Microfinance: A catalyst for driving inclusive growth

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Abstract

The microfinance sector in India is varied, with a variety of firms providing low-income people with financial services like lending, insurance, and pensions. **Five broad categories can be used to classify the various microfinance industry participants: Small Finance Banks, NBFC, MFIs, Banks, and Non-profit MFIs.** Broadly, two different approaches are followed in India for extending microfinance services:

The bank-led approach, Self-Help Groups-Bank Linkage Program (SHG-BLG),

The Micro Finance Institution (MFI)-led approach

The RBI has instructed every bank to have Basic Saving Bank Deposits (BDSD) accounts for the economically weaker sections of the society. The Agency-wise Average Savings, Loan Disbursement and Loan Outstanding per SHG is been analysed in the study.

Key Words: NBFC, MFIs, Financial inclusion, KYC norms, Joint Liability Group

Introduction

In a developing country like India, there is a need to support low-income families as well as uplift and provide them with a better standard through supporting them financially in a more efficient way, and there came the concept of "microfinance," which is a form of financial service that provides small loans and other financial services to poor and low-income households in a consistent and legitimate way. It is an economic tool designed to promote financial inclusion, which enables poor and low-income households to come out of poverty, increase their income levels, and improve their overall living standards. It can facilitate the achievement of national policies that target poverty reduction, women's empowerment, assistance to vulnerable groups, and an improvement in the standard of living.

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The microfinance sector in India is varied, with a variety of firms providing low-income people with financial services like lending, insurance, and pensions. **Five broad categories can be used to classify the various microfinance industry participants: Small Finance Banks, NBFC MFIs, Banks, and Non-profit MFIs.** All of these, with the exception of non-profit MFIs, are under RBI regulation. The majority of non-profit MFIs are registered as trusts or societies, and they are regulated by the corresponding acts while majorly the non-profit organizations (NGOs) that have been operating in the industry as financial intermediaries are registered as trusts or societies.

In a development perspective, microfinance has evolved into a program for women's economic empowerment and poverty alleviation. One of the most successful methods for enabling the financial inclusion of the poor is microfinance. Microfinance companies in India have played a critical role in expanding access to financial services for low-income households, especially women. This has essentially meant offering no-collateral loans to financially underprivileged women, who are frequently grouped into self-help or joint liability groups. The not-for-profit sector was where microfinance first emerged. The majority of Microfinance Institutions (MFIs) that were founded in the middle of the 1990s were non-profit charity trusts and societies. They eventually changed into for-profit Non-Banking Financial Companies as they expanded because this was necessary for them to draw risk capital.

When social enterprises started financing to the working poor on a large basis in the 1970s, microfinance had its start. One person who has achieved international recognition for his work in microfinance is Prof. Muhammad Yunus, who received the Nobel Peace Prize in 2006 alongside Grameen Bank. Microfinance was created to assist people in escaping poverty. Various development strategies aimed at lowering poverty in developing countries have been created over the past 20 years by governments, international development organisations, non-governmental organisations, and many others. Among these programmes that have gained prominence since the early 1990s is microfinance, which offers financial services in the manner of savings and credit prospects to the working poor.

What is the Need for Financial Inclusion?

Financial inclusion enhances the financial system of the country comprehensively. It strengthens the availability of economic resources. Most importantly, it toughens the concept of savings among poor people living in both urban and rural areas. This way, it contributes towards the progress of the economy in a consistent manner. Many poor people tend to get cheated and sometimes even exploited by rich landlords as well as unlicensed moneylenders due to the vulnerable condition of the poor people. With the help of financial inclusion, this serious and hazardous situation can be changed. Financial inclusion engages in including poor people in the formal banking industry with the intention of securing their minimal finances for future purposes. There are many households with people who are farmers or artisans who do not have proper facilities to save the money that they earn after putting in so much effort.

Financial Inclusion Programmes Organised by the Reserve Bank of India (RBI)

The Reserve Bank of India works on exclusive programmes and plans in order to have financial inclusion in the nation effectively. It applies a bank-led strategy in order to attain financial inclusion smoothly. The central bank of India also has firm regulations in place that need to be followed by every bank. The RBI also is offering qualified assistance to every bank in the nation in order to attain its financial inclusion objectives.

Let us take a look at some of the programmes introduced by the RBI in order to achieve its goals:

The RBI instructed every bank to have Basic Saving Bank Deposits (BDSD) accounts for the economically weaker sections of the society. These are no-frill accounts where account holders do not have to maintain any minimum balance or minimum deposit. These account holders can withdraw cash at any ATM or at the bank branch. They should also be given the opportunity to make use of electronic payment channels for receiving and transferring money to others.

The RBI also asked banks to have simple Know Your Client (KYC) regulations for the less fortunate people of the society. There are many people in rural areas that are unable to open bank accounts due to strict KYC norms. Hence, the RBI wants banks to have simplified KYC requirements particularly if a low-income individual is interested in opening a bank account with an amount not above Rs.50, 000. It also wants minimal KYC norms if the overall credit in the accounts does not go above Rs.1 lakh for 1 year. Recently, banks have been asked to accept Aadhaar Card as identity proof as well as address proof since most people belonging to low-income groups have made Aadhaar card in their names.

Keeping in mind about the lack of bank branches in rural areas, the RBI has asked all banking institutions to open more and more branches in villages across the nation in order to provide good banking services to the villagers. There are many remote villages where there are no banks and also no good transportation services. It is very difficult for residents of these areas to commute to a far-off bank branch for availing banking services. Hence, with the compulsory rule of the RBI, banks are distributing the ratio of banks in villages and cities

Role of Microfinance in India

A microfinance institution is focused on providing low-income individuals and groups with banking services. These organizations get funding from established financial institutions and aid the underprivileged. As a result, microfinance institutions are becoming one of the best tools for reducing poverty in India.

The following sources provide microfinance services

Formal institutions, such as rural banks and cooperatives

Semiformal organizations, such as non-governmental ones

Informal sources, including small-scale lenders and store owners

Institutional microfinance includes both formal and semiformal institutions' offerings.

While some MFIs are well-managed and have a stellar record of accomplishment, others are self-sufficient in terms of operations.

The various categories of institutions providing microfinance in India are as follows

Commercial banks

Credit unions

NGOs

Sectors of government banks

Cooperatives

The services provided by banks are supplemented by microfinance organizations. Financial services like insurance, savings, and remittance are additionally offered in addition to microcredit. Additionally, non-financial services like training, counselling, and support for borrowers are provided in the most practical way possible. The borrower receives the mentioned services at their convenience, as noted below. Interest rates charged by MFIs are typically higher than those of traditional banks. Interest rates vary depending on the loan purpose and borrower history. Borrowers also determine the repayment schedule.

Objectives of the Study

1. Understanding the role of microfinance in India

2. To Analyse the importance of Microfinance

3. Identifying the Financial Inclusion Programmes Organised by the Reserve Bank of India (RBI)

4. Analysing Agency-wise Average Savings, Loan Disbursement and Loan Outstanding per SHG

Literature Review

Y. Chitra Rekha, C.S.Sai Prasad Reddy: At a time when financial inclusion is at the center stage of the regulatory landscape, the last mile connectivity provided by the MFIs has to be leveraged upon, to include the hitherto financially excluded. Although the MFIs are facing tough times, there is a fair degree of opportunity to build long-term sustainable business around microfinance. Balancing the interests of the vulnerable borrowers as also the microfinance institutions; effective regulations, well calibrated transition time and some breathing space to the institutions could help the microfinance sector to turn around, expand and help achieve inclusive growth. The recent episodes in the MFI sector have raised certain serious concerns on the governance issues. MFIs should identify their unique role in the financial system and should put in place robust governance standards to balance the dual objectives of social utility and financial sustainability.

Prof. Dr. Pavnesh Kumar[1], Prof. Dr. Sudhir Kumar Sahu[2], Raushan Kumar[3](2021)

The significant outcome of micro finance institutions is an affordable and accessible financial credit services to the rural parts of India. Poor sections of our population need assistance rather than subsidies and now there is paradigm shift from subsidies to access of credit. Micro finance can also play a vital role in women developments who are now leading the economy through micro finance credit with the help of good decision making. But there is still a big challenge since independence that in most of the rural parts of India credit is providing by moneylenders at very high interest rates, but this is a work of financial institution. There is a big gap between haves and haves not people due to unequal income distributions of the people and they are financially excluded. So, micro finance institutions bridge the gap between two gaps. The paper discusses the role of micro finance in inclusive growth, through various financial programmes of state and challenges faced by micro finance in providing access of credit.

Ramesh Kumar Chaturvedi* and Roshni Kumari (2022):** Studying the role of microfinance in facilitating the availability of credit is an important field of research. A review of the literature on microfinance highlights the growing attention of the researchers on its various aspects. Therefore, this review attempts to present a systematic summary of research in the domain of microfinance in India over the last two decades. This includes 95 published research articles on microfinance. These articles are identified through a systematic search of electronic databases by focusing on the major keywords microfinance, poverty, sustainability, and India. Seven major themes have been identified, and each theme is further grouped into sub-themes. The identified main themes include women empowerment, self-help group, financial inclusion, sustainability, Andhra Pradesh crises, status of microfinance in India, and poverty. The key findings of the articles are briefly summarised. Thus, this paper attempts to highlight the current trend and pattern of research in this field of study. It will provide direction for future research in the field of microfinance and also offer insights to policy makers on various issues pertaining to microfinance.

Ms Neha Saini, Dr. Bhupendra Kumar, Dr O P Pathak (2017): In a country like India where 70 percent of its population lives in rural area and 60 percent depend on agriculture (according to the World Bank reports), micro-finance can play a vital role in providing financial services to the poor and low income individuals. Microfinance is the form of a broad range of financial services such as deposits, loans, payment services, money transfers, insurance, savings, micro-credit etc. to the poor and low income individuals. The importance of micro-finance in the developing economies like India cannot be undermined, where a large size of population is living under poverty and large number of people does not have an access to formal banking facilities. The taskforce on Supportive Policy and Regulatory Framework for Microfinance constituted by NABARD defined microfinance as " the provision of thrift, saving, credit and financial services and products of very small amount to the poor's in rural, semi urban and urban areas for enabling them to raise their income level and improve their standard of living." (Sen, 2008) Micro-finance is regarded as a useful tool for socioeconomic up-liftmen in a developing country like India. It is expected to play a significant role in poverty alleviation and development. There are two broad approaches that characterize the microfinance sector in India is Self Help Groups (SHGs)-Bank linkage programme and Microfinance Institution (MFIs). In India microfinance is dominated by Self Help Groups (SHGs)-Bank linkage programme aimed at providing a cost effective mechanism for providing financial services to the unreached poor.

Research Methodology

This research paper is based on secondary data. The help of secondary data, collected from various journals and magazines such as economic survey. The planning commission report, RBI report, NABARD report, books, websites and records etc.

Statistical Analysis: Agency-wise Average Savings, Loan Disbursement and Loan Outstanding per SHG:

Agency-wise Average Savings, Loan Disbursement and Loan Outstanding per SHG									
Category of Agency	**Average Savings of SHGs with Banks**			**Average Loans disbursed to SHGs by Banks**			**Average Outstanding Bank Loans against SHGs**		
	2022-23	**2021-22**	**Change (%)**	**2022-23**	**2021-22**	**Change (%)**	**2022-23**	**2021-22**	**Change (%)**
Commercial Banks	44,743	44,612	0.29	3,76,659	2,94,460	27.92	3,07,568	2,45,495	25.28
Regional Rural Banks	44,969	38,488	16.84	2,82,020	2,94,896	-4.37	2,19,851	1,94,620	12.96
Cooperative Banks	37,450	19,143	95.63	3,08,381	2,76,485	11.54	1,89,014	1,68,247	12.34
Total	**43,940**	**39,721**	**10.62**	**3,38,027**	**2,93,471**	**15.18**	**2,70,343**	**2,24,113**	**20.63**

Source: NABARD Report 2022-2023

In the above Table average savings of SHGs with banks have increased across all agencies. The average savings have gone up from Rs. 39,721 in 2021-22 to Rs. 43,940 in 2022-23 and average loans disbursed to SHGs have increased by 15% from the previous year with an increase observed in case of Commercial Banks and RCBs whereas in the case of RRBs there was a decline of 4%. Union Bank of India has 21.2% share of the total savings of Public Sector Commercial Banks and has highest average savings of Rs. 83,000 per SHG. Among the Private Sector Commercial Banks, ICICI Bank has highest number of savings linked SHGs i.e. 5.29 lakh, followed by HDFC Bank (3.10 lakh) and DCB Bank (2.45 lakh). Among the RRBs, Assam Gramin Vikas Bank has highest number of savings linked SHG accounts at 3.15 lakh. Bank of India registered the highest average loan disbursed per SHG at Rs. 5.26 lakh, followed by Rs. 4.80 lakh by Indian Bank. The average loans outstanding per SHG have increased for all agencies, with the highest percentage increase in respect of Commercial Banks.

Importance of Microfinance

For a country like India, where even more than 80% of individuals work in the unorganised sector, microfinance institutions are crucial. Because of the massive fees, local banks are often not an option for small business owners. People can lack the paperwork needed to create an account, such as identity cards and income verification. Or they are unable to read and write clearly enough to complete the forms. Microfinance performs this responsibility and fills this void. In India; microfinance has a significant impact on the country's economic development. It serves as an antidote against poverty for those who reside in rural areas. Its goal is to support financially disadvantaged communities in achieving higher levels of wealth development and income security for both households and entire communities. The most important function of microfinance in India is to provide small business owners with access to money. As was already said, microfinance in India offers access to loans, insurance, and savings accounts.

By providing them with loans, the microfinance philosophy focuses on women as well. It serves as a tool for the strengthening of low-income women because as they gain independence, they can immediately improve the lives of their families and challenge all forms of gender inequality. The poor households in rural and urban areas, as well as women, are the main focus of microfinance. Regarding the minimum and maximum sums that can be loaned, the Reserve Bank of India does not impose any restrictions. For the impoverished to continue earning money and meeting their expenses, credit is crucial. Additionally, it is essential to the impoverished for revenue activities like investing in small-scale self- employment projects like marginal farms. Due to resource constraints and the structure of formal credit organisations, their access to traditional banking channels is limited. As a result of meeting the credit needs of the poor, microfinance institutions and self-help organisations in India are influencing other conventional banking institutions. It has made significant contributions to raising the standard of living for those in poverty.

Thus, microfinance is not a financial system but rather a weapon for eradicating poverty, bringing about social transformation, and, particularly, elevating the status of women in our nation so that they can become self-sufficient. Microfinance serves a public purpose, which qualifies it as a legitimate objective for social policy. There are several microfinance companies in Karnataka and specifically microfinance companies in Bangalore that are providing extremely agreeable small loans to underprivileged households, particularly to women who are starting to seek their financial independence. These microfinance companies in Karnataka serve as the backbone for uplifting numerous communities in the state through their financial aid.

Structure of Microfinance and the Road Ahead

The structure of MFI has been created to address the difficulties that the traditional financial services sector encountered in satisfying the low-income segment's credit requirement at a reasonable and sustainable cost.

a) A Joint Liability Group (JLG) is an informal association of 4-10 people who work as a team to apply for bank loans either individually or collectively under mutual guarantee.

b) A SHG is a group of registered or unregistered micro-entrepreneurs with similar socioeconomic origins that get together voluntarily to save modest amounts of money monthly, mutually agreeing to contribute to a common fund, and meeting their emergency needs through mutual assistance. To ensure proper credit use and prompt repayment, the group members typically rely on their collective knowledge and peer pressure.

Microfinance is very necessary for India to achieve financial inclusion for the poor in rural and urban areas. Lending to the poor population, if handled in an effective manner, can be a miracle for the development of the country and the alleviation of poverty. When the government and MFIs work together, Microcredit can play a significant role in poverty alleviation. The challenging issue of microfinance helps to reduce the financial problems faced by poor people. The inability of MFIs to get sufficient funds is a major challenge for the microfinance industry's growth, so these institutions should look for alternative sources of funding. Microfinance has a significant impact on poor people's confidence, courage, and skill development. Thus, external factors such as microfinance institutions are needed to help fix these problems.

Conclusion

Microfinance is very necessary for India to achieve financial inclusion for the poor in rural and urban areas. In India, microfinance has a significant impact on the country's economic development and financial institutions play a crucial role in the growth of our economy. Microfinance has a significant impact on reducing poverty in societal structure. Five broad categories can be used to classify the various microfinance industry participants: Small Finance Banks, NBFC, MFIs, Banks, and Non-profit MFIs**.** In India, several banks have started lending money to microfinance institutions. It promotes women's empowerment, which is a significant step in the growth of the nation. In a development perspective, microfinance has evolved into a program for women's economic empowerment and poverty alleviation.

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