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Microfinance - As a Catalyst for the Growth of Rural India

***Ashima Mittal,**
***Palak Bajaj**
***Anuja Goyal**

Abstract

Microfinance is emerging as a powerful tool for poverty alleviation in India. Microfinance refers to small savings, credit and insurance services extended to socially and economically disadvantaged segments of society. Microfinance began in India in the 1990s as a way of alleviating poverty, by encouraging income generating activities by poor households. The prospect of Micro-finance is dominated by SHGs (Self Help Groups)–Banks linkage Programme. Its aim is to provide a cost effective mechanism for providing financial services to the poor. A large variety of sectors provide microfinance in India, using a range of microfinance delivery methods. Since the ICICI Bank in India, various actors have endeavored to provide access to financial services to the poor in creative ways. Governments also have piloted national programs, NGOs have undertaken the activity of raising donor funds for on-lending, and some banks have partnered with public organizations or made small inroads themselves in providing such services. The range of activities undertaken in microfinance include group lending, individual lending, the provision of savings and insurance, capacity building, and agricultural business development services. This paper outlines three distinct aspects of microfinance, first growth of microfinance in India; secondly it discusses the role played by NABARD and other National Banks in the growth of SHGs and Grameen Bank. Third, it deals with the role of government in framing legislation for protection of right of micro borrowers.

KEYWORDS: Microfinance, SHGs, NABARD, Grameen Banks

Introduction

Microfinance is defined as an activity that includes the provision of financial services such as credit, savings and insurance to low income individuals which falls just above the nationally defined poverty line, and poor individuals which fall below that poverty line, with the goal of creating social value. The creation of social value includes poverty alleviation and the broader impact of improving livelihood opportunities through the provision of capital for micro enterprise, and insurance and savings for risk mitigation and consumption smoothing. Government also have piloted national programs, NGOs have undertaken the activity of raising donor funds for on-lending, and some banks have partnered with public organizations or made some inroads themselves in providing such services. This has resulted in a rather broad definition of microfinance as any activity that targets poor and low-income individuals for the provision of financial services. Microfinance may be called a novel approach to provide saving and investment facility to the poor around world. Improved access and efficient provision of savings, credit and insurance facilities in particular can enable the poor to smoothen their consumption, manage their risks better, gradually build their asset base, develop their business, enhance their income earning capacity and enjoy an improved quality of life. In India, microfinance mainly operates through Self Help Group (SHGs), Non Government Organization (NGOs) and Credit Agencies. It provides poor people with the means to find their own way out of poverty.

According to International Labour Organization (ILO), "Microfinance is an economic development approach that involves providing financial services through institutions to low income clients."

Activities in Microfinance

Microcredit: It is a small amount of money loaned to a client by a bank or other institution. Microcredit can be offered, often without collateral, to an individual or through group lending.

Micro savings: These are deposit services that allow one to save small amounts of money for future use. Often without minimum balance requirements, these savings accounts allow households to save in order to meet unexpected expenses and plan for future expenses.

Micro insurance: It is a system by which people, businesses and other organizations make a payment to share risk. Access to insurance enables entrepreneurs to concentrate more on developing their businesses while mitigating other risks affecting property, health or the ability to work.

Remittances: These are transfer of funds from people in one place to people in another, usually across borders to family and friends. Compared with other sources of capital that can fluctuate depending on the political or economic climate, remittances are a relatively steady source of funds.

Assistant Professor's, Seth Jai Prakash Mukandlal Institute of Management & Technology (JMIT), Radaur, Yamunanagar
E-mail: mittal_ashi@rediffmail.com, palakbajaj86@gmail.com, anujagoyal@jmit.ac.in

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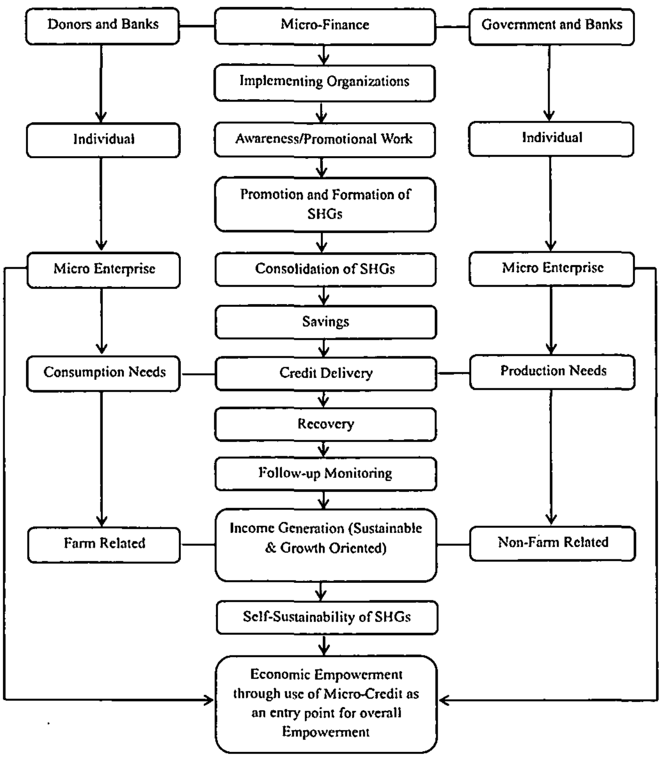
Development Process Through Micro Finance



Review of Literature

R.Prabhavathy (2012) has examined that collective strategies beyond micro-credit to increase the endowments of the poor/women enhance their exchange outcomes the family, markets, state and community, and socio-cultural and political spaces are required for both poverty reduction and women empowerment. Even though there were many benefits due to micro-finance towards women empowerment and poverty alleviation, there are some concerns.

Chintamani Prasad Patnaik (March 2012) has examined that microfinance seems to have generated a view that microfinance development could provide an answer to the problems of rural financial market development. While the development of microfinance is undoubtedly critical in improving access to finance for the unserved and underserved poor and low-income households and their enterprises, it is inadequate to address issues of rural financial market development.

Crabb, P. (2008) has examined that the relationship between the success of microfinance institutions and the degree of economic freedom in their host countries. Many microfinance institutions are currently not self-sustaining and research suggests that the economic environment in which the institution operates is an important factor in the ability of the institution to reach this goal, furthering its mission of outreach to the poor.

Mohammed AnisurRahaman (2007) has examined that about microfinance and to investigate the impact of microfinance on the poor people of the society with the main focus on rural India. We mainly concise our thesis through client's (the poor people, who borrowed loan from microfinance institutions) perspective and build up our research based on it.

Srinivasan, Sunderasan (2007) has examined that micro banking facilities have helped large numbers of developing country nationals by supporting the establishment and growth of microenterprises. And yet, the microfinance movement has grown on the back of passive replication and needs to be revitalized with new product offerings and innovative service delivery.

Mallory A. Owen (2006) has examined that microfinance has signaled a paradigm shift in development ideology. Using my experiences with microfinance in a fishing village in Senegal, this study will address the claims driving the microfinance movement, debate its pros and cons and pose further questions about its validity and widespread implementation. Instead of lifting people out of poverty and empowering women, microfinance may have regressive long term potential for borrowers.

Linda Mayoux (Feb 2006) has examined that Micro-finance programmes not only give women and men access to savings and credit, but reach millions of people worldwide bringing them together regularly in organized groups. Through their contribution to women's ability to earn an income, micro-finance programmes can potentially initiate a series of 'virtuous spirals' of economic empowerment, increased well-being for women and their families and wider social and political empowerment Banks generally use individual rather than group-based lending and may not have scope for introducing non-financial services.

Fehr, D. and G. Hishigsuren. (2006) has examined that microfinance institutions (MFIs) provide financial services to the poorest households. To date, funding of MFI activities has come primarily from outright donor grants, government subsidies, and often debt capital, including debt with non-market terms favorable to the MFI. These traditional sources of MFI financing may not be sufficient to allow MFIs to provide maximum services.

Basu, P., Srivastava (2005) has examined that the current level and pattern of access to finance for India's rural poor and examines some of the key microfinance approaches in India, taking a close look at the most dominant among these, the Self Help Group (SHG) Bank Linkage initiative. It empirically analyzes the success with which SHG Bank Linkage has been able to reach the poor, examines the reasons behind this, and the lessons learned.

Jennifer Meehan (2004) has examined that it will need to do three things simultaneously. First, it will need to rapidly scale up, in key markets, like India, home to high numbers of the world's poor. Second, in this process, clear priority is needed for philanthropic, quasi-commercial and commercial financing for the business plans of MFIs targeting the poorest

Objectives of the Study

- To study the impact of micro finance in empowering the social economic status of rural India.
- To analyze the growth of microfinance sector developed in India and see the potential for the microfinance institutions, NGOs and SHGs.
- To find out the role of government in framing legislation for protection of right of micro borrowers.
- To study the importance and role of microfinance in poverty alleviation and profitable agriculture activities.

Research Methodology

This is a descriptive research paper based on secondary data. Data have been find out by googling in different websites, research paper and magazines.

Entities in Micro Finance

Indian Microfinance dominated by two operational approaches:

- SHG
  ✓ Initiated by NABARD through SHG Bank Linkage Program.
  ✓ Largest outreach to microfinance clients in the world.
- MFIs
  ✓ Emerged in the late 1990s to harness social and commercial funds.
  ✓ Today the number of Indian MFIs has increased and crossed 1000.

As we broaden the notion of the types of services micro finance encompasses, the potential market of micro finance clients also expands. It depends on local conditions and political climate, activeness of cooperatives, SHG & NGOs and support mechanism. Central Government in India has established a strong & extensive link between NABARD (National Bank for Agriculture & Rural Development), State Cooperative Bank, district and village level. The Grameen model follows a fairly regimented routine. It is very cost intensive as it involves building capacity of the groups and the customers passing a test before the lending could start. The group members tend to be selected or at least strongly vetted by the bank. One of the reasons for the high cost is that staff members can conduct only two meetings a day and thus are occupied for only a few hours, usually early morning or late in the evening. They were used additionally for accounting work, but that can now be done more cost effectively using computers. The model is also rather meeting intensive which is fine as long as the members have no alternative use for their time but can be a problem as members go up the income ladder.

Need of Micro Finance In India

- India is said to be the home of one third of the world's poor; official estimates range from 26 to 50 percent of the more than one billion population.
- About 87 percent of the poorest households do not have access to credit.
- The demand for microcredit has been estimated at up to \$30 billion; the supply is less than \$2.2 billion combined by all involved in the sector.

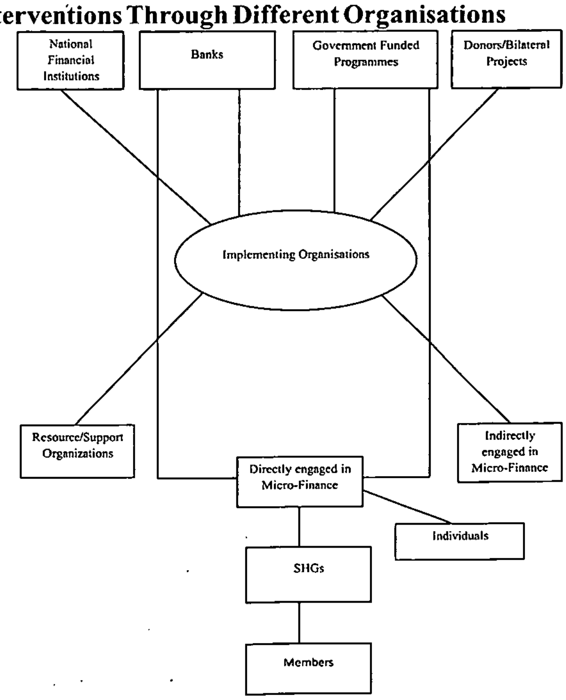
Due to the sheer size of the population living in poverty, India is strategically significant in the global efforts to alleviate poverty and to achieve the Millennium Development Goal of having the world's poverty by 2015. Microfinance has been present in India in one form or another since the 1970s and is now widely accepted as an effective poverty alleviation strategy. Over the last five years, the microfinance industry has achieved significant growth in part due to the participation of commercial banks. Despite this growth, the poverty situation in India continues to be challenging.

Role of Microfinance

The micro credit of microfinance programme was first initiated in the year 1976 in Bangladesh with promise of providing credit to the poor without collateral , alleviating poverty and unleashing human creativity and endeavour of the poor people. Microfinance impact studies have demonstrated that:

- Microfinance helps poor households meet basic needs and protects them against risks.
- The use of financial services by low-income households leads to improvements in household economic welfare and enterprise stability and growth.
- By supporting women's economic participation, microfinance empowers women, thereby promoting gender-equity and improving household well-being.
- The level of impact relates to the length of time clients have had access to financial services.

Interventions Through Different Organisations



Legal Regulation
Banks in India are regulated and supervised by the Reserve Bank of India (RBI) under the RBI Act of 1934, Banking Regulation Act, Regional Rural Banks Act, and the Cooperative Societies Acts of the respective state governments for cooperative banks.
NBFCs are registered under the Companies Act, 1956 and are governed under the RBI Act. There is no specific law catering to NGOs although they can be registered under the Societies Registration Act, 1860, the Indian Trust Act, 1882, or the relevant state acts. There has been a strong reliance on self-regulation for NGO MFIs and as this applies to NGO MFIs mobilizing deposits from clients who also borrow. This tendency is a concern due to enforcement problems that tend to arise with self-regulatory organizations. In January 2000, the RBI essentially created a new legal form for providing microfinance services for NBFCs registered under the Companies Act so that they are not subject to any capital or liquidity requirements if they do not go into the deposit taking business. Absence of liquidity requirements is concern to the safety of the sector.

Strategic Policy Initiatives
Some of the most recent strategic policy initiatives in the area of Microfinance taken by the government and regulatory bodies in India are:
- Working group on credit to the poor through SHGs, NGOs, NABARD, 1995
- The National Microfinance Taskforce, 1999
- Working Group on Financial Flows to the Informal Sector (set up by PMO), 2002
- Microfinance Development and Equity Fund, NABARD, 2005
- Working group on Financing NBFCs by Banks- RBI

Microfinance Changing the Face of Poor India
Micro-Finance is emerging as a powerful instrument for poverty alleviation in the new economy. In India, micro-Finance scene is dominated by Self Help Groups (SHGs) - Banks linkage Programme, aimed at providing a cost effective mechanism for providing financial services to the 'unreached poor'. In the Indian context terms like "small and marginal farmers", " rural artisans" and "economically weaker sections" have been used to broadly define micro-finance customers. Research across the globe has shown that, over time, microfinance clients increase their income and assets, increase the number of years of schooling their children receive, and improve the health and nutrition of their families.
A more refined model of micro-credit delivery has evolved lately, which emphasizes the combined delivery of financial services along with technical assistance, and agricultural business development services. When compared to the wider SHG bank linkage movement in India, private MFIs have had limited outreach. However, we have seen a recent trend of larger microfinance institutions transforming into Non-Bank Financial Institutions (NBFCs). This changing face of microfinance in India appears to be positive in terms of the ability of microfinance to attract more funds and therefore increase outreach.

Present Scenario of Micro Finance in India
India falls under low income class according to World Bank. It is second populated country in the world and around 70 % of its population lives in rural area. 60% of people depend on agriculture, as a result there is chronic underemployment and per capita income is only $ 3262. This is not enough to provide food to more than one individual. The obvious result is abject poverty, low rate of education, low sex ratio, and exploitation. The major factor account for high incidence of rural poverty is the low asset base. According to Reserve Bank of India, about 51 % of people house possess only 10% of the total asset of India .This has resulted low production capacity both in agriculture (which contribute around 22-25% of GDP) and Manufacturing sector. Rural people have very low access to institutionalized credit (from commercial bank).

Poverty Alleviation Programmes and Conceptualization of Microfinance
There has been a continuous effort of planners of India in addressing the poverty. They have come up with development programmes like Integrated Rural Development progamme (IRDP), National Rural Employment Programme (NREP), Rural Labour Employment Guarantee Programme (RLEGP) etc. But these programme have not been able to create massive impact in poverty alleviation. The production oriented approach of planning without altering the mode of production could not but result of the gains of development by owners of instrument of production. The mode of production does remain same as the owners of the instrument have low access to credit which is the major factor of production. Thus in Nineties National bank for agriculture and rural development (NABARD) launches pilot projects of Microfinance to bridge the gap between demand and supply of funds in the lower rungs of rural economy. Microfinance the buzzing word of this decade was meant to cure the illness of rural economy. With this concept of Self Reliance, Self Sufficiency and Self Help gained momentum. The Indian microfinance is dominated by Self Help Groups (SHGs) and their linkage to Banks. Deprived of the basic banking facilities, the rural and semi urban Indian masses are still relying on informal financing intermediaries like money lenders, family members, friends etc.

Discussion And Conclusion
Microfinance is multifaceted and works in an integrated system. There are many stakeholders and each one has a definite role to play. There is a second level called micro level where MFIs, NGOs, SHGs and Grameen work to provide financial support to individual client. Apex institutions like NABARD, SIDBI and other nationalized banks operate in

Meso-Level to provide infrastructure, information and technical support to micro level players. Around all these levels, there are financial environment, Regulations, legislations and regulators called Macro level. With passage of time new opportunities and new challenges are being felt in the field of microfinance. In recent years microfinance is in news for bad reasons. There are a number of suicide cases of micro credit clients all over. India for excess interest charges and high handedness of recovery agents in recovery of loans. So, government of India has bought out a legislation to check the high interest rate on micro credit and protect the poor from clutches of greedy MFIs. Government of India introduced Micro Finance Institutions (Development and Regulation) Bill 2012 on May 22, 2012 to establish a regulator under RBI to regulate and supervise the activities of NGOs and MFIs. The main features of the Bill are as follows: the Bill allows the central government to create a Microfinance Development Council with officers from different ministers and Departments. The Bill requires all MFIs to obtain a certificate of registration from RBI. These initiatives may go long way in strengthens the micro finance status in India. Lending to the poor through microcredit is not the end of the problem but beginning of a new era. If effectively handled, it can create miracle in the field of poverty alleviation.

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