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Micro Finance - An instrument for Poverty Alleviation

Abstract :: *The main objective of micro-finance is to alleviate poverty and to make the poor people self dependent. Providing employment opportunities to the rural women and developing the living status of the rural folk by providing credit with less interest is the major concern of micro-finance. Rural development is the major women area for social change. Society, culture and economic development are intertwined and have relation with other social factors. Economic development and micro-finance were two major concepts on which Grameen Bank on Bangladesh was established. Lasting peace can not be achieved unless large population groups find ways in which to break out of poverty. Micro-credit is one such means.*

This conceptual paper, traces the evolution of Micro-finance in India as a powerful tool for poverty alleviation and women empowerment. The paper also highlights the legal forms of the Micro-finance Institutions (MFI's) in India, the contribution of self-help groups (SHGs) in India and also highlights other aspects of Micro-financing in India.

Key words :: - Micro Finance, Poverty Alleviation, Micro-credit, SHGs **Introduction:**

There have been notable researches in the field of finance and credit over the last two decades, however most have them have been on the main stream financing and the role of commercial banking and financing. But the most important finding did not come from the world of the rich or the relatively well off. More important than the hedge fund or the liquid-yield option note was the finding that the poor can save, can borrow (can indeed decide on loans to fellow poor), and will certainly repay loans. This is the world of microfinance.

Over the past few decades, micro-finance has evolved as a powerful mechanism to deliver financial services (particularly credit) to sections of the community that have been excluded from the services of the mainstream institutions like commercial banks as well as the Cooperative banks. This conceptual paper, traces the evolution of the Microfinance revolution in India as a powerful tool for poverty alleviation and women empowerment. Where institutional finance failed Microfinance delivered, but the outreach is too small. There is a question mark on the viability of the Microfinance Institutions. There is a need for an all round effort to help develop the fledgling Microfinance Industry while tackling the tradeoff between outreach and sustainability. The paper also highlights various aspects of Micro-financing in India viz. models of microfinance, the future prospects and the challenges it has to face in the future.

Concept of Micro-Finance:

Micro Finance can be defined as the extension of small loans to population, too poor to qualify for traditional bank loans. These schemes are characterized by relatively small loans. The repayment period is relatively short, about a year or so. Women are the major beneficiaries of these schemes and the destination of the funds primarily includes agriculture, distribution and trading, small craft, processing industries and consumption credits too. The administrative structure is generally light and the entire process is particularly in nature.

A good definition of microfinance as provided by Robinson: "Microfinance refers to small-scale financial services—primarily credit and savings—provided to people who farm or fish or herd; who operate small enterprises or micro-enterprises where goods are produced, recycled, repaired, or sold; who provide services; who work for wages or commissions; who gain income from renting out small amounts of land, vehicles, drafts animals, or machinery and tools; and to other individuals and groups at the local levels of developing countries, both rural and urban."

Evolution and Growth of Microfinance in India:

India has supported social banking for a long time. Policy directions to rapidly expand rural branches, mandate credit allocations for priority sectors (including agriculture), deliver large subsidy oriented credit programmes to serve marginal communities and poor households and control interest rates have been tried for over 35 years.

Banking activity in rural India was not all that smooth a decade ago. Political interference, frequent policy shifts, urban bias among bankers and the lack of awareness among villagers about credit utilization are some of the major problems, which the bankers encountered in the past.

Historically, microfinance movement was started by small NGOs, grass-root level microfinance organizations and poor women themselves. Poor proved to be bankable and Government, NABARD and SIDBI came forward and helped these organizations to grow. However, the situation continued to be the same until SHG (self-help group) banking came into existence. When banks started financing SHG groups, the members learned to be more responsible in utilizing the credit. As a result the repayment started ticking to the banks. The recovery from SHG groups all over India is always above 90%. SHG or people's banking was launched by NABARD in 1992 when 500 SHGs were operational across the country on a pilot basis. As on March 31 2004, 1,079,091[1] SHGs in 563 Indian districts have utilized bank credit of Rs 39.04 billion. More than 16 million rural households have gained access to bank credit through 60,000 retail credit outlets of the banking sector in rural India. The SHG movement in India is considered as the largest-ever social movement in the world, which has targeted one third of India's poor. In order to take banking to the doorsteps of each rural household, selected post office branches in Kanchipuram and Pudukottai districts of Tamil Nadu have been utilized, on pilot basis, to extend credit to 200 SHGs.

The new generation microfinance was slow in coming to India. Low levels of grants to microfinance institutions, an unfavorable policy environment, substantial traditional banking infrastructure and a search for context specific solutions has constrained rapid scale up. The first breakthrough emerged from policy support to enable informal self help groups of 15-20 members (mainly women) to transact with commercial banks. These groups build up and rotate savings amongst themselves, open bank accounts and take responsibility for lending and recovering money financed by banks. With the missionary zeal of the National Bank for Agriculture and Rural Development (NABARD), insights gained by NGOs, the increasing enthusiasm of bankers and politicians and emerging successes in repayment and social impacts, this national movement now encompasses 1.4 million such groups (over 20 million members).

Highlights of the evolution of Microfinance in India:

- Microfinance has been in practice for ages (though informally).
- Legal framework for establishing the co-operative movement set up in 1904.
- Reserve Bank of India Act, 1934 provided for the establishment of the Agricultural Credit Department.
- Nationalization of banks in 1969
- Regional Rural Banks created in 1975.
- NABARD established as an apex agency for rural finance in 1982.
- Passing of Mutually Aided Co-op. Act in AP in 1995.

Models of Micro Finance in India

Model – 1

Self Help Group (SHG) – This is the dominant microfinance methodology in India, a version of the village banking model. The group is a collection of 15-20 members and its operations are based on the principle of revolving the members own savings. Such resources are many a times augmented by funds borrowed from MFIs or banks. Savings therefore precede borrowings by members. The volume of individual borrowings is determined either by the volume of member saving or by the saving of the group as a whole.

Model – 2

Individual Banking (IB) – This model entails provisions of financial services to individual clients. These may sometimes be organised into joint liability groups, co-operative or even SHGs. In the case of co-operatives, all the borrowers are members of the organization either directly or indirectly by being members of primary co-operative or associations which are members of the apex society. Creditworthiness and loan security are a function of co-operative membership within which member savings and peer pressure are assumed to be a key factor. Although the magnitude and timing of savings and loans are unrelated, a special effort is made to mobilize savings from members.

Model – 3

Grameen Model (GM) – This model was initially promoted by the Grameen Bank of Bangladesh. Grameen MFIs undertake individual lending but all borrowers are members of a 5 member joint liability group which in turn gets together with 6-9 other such groups from the same village or neighbourhood to form a centre. Within each centre, peer pressure and the desire to maintain credit – worthiness in order to qualify for a larger loan in the next cycle are key factors which ensure repayment.

Model – 4

Mixed Model (MM) – Some MFIs started with the Grameen Model and then at a later stage embraced the SHG Model without completely doing away with the Grameen Model.

Growth of SHG in India
(Nos. in '000)

Sr.No.	Year	No.of SHG	Bank Loan	Refinance
1.	2002-02	717	2049	1419
2.	2003-04	1079	3904	2125
3.	2004-05	1618	6898	3092
4.	2005-06	2239	11398	4160
5.	2006-07	2924	18041	5459

Source: - RBI Annual Report 2006-07.

The Profile and Features of Microfinance in India:

- Estimated that 350 million people live Below Poverty Line
- This translates to approximately 75 million households.
- Annual credit demand by the poor in the country is estimated to be about Rs. 60,000 crores.
- Cumulative disbursements under all microfinance programmes is only about Rs. 5000 crores.(Mar. 04)
- Total outstanding of all microfinance initiatives in India estimated to be Rs. 1600 crores. (March

04)

- Only about 5 % of rural poor have access to microfinance.
- Though a cumulative of about 20 million families have accessed microfinance to the extent of Rs. 5000 crores, the total outstanding is estimated to be only about Rs. 1600 crores. The active borrowers are estimated to have a per capita outstanding of only Rs. 2500.
- While 10 % lending to weaker sections is required for commercial banks, they neither have the network for lending and supervision on a large scale nor the confidence to offer term loans to big MFIs.
- The non poor comprise of 29 % of the outreach.
- About 60 % of the MFIs are registered as societies.
- About 20 % are Trusts.
- About 65 % of the MFIs follow the operating model of SHGs.
- Large concentration in South India.
- 600 MFI initiatives have a cumulative outreach of 1.25 crores poor households.
- NABARD's bank linkage program has cumulatively reached a total of 9.4 lakh SHGs with about 1.4 crores households.

Projections for the future of Micro Finance in India:

- Annual growth rate of about 20 % during the next five years.
- 75 % of the total poor households of 80 million (i.e. about 60 million will be reached in the next five years.
- The loan outstanding will consequently grow from the present level of about 1600 crores to about 42000 crores.

Challenges ahead:

- Appropriate legal structures for the structured growth of MF operations
- Finding adequate levels of equity for the new entities to leverage loan funds
- Ability to access loan funds at reasonably low rates of interest.
- Ability to attract and retain professional and committed human resources.
- Design of apt MIS including user friendly software for tracking accounts and operations.
- Appropriate loan products for different segments.
- Ability to innovate, adapt and grow.
- Bring out a compendium of small and micro enterprises for the MF clients.
- Identify and prepare a panel of locally available trainers.
- Ability to train trainers.
- Capacity to provide backward linkages or create support structures for marketing.

Conclusion:

Micro-financing in India is the neglected daughter of the family of financial services. This is evident from the sustained discrimination against and frequent disregard for Micro-finance, despite their productive and reproductive role in financial services. This is evident from different nomenclature used at both the international (UN International Year of Micro credit, Micro credit summit) and national levels (Priority Sector Lending; Annual Credit Policy; Credit/ deposit ratio). Micro-finance can be a useful entry point for the unbanked to build up a history with the formal financial institutions before customers are entitled to other financial services. With the greater spotlight on knowing the customer and the fact that poor households do not have a salary slip, utility bills, clear land titles or unique identity papers, a regular savings record could be the first building block to membership of the formal financial sector. What is more, with savings services, poor customers need to trust the financial institution and not the other way round.

The financial service needs of the poor are simple but their satisfaction can be life enhancing. The poor need access to convenient, liquid and safe deposit services which are protected against inflation by positive real rates of interest. With savings in reserve the poor are able to smooth their consumption expenditures in the face of uncertain income streams. Savings provide a shield against catastrophic events which, by forcing the vulnerable to divest productive assets, would otherwise tip them over the dividing line between meager sufficiency and poverty. "Micro-Insurance" is a related financial product with potentially profound welfare benefits

Microfinance is not yet at the centre stage of the Indian financial sector. The knowledge, capital and technology to address these challenges however now exist in India, although they are not yet fully aligned. With a more enabling environment and surge in economic growth, the next few years promise to be exciting for the delivery of financial services to poor people in India.

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