

A Contemporary study of microfinance: A study for India's underprivileged

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Abstract: PM Narendra Modi's ambitious plan of "banking for all" to end financial untouchability is expected to reach out to 75 million people, almost 65% of the Indian population. Micro financing is the buzz word today. Mohammed Yunus laid the foundation of micro finance through Grameen Bank, Bangladesh in 1976. Microfinance Institutions (MFIs) in India exist under various legal structures such as NGOs, Section 25 companies and Non-Banking Financial Companies (NBFCs). The banking system of the country including commercial Banks and Regional Rural Banks (RRBs) and other sources such as cooperative societies and other large lenders have played an important role in the development of the sector by providing refinance facility to MFIs. Self help groups (SHGs) have been utilized by banks to enable reach to the most marginalized of their target consumers.

Financial inclusion has emerged as a major policy objective in the country; Microfinance has become a medium of extending financial services to unbanked sections of population through the Jan Dhan Yojana. Financial literacy too plays an important role as people have to be informed about how to use financial services. Transparent pricing plays a crucial role as it increases fair competitiveness and the borrowers don't end up borrowing more than they can repay. Reforms in terms of proper regulations, offering complete financial products, entering rural markets, technology to reduce operation costs, can help turn the dream of achieving universal digital financial inclusion into reality and give a boost to the Indian economy. The paper trails the advent of financial inclusion in India, understands the current status, analyzes the gaps and reviews the reforms the present government has brought about to boost India's rural economy.

Key words: Financial inclusion, microfinance, financial literacy, rural economy.

I. Introduction:

Microfinance can be defined as the provision or the source of providing financial services to those sections of the society to whom these services are not available. This would include people from the lower end of the economic spectrum, the so called 'bottom of the pyramid'. According to Patrick Meagher, "Microfinance is defined as lending small amounts of money for short periods with frequent repayments" (Meagher 2002:7). For Van Maanen, "Microfinance is banking the unbankables, bringing credit, savings and other essential financial services within the reach of millions of people who are too poor to be served by regular banks, in most cases because they are unable to offer sufficient collateral" (Maanen 2004:17). Micro finance acts as the means to financial security for them. In a country like India with almost 30% (more than 360 million) people still below poverty line and according to latest census figures, more than 70% or 840 million people living in rural areas with little or no access to formal banking and other financial services, microfinance has a big role to play in order to bridge this gap

The history of micro financing can be traced back as long to the middle of the 1800s when the theorist Lysander Spooner was writing over the benefits from small credits to entrepreneurs and farmers as a way getting the people out of poverty. The current day use of the expression microfinancing has its roots in the 1970s when organizations, such as Grameen Bank of Bangladesh with the microfinance pioneer Mohammad Yunus, were starting and shaping the modern industry of microfinance.

In the Indian context, true expansion of financial services in India started with the nationalization of all banks in the country during the late 1960s. This was reinforced with the establishment of Regional Rural Banks (RRBs) in 1976, and directed credit became the mantra of the Indian financial sector. The microfinance sector in India gained real impetus with the establishment of the National Bank for Agriculture and Rural Development (NABARD) in 1982. From humble beginnings, the sector has grown significantly over the years to become a multi-billion dollar industry, with bodies such as the Small Industries Development Bank of India and the NABARD devoting significant financial resources to microfinance. Today, the top five private sector MFIs reach more than 20 million clients in nearly every state in India and many Indian MFIs have been recognized as global leaders in the industry.

Successful microfinance stories from around the world:

There are many successful micro finance stories across the globe but no study is complete without mentioning Muhammad Yunus and Grameen Bank. Yunus, widely credited as the inventor of microfinance started the Grameen Bank in 1976 (formally authorized in 1983) with his own money and made it into one of the largest microfinance movements in the world. He also shared the 2006 Nobel Peace Prize along with Grameen Bank. As of Oct, 2011 the bank has more than 8.349 million borrowers, 97% of whom are women and has disbursed loans worth \$17.733 bn since its inception to Sept, 2015. The Grameen model has been replicated across more than 40 countries.

Apart from this there are many other success stories in this sector. Some of them are ASA, Bangladesh. Banco Do Nordeste. Brazil and FONDEP Micro Credit in Morocco.

SHG-Bank Linkage Programme

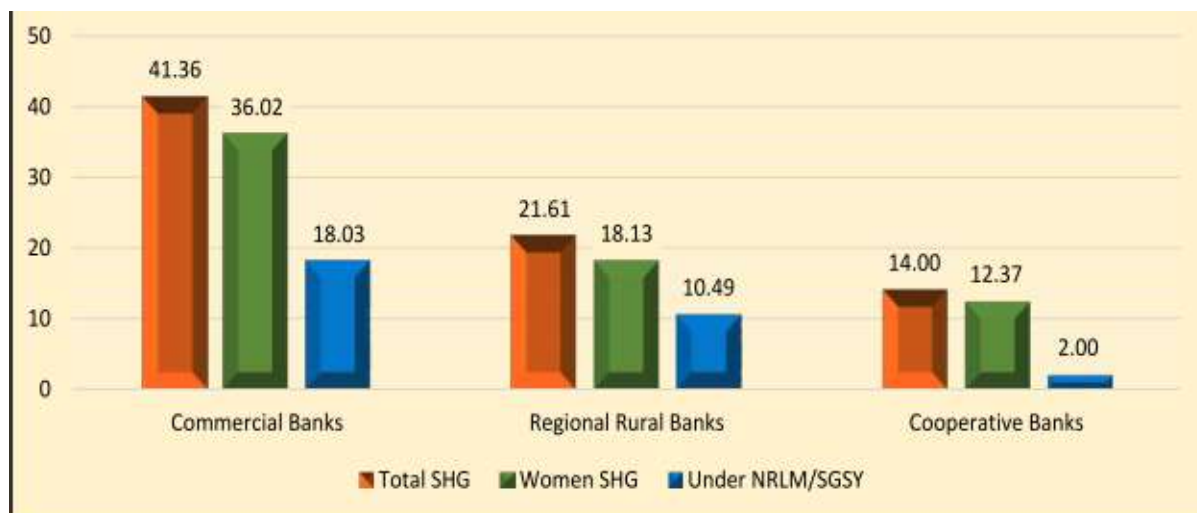
Micro finance in India was majorly dependent on subsidies and the concept of providing finance to the people at exceedingly low rates of interest. It also inculcated a culture of increased tolerance for loan defaults, waivers and lax appraisals and monitoring of loans. In this backdrop, informal groups of people came into existence. These groups known as Self Help Groups (SHGs) were a way for people to come together in order to pool their savings and dispense small unsecured loans. NABARD recognized the potential of these groups and realized that they are constrained only due to the meagreness of their financial resources. In order to overcome this problem the concept of linking the groups to a bank was to overcome financial constraints was designed, popularly known as the SHG Bank Linkage programme. It was started as a pilot project in 1992 and has come a long way since then. As of March 2011, there were 7.4 million SHGs under this scheme covering over 10 crore households with savings balance of over Rs 70 billion (7000 crores). About 49 lakh of these SHGs have also accessed bank credit and have over Rs 31,000 crore as outstanding credit from the banking system. In other words, the SHG-BLP has so far been the most preferred and viable model for financial inclusion of the hitherto unreached poor.

Figure 1: SHG-Bank Linkage Highlights (₹ Crores)



Source: Status of Microfinance in India report, 2014-15, NABARD

Figure 2: Agency-wise distribution of SHG savings (No. in lakhs)



Source: Status of Microfinance in India report, 2014-15, NABARD

Gaps in govt programs and need for microfinance:

Even after 68 years of gaining independence, India has still not managed to achieve financial inclusion for all its citizens. In fact almost half of the people in the country do not own a bank account and don't have access to even the most basic of financial services. Most of these people belong to the economically weaker sections of the society residing in both rural and urban areas. Most of these people were dependent on traditional moneylenders or 'sahukars' in order to meet their credit needs who charge exorbitant rates of interest which can go up to 200% at times. MFIs have helped to fill this gap in a big way. They have provided these people with affordable credit facilities along with other facilities such as savings, insurance, remittances, financial education and non financial services such as individual training and counselling in order to start their own business. Microfinance has also contributed a great deal to poverty alleviation. All the governments have had poverty alleviation as one of their objectives but had very limited success in achieving the same. Over the years, it has been observed that people who have availed micro finance have managed to increase their income and in turn their standard of living.

Financial Inclusion – Role of Indian banks in reaching out to the unbanked

Policy makers have been pushing for reforms due to 3 pressing needs:

1. Create a platform to inculcate the habit of saving

India has been an economy with a high savings rate. But a large part of this savings does not find its way into the financial system of the country due to the lack of proper banking facilities for millions of households. These people have had to depend on traditional means of savings such as bullion, land and money saved up in their houses. Presence of comprehensive banking services and financial inclusion for all will help to bridge this gap and bring at least some portion of this money into the formal financial system of the country and help in capital formation.

2. Providing formal credit avenues

As stated earlier in the paper, most of the population at the bottom of the pyramid which lacks access to formal banking channels has to depend either on family and friends or moneylenders for their credit needs. Availability of proper banking facilities will help to provide them with easier, more transparent and substantially cheaper credit which can help boost their entrepreneurial spirit.

3. Plug gaps and leaks in public subsidies and welfare programs

Until very recently, most of the benefits provided by the state to the people were done either through subsidizing products or making cash payments. This left a huge scope for corrupt practices to develop and hinder the motive of these benefits. With the development of the banking system and financial inclusion these benefits can be provided through direct cash transfers through bank accounts. The Government is pushing for this move to be implemented as this would help in reducing the subsidy bill and provide relief only to the real

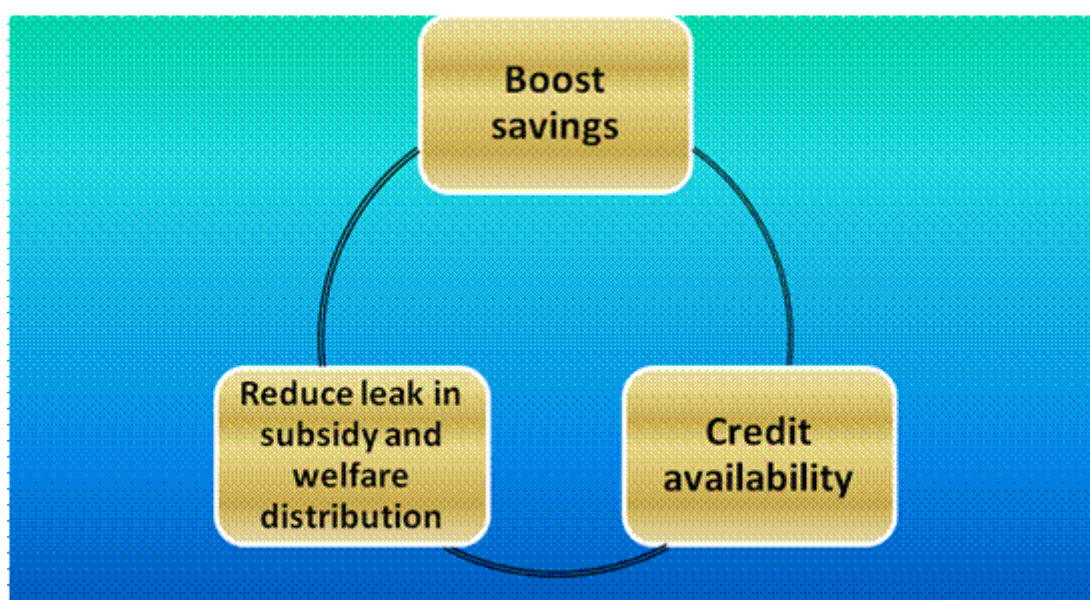
beneficiaries. All these efforts will require an efficient, affordable and transparent banking system that can reach out to all.

□ Financial Inclusion data –India

Key Indicators

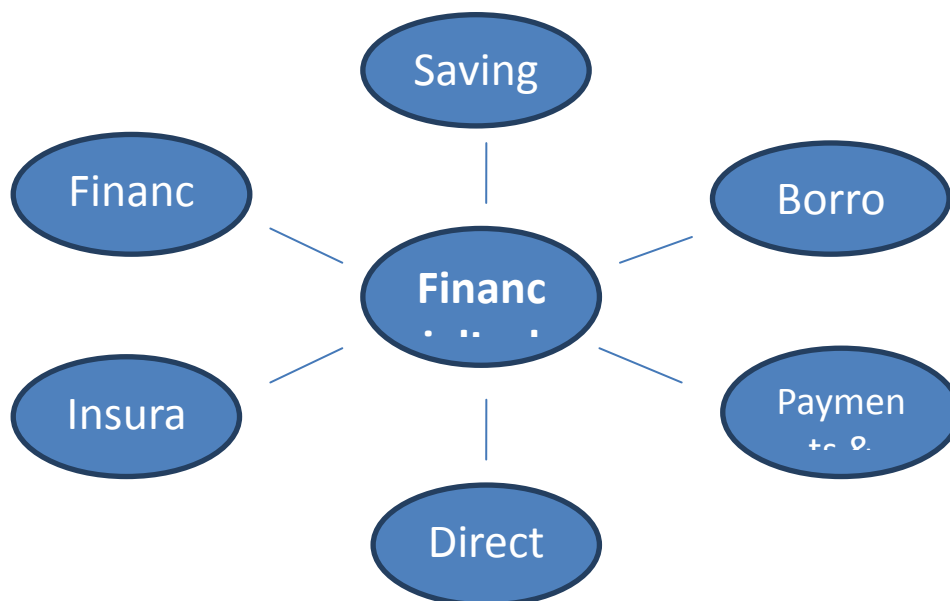


Source: <http://datatopics.worldbank.org/financialinclusion/country/india>



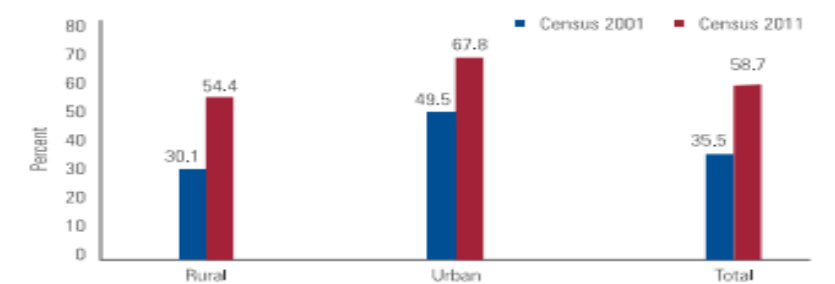
Jan DhanYojana and its effect on micro finance:

The Pradhan Mantri Jan DhanYojana (**PMJDY**) official website (www.pmjdy.gov.in) defines the PMJDY as a ‘National Mission for Financial Inclusion to ensure access to financial services, namely, Banking/ Savings & Deposit Accounts, Remittance, Credit, Insurance, Pension and financial literacy in an affordable manner’. Financial inclusion or inclusive financing is the delivery of financial products and services to people to whom these are not available at an affordable cost. These people generally belong to the economically and socially weaker sections of the population and have little or no access to the financial system of the country.



The scheme was launched in order to facilitate financial inclusion in India. The scope for the scheme can be understood from the fact that out of the **25 crore** households in the country, more than **10 crore** did not have a bank account. 44% households in the rural areas and 33% in the urban areas did not have a bank account. This meant that almost half of the population of the country was not linked to the financial system and were dependent on moneylenders and sahu-kars in order to meet their financial needs.

Availability of Banking Services



Source: http://pmjdy.gov.in/Pdf/PMJDY_BROCHURE_ENG.pdf

II. Objectives

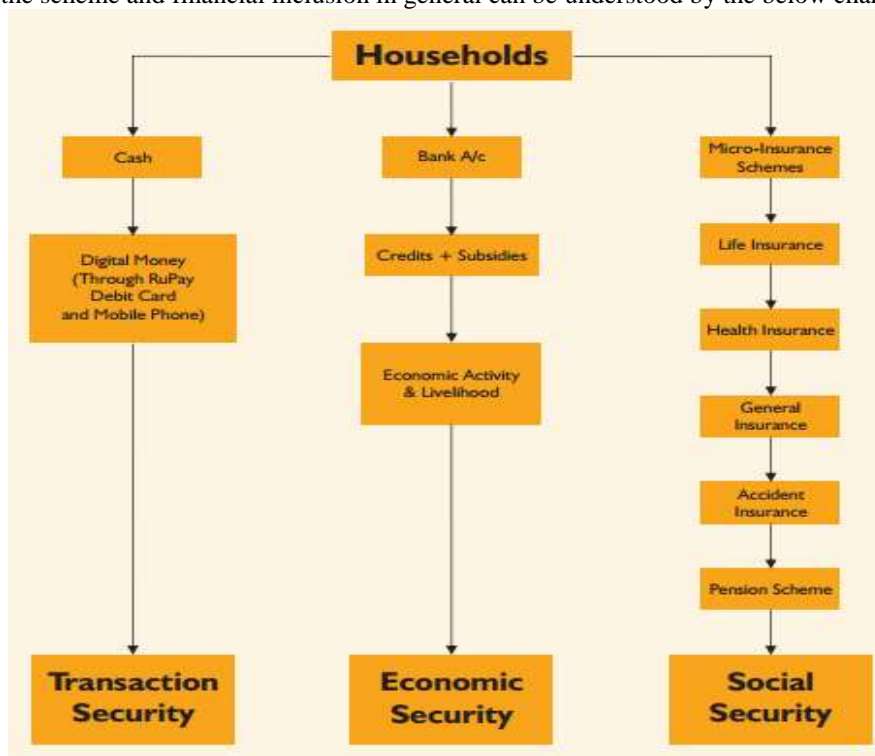
The major objectives of the mission can be seen from the below:



Source: http://pmjdy.gov.in/Pdf/PMJDY_BROCHURE_ENG.pdf

Impact:

The impact of the scheme and financial inclusion in general can be understood by the below chart:



Source: http://www.pmjdy.gov.in/Pdf/PMJDY_BROCHURE_ENG.pdf

Pradhan Mantri Jan - Dhan Yojana (Accounts Opened As on 19.08.2015)

Disclaimer: Information is based upon the data as submitted by different banks/SLBCs
 (All Figures in Crores)

S.No		No Of Accounts			No Of Rupay Debit Cards	Balance In Accounts (In Rupees Crores)	% of Zero Balance Accounts
		Rural	Urban	Total			
1	Public Sector Bank	7.61	6.25	13.86	12.7	17758.39	44.95
2	Rural Regional Bank	2.71	0.46	3.17	2.33	3807.15	47.00
3	Private Banks	0.42	0.29	0.7	0.62	1081.8	45.71
	Total	10.74	7	17.74	15.65	22647.35	45.32

Source: <http://www.pmjdy.gov.in/account-statistics-country.aspx>

As can be seen from the table above, the unrealized potential of the weaker sections of the Indian society is immense. The scheme targets to utilize this potential for their betterment. It is a perfect example to show the power of collective savings and the potential of the economically weaker sections of the country. As can be seen from the above table, a total amount of Rs 22,647 crores was deposited in the bank accounts opened under this scheme which could further be used for credit creation.

Challenges facing the microfinance sector in India:

It is undeniable that micro finance has had a great impact on the lives of poor Indians and that it has been one of the major contributors towards the goal of poverty eradication, but it has still not managed to have

its desired impact. There are several challenges facing the sector. Some of the major challenges are discussed below:

Financial Illiteracy:

Financial illiteracy is one of the biggest challenges being faced by the microfinance industry. In most cases, the target clients of MFIs of SHGs are people who are either illiterate or have a very basic level of education which makes them highly ignorant about the financial system. Although most of the SHGs and MFIs claim to have their awareness programs but these are rarely successful.

Case Study: Project Finlit by Enactus Somaiya Social Cell

Project Finlit (Financial Literacy) was started by the Somaiya Social Cell in 2008 with the objective to impart awareness about finance related topics whose knowledge is essential for personal and community development. The project conducted in association with IIFL targets a diverse set of students including school going children, differently able people and people undergoing vocational trainings and has close to 500 students as of now. The project focuses on providing both theoretical and practical learning through classroom teachings, bank visits,

Deepening of outreach:

Even though MFIs and SHGs have been able to reach a large number of people, they still have not managed to reach the poorest of the poor. Most of the efforts are utilized for people who are just below the poverty line and can be upgraded by increasing the availability of credit. However, there is little effort made to uplift people who are at the absolute bottom as these are seen as very high risk and are left to survive on Government subsidies.

The problem of multiple lending :

With an increasing number of MFIs and expansion of operations, the issue of overlapping membership and potential over-indebtedness is beginning to emerge, particularly in certain areas of the country. This is an area that needs more research, and clearer guidelines for the sector on appropriate practice.

High NPAs in the sector:

The overall NPAs under the SHG-Bank linkage programme for the year 2014-15 is 7.40% with the maximum NPAs in rural areas. A very small minority of people undertake any new economic activity after taking a loan. Majority of such loans are utilized by the people for consumption purposes. Political, social and economic factors also affect the repayment rates for these loans.

Non Performing assets of Self Help Groups

(Amount ₹ crore)

Year	NPA of Loans to All SHGs		NPAs against NRLM/SGSY		NPAs against other than NRLM / SGSY	
	Amount of Gross NPAs	NPA %	Amount of Gross NPAs	NPA %	Amount of Gross NPAs	NPA %
2012-13	2786.90	7.08	859.70	9.39	1927.20	6.38
2013-14	2932.70	6.83	975.20	9.58	1957.50	5.98
2014-15	3814.70	7.40	1720.92	8.71	2093.70	6.58

Source: Status of Microfinance in India report, 2014-15, NABARD

Dropouts and migration of group members:

Most of the microfinance loans are disbursed on the group lending concept under which the entire group is responsible for the loan taken by one of its members. The past record of the group plays an important part under both the SHG Bank linkage and MFIs in order to secure credit. The two major problems related to groups are dropouts and migration of members. A dropout happens when a member of the group leaves the group and a migration refers to movement of the member from one group to another. This affects the continuity of the group and diminishes its record in the eyes of the lenders which can hinder their ability to borrow.

Recommendations

1. Forming of regulations – With the new government policies, the microfinance sector is expected to see a major thrust, hence proper policies are needed to protect the interest of the stake holders and promote growth.
2. Enhancing bargaining power through transparent pricing – A common practice for charging interest across the micro finance industry so that the buyer gets to understand the different products and services and make a comparative choice.
3. Use of technology to reduce operations cost: Use of development of common MIS and other software technology to reduce operational costs for micro financing.
4. Reach out to the rural population – New branches of micro finance institutions must be opened in the interiors of rural India
5. Encouraging financial literacy – Financial institutions can align their Corporate Social Responsibility programs to encourage financial literacy campaigns which should go beyond the beneficiary learning to put in her/his signature.
6. Offering a complete range of products and services – Micro financing institutions should provide complete range of products including credit, savings, remittance, financial advice and also non-financial services like training and support.
7. Monitoring of services: The quality of the services provided has to be monitored and supervised.

III. Conclusion:

Microfinance is the need of the hour. It is one of the strongest tools available to fight poverty and uplift millions of Indians to a better standard of life. With more than 10 million young Indians joining the workforce every year, microfinance can be of immense use to provide gainful employment to some of them. Financial inclusion and financial literacy through digital means can change the way rural India banks. Inclusive growth is possible when all the parameters surrounding these go hand in hand. Ambitious projects like the Jan Dhan yojana etc have given a boost to the rural economy but the entire efforts of the corporates, banks and the government should be together geared towards development, only then will India rise and India shine.

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