TEST Engineering & Management

July-August 2020
ISSN:0193-4120 Page No. 6720 – 6728

Role of Micro Finance in Developing Indian Economy

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Article Info
Volume 83
Page Number: 6720 – 6728
Publication Issue:
July - August 2020

Article History
Article Received: *25 April 2020*
Revised: *19 May 2020*
Accepted: *22 June 2020*
Publication: *23 August 2020*

ABSTRACT
Microfinance is a term used to describe modest savings, credit, and insurance services provided to those who are socially and economically disadvantaged. In India, it is proving to be a potent instrument for poverty reduction. This working paper attempts to summarise the current state of microfinance in India from its inception to the present. Poverty is one of the most pressing issues facing the Indian subcontinent, which is home to more than a third of the world's population. Many developed countries consider India, one of the BRIC nations with a population of over 1.2 billion, to be an emerging economy. India's economic expansion has failed to significantly reduce poverty, with 400 million people still living in poverty, more than the whole population of the poorest African countries. With this concern, the Indian government launched a number of poverty reduction schemes, however they have failed to achieve the expected results. There might be a variety of causes, including inability to reach the target population, system flaws, and the development of a robust mechanism, to mention a few. Subsidized credit was tried in several countries, including India, however it only resulted in an increase in nonperforming assets (NPAs). Microfinance has stepped up to fill the need. However, in comparison to the demand and potential, the outreach is insufficient. However, with NABARD's active engagement and the development of SHG groups, there has been some success in this area. A number of non-governmental organisations (NGOs) and microfinance institutions (MFIs) have also entered the market. Some of them have also started in a significant way and have begun generating money by launching initial public offerings (IPOs) (Initial public offers).

However, recent events have thrown a renewed spotlight on the issue of regulation in the sector of microfinance. The article examines three elements of microfinance: first, the rise of microfinance in India and other countries; second, the involvement of NABARD and other national banks in the growth of SHGs and Grameen Bank. Third, it discusses the government's involvement in drafting legislation to defend micro-lenders' rights. The report also addresses the need for a regulatory agency to oversee, manage, and advise the various microfinance institutions and non-governmental organisations that engage in the industry. The study addresses the elements that influence the evolution of microfinance and its role in the global scene from both a practical and theoretical standpoint.

Keywords: Grameen Banks, Microfinance, NABARD, Poverty, SHGs.

I.INTRODUCTION

"A sort of banking service given to jobless or low-income people or organisations who would otherwise have no other means of obtaining financial services," according to the definition of microfinance (refer to bibliography). In other terms, it is the provision of financial services to those who are poor, such as savings, credit, and insurance. Microfinance may thus be defined as the development of social value for these persons by improving their situations and assisting them in envisioning potential sources of income. The objective or goal for the sustainability of rural development is achieved by the availability of finance for micro enterprises, savings for risk reduction, and insurance. Private businesses, individual contributors, and government programmes are all said to use a variety of microfinance approaches. Some banks, such as ICICI, offer financial services to assist rural development. The Indian government has implemented experimental national programmes to support rural development microfinance. On the other hand, non-governmental organisations (NGOs) engage in fund-raising operations and encourage funders to join in microfinance as much as possible. The goal of this study is to not only comprehend the broad definition of microfinance, as well as its structure and purpose, but also to project the production of social value by demonstrating and proving how microfinance has proven itself to rural residents.

II.CONCEPT OF MICRO FINANCE

Microfinance in India has a long history dating back to the foundation of Syndicate Bank in the private sector in 1921. Syndicate Bank focused its early years on generating micro deposits on a daily/weekly basis and sanctioning micro loans to its clients for a shorter length of time. But it wasn't until Dr. Yunus' Grameen Bank experiment that microfinance became well-known.

Microfinance is an innovative way to provide savings and investing opportunities to the impoverished all over the world. Improved access to and efficient provision of savings, credit, and insurance facilities, in particular, can help the poor smooth out their spending, better manage their risks, gradually build their asset base, expand their business, increase their income earning capacity, and enjoy a higher quality of life. Microfinance in India is mostly carried out through Self Help Groups (SHGs), Non-Governmental Organizations (NGOs), and Credit Agencies. It gives disadvantaged individuals the tools they need to get out of poverty on their own. It put the

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power in their hands, giving them a bigger interest in their own success than a one-time food, commodities, or cash contribution. Government measures to alleviate poverty have failed to achieve the anticipated results, maybe because they do not recognise the poor's ability to solve their own issues. The government tries to aid people through subsidies and other means, but these efforts are ineffective and do not provide a long-term solution. If given the right leadership, funding, and productive assets, this segment of society may become a successful entrepreneur. This is simply accomplished by providing them with access to microcredit. The impoverished don't have any valuable assets.

III.SELF HALF GROUPS (SHGS)

In India, Self Help Groups (SHGs) are the most popular microfinance strategy. In this example, members of Self Help Groups pool their tiny savings on a daily or weekly basis at a certain sum, and SHGs make loans to members for a set length of time. SHGs are essentially a formal and volunteer group of 15 to 20 persons who have come together to achieve a shared goal. People from similar social backgrounds and occupations get together voluntarily to create a club and pool their savings for the benefit of all members. External financial help from MFIs or banks supplements the group's revolving fund's resources. As a result, members' savings take precedence over their borrowing. NABARD has helped to arrange and fund a programme in which commercial banks lend directly to SHGs rather than through MFIs in bulk. If SHGs are shown to be effective for at least six months, the bank normally extends loans in the amount of four times their funds.

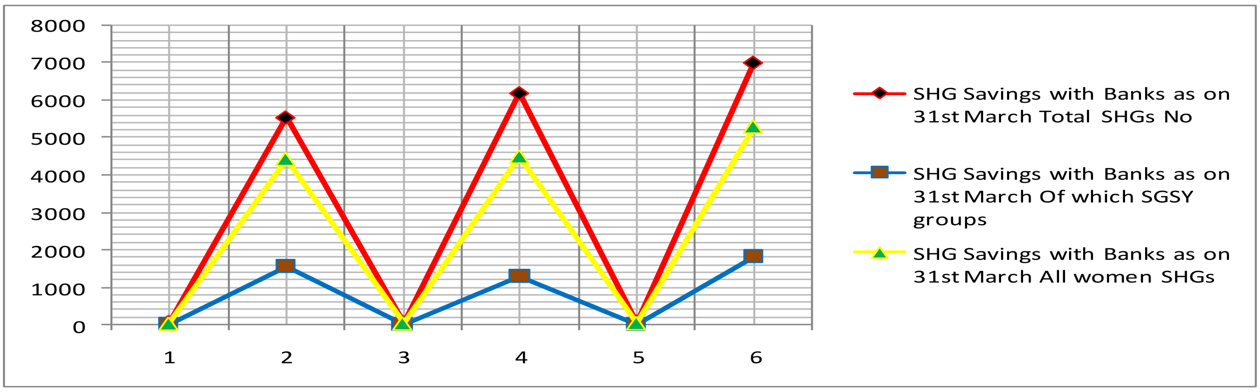
IV.GRAMEEN BANK MODEL

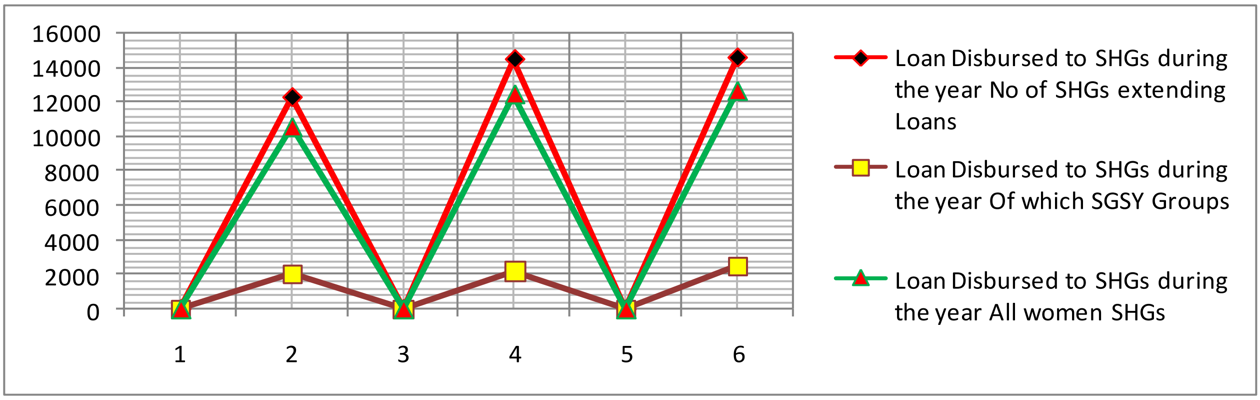
In Bangladesh, the Grameen Bank concept has proven to be a huge success. It turns out that the Grameen Bank model has been implemented by numerous organisations in India with little alteration and great success. SHARE Microfinance Limited, Activists for Social Alternatives (ASA), and CASHPOR Financial and Technical Services Limited are three significant instances. Low transaction costs, no collateral (peer pressure is sufficient), repayment of loans in modest and short intervals, and speedy loan sanctioning with little or no paper work and no formalities are some of the important elements of the Grameen bank concept. One of the main reasons for a Grameen Bank's high loan recovery rate is the repayment of loans in small chunks. Furthermore, loans are available for a variety of objectives, including home loans, sanitation loans, and supplemental loans, among others. Furthermore, the interest rates are low, making it simple for disadvantaged individuals to repay their loans on time.

Table 1.1
OVERALL PROGRESS UNDER SHG-BANK LINKAGE
(Amount is in Rupees crore and number in lakhs)

Particular		**2011-2012**		**2012-2013**		**2013-2014**	
		No of SHGs	**Amount**	**No of SHGs**	**Amount**	**No of SHGs**	**Amount**
SHG Savings with Banks as on 31st March	Total SHGs No	61.21	5545.62	69.53	6198.71	74.62	7016.3
	Of which SGSY groups	15.06	1563.38	16.94	1292.62	20.23	1817.12
	All women SHGs	48.64	4434.03	53.1	4498.66	60.98	5298.65
Loan Disbursed to SHGs during the year	No of SHGs extending Loans	16.1	12253.51	15.87	14453.3	11.96	14547.7
	Of which SGSY Groups	2.65	2015.22	2.67	2198	2.41	2480.37
	All women SHGs	13.75	10527.38	12.94	12429.37	10.17	12622.3
Loan outstanding Against SHGs as on 31st March	Total No SHGs Linked	42.24	22679.84	48.51	28038.28	47.87	31221.2
	Of which SGSY Groups	9.77	5861.72	12.45	6251.08	12.86	7829.39
	All Women SHGs	32.77	18583.54	38.98	23030.36	39.84	26123.8

***Source** : Status of microfinance in India report 2013-14,NABARD*





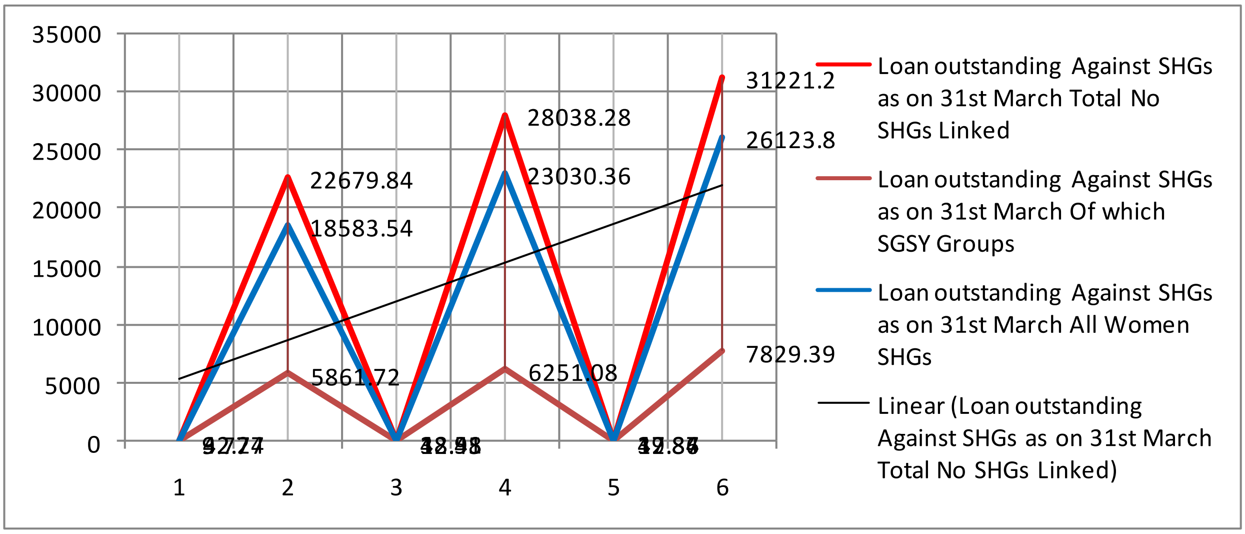


Table 1.2

PROGRESS UNDER MFI-BANK LINKAGE PROGRAMME

(Amount is in Rupees crore and number in lakhs)

Particulars	**2011-2012**		**2012-2013**		**2013-2014**	
	No of MFIs	**Amount**	**No of MFIs**	**Amount**	**No of MFIs**	**Amount**
Loans Disbursed by Banks To MFIs	581	3732.33	691	8062.74	471	8448.96
Loans outstanding against MFIs as on 31st March	1915	5009.09	1513	10147.54	2315	13730.62

Source *: Status of microfinance in India report 2013-14,NABARD*

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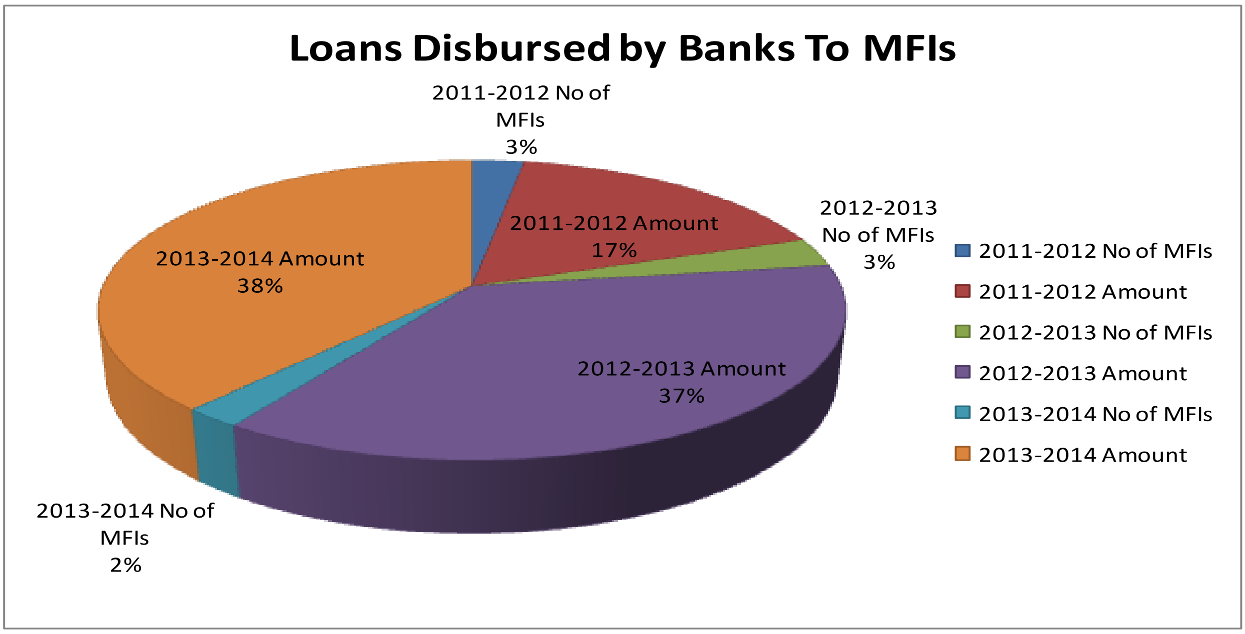


Channels Of Micro Finance:

In India Micro Finance operates through two channels:

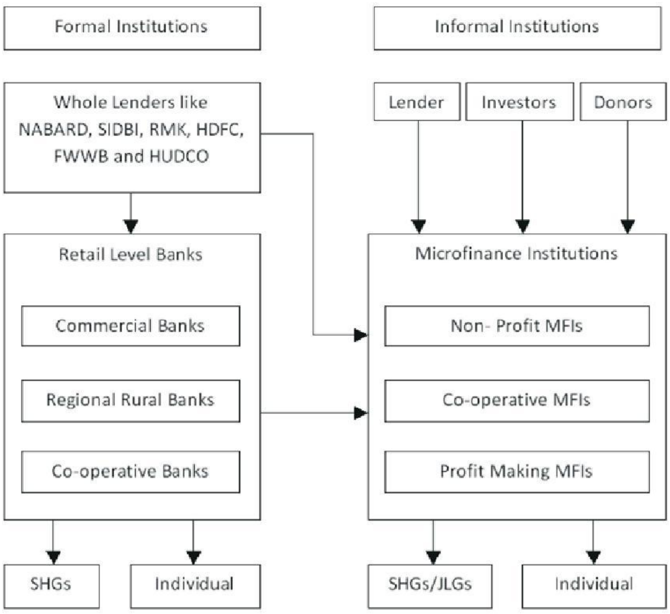
1. Shg- Bank Linkage Programme (Sblp).
2. Micro Finance Institutions (Mifs).

V.MODES OF DELIVERY OF MICRO FINANCE

Various approaches are used by Micro Finance Institutions (MFIs) all around the world. Women, rather than males, are the target of such service since women are more frugal and cost-conscious than men. The following are some of the most common approaches used by MFIs to provide financial services to low-income families.

Hierarchy of Financial Institutions for Microfinance Disbursement:

VI.DISCUS ABOUT MICROFINANCE



1. Proper Regulation: When microfinance was in its infancy, regulation was not a big issue, and individual institutions were free to experiment with new operating models. However, as the industry approaches two decades of strong growth, an enabling regulatory environment that safeguards stakeholders' interests while also promoting expansion is required.

2. Field Supervision: Field visits can be used to monitor circumstances on the ground and take remedial action if necessary, in addition to adequate supervision of the microfinance industry. This will keep track of the performance of various MFIs' ground workers as well as their recovery techniques. This will also encourage MFIs to follow a suitable code of conduct and work more effectively as a result of this. However, the question of practicality and expense associated with physical surveillance of this enormous industry continues to be a concern.

3. Encourage rural penetration: MFIs have been spotted opening branches in regions where there are already a few MFIs functioning, rather than lowering the initial cost. Providing financial incentives to MFIs to build new branches in low-microfinance-penetration areas will boost the state's microfinance outreach and reduce duplicate lending. This will also enhance the state's rural microfinance penetration.

4. Complete range of Products: MFIs should offer a full variety of products, such as credit, savings, remittance, financial counselling, and non-financial services such as training and assistance. Because MFIs function as a bank replacement in places where people do not have access to banks, offering a full variety of goods will allow the poor to take use of all services.

5. Transparency of Interest rates: MFIs adopt various methods of charging interest rates, and a few even charge extra costs and interest-free deposits, as has been noticed (a part of the loan amount is kept as deposit on which no interest is paid). All of this makes pricing exceedingly complex, and the borrower feels helpless in terms of negotiating power as a result. As a result, all MFIs should adopt a similar practise for collecting interest, making the industry more competitive and allowing beneficiaries to examine different financial products before purchasing.

6. Technology to reduce Operating Cost: MFIs should lower their operational expenses by utilising modern technology and IT tools and apps. Though most NBFCs are implementing cost-cutting strategies, as seen by their low cost per unit of money provided (9 percent to 10%). NGOs and Section 25 firms have a high cost per unit of money lent, ranging from 15 to 35 percent, and should be encouraged to pursue cost-cutting initiatives to lower their operational expenses. Initiatives such as the establishment of a standard MIS and other tools for all MFIs can also be done to improve transparency and efficiency.

7. Alternative sources of Fund: In the absence of sufficient money, MFIs' development and reach are limited, and to address this issue, MFIs should explore for alternative sources of funding for their loan portfolio. MFIs can raise funds in a variety of methods, including:

By getting converted to for-profit company i.e. NBFC: MFIs can only borrow a multiple of their entire profits and equity investment if they do not have outside investment. MFIs must seek equity from outside investors in order to boost their borrowings. Converting to a for-profit NBFC is the first and most important stage in receiving equity investment. To attract potential investors, the MFI should build a strong board, a quality management information system (MIS), and achieve a credit rating in addition to the change in status.

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Portfolio Buyout: It occurs when banks or other financial institutions buy the rights to a future payment stream from a group of existing MFI loans. MFIs are responsible for making up any repayment loss up to a particular proportion of the portfolio in such transactions, and this condition is known as the "first loss default guarantee." The paragraph above guarantees that the MFI has the appropriate motivation to recover these loans. MFIs are authorised to sell off as much of the outstanding portfolio as is financed by accumulated earnings or equity to assure the buying institution's security.

Securitization of Loans: This is a transaction in which the repayments from a group of MFI microloans are bundled into a special purpose entity from which tradable securities are created. Because many MFI loans can be pooled together, the risk is spread out. Though loan securitization and portfolio buyout are similar in many aspects, such as a first-loss default guarantee provision and a limit on the number of loans that may be sold off, there are some differences. Securitizations, on the other hand, require a credit rating from a credit rating agency and may be resold, making securitized loans more appealing to potential purchasers. In addition, unlike portfolio buyout, securitization of loans can have several buyers and sellers for each transaction, whereas portfolio buyout only has a single buyer and seller. MFIs can access new sources of funding through securitization since some types of funds, such as mutual funds, which are prohibited from participating directly in MFIs, can invest through securitized loans.

VII.CONCLUSION

Microfinance is a multidimensional field that operates as part of a larger system. There are several stakeholders, each with a distinct role to perform. Client is at the heart of everything. A second level, known as the micro level, is where MFIs, NGOs, SHGs, and Grameen work together to give financial assistance to individual clients. Meso-level players benefit from infrastructure, information, and technical assistance provided by apex institutions like as NABARD, SIDBI, and other nationalised banks. Macro level refers to the financial environment, regulations, laws, and regulators that exist around all of these levels. In the realm of microfinance, new possibilities and difficulties emerge with the passing of time. Microfinance has been in the headlines recently for all the wrong reasons. Excessive interest rates and high-handedness of collection agencies in recovering debts have resulted in a number of micro credit consumers committing suicide across India. As a result, the Indian government has enacted regulations to curb exorbitant interest rates on microcredit and safeguard the poor from the clutches of unscrupulous MFIs. On May 22, 2012, the Indian government tabled the Micro Finance Institutions (Development and Regulation) Bill 2012, which would create a regulator under the Reserve Bank of India to oversee and monitor the operations of NGOs and MFIs. The following are the Bill's primary features: The Bill empowers the federal government to establish a Microfinance Development Council comprised of officials from several ministries and departments. All MFIs must get a certificate of registration from RBI, according to the bill. The RBI has the ability to determine the maximum annual percentage rate that MFIs can charge, as well as a maximum margin that they can make. The gap between the loan rate and the cost of financing is known as margin. It is also in

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charge of resolving complaints from microfinance programme recipients. These measures may go a long way toward improving India's microfinance standing. Microcredit lending to the poor is not the solution to the problem, but rather the start of a new age. It has the potential to generate miracles in the realm of poverty reduction if handled correctly. It must, however, be combined with capacity-building initiatives. Governments cannot shirk their responsibilities for the social and economic development of the poor and underprivileged. Due to a lack of unique expertise with microcredit customers, the capital is being utilised for non-productive asset consumption and acquisition. As a result, skills development training programmes such as handicraft, weaving, carpentry, poultry, goat rearing, masonry, beekeeping, vegetable gardening, and a variety of other agricultural and non-agricultural training are critical. In this instance, the government must take the initiative. Priority should be given to those with certain abilities when it comes to giving microcredit. These customers should also receive post-loan technical and professional assistance to ensure the viability of their microbusinesses. Microcredit can play a significant role in poverty eradication if the government and MFIs work cooperatively.

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