MICRO FINANCE AND POVERTY ERADICATION IN INDIA

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Abstract

The poverty eradication has been the primary concern of the State and its planners since long time. These poverty alleviation efforts through State driven credit supply schemes produced only sub optimal results. In order to get effective use of these programmes, sufficient arrangements shall be made for provision and delivery of credit to the rural poor. The failure of the formal credit institutions in meeting the credit requirements of rural poor has been the major reason for innovations in micro finance. The most complex problem in rural credit delivery system is serving small loans and making available the credit to the unreached and uncared so far, that too, an adequate amount at the right time with minimum documentation requirements. In this direction, a non – formal agency for credit supply to the poor, in the name of Self – Help Group (SHG) could emerge as a promising partner to the formal credit system. Thus, the SHGs formed as instruments for the socio – economic development of the rural people. It shows that access and efficient provision of microcredit can enable the poor to smooth their consumption, better manage their risks better, gradually build their assets, develop their micro enterprises, enhance their income earning capacity and enjoy an improved quality of life. Microfinance services can also contribute to the improvement of resource allocation, promotion of markets, and adoption of better technology; thus, Microfinance helps to promote economic growth and development.

***Keywords**: poverty, rural poor, Self – Help Group, Microfinance, micro enterprises, NABARD*

Introduction

Microfinance is the provision of financial services to low-income clients, including consumers and the self-employed, who traditionally lack access to banking and related services. More broadly, it is a movement whose object is “a world in which as many poor and near-poor households as possible have permanent access to an appropriate range of high quality financial services, including not just credit but also savings, insurance, and fund transfers.” Those who promote microfinance generally believe that such access will help poor people out of poverty. Microfinance is considered as a tool for socio-economic development and can be clearly distinguished from charity. Families who are destitute or so poor they are unlikely to be able to generate the cash flow required to repay a loan, should be recipients of charity. Others are best served by financial institutions.

The microfinance industry in India emerged in the 1970’s to provide poor with access to credit. It has become responsible to fulfil the small financial needs of the core poor of the society. This industry has broken the centuries old social customs of seclusion of people and highly successful in bringing them to the near main stream. To support that microfinance can be an important tool to fight poverty, the UN declared 2005 to be the international year of Micro Credit. The Noble committee also viewed that microfinance can help the people to break of poverty. Poverty alleviation is considered to be socially desirable goal in any developing country. The inclusive micro finance policy wherein the core poor have can easy access where the poor could access savings, credit, insurance and other services is making the core poor to come art of strong clutches of poverty hold.

Micro Finance Approaches

Indian micro finance is dominated by two operational approaches viz, Self – Help

Groups (SHGs) and Micro Finance Institutions (MFIs) in addition to a few cooperative forms. The first approach is popularly known as SHG-Bank linkage model. This model is the dominant model, initiated by the NABARD through the SHG- Bank linkage programme in the early 1990s. Today the SHG model also links the informal groups of women to the mainstream system and it has the largest outreach to micro financial clients in the world.

The second approach also called financing through MFIs is the emerging model. This model emerged in the late 1990s to harness social and commercial funds available for open – lending to clients. Today there are over 1,000 Indian MFIs. These institutions assume the responsibility of making available much needed micro credit to the poor section of the society. Generally MFIs /NGOs take on the additional role of financial intermediaries. In areas where the formal baking system faces constraints, the NGO are encouraged to approach a suitable bank for bulk loan assistance.

Role of Microfinance in Poverty Eradication

Microfinance is about providing financial services to the poor who are not served by the conventional formal financial institutions - it is about extending the frontiers of financial service provision. The provision of such financial services requires innovative delivery channels and methodologies. The needs for financial services that allow people to both take advantage of opportunities and better management of their resources. Microfinance can be one effective tool amongst many for poverty alleviation. However, it should be used with caution -despite recent claims, the equation between microfinance and poverty alleviation is not straight-forward, because poverty is a complex phenomenon and many constraints that the poor in general have to cope with. We need to understand when and in what form microfinance is appropriate for the poorest; the delivery channel, methodology and products offered are all inter-linked and in turn affect the prospect and promise of poverty alleviation.

Access to formal banking services is difficult for the poor. The main problem the poor have to take when trying to acquire loans from formal financial institutions, is the demand for collateral asked by these institutions. In addition, the process of acquiring a loan entails many bureaucratic procedures, which lead to extra transaction costs for the poor. Formal financial institutions are not motivated to lend money to them. In general, formal financial institutions show a preference for urban over rural sectors, large-scale over small scale transactions, and non-agricultural over agricultural loans. Formal financial institutions have little incentives to lend to the rural poor for the following reasons.

- **Administrable Difficulties**
  Small rural farmers often live geographically scattered, in areas with poor communication facilities, making loan administration difficult.
- **Systematic Risks**
  Agricultural production is associated with some systemic risks, such as drought and floods, which is reflected in a high covariance of local incomes.

- **Lack of Information**
  The absence of standardized information, Standard lending tools, such as financial statements or credit histories, do not exist in these areas.
- **Repayment Problems**
  The repayment of working capital may be required only once a year for example during the harvest season. On the other hand, access to informal loans is relatively easy, convenient, and available locally to low income households for the following reasons:-

Informal moneylenders use interlinked credit contracts to reduce default risk such as development of business relationship with the clients.

a. Informal moneylenders have local information which helps them to appraise credit needs and credit worthiness of the client.
b. Informal moneylenders are considering the needs and requirements of clients even for small amount of loan.
c. Informal money lenders will profit from social sanctions such as those that may exist among members of a family. These sanctions may serve as a substitute for legal enforcement.
d. Informal money lenders use specific incentives to stimulate repayment, such as repeat lending to borrowers who repay promptly, with gradually increasing loan size.

Despite the fact that many rural poor acquire their loans from the informal financial sector in rural areas of developing countries; the sector has some basic limitations. A common feature of many rural communities is that much of the local information does not flow freely; it tends to be segmented and circulates only within specific groups. Usually the informal credit market is based on local economies and is thus limited by local wealth constraints and the covariant risks of the local environment. Since most of the world's poor do not have access to basic financial services that would help them manage their assets and generate income. To overcome poverty, they need to be able to borrow, save, and invest, and to protect their families against adversity. Another shortcoming of the two financial sectors in developing countries is their inability to satisfy the credit needs of the poor that has led to the new development of microfinance. Microfinance is believed to be able to reduce the above-mentioned inadequacies of formal and informal financial institutions and is emerging as an important credit partner to the poor in the developing world.

Progress in Micro Finance

Credit lines to SHGs are critically limited, as they are based on a certain multiple of SHG member's savings accounts within banks. While the cumulative savings of SHGs could serve as a low- cost source of funds for on – lending, their potential is limited by the lack of aggregated savings across SHGs. Commercial equity investments are not available to for SHGs due to their informal status.

MFI-Banks Linkage Programme

Micro Finance Institutions (MFIs) act as an important conduit for extending financial services to the microfinance sector in the country by raising resources from Banks and other institutions and extending loans to individuals or members of SHGs/ JLGs. The MFIs have been allowed to mobilize resources through various ways including obtaining of bulk loans from Banks/ other Financial Institutions. Though most of the MFIs entered the microfinance arena only after the SHG-Bank linkage programme was well entrenched, business of these institutions grew at a much faster pace than the former. MFIs are more aggressive and innovative in reaching out to the rural poor with well-oiled distribution channels as compare to the formal banking system. Post Andhra crisis, the Reserve Bank of India has notified guidelines for the lending operations of MFIs based on the Malegam Committee recommendations. A new class of financial organisations named as NBFC–MFIs have been created subject to satisfying certain conditions regarding the capital to be employed, lending to members, cap on interest to be charged and margin to be retained, etc. The loans extended to the MFIs by banks qualify for priority sector category. RBI's upgraded regulations and guidelines on NBFC-MFIs and inclusion of loans to MFIs by banks under priority sector have resulted in phenomenal growth of MFIs during the last three years.

Table 1 Progress under MFI-Bank Linkage

(Amount Crore)

Particulars	2013-2014		2014-2015		2015-2016	
	No.MFIs	Amount	No.MFIs	Amount	No.MFIs	Amount
Loans disbursed by banks to MFIs	545	10282.49 (31.16%)	581	15190.13(47.73%)	647	20795.57 (36.90%)
Loans outstanding against MFIs as on 31 March	2422	16517.43 (14.50%)	4662	22500.46 (36.22%)	2020	25580.84 (13.69%)
Loan Outstanding as % of Fresh Loan		160.64		148.13		123.00

Source: NABARD Report 2015-2016

Table 2 Progress under Microfinance - Savings of SHGs with Banks Region-Wise Position as on 31 March 2016

(Rs. In Crore)

Region	Commercial Banks		Regional Rural Banks		Co-operative Banks	
	No. of SHGs	Saving Amount	No. of SHGs	Saving Amount	No. of SHGs	Saving Amount
Northern Region	154137	26059.08	120455	11782.03	118883	7172.93
North Eastern Region	107737	7609.42	271305	9713.27	50781	1703.64
Eastern Region	694646	88910.82	553014	86688.88	452446	72752.08
Central Region	324838	51811.44	452386	29941.31	38429	2355.92
Western Region	476739	52221.90	155687	10159.21	385623	43322.75
Southern Region	2382014	676776.11	703964	100143.43	459918	90014.79
Total	4140111	903388.77	2256811	248428.13	1506080	217322.11

Source: NABARD Report 2015-2016

Table 3 Progress under Microfinance - Bank Loans Disbursed to SHGs Agency-Wise Position During 2015-16

(Rs. In Crore)

Name of the Agency	Loans disbursed to SHGs by Banks during the year		Out of Total - Under SGSY		Out of Total –Exclusive Women SHGs	
	No. of SHGs	Loan disbursed	No. of SHGs	Loans disbursed	No. of SHGs	Loans disbursed
Commercial Banks	1132281	2518497.23	511745	1137201.78	972524	2296692.09
Regional Rural Banks	470399	916492.88	271423	482639.00	456352	900746.18
Co-operative Banks	229643	293699.98	32364	58737.52	199795	243703.67
Total	**1832323**	**3728690.09**	**815532**	**1678578.30**	**1628671**	**3441141.94**

Weakness of Microfinance

Microfinance in India, has evolved significantly in the recent past both in concept and practice. Over the years micro finance has emerged as a firm basis for rural and developmental financing in India. There are certain weaknesses associated with micro finance. Traditionally, the formal sector banking institutions in India have been serving only the needs of the commercial sector and proving loans for middle and upper income groups. Similarly, for housing the HFIs have generally not evolved a lending product to serve the needs of the very low income group primarily because of the perceived risks of lending to this sector. Most of the existing microfinance institutions are facing problems regarding skilled labour which is not available for local level accounting. Drop out of trained staff is very high.

Suggestion

- It is very difficult to make illiterate poor to understand SHG. Groups formed may be not homogeneous. Therefore much attention should be given to the formation homogeneous SHGs.
- The stories of successful SHGs may be live telecasted.
- NABARD should show interest to motivate the bank people.
- Operating cost is still higher in some cases. So they should bring down.
- Government should promote more and more number of SHGs.
- Micro finance programme should no longer be a sub – programme of SGSY. It should rather be an independent economic programme. There is also a need to develop the capacity of SHGs.
- More innovation in the form of business facilitators and correspondents will be needed for banks to increase their outreach for banks to ensure financial inclusion.

Conclusion

Microcredit and microfinance have received extensive recognition as a strategy for poverty eradication and for economic empowerment. Microfinance is a way for fighting poverty, particularly in rural areas, where most of the world's poorest people live. Accessing small amounts of credit at reasonable interest rates give poor people an opportunity to set up their own small business. Many studies show that poor people are trustable, with higher repayment rates than conventional borrowers. When poor people have access to financial services, they can earn more, build their assets, and cushion themselves against external shocks. Poor households use microfinance to move from every day survival to planning for the future: they invest in better nutrition, housing, health, and education.

Most poor people cannot get good financial services that meet their needs because there are not enough strong institutions that provide such services. Strong institutions need to charge enough to cover their costs. Cost recovery is not an end in itself .Rather, it is the only way to reach scale and impact beyond the limited levels that donors can fund. In many cases, other tools will alleviate poverty better—for instance, small grants, employment and training programs, or infrastructure improvements. Where possible, such services should be coupled with building savings. It shows that access and efficient provision of microcredit can enable the poor to smooth their consumption, better manage their risks better, gradually build their assets, develop their micro enterprises, enhance their income earning capacity and enjoy an improved quality of life. Microfinance services can also contribute to the improvement of resource allocation, promotion of markets, and adoption of better technology; thus, Microfinance helps to promote economic growth and development

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