IOSR Journal of Business and Management (IOSR-JBM)
e-ISSN:2278-487X, p-ISSN: 2319-7668. Volume 26, Issue 12. Ser. 16 (December. 2024), PP 59-62
www.iosrjournals.org

Micro Finance Financial Institutions' Influence on India's Economic System

Dr. Yogesh Kumar
Assistant Professor, Department of Commerce
Seth P.C. Bagla P.G. College, Hathras

Abstract:
India is a populous country with a population of roughly 138 crores. It has a low per capita income, with a GDP per capita of 1,750.00 USD at the end of 2011 and a predicted GDP per capita of 1850.00 USD at the end of 2022. In India, the majority of loan/credit requirements are modest. These loan/credit obligations, if not met through proper channels and financial institutions, can lead to a slew of social issues. Furthermore, India's banking sector is critical to the country's economic progress. This article examines the role and influence of small finance banks on the Indian economy and growth.

Keywords: *small finance banks, loan and credit requirements, financial inclusion, banking system, Indian economy, and growth.*

I. Introduction

India is a low-income, densely populated, impoverished, and developing nation. It aims to achieve stronger growth and greater social and financial equality. In this regard, for the country's high and balanced economic growth, India must prioritize the development of rural/urban impoverished people as well as the development of rich/posh class gentry and moderate/middle-class citizens. This cannot happen without the implementation of new updated financial systems or services that are technically sound and viable, as well as catering to the diverse demands of disadvantaged people.

To finance Indian growth, there are two options: domestic financing and external sector financing. External sector financing has major implications due to both exchange rate risk and political effects. As a result, nations take a conservative approach, limiting the current account deficit to less than 2% of GDP. As a result, domestic financing bears the lion's share of the growth financing burden.

The overall health of the economy is reflected in the health of its banking system. The slowdown of the economy immediately gets reflected in the increase of non-performing assets of the banking system. RBI indicated that recently the Commercial Banking System’s Gross Non-Performing Assets are 9.1% of advances in March 2019. This was 8.2% in March 2020. The Gross Non-Performing Assets have become doubled in the last seven years.

BANK	Gross NPA as on 30/06/2014	Gross NPA as on 30/09/2021	% increases
Bank of Baroda	15,879	46,382	192%
Bank of India	11,160	40,915	267%
Bank of Maharastra	3,716	6,403	72%
Canara Bank	12,647	52,494	315%
Central Bank of India	11,449	27,252	138%
Indian Bank	12,013	36,081	200%
Indian Overseas Bank	8,781	13,935	59%
Punjab and Sind Bank	3,010	9,823	226%
Punjab National Bank	32,416	98,484	204%
State Bank of India	74,482	1,20,811	62%
Uco Bank	5,982	10,182	70%
Union Bank of India	22,199	77,781	250%
IDBI Bank	10,762	.-	
Total	2,24,496	5,40,543	

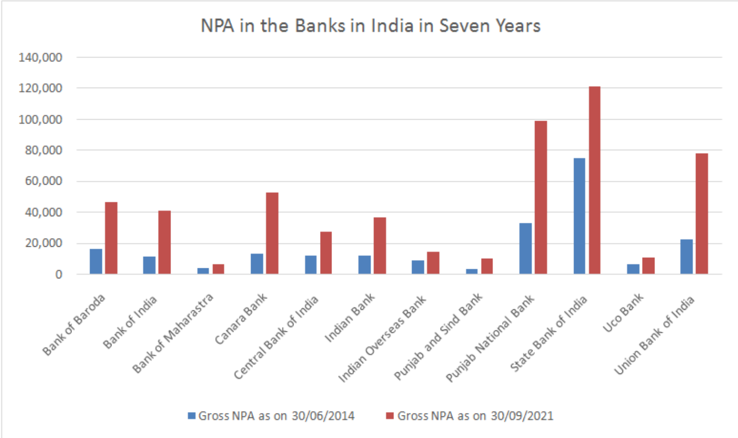

Fig:1 NPA in the Banks in India in Seven Years

In landing operations, the Indian Banks have low profitability, irregularity; rising operation costs, etc. have led to decreasing.

With this objective of Inclusive Indian Growth in the focus, the Indian government conceived about the 'Small Finance Banks (SFBs)' and these banks are expected to on rural/urban banking, priority sector, and micro and small enterprises. Additionally, these Banks will bring more unbanked people or sections of society under the ambit of the banking system. These SFBs have been introduced in the Indian Banking Structure in the year 2015. The aims of the Indian government are to strengthen financial inclusion and extend basic banking services in the country.

The primary objective of the SFBs is to provide basic banking services to uncovered and conventionally underserved sections of society. The SFBs are allowed to accept deposits from customers and lend money to people. These aim to strengthen financial inclusion and to promote small business units, small and marginal farmers, micro and small industries, and unorganized sector entities.

Following are the RBI's guidelines for SFBs:

- Minimum paid-up equity capital requirement of Rs 100 crore only.
- Every small finance bank must have the words - Small Finance Bank - in its name.
- Small Finance banks can carry out financial services like distribution of mutual fund units, insurance products, pension products, and so on, but not without prior approval from the RBI.
- A fundamental requirement is that it must have 25% of its branches set up in unbanked areas.

And, the following are the actions to be avoided for SFBs:

- SFBs cannot lend to big corporates and groups.
- A small bank cannot transform into a full-fledged bank without RBI's approval.
- It cannot set up subsidiaries to undertake non-banking financial services activities.
- Not allowed to be a business correspondent of any bank.

2. Impact analysis

Move of giving licenses to small finance banks is a major step towards pushing financial inclusion in the country. The main target for the small finance banks is small businesses and low-income households by providing them financial services at low transaction costs. It is uneconomical for big banks to open branches in every village, but with smaller units that have wider reach and penetration, a small unit bank can provide a low-cost platform for taking banking services to every citizen. This will include people who mainly transact in cash to take their first step into the banking system and also slowly accelerate India's journey as a cashless economy.

It is expected that the cost of banking will come down due to competition from small banks. At present, private banks like ICICI, HDFC, Axis, etc. are making unreasonably and unjustifiable huge profits by collecting funds at lower costs from savings accounts and current accounts (CASA deposits account for 40% of bank deposits) and lending it to small borrowers at much higher rates. Here, the small finance banks will get a big chunk from this by providing higher interest rates on deposits and giving credit (small finance banks only) at lower rates. This will increase competition and lower-income groups and small businesses will be benefitted the most.

For low-income customers, the real attraction will not be higher interest rates, but the convenience of carrying out banking transactions with ease, comfort, and security. Also, as SFBS will mainly have poor people as a borrower of small money, there are very few chances of huge defaults. Poor people will also get benefitted as a borrower, as SFBs will expand access to cheap funds.

Furthermore, there is a chance for us also to eliminate the black money from a large part of the financial system by reducing cash transactions and encouraging people for the usage of the money through banks. This is achievable within the next 5 to 10 years with investment in financial literacy and educating urban and rural poor citizens, especially women.

The SFBs will reduce dependency on cash and will increase banking commerce, as banks can offer a variety of payment options. It will also transform our subsidy and social welfare schemes. With the usage of the Aadhaar card, Jan Dhan Yojana and SFBs Indian government will be enabled to provide direct subsidy through bank account transfer.

At present, there is a large unmet need for those at the bottom of the population pyramid not just to have a bank account but also to get a low credit/loan to run their small businesses and to move out of the heart-wrenching poverty. Different models of the rural and cooperative banks have largely failed to deliver these. However, the organizations that are selected for small finance banks have successfully done this job of giving/lending/-crediting small amounts and they know their borrowers' needs. Hence, we believe that they shall have high chances of success.

We believe that the SFBs will extend formal financial access to poor people and small enterprises that are currently dependent on high-cost unorganized sector lending. According to an RBI estimate, around 90 percent of small enterprises do not have access to formal financial institutions. Because of this, the SFBs will be a big and transformative step towards full financial inclusion.

In India, at present, the commercial banks largely fund big and medium industries or give loans for home, education or vehicle purposes. But it is almost impossible for the diamond cutting units or restaurants or any other small enterprises to get working capital funding. The SFBs are expected to fill this gap. The RBI expects them to be high technology-driven and low-cost operators, and these will bring new innovations in the industry.

It is expected that the customer base of commercial banks will reduce due to the shifting of savings account money into SFBs and because of this the low-cost deposits of banks will reduce. Due to this shift, the commercial banks' regular fee incomes (i.e. cash transfers, cheques withdrawals, and fees for making demand drafts or ATM transactions, etc.) will reduce. At present, the commercial banks park 21.5% of their deposits as Statutory Liquidity Ratio (SLR). This gives the government a ready market for borrowings. However, this also encourages lazy banking. As the SFBs will have to invest some of their deposits in G-sec and when they become large and successful, then it will also reduce the Statutory Liquidity Ratio (SLR) burden on commercial banks.
Finally, the names of the approved SFBs' licensees are listed in Table 1.

Table no 2: Names of the approved SFBs' licensees as per RBI's approvals.

Original licensee/promoter	**Commenced**	**Bank name**	**Headquarters**
Ujjivan Financial Services Pvt Ltd	1 February 2017	Ujjivan Small Finance Bank	Bangalore
Janalakshmi Financial Services Pvt Ltd	29 March 2018	Jana Small Finance Bank	Bangalore
Equitas Holdings Pvt Ltd	5 September 2016	Equitas Small Finance Bank	Chennai
Au Financiers India Ltd	19 April 2017	AU Small Finance Bank	Jaipur
Capital Local Area Bank Ltd	24 April 2016	Capital Small Finance Bank	Jalandhar
DishaMicrofinPvt Ltd	21 July 2017	Fincare Small Finance Bank	Bangalore
ESAF Microfinance	17 March 2017	ESAF Small Finance Bank	Reg: Chennai, Corp: Thrissur
RGVN North East Microfinance Ltd	17 October 2017	North East Small Finance Bank	Guwahati
Suryoday Microfinance Pvt Ltd	23 January 2017	Suryoday Small Finance Bank	Navi Mumbai
Utkarsh Microfinance Pvt Ltd	23 January 2017	Utkarsh Small Finance Bank	Varanasi

II. Conclusions

We are confident that the inclusion of SFBs will usher in a significant shift in the Indian banking system following bank nationalization. This would ensure that the Indian banking sector becomes more competitive and inclusive for both borrowers and depositors, hence making banking more accessible to the general public. With comprehensive and efficient financial inclusion, poor Indians would have a proper mechanism to assist their efforts to break free from the fatal trap of poverty, implying that the era of poor consumers has finally arrived in India.

References

[1]. "RBI issues final norms for payment, small finance banks". Zee News. 28 November 2014.
[2]. "Guidelines for Licensing of Small Finance Banks in the Private Sector". Reserve Bank of India, 2014.
[3]. "RBI releases Draft Guidelines for Licensing of Payments Banks and Small Banks". Reserve Bank of India, 17 July 2014.

[4]. "RBI releases applicants list of payment, small bank license". The Hindu Business Line. 4 February 2015.
[5]. https://timesofindia.indiatimes.com/business/india-business/gross-npas-of-public-sector-banks-double-in-last-seven-years-sbi-tops-list/articleshow/88316357.cms
[6]. https://www.investopedia.com/terms/n/non-performing-assets.asp
[7]. https://rbi.org.in/scripts/NotificationUser.aspx?Id=5090&Mode=0
[8]. https://rbi.org.in/
[9]. https://www.investopedia.com/articles/investing/112714/regulations-govern-banking-india.asp#:~:text=Banks%20in%20India%20are%20required,95%25%20of%20the%20required%20reserves.
[10]. https://rbi.org.in/Scripts/OccasionalPublications.aspx?head=Banking%20Regulation%20Act
[11]. Kasali, Taofeek Aremu. 2020. Influence of Microfinance Intervention on Rural Poverty Alleviation in South-west Nigeria: An Application of Propensity Score Marching Technique. *Asian Journal of Economics and Finance* 2: 411–22.
[12]. Khan, Arshad A., Sufyan U. Khan, Shah Fahad, Muhammad A. S. Ali, Aftab Khan, and Jianchao Luo. 2020. Microfinance and poverty reduction: New evidence from Pakistan. *International Journal of Finance & Economics* 26: 4723–33.
[13]. Khandker, Shahidur R. 2003. Microfinance and Poverty: Evidence Using Panel Data from Bangladesh. *The World Bank Economic Review* 19: 263–86.
[14]. Kim, Nguyen Thien, and Nguyen Minh Sang. 2018. Evaluating the efficiency of microfinance institutions in Vietnam and the Impact of this efficiency on poverty reduction. In *Global Tensions in Financial Markets*. Bingley: Emerald Publishing Limited.
[15]. Manzoor, Faiza, Longbao Wei, Mohammad Nurunnabi, and Qazi Abdul Subhan. 2019. Role of SME in poverty alleviation in SAARC via panel data analysis. *Sustainability* 11: 6480.
[16]. Matzana, Velisaria, Aikaterina Oikonomou, and Michael Polemis. 2022. Tourism Activity as an Engine of Growth: Lessons Learned from the European Union. *Journal of Risk and Financial Management* 15: 177.
[17]. Mhlanga, David, Steven Henry Dunga, and Tankiso Moloi. 2020. Financial inclusion and poverty alleviation among smallholder farmers in Zimbabwe. *Eurasian Journal of Economics and Finance* 8: 168–82.
[18]. Oshora, Betgilu, Goshu Desalegn, Eva Gorgenyi-Hegyes, Maria Fekete-Farkas, and Zoltan Zeman. 2021. Determinants of Financial Inclusion in Small and Medium Enterprises: Evidence from Ethiopia. *Journal of Risk and Financial Management* 14: 286.
[19]. Pham, Duong Phuong Thao, and Thi Cam Ha Huynh. 2020. The impact of trade credit investment on manufacturing firms' profitability: Evidence from Vietnam. *Acta Universitatis Agriculturae et Silviculturae Mendelianae Brunensis* 68: 775–96.
[20]. Samer, Sayed, Izaidin Majid, Syaiful Rizal, Mohd Razali Muhamad, and Nlizwa Rashid. 2015. The impact of microfinance on poverty reduction: Empirical evidence from Malaysian perspective. *Procedia-Social and Behavioral Sciences* 195: 721–28.
[21]. Simatele, Munacinga, and Martin Kabange. 2022. Financial Inclusion and Intersectionality: A Case of Business Funding in the South African Informal Sector. *Journal of Risk and Financial Management* 15: 380.
[22]. Winarno, S., Mustofa Usman, and D. Kurniasari. 2021. Application of Vector Error Correction Model (VECM) and Impulse Response Function for Daily Stock Prices. In *Journal of Physics: Conference Series*. Bristol: IOP Publishing, p. 012016.
[23]. Zainal, Nurazilah, Annuar Md Nassir, Fakarudin Kamarudin, S. H. Law, Fadzlan Sufian, and Hafezali Iqbal Hussain. 2019. The social role of microfinance institutions in poverty eradication: Evidence from ASEAN-5 countries. *Internafional Journal of Innovafion, Creafivity and Change* 5: 1551–76.
[24]. Zezza, Alberto, and Luca Tasciotti. 2010. Urban agriculture, poverty, and food security: Empirical evidence from a sample of developing countries. *Food Policy* 35: 265–73.
[25]. ZIMSTAT. 2019. *Zimbabwe Poverty Update 2017–19*. ZIMSTAT and World Bank: Available online: https://www.zimstat.co.zw/wp-content/uploads/publications/Income/Finance/Zimbabwe_Poverty_Updat_2017_19_Final.pdf (accessed on 15 February 2022).
[26]. ZIMSTAT. 2020. Zimbabwe Poverty Datum lines 2020. Available online: http://-www.zimstat.co.zw/-wp-content/uploads/-2021/01/Poverty-Leaf-Logo-December-2020.pdf (accessed on 15 February 2022).