cf. Kundu 1993). This trend has not been reversed yet by the new economic policy the Government of India adopted in July 1991 for achieving higher economic growth rates. On the contrary, it is mainly the urban poor who have to burden the negative social impact of the ongoing adjustment process (Moser/Herbert/Makonnen 1993).

These unfavourable labour market developments in combination with an increase in urban poverty prompted the Government of India to set new priorities in poverty alleviation during the Seventh Five Year Plan (1985–1990) and to initiate employment programmes in urban areas. The challenge was quite clear: the key to alleviate urban poverty was the creation of sufficient productive employment opportunities for the urban poor. However, economic growth alone does not necessarily lead to a decline in poverty through trickle down effects. For this reason, employment generating schemes for disadvantaged groups are an important instrument for poverty alleviation. In view of the failure of labour markets to provide adequate wage employment opportunities, the Government of India placed emphasis on the direct promotion of microenterprises which have generally come into new focus in the development debate in the 1980s (cf. Levitzky 1989; OECD 1993). Therefore several employment programmes aimed at supporting entrepreneurial initiatives of the urban poor have been introduced since the mid 1980s.

The new emphasis on self-employment promotion corresponded with the changing views on the informal sector where self-employment predominates and which has increasingly been perceived by development planners as a breeding ground for poor entrepreneurs operating successfully even under highly unfavourable economic conditions (Kabra 1993: 526; cf. De Soto 1988). The development of the microenterprise sector also closely corresponded to many of the priorities emerging in the liberalising economy in India such as developing the private sector, creating employment, alleviating poverty and encouraging more equitable income distribution.

One of the first Indian urban employment programmes was the Nehru Rozgar Yojana (NRY) introduced in 1989. This target group oriented programme seeks to enable the urban poor to set up their own small businesses by way of subsidised bank credits and the provision of training. With access to productive resources such as credit, the poor are supposed to make more productive use of their labour and progressively increase their income through self-employment and thus cross the poverty line over time. NRY follows a rather standardised approach similar to other programmes designed for self-employment generation in rural as well as urban areas. Whereas India has wide experience in implementing rural programmes, analogous experience in urban areas is still limited (Drèze 1990: A-95; Papola 1993: 24). As these programmes are often considered to be vote catching programmes, and therefore tend to be heavily politically oriented, their impact is said to be marginal. In most cases they are seen as examples of ineffective bureaucratic approaches to alleviate poverty because they cannot reach out to the poor effectively and tend to exclude the poorest of the poor.

The provision of credit to the poor often is a major component of many employment programmes such as the NRY. The lack of access to productive assets is one of the main factors preventing the poor from breaking away from the 'poverty trap' (Getubig 1993: 104). Therefore, it is important that the poor have continuous access to credits for investment as well as for consumption purposes. There are different views on the success of state controlled subsidised credit programmes in assuring access to credits for economically disadvantaged groups. In most cases, it is believed that these programmes mainly benefit the non-poor. Innovative credit programmes of NGOs and some commercially oriented banks have, by contrast, shown remarkable success in supplying credit to the poor (Getubig 1993, Lipton 1996).

Evaluation studies and insights from my own fieldwork in Delhi suggest that the performance of centrally initiated self-employment programmes such as NRY is weak for various reasons. Nevertheless, the Indian Government adheres to the standardised design of these employment programmes where subsidised credit channelled through the banking system form the major component. The Government mainly attributes the low performance to deficiencies in implementing these programmes rather than questioning the basic approach.

In this article the credit component of NRY as a given example for a self-employment programme in the urban context of India will be evaluated using the experience of other more successful innovative credit programmes. The objective is to reveal the underlying logic of the failure of the NRY credit delivery system. The main argument is that in the present conceptional design of NRY it is difficult to open access to individual bank credits for poor first time borrowers and to establish long-term credit links with banks. Thus, no structural change in urban poverty can be expected from NRY and similar programmes in the near future.

2 Main Features of the Nehru Rozgar Yojana

The NRY operates under the auspices of the former Ministry of Urban Development, now the Ministry of Urban Affairs and Employment after the reshuffle of the cabinet in 1995. It consists of three subschemes for the promotion of employment (Government of India, Ministry of Urban Development 1992):

a. Scheme of Urban Wage Employment (SUWE)
b. Scheme of Employment through Housing and Shelter Up gradation (SHASU)
c. Scheme for Urban Micro Enterprises (SUME)[1]

Under SUME, unemployed or under-employed urban poor should be encouraged to start microenterprises in the informal sector with the help of subsidised bank loans and training. The promotion of microenterprises or self-employment ventures also should have multiplier and employment effects through the creation of wage-employment in the

[1] The following analysis only refers to the 'Scheme for Urban Microenterprises'. In the following the terms NRY and SUME are used interchangeably.

newly created or expanding units. A further objective which is not explicitly stated in the stipulations of the scheme is to open access for the urban poor to institutional finance thereby reducing their dependency on informal money lenders (Bank of India 1992: 16; cf. Lipton 1996: 26).

Eligible beneficiaries, i.e. a permanent resident of the city or town, a ration card holder living in a household with an annual income of less than Rs 11,850, can apply for a loan up to an amount of Rs 16,000, which includes a 25 per cent subsidy of Rs 4,000 from the government. For disadvantaged low caste groups such as Scheduled Castes/Scheduled Tribes and female beneficiaries the maximum amount is fixed at Rs 20,000 inclusive of a subsidy of Rs 5,000. Training courses with the duration of three months are also part of the scheme. Monthly stipends of up to Rs 250 per participant are provided and infrastructural support to training institutions is given.

The terms and conditions for loans are the following: loans up to Rs 7,500 carry an interest rate of 10 per cent, and the interest rate for higher loan amounts is 11.5 per cent. The loans have to be paid back within three to five years, with a grace period which should not exceed six months. Instalments are fixed on a monthly or quarterly basis depending on the surplus cash generation of the financed unit. Margin money, i.e. the financial contribution by the beneficiaries themselves, and collaterals are not required. The subsidy is supposed to be disbursed to the borrower along with the loan.

As under other anti-poverty programmes, the nationalised commercial banks are supposed to supply credits according to priority sector lending quotas. The subsidy and training component is funded by the Central Government and the State Governments. The ratio for sharing the financial burden between the Central and State Governments is 60:40. Central government funds with an outlay of Rs 227 Crores (1 Crore = 10,000,000) during the Eighth Five Year Plan period are channelled through the State Governments. A department or office as the nodal agency at the state level and a District Urban Development Agency (DUDA) coordinate and administer the scheme. They are responsible for handling the funds and identifying and selecting eligible beneficiaries. Identified potential borrowers have to fill in application forms which are sent to DUDA. In this connection, committees are organised at local level to assess the financial needs of applicants and to select the beneficiaries. The applications of the pre-selected cases are forwarded to the banks and again assessed by the bank staff. In case of their approval DUDA makes the subsidies available for the banks. The bank loans together with the subsidies are then disbursed through the existing banking system to the urban poor.

3 Operational and Institutional Constraints

Six years after the introduction of NRY, the number of beneficiaries assisted through bank loans was 742,541, whereas the number of people who have completed training courses or are presently undergoing training was much lower, amounting to 188,235. A total subsidy amount of Rs 133.30 crores was sanctioned under SUME according to official figures, as on 31.12.95, calculated on the basis of reported performance by the States and the Union Territories.[2] NRY has not taken off as it was expected and planned (Government of India, Ministry of Urban Development 1994: 10).

The effectiveness of this approach to bring down the level of poverty considerably is being questioned by various studies of NRY and of similar programmes such as the Self-Employment Programme for the Urban Poor (SEPUP) and the Integrated Development Programme (IRDP).[3] The programmes are criticised on various grounds. It is generally believed that self-employment has great potential, but it could not fully be exhausted because of operational and institutional constraints (cf. e.g. Jain 1990; Reddy 1994; Lall 1994; Muqtada 1989). Major criticism refers to the standardised top down approach, the identification and selection of beneficiaries and the role of the banking sector.

[2] These figures were given by the Government of India, Ministry of Urban Affairs and Employment, New Delhi, January 1996.

[3] SEPUP, introduced in 1985, has been absorbed by NRY in 1992. IRDP, introduced in 1980, is the sister programme for rural areas. The main feature of these programmes is the provision of subsidized bank credit channeled through the nationalised banking system.

Top Down Approach
A major problem area is that these schemes follow a top down approach with minutely elaborated operational guidelines from the Central Government, which add to bureaucratic inertia and cause a range of managerial problems. These guidelines bind upon state governments as well as local bodies. Under the existing administrative set-up they leave hardly any flexibility and very little scope for experimentation by the project officers or bank officials. Programme implementation is suffering from a large number of problems such as difficulties in coordination, inadequate follow-up and monitoring, unnecessary delays in implementation caused by complicated procedures and shortage of qualified personnel, and lack of commitment, corruption etc. (cf. Jagannathan 1987: 108ff).

Government and bank officials are primarily interested in fulfilling their targets in terms of number of participants and amount of credit and subsidy. Therefore they are less concerned about the sustainability of activities taken up under the scheme (cf. Bhole 1994: 182). Nevertheless, the targets are frequently missed and, particularly, the poorest of the poor often remain excluded for the various reasons elaborated in Section 4.

Identification and selection of beneficiaries
The stipulation concerning the eligibility of beneficiaries on the basis of an annual income limit fixed at Rs 11,850 is controversial. Government officials often claim that it is extremely difficult to identify and select beneficiaries in a metropolis like Delhi with a household income of less than the official poverty line under NRY. In many cases, even poor people often survive on a higher income, and the poorest of the poor are, in general, hard to reach, especially by state agencies (Mishra 1994). There is a uniform income limit for All-India and officials suspect that it is an incorrect income limit. However, it seems that it is only a welcome excuse for their low engagement in the scheme. In addition to that, income assessments by field surveyors or bank staff are difficult to make and somewhat arbitrary, in particular for self-employed persons because they often do not keep any records on their income.

Furthermore, the identification and selection process of eligible beneficiaries is rather long and cumbersome. From the perspective of the beneficiaries, this bureaucratic approach to poverty alleviation has various kinds of problems. It may be argued that in view of the elements of bureaucracy and arbitrariness, the identification and selection is not necessarily directed towards the financial needs of the poor. First, it is often very difficult to get the loan when it is most needed. Second, the loan amount is often considered to be too small to finance economically viable projects. The limited scope for setting up viable self-employment activities often leads to a low repayment capacity for the poor, and this again makes banks very reluctant to lend out to the poor.

Involvement of the banks
A major critical problem area is the involvement of the nationalised banks in the programme. In the past, banks had little interest in providing bank loans to the poor and financing informal sector enterprises. The reforms in the banking sector since 1991 will probably further contribute to the low engagement of the banks in the scheme. The reforms will lead to a neglect of priority sector lending and to a diminishing role of social banking. Due to the new emphasis on efficiency and profitability banks are increasingly reluctant to lend to small borrowers (Majumdar 1995: 2169). The share of the priority sectors in total net bank credit declined consistently from 40.9 per cent in June 1991 to 35 per cent in June 1993, although the target of 40 per cent remained unchanged.

The reasons behind this are well known (Anagol/Sundaram 1995). The risks involved in lending to the poor are too high and the recovery of loans is thought to be low because of their low repayment capacity. They cannot open a bank account for their savings or provide any other bank securities or collaterals. Since the NRY loan amount is rather small, high transaction costs occur. In addition to this, the follow-up of loan repayment is difficult because borrowers are not always easy to trace, especially in urban areas where they tend to be scattered over the whole city or town and they may not have a permanent address. There is also the risk that immigrants take the loan and then go back to their villages. In these cases, the banks must write off their credits. Consequently, applications by NRY borrowers are rejected by the banks on a large scale and a large number of applications are kept pending.

As a result, the provision of subsidised bank credits under NRY is not geared to the financial needs of the poor. As they get in most cases only one credit under NRY, access to institutional finance has not increased, thus hampering their ability to operate microenterprises or income activities successfully.

As will be argued below, the behaviour of banks is rational from their point of view, which is one major factor for the low performance of employment programmes, and this has an important bearing on the effectiveness of NRY as an instrument for urban poverty alleviation.

4 Weaknesses of the Credit Delivery System under NRY

The basic objective of any credit programme aimed at alleviating poverty must be to eliminate access barriers to credits for the poor and to make credits available to them. This implies that the programmes must attain sustainability, thereby increasing long-term credit access (Rudkin 1994). Experiences with innovative credit models (e.g. Grameen Bank in Bangladesh, SEWA in India) more informal by nature, have shown that this is not an impossible task. The poor are a bankable group (Stearns 1985; Tendler 1989; Rhyne 1992; Getubig 1993; Krahnen/Schmidt 1994). The basic questions to be asked are: what are the underlying reasons why the urban poor are unlikely to gain access to the banking system and how can these constraints be overcome?

Theoretically, an important element in a credit transaction is uncertainty. In the case of informal finance, personalised credit contracts and a personal relationship between borrower and lender reduces the uncertainty of the credit transaction. The principle of reciprocity plays a major role for lenders as well as for borrowers who are interested in the stability of their relationship (Ghate *et al.* 1992: 5). Thus, there are built-in incentives for providing and paying back credits. The formal credit transactions are by comparison more anonymous and therefore tend to be more uncertain by nature. Uncertainty causes so-called information and transaction costs for all parties involved in establishing mechanisms to ensure that the required credit amount is available when needed or paid back according to the repayment schedule agreed.

The level of information and transaction costs that the suppliers and consumers of financial services have to pay largely depends on the behaviour of the actors (BMZ 1994: 11; Richter 1994: 9). The prevailing incentive and sanction structures govern the behaviour of institutions, of the people inside the institutions and of the people with whom the institutions have to deal (Krahnen/Schmidt 1992: 80ff). With reference to the economics of information, it can be said that formal, more anonymous credit transactions in particular are characterised by asymmetrically distributed information between the borrower and the lender. This applies especially to urban areas where transactions between borrowers and bank staff are highly impersonal.

From the perspective of the banks, uncertainty as to how the borrower will behave or whether he or she will default or refuse the repayment of the credit cannot be eliminated completely. Thus, there must either be incentives for borrowers to pay back or sanctions need to be imposed on the defaulter. In the latter case, it is important whether contracts can be legally enforced. In commercial banking, for example, credit is secured by providing collaterals and often depends on how banks can materialise their claims towards the borrower.

Since the urban poor cannot normally provide tangible collaterals, other techniques to motivate repayment should be applied to substitute repayment motivators for costly information gathering by bank staff and legal procedures (Rhyne 1993: 29). Experience from informal finance delivery systems show that in the absence of tangible collaterals and legal enforcement mechanisms, techniques to ensure repayment can include:

a. group guarantees or pressure from the borrowers' networks

b. the promise of repeat loans, in increasing amounts

c. savings requirements

The substitution of costly information gathering by repayment incentives reduces lender risks and lowers information and transaction costs. The reduction of default rates and information and transaction costs contributes to the reduction of the total credit costs, thus indirectly contributing to the profitability of banking operations and probably higher lending rates for poor borrowers.

Against this more theoretical background the reasons for the reluctance of the nationalised commercial banks under NRY can be illustrated. The basic problem is that banks have no genuine incentives to provide credits to the urban poor in their own interest, nor do the poor borrowers have any incentives to pay NRY credits back, which in turn reinforces the indifference of banks towards NRY. However, according to priority sector lending quotas imposed by the Indian Government, banks have to lend out to the urban poor under schemes like NRY. Under these circumstances the risks for banks to lend out to this group are comparatively high given the anonymous nature of credit transactions in urban agglomerations.

The banks are forced, therefore, to minimise their lending risks by gathering information on borrowers and their creditworthiness as well as establishing complicated and lengthy procedures for the identification and selection of reliable borrowers. This process is quite costly for banks, especially as hardly any sanctions as alternatives for reducing lending risks can be imposed on defaulting or non-paying borrowers. Tangible collaterals are not required and since most of the poor borrowers operate outside the reach of legal enforcement systems it is rather difficult to execute credit contracts by legal procedures. These relatively high information and transaction costs connected with the selection of poor borrowers cannot be covered by a corresponding increase in the interest rates since they are fixed at 10 per cent and 11.5 per cent respectively. Through the public provision of subsidies the government seeks to ease the financial burden of banks, but the attitude of banks towards this lending group has not changed substantially. In some cases, there are even indications that the banks probably provide the subsidies given by the states as bank loans to the poor.[4]

Another way to reduce information and transaction costs for banks is the involvement of DUDA, the nodal agency at district level responsible for the implementation of NRY or through NGOs. However, the costs are not reduced by shifting the responsibility of selecting eligible borrowers from banks to this agency or to the NGOs, they are simply transferred outside the banking system. This transfer may encourage bank lending and contribute to higher profitability of their operations. However, it entails an even more complicated selection process with increasing bureaucracy and inner and intra agency problems due to necessary co-ordination efforts. This also corresponds with an increase in administrative costs for implementing NRY and delivering credits to the poor.

Also from the perspective of the borrowers, relatively high transaction costs occur. They are often prepared to bear these costs because no other source of credit is available to them (cf. Lipton 1996: 27). They have to meet the information requirements of DUDA and the banks, which include frequent visits, and the clearance from other banks and financial institutions to confirm that no credits are taken under other schemes. These visits entail transport costs and, in addition, opportunity costs in terms of lost income due to absence from their business. Since no established links to the formal banking system exist the borrowers often depend on intermediaries or more dubious middlemen to help them to get a NRY credit. In the latter case, the borrowers often have to pay bribes, not only to DUDA or bank staff but to the middlemen as well. They distribute the application forms and charge the poor with fees for forms which are free of cost. However, the poor cannot be sure whether these applications are actually forwarded to the banks.

The repayment mentality of the borrowers largely depends on the ability to pay and the willingness to pay. The ability to pay depends on the income generating capacities of the activities financed with the NRY credit. The latter is influenced by a host of factors which determine whether the borrower willfully defaults on the repayment. This again depends on the existing incentive and sanction structure. As there are no effective sanction mechanisms which can be imposed by the banks for defaulting the willingness to pay rests on the incentives built in to the credit delivery system. But, since there are no repayment incentives other than the casual follow-up by the bank or DUDA staff, the repayment rate is likely to remain low.

[4] During fieldwork in Delhi it was observed that the amount of credits applied for is considerably less than the amount of credit disbursed. As the amount of subsidies is calculated on the basis of the amount stated in the application forms, there may be some cases where only the subsidies are disbursed as credits.

5 Conclusions

There is a consensus that credit is one of the most important instruments to alleviate poverty. However, it is rather difficult to reach the urban poor because banks perceive them as a non-bankable group. In this context, the disenchantment with traditional subsidised credit programmes aimed at supporting the poor to widen their productive asset base and to develop sustainable self-employment activities is not of recent origin. Several studies on successful programmes suggest that informal credit is more effective than formal arrangements in reaching precisely those categories of borrowers sought to be benefited by credit quotas.

Nevertheless, the Indian government still follows a standardised design of centrally sponsored employment programmes where subsidised credit is the major component. Thus, in the present framework, the nationalised commercial banks play a key role in alleviating urban poverty. Their low engagement in these programmes such as NRY, therefore, has serious repercussions on the performance and effectiveness of direct programmes to reduce urban poverty sustainably and on a large scale.

Fixing targets and credit quotas does not ensure that the urban poor have easy access to formal finance. A major reason for the limited access to individual bank credits is the existing incentive and sanction structure in the credit delivery system. It implies high information and transaction costs for those who supply credits, and for those demanding credit. The banks simply do not show much interest in the programmes which is reflected by the large numbers of applications rejected and kept pending for a long time to discourage the poor from borrowing.

Poor borrowers are set at serious risk in the sense that they do not necessarily benefit from these programmes, and indeed may be worse off than before. This is the case when borrowers have to face high transaction costs in form of pre-credit expenses and foregone income which are not compensated by the availability of higher bank finances later on. The money for pre-credit expenditures is lost. In extreme cases, the shortening of their own financial resource base ruins their chances for undertaking (smaller) self-financed self-employment ventures.

In conclusion, NRY and similar self-employment programmes have failed so far to open continuous access to institutional finance for the urban poor. Thus, no structural change in urban poverty due to NRY and similar programmes can be expected in the near furture. However, this is not to say that the state cannot play a major role in urban poverty alleviation, but more lessons must be learnt from other more successful credit programmes and translated into appropriate action for reducing urban poverty effectively.

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