Micro Finance in India – A Key Driver for Inclusive and Sustainable Growth

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ABSTRACT

Microfinance is an economic development tool whose objective is to assist the poor to work their way out of poverty. It covers a range of services which include, in addition to the provision of credit, money transfers, counseling and enables women’s empowerment by routing credit directly to women, thereby enhancing their status within their families, the community and society at large.

Microfinance sector has transverse a long journey from micro savings to micro credit and then to micro enterprises and now entered the field of micro insurance micro remittance and micro pension. This gradual and evolutionary growth process has given great opportunity to the rural poor in India to attain reasonable economic, social and cultural empowerment, leading to better standard of living and sustainable growth. Microfinance has demonstrated the potential of building the social capital of the poorest communities.

This paper gives the brief idea about the models used for micro financing. The study focuses on intervention of government through microfinance institutions and growth rate for sustaining in rural area as well as for overall development. Paper critically evaluates the capacity building programme for sustainable development in India.

INTRODUCTION

Sameer is a farmer who subsists on three acres in rural India. While much of the land is fertile, nearly 50% of his income goes towards just the interest payments from money-lender loans, loans which are necessary to finance the crops he plants. Moreover, some of his land is unused because he cannot profitably finance irrigation at the money-lender’s rates (5 to 10% per month). As a result, his family’s nutrition and education are compromised.

Micro credit is a component of microfinance and is the extension of small loans to entrepreneurs, who are too poor to qualify for traditional bank loans. Especially in developing countries, micro-credit enables very poor people to engage in self-employment projects that generate income, thus allowing them to improve the standard of living for themselves and their families. Microfinance is an economic development tool whose objective is to assist the poor to work their way out of poverty. It covers a range of services which include in addition to the provision of credit many other services such as Savings, Insurance, Money Transfers, and Counseling. Microfinance is an economic development approach that involves providing financial services, through institutions, to low-income clients, where the market fails to provide appropriate services. The services provided by the Microfinance Institutions (MFIs) include credit saving and insurance services. Many microfinance institutions also provide social intermediation services such as training and education, organizational support, health and skills in line with their development objectives. A microfinance institution is an organization, engaged in extending micro credit loans and other financial services to poor borrowers for income generating and self-employment activities. An MFI is usually not a part of the formal
banking industry or government. It is usually referred to as a NGO (Non-Government Organization) for the poor.

**Postulates of Microcredit in Microfinance Institutions:**

- Concern of poverty alleviation.
- Women’s empowerment by routing credit directly to women.
- Easy access to credit.
- Transaction costs are reduced through economies of scale.

**Classification of Players in Micro Finance Industry:**

<table>
<thead>
<tr>
<th>Model</th>
<th>Outstanding Loan Portfolio</th>
</tr>
</thead>
<tbody>
<tr>
<td>SHG Linkage Model</td>
<td>58%</td>
</tr>
<tr>
<td>NBFC</td>
<td>34%</td>
</tr>
<tr>
<td>Trusts &amp; Societies</td>
<td>8%</td>
</tr>
</tbody>
</table>

*Source: Malegam Report, RBI January 2013.*

The SHG-Bank Linkage Model was pioneered by NABARD in 1992. Under this model, women in a village are encouraged to form a Self help Group (SHG) and members of the Group regularly contribute small savings to the Group. These savings which form an ever growing nucleus are lent by the group to members, and are later supplemented by loans provided by banks for income-generating activities and other purposes for sustainable livelihood promotion. The Group has weekly/monthly meetings at which new savings come in, and recoveries are made from members towards their loans from the SHGs, their federations, and banks.

Under the NBFC model, NBFCs encourage villagers to form Joint Liability Groups (JLG) and give loans to the individual members of the JLG. The individual loans are jointly and severally guaranteed by the other members of the Group. Many of the NBFCs operating this model started off as non-profit entities providing micro-credit and other services to the poor. However, as they found themselves unable to raise adequate resources for a rapid growth of the activity, they converted themselves into for-profit NBFCs. Others entered the field directly as for-profit NBFCs seeing this as a viable business proposition. Significant amounts of private equity funds have consequently been attracted to this sector.

Self Help Groups (SHGs) are major sources of finance these SHGs are refinanced by banks or institutions like NABARD, SIDBI etc. but these days SHGs are also financing micro activities of the economy as they are transforming themselves into Microfinance Organizations (MFOs). Study focuses five issues: Size, diversity, sustainability, focus and taxation which trigger the transformation of SHGs into MFOs.

- **Size:** The most significant issue that triggers a transformation is growth. This affects the promoters as well as providers of microfinance. In organization like Mysore Resettlement and Development Agency (MYRADA) and South Indian Federation of Fishermen Societies (SIFFS), which promoted credit groups, banks were unwilling to provide loans at the same pace at which microfinance customers needed them. In several instances it was an enthusiastic bank manager who made the difference and this was not institutionalized. NGOs tend to get into action by opening a microfinance division or by setting up a separate MFO. The genesis of several Indian MFOs is rooted in the failure of banks to meet the needs of the poor.

- **Diversity:** Another trigger for transformation is the diverse financial services that an MFO wants to offer. In most cases NGOs start with credits but soon realize the need to provide other support services. MFOs offer combination of savings and risk mitigation products.

- **Sustainability:** Sustainability is closely linked to growth. Beyond a certain level MFOs have to seek external funds for keeping the credit activity going. When MFOs seek funds from financial institutions issue like ownership structure and capital adequacy become critical. For MFOs to
survive in long run it has to transform itself into an institution with transparent system and accountability. In most cases the promoters of MFOs do not have sufficient capital to invest and therefore the main constraint is that are dealing with other people's money. NGOs have to clear cut ownership structure and making people liable under this format is a problem. The only option they have in order to be sustainable is to deal with mainstream institutions.

The Value Chain

- **Focus**: NGOs need to maintain focus on their original mandate. For NGOs there is always a conflict between microfinance which earns returns and therefore commercial and other activities that are developmental. This is the reason why NGOs spin off their own microfinance activities. The entity that emerges to carry out microfinance should be understood by the mainstream and therefore it should have an appropriate institutional form.

- **Taxation**: When an NGO carries out commercial activities (microfinance) on a large scale it is liable to lose its tax free status and is likely to jeopardize its other activities even grants may become taxable. This is major concern for NGO-MFOs. This also triggers a search for an alternative source where microfinance could be kept isolated.

**NABARD and Innovation**

The National Bank for Agriculture and Rural Development (NABARD), an apex financial institution has been working closely with rural Development. Provisioning refinance to eligible financial institutions and undertaking related activities to achieve rural prosperity through credit are the core mandate of this organization.

**Innovative Investment Opportunities**

The investment credit is being provided by NABARD for a variety of purpose. The Bank has encouraged the adoption of water management devices like drip irrigation, sprinkler irrigation as well as program like waterhed development. With a focus on diversification of lending the banks are encouraged to finance support. Investment in allied activities such as dairy, poultry, fisheries, etc. are also encouraged. A beginning had also been made in direct lending through co-financing with financial institutions.

For reducing poverty and achieving rural prosperity, knowledge dissemination, skill updating and grounding of laboratory experiments on farm sector need expansion. Diversification,
commercialization and market-driven agricultural production are the key factors for achieving higher production and productivity. It would also help in generating more employment and income. Group approach would promote collective action, responsibility and knowledge sharing. It also lowers the extension cost in the field of agricultural development. NABARD’s initiatives of farmers club, Self Help Groups, Contract farming, corporate farming.

**Infrastructure Base**

Setting up of market yards, agri-clinics and agriculture business centers are some other innovative activities undertaken by NABARD. For promotion and development of industries undertaken by NABARD has been developing rural clusters. The bank has identified 65 clusters spread over 18 states and has so far launched promotional programs in 55 clusters. To strengthen rural industries NABARD launched District Rural Industries Projects (DRIP). The project has been extended to 61 districts. Special fund; Rural Infrastructure Development Fund (RIDF), has been set up with NABARD for providing loans to State Government for completion of on-going projects relating to agriculture and rural development.

**Leadership/ Entrepreneurship**

NABARD designed Rural Entrepreneurship Development Program (REDP) and Rural Corpus Fund supporting developmental and promotional activities of tiny, cottage and village industries for creating employment opportunities in rural areas. As a step towards women empowerment NABARD has introduced many programs like ARWIND (Assistance to Rural Women In NON Farm Development), MAHIMA (Marketing of Non farm Products of Rural Women) and Self Help Groups. ARWIND scheme satisfied credit need of women entrepreneurs. MAHIMA scheme supported agencies engaged in marketing of products produced by rural women.

**Credit Planning**

NABARD has the objective of exploring existing potential for development and evolving an appropriate mechanism through which such potential could be harnessed with credit. NABARD undertakes credit planning Potential Linked Plans (PLPs) on an annual basis NABARD has been preparing PLPs for each district, co-terminating with Five Year Plan periods.

**Research and Development Activities**

NABARD has set up a Research and Development fund to support research studies surveys seminars, conferences symposia workshops etc. in the area of agriculture and rural development.

**Kisan credit Cards: Growing popularity**

The Kisan credit card (KCC) scheme introduced in August 1993 for short term loans for seasonal agricultural operations has made significant progress in outreach and making available timely and cost effective credit to the agricultural sector. The co-operative banking sector has made the most significant progress in expanding the KCC’s outreach. In order to fulfill the investment credit needs of farmers, NABARD enlarged the scope of the scheme to cover term loans for agriculture and allied activities.

NABARD has also advised banks to:-

i. Make all possible efforts to identify and lend to farmers including oral lessees and ensure that KCCs are renewed

ii. Launch a time bound programme to motivate defaulters to clear their dues to enable them to avail the benefits from the scheme and

iii. Issue suitable guidelines to their branches to route crop loans only through KCC.
DIFFERENT MODELS OF MICROFINANCE

(i) SHG - Bank Linkage Model: This model involves the SHGs financed directly by the banks viz., CBs (Public Sector and Private Sector), RRBs and Cooperative Banks.

(ii) MFI - Bank Linkage Model: This model covers financing of Micro Finance Institutions (MFIs) by banking agencies for on-lending to SHGs and other small borrowers.

SHG - Bank linkage Model

Savings of SHGs with Banks

As on 31 March 2010, a total of 69.53 lakh SHGs were having saving bank accounts with the banking sector with outstanding savings of Rs. 6198.71 crore as against 61.21 lakh SHGs with savings of Rs. 5545.62 crore as on 31 March 2009, thereby showing a growth rate of 13.6 per cent and 11.8 per cent, respectively. Thus, more than 97 million poor households were associated with banking agencies under SHG-Bank Linkage Programme. As on 31 March 2010, the Commercial Banks lead with savings accounts of 40.53 lakh SHGs (58.3%) with savings amount of Rs. 3673.89 crore (59.3 %) followed by RRBs having savings bank accounts of 18.21 lakh SHGs (26.2% ) with savings amount of 1299.37 crore (21.0%) and Cooperative Banks having savings bank accounts of 10.79 lakh SHGs (15.5 %) with savings amount of Rs. 1225.44 crore (19.8%). The share under SGSY was 16.94 lakh SHGs with savings of Rs. 1,292.62 crore forming 24.4 per cent of the total SHGs having savings accounts with the banks and 20.8 per cent of their total savings amount.

MFI BANK LINKAGE

(i) Capital support to MFI’s

(a) Micro Finance Development Fund

The Micro Finance Development Fund (MFDF) was set up with NABARD by Government of India in 2000-01 with the initial corpus of Rs. 100 crore to be contributed by Reserve Bank of India (40%), NABARD (40%) and Commercial Banks (20%). The MFDF was re designated to Micro Finance Development and Equity Fund (MFDEF) in 2005-06 and the corpus was increased to Rs. 200 crore and same has been further increased to Rs. 400 crore during 2010-11. Accordingly, NABARD formulated a scheme called “Capital/Equity Support to MFIs” in 2007-08 for providing Capital/equity support to various types of MFIs to enable them to leverage commercial and other funds from banks. This would help MFIs in providing financial services at an affordable cost to the poor. During 2009-10, NABARD introduced a new scheme for "Capital Support to start-up MFIs" having potential to scale-up their activities but lacking in capital, infrastructural facilities and managerial skills. Micro-Finance Organizations (MFOs) and MFI-NBFCs, identified as „Start ups „ on the basis of area of operation, client outreach, lending model, borrowing history, etc., are eligible for support under the scheme. Financial support will be in the form of subordinated debt which shall be sub-ordinate to the claims of all other creditors. The quantum of support will be commensurate with the business plan of the MFO / MFI-NBFC but not exceeding Rs. 50 lakh in any case. The rate of interest has been fixed at 3.5 per cent to be repaid over a period of 7 years including moratorium of 2 years.
Friends of Women World Banking

FWWB, India was promoted in 1982 by SEWA Bank, as an affiliate of Women’s World Banking, a global network created to focus on the need for women’s direct access to financial services, recognizing women’s role in building a nation’s economy. Over these years, FWWB combined its loans with technical assistance to ensure sustainable growth of Micro Finance Institutions (MFIs). FWWB supported more than 300 institutions with technical assistance and nearly 200 with loan support of around Rs. 11 billion benefiting 2.6 million women. The loan disbursed to the partner organizations increased from Rs. 403 crores in the year 2008 – 09 to Rs. 498 crores in 2009 – 10, a 23% increase. Loan outstanding portfolio increased from Rs. 294 crores to Rs. 375 crores, a 28% increase. FWWB focused on expanding underserved / underdeveloped regions / areas. During 2009 – 10, FWWB worked in 17 states and supported 117 partner organizations. The outreach increased to 12,68,747 from 10,39,260 active women borrowers. FWWB targeted North and North–Eastern regions of India while supporting organizations working in urban areas of India. FWWB programs were revived or initiated in this year as part of the management effort to increase social impact. Efforts made in
2008 to introduce renewable energy products for our partners in Manipur, made it possible for the women in Manipur to purchase solar lamps this year. The pilot project was supported by SIDBI and 5000 solar lamps were made available this year.

FWWB once again focused on Community Owned MFIs with the support of Repo bank Foundation both in terms of loan and technical support. Inline with FWWB’s focus on women, a new Microfinance product was introduced the Water and Sanitation loan. This was funded by National Housing Bank (NHB) and Michael and Susan Dell Foundation. During this year, 1300 toilets were constructed and 504 water connections were availed through 5 MFI partners in the states of Orissa, Maharashtra and Karnataka. The Citi Foundation continued its funding support to the Livelihood and Enterprise Development (LEAD) program by sanctioning additional funds of Rs.1.6 crores through United Way Worldwide, USA. FWWB continued to support organizations in the states of Assam, Bihar, Gujarat and Tamil Nadu. FWWB, being a member of various networks, has played a significant role in the building of the Microfinance sector. To expand outreach to more institutions and products and services that have significant impact on enhancing the lives of the poor, especially that of women, FWWB had taken the decision to promote a trust India Foundation for Inclusive Growth (IFIG) and a Non Banking Financial Company (NBFC) Ananya Finance for Inclusive Growth Private Limited (Ananya). This year has been truly historical for FWWB as the efforts put in during the last three years. to form an NBFC have borne. Ananya has been registered under The Companies Act, 1956. The FWWB credit portfolio was moved to Ananya on 1st April 2010 FWWB will continue to promote livelihood and self reliance of poor women in the areas of women’s empowerment, strengthening Community Based Institutions, initiating pilots in the areas of livelihood promotion and need based financial products and services that impact the lives of the poor. In this endeavor, FWWB remains guided by Ms. Elaben Bhatt, who is continuing source of guidance and inspiration.

PROGRAMS UNDER FWWB

(i) Institutional and Capacity Building Community Based Organizations (ICB CBO)

The mission of this Program is to identify start-up CBOs and build successful and sustainable organization by providing relevant support.

Support Provided to CBOs:

- Broaden the basket of products/services offered by the CBOs by building/strengthening institutional, functional and operational linkages
- Analyze the grant fund requirement to bring sustainable growth and assist them in accessing the same
- Provide ICB support, which includes but is not limited to providing strategic planning, streamlining accounting procedures, building strong Management Information System (MIS), Human Resource(HR) planning/motivation, facilitating workshops/trainings on good governance & leadeRs.hip training at various organizational levels, legal compliance, financial literacy and financial management
- Assist and guide in leveraging loan support
- Comprehensive on-field need assessment
- Designing plans for long term sustainability
- Customized ICB to cater to the specific needs of the CBOs through class room trainings, on field assistance, workshops, exposure visits and any other inputs
- Designing and implementing high leverage interventions along with the CBO leaders thereby building owneRs.hip of the CBO and the Promoting organizations.

(ii) Institutional and Capacity Building Micro Finance Institutions (ICB MFI)

Over the years FWWB-I as an „apex institution has been supporting and strengthening Microfinance Organizations through its various programs on providing technical assistance, training,
loan and grant support etc. Continuing with institution and capacity building support, FWWB-I is actively engaged in the Institutional Strengthening of startup/nascent organizations. Objective of this Program is to identify and strengthen MFIs that are socially oriented, are new or have been trying to create a successful and sustainable organization but need help, by providing them handholding support to make them self sufficient. The FWWB-I MFI selection process, a fairly intensive process, starts with a desk appraisal followed by a validation and need assessment visit to the organizations. Based on the need assessment, the selected organizations are provided support through class room trainings, on field assistance, workshops, exposure visits and other inputs. Additionally, during the support period, the organizations are monitored at regular intervals. FWWB-I has provided support to over 300+ organizations since 1982. This Program can be fee based or free of cost for organizations that meet criteria of Grant funded Projects.

(iii) Livelihood and Enterprise Development (Lead)

LEAD project was initiated in April 2007, with the aim of providing support to organizations working innovatively for addressing issues of financial inclusion of economically deprived households, by introducing or enhancing livelihood activities. The main objective of the LEAD Program is to support Partner Organizations – Producer Companies, Cooperatives, NGOs, and Enterprises creating alternative livelihood means or additional income sources so as to improve the economic conditions of the very poor household and to promote innovation as one of the solutions of poverty eradication. The experience of supporting and working with enterprises/organizations in the last two years has made us appreciate the fact that along with credit, institution and capacity building support are critical for sustainable interventions in livelihood support. To address this need FWWB-I has now included an intensive Credit plus approach for all organizations that it will be supporting under LEAD. Credit Plus activities start from conducting workshops on creating business plans and the loan application process, providing services basis our need assessment through common and customized technical assistance programs. FWWB-I is currently working with partner organizations in Assam, Bihar, Gujarat, Kerala and Tamil Nadu and has reached out to more than 30,000 underprivileged Households FWWB-I is also working with VIMO SEWA and ISMW to provide an integrated Financial Security Awareness Package. The Financial Security module consists of Financial Literacy and Social Security products.

(iv) Financial Security

FWWB-I has been actively leading and participating in social change through empowerment. While FWWB focuses on income generation, studies world over show that increases in income doesn’t necessarily lead to sustainable improvement in the standard of living. Financial education is one of the proven ways to address this gap. FWWB-I has over the years promoted financial education at the client level through direct interventions and providing grants to Partner Organizations. A new program – „Financial Security“ has been designed in partnership with sister concerns – Indian School of Microfinance for Women (ISMW) and VIMO SEWA. The program is a combination of financial literacy and social security awareness creation along with support for providing linkages.
(v) Solar Energy

Solar Energy program was initiated in December 2009 with an aim to provide access to energy efficient devices for poor households, through our Partner MFIs. Over the years, FWWB-I has been working closely with various micro finance organizations across India. FWWB-I with its various interventions and support from partner organizations has been able to make a positive impact on the lives of the poor households. It was observed that there was a strong need for providing credit plus services to the poor. In a survey of households in the underserved regions, it was observed that there was limited electrification and where available, frequent power cuts. This led to increased household expenditure on usage of alternate sources like candles/kerosene for lighting. This greatly impacted their health and also reduced the productive time available to the women to work, children for studying, etc. The FWWB-I Solar Energy program, was initiated in the state of Manipur, which owing to its geographical location has less than 9 hours of sunlight available during summers. And even lesser during winters. The state also faces frequent power cuts which forces increased usage and spending towards alternate sources of lighting. Till date, FWWB-I have provided loan support towards 30,000 plus solar lamps to the poor through 5 micro finance organizations of Manipur. FWWB-I will be expanding this program across India and look to increasing its partnership with service providers and MFIs and to deepen Social impact by directly impacting the lives of poor households as well as promoting green technologies.

(vi) Water and Sanitation Program (WATSAN)

Access to portable drinking water and proper sanitation is a primary requisite of every human being. In addition to its direct impact on improving the health, particularly of women and children, water and sanitation has indirect impact on life expectancy and the number of working days, and has a big influence on dignity of a woman. FWWB-I initiated interventions on Infrastructure Credit from the year 2000 which took a full swing in the year 2008 – 09 with launch of FWWB-I – Water and Sanitation Program. The main objective of the program is to improve the overall quality of life of women by facilitating access to Water and Sanitation through credit services and awareness creation on hygiene and sanitation. FWWB-I also assists its partner MFI organizations in Training and Capacity Building initiatives, especially in linking with technical consultants for developing training materials on hygiene and sanitation awareness, technical training etc. FWWB-I has supported various MFIs across the country in states like Orissa, Maharashtra, Madhya Pradesh, and Karnataka. It has been very successful in the project and has reached out to about 2000 households by providing credit support through loans for toilet construction and obtaining legal water connections. FWWB-I is planning to reach out to more partners, while supporting the existing ones. With focus on Urban Slums and Rural areas, FWWB-I looks forward to providing holistic support to our partners and beneficiaries. This was reinforced in our discussions with WATSAN partner organizations and industry experts. We believed one of the most effective ways would be to create a platform where our partner organizations can share their experience, brainstorm about “Dos and Don’ts and assimilate best practices in the field of Water and Sanitation. The first of such initiatives was a Workshop on „Best Practices for MFIs on Water and Sanitation‟, scheduled on 1st and 2nd of February, 2011 in Ahmadabad, with participation from more than twenty organizations; including MF Partners., Funders. Technical Experts, etc. Creating this platform and implementing learning emerging from this will go a long way in benefitting women demonstrating much needed sanitation facilities by contributing financially from their meager family income.
CONCLUSION

- 96 per cent of the SHGs constituted women's group with an average of 17 members per SHG.
- 90 per cent of the members owned less than two acres of land.
- Around 40 per cent SHGs were credit linked to RRBs; 30 per cent to CBs and thirty per cent to Co-operatives.
- In developed district of Mysore 22 per cent the members lost interest in attending meetings and meetings were held less frequently.
- Government department promoted groups expected subsidized loans and depended on Anganwadi workers for maintenance of accounts and further guidance.
- NGOs and Govt departments provided better opportunities for training for taking up income generating activities than the banks whose role in the area appeared to be low.
- Training imparted by NGOs / Government agencies, however, was not of substantial help and useful as training imparted did not match the needs of the members.
- Training on routine activities like papad and pickle making etc., were not preferred by the members.
- Average loan amount increased from ` 56,307 in the first linkage to ` 2,13,333 in the fifth dose in all the districts covered under study. Maximum loan availed amounted to
- 45 lakh for a group based activity.
- Nearly 57 per cent SHGs availed loan less than three times of their savings, 24 per cent between three and five times.
- Dependency on money lenders was reduced as about 96 per cent of the SHGs stopped going to money lenders.
- Repayment of loans was made regularly on monthly basis.
- The SHG BLP has led to social and economic empowerment of the rural poor, such as: Ninety two per cent of the SHG members came out of the four walls of the their houses and 76 per cent of the them were able to interact with officials/ give speeches and 28 percent of the members were able to save in banks; the result were seen in decision making in household matter, sending children to school, changing undesirable habits of their spouse, participating in Gram Panchayat election, access to bank credit after joining SHG (98%) as compared to mere two per cent before joining, increase in income by undertaking income generating activities, etc.

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