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MICRO-FINANCE: A TOOL TO ALLEVIATE POVERTY

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ABSTRACT

Microfinance emerged as a noble substitute for informal credit and an effective and Powerful instrument for poverty reduction among people, who are economically active, but financially constrained and vulnerable in various countries. Microfinance covers a broad range of financial services including loans, deposits and payment services and insurance to the poor and low-income households and their micro enterprises. Microfinance institutions have shown a significant contribution towards the poor in rural, semi urban or urban areas for enabling them to raise their income level and living standards in various countries.

In developing countries like India the structure of economy is dualistic. This worsens the access of poor to economic opportunities and financial services. One of the greatest challenges before the Indian sub- continent which accommodates more than one-third of the population is poverty. India, one of the BRIC nations with more than 1.2 billion population is seen by many developed countries as an emerging economy. India's economic growth has failed to make a significant improvement in its poverty figures with 400 million more than the total in the poorest African Nations- still stuck in poverty. Government of India with its concern started various poverty alleviation programs but they have failed to deliver the objectives to the level which is desired. Thus microfinance has come forward to fill up the gap. The Paper discusses the role of microfinance in poverty alleviation.

I. INTRODUCTION

Microfinance is an old concept. It was started in the 19th century during which money lenders were informally performing the role played by formal financial institutions nowadays. Over the past 20 years, various development approaches have been brought in by the policymakers, international development agencies, non-governmental organizations, and others whose aim is to reduce poverty in developing countries. One of these strategies, which have become increasingly popular since the early 1990s, involves microfinance schemes, which provide financial services in the form of savings and credit opportunities to the working poor (Johnson and Rogaly, 1997).

Poverty alleviation has been one of the main principles of the planning process in India. Government has considerably raised allocation for the provision of education, health, sanitation and other facilities which promotes well being of the poor. The Indian government emphasizes on providing financial services to the poor and underprivileged section since independence. The commercial banks were nationalized in 1969 and were aimed to lend 40% of their loans at concessional rate to priority sector. The priority sector included agriculture and other rural activities and weaker section of society in general. The aim was to provide resources to help the poor to start their micro enterprise to attain self sufficiency.

Microfinance is the provision of financial services to low-income, poor and very poor self-employed people (Otero, 2000). Robinson (2001) as cited in Ogunleye (2009) defined microfinance as small scale financial services that involve mainly savings and credit services to the poor. (Samson Alalade Y., Olubunmi Amusa B., Adekunle Olusegun A. 2013) According to Alemu Kassa, T. (2008) The Concept of Microfinance have very important thing. According to Patrick Meagher, microfinance is defined as 'lending small amounts of money for short periods with frequent repayments' (Meagher 2002:7).

The concept of microfinance was created by Professor Muhammad Yunus founder of Grameen bank in Bangladesh and noble price winner in 2006.

Microfinance is the provision of a broad range of financial services such as deposits, loans, payment services, money transfers and insurance to the poor and low income households and their micro-enterprises. Microfinance is defined as Financial Services (savings, insurance, fund, credit etc.) provided to poor and low income clients so as to help them raise their income, thereby improving their standard of living.

II. REVIEW OF LITERATURE

Microfinance is multifaceted and works in an integrated system. There are many stake holders and each one has a definite role to play. In the core there is client. 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 (Mahanta, 2012). Microfinance has been a panacea for poverty reduction in India and thus it is profoundly promoted by our financial system throughout the economy. Financial constraints need to be removed by make favourable Microfinance policy which can lead to entrepreneurial development in India. , Poor people respondents reported an improvement in their quality of food, clothing, education, housing, health services and access to quality life (Tripathi, 2014). Demirguç-kunt, A. & Morduch, J.(2007). "Financial Performance and Outreach: A Global Analysis of Leading Microbanks". They showed that the number of poor people is inferior in countries, where the number of micro-finance institutions is higher compared with countries, where the number of MFIs is lower. (Imai & al, 2010). Recent work macroeconomic levels as Imai Gaiha, Thapa and Annim, 2010; Ahlin & al, 2011 concluded that microfinance is a powerful tool against poverty.

Rationale of Study
The need of microfinance arises because India requires sources of finance for alleviation of poverty. Micro-finance is programme to support the poor section of the society and maintain their economic and social status. The purpose of this study is to examine the overview of micro-finance in India and its growing need for alleviation of poverty.

Objectives of the study
- To study the concept of Micro Finance.
- To study the working and modes of Micro Finance.
- To examine the growth of Micro finance in India.
- To suggest measures to improve the efficiency of Micro Finance institutions.

III. METHODOLOGY

The paper research methodology is based on literature review and secondary data. In the initial section a detailed literature review is done on Microfinance to find the emergence and working of Microfinance institutions and suggested various measure to improve the efficiency. In the latter one published sources and reports were being studied to know the growth of micro finance sector and outreach of micro finance institutions.

Phases of Micro- Finance:
The Indian Microfinance sector has mainly four distinct phases:

Phase 1: (1900-1960)
During this phase, credit cooperatives were the channel to extend subsidized credit to villages under government sponsorship.

Phase 2: (1960s - 1990)
When the cooperatives failed, the government focused on measures such as nationalization of Banks, expansion of rural branch networks, establishment of Regional Rural Banks (RRBs) and the setting up of apex institutions such as the National Bank for Agriculture and Rural Development (NABARD) and the Small Scale Industries Development Bank of India (SIDBI), including initiation of a government sponsored Integrated Rural Development Programme (IRDP). While all these led to covering a large population, this period was pointed as a big misuse of credit, creating a negative perception about the credibility of micro borrowers among bankers, thus further hindering access to banking services for the low-income people.

Phase 3: (1990 - 2000)

When the subsidized social banking failed it triggered a radical shift in delivery of rural credit with NABARD introducing the Self Help Group (SHG) Bank Linkage Programme (SBLP), which aimed to link informal women's groups to formal banks. The program helped increase banking system to cover unreached people and initiate a change in the bank's outlook towards low-income families from 'beneficiaries' to 'customers'. This model created a lot of interest among freshly emerging Microfinance Institutions (MFIs), largely of non-profit origin, to collaborate with NABARD under this program.

Phase 4: (2000-2010)

During the First Decade of the New Millennium Post reforms, rural markets emerged as the new growth drivers for MFIs and banks, the latter taking interest in the sector not only as part of their corporate social responsibility but also as a new business line. On the demand side, NGO-MFIs increasingly began transforming themselves into more regulated legal entities such as Non Banking Finance Companies (NBFCs) to attract commercial investment. The microfinance sector as it exists today essentially consists of two predominant delivery models the SBLP and MFIs. Four out of five microfinance clients in India are women.

IV. MODES TO DELIVER MICRO FINANCE

1. **SELF HELP GROUPS (SHGS)** The Self Help Groups (SHGs) is the predominant microfinance methodology in India. In this the members of Self Help Group pool their little savings regularly at a prefixed amount on daily or weekly basis and SHGs provide loan to members for a fixed period. SHGs are mainly formal and voluntary association of 15 to 20 people formed to achieve common objectives. People from similar groups and common social back ground and occupation voluntarily form such group and pool their savings for the benefit of all of members of the groups. External financial assistance by MFIs or banks raise the resources available to the group. If SHGs are found successful for at least a period of six months, then the bank gives credit usually amounting 4 times more than their savings.
2. **Micro Finance Institutions (MFIs**):**-** The MFI model has also gained importance in India in the recent past. MFI model is found worldwide. In MFI model MFIs borrow huge amount of funds from the apex financial institutions, donors and banks for on-lending to the individuals or groups. These MFIs provide financial services to the individuals or to the groups like SHGs and these institutions lend through the concept of Joint Liability Group (JLG). A JLG is an informal group comprising of 5 to 10 individual members who come together for the purpose of availing bank loans either individually or through the group mechanism against a mutual guarantee. MFIs in India exist in a variety of forms like trusts registered under the Indian Trust Act, 1882/Public Trust Act, 1920; societies registered under the Societies Registration Act, 1860; Cooperatives registered under the Mutually Aided Cooperative Societies Acts of the States; and nonbanking financial companies (NBFC)-MFIs, which are registered under Section 25 of the Companies Act, 1956 or NBFCs registered with the Reserve Bank.
3. **Grameen Model**: **-** Grameen Model was founded by DR Mohammed Yunus of Grameen Bank of Bangladesh. It is the most well known and widely practiced model in the world. In this model the groups are formed voluntarily which consists of five borrowers each. The lending is made first to two, then to the next two and then to the fifth. These five members of the group meet weekly, with seven other groups, so that bank staff meets with forty clients at a time. While the loans are made to the individuals, all in the group are held responsible for loan repayment. According to the rules, if any member defaults, all in the group are denied subsequent loans.
4. **Mixed Model**: **-** Some MFIs were started with the Grameen model but converted to the SHG model at a later stage. They are basically a mix of SHG and Grameen model and the main difference between them is very marginal. According to Vijay Mahajan (2003), Managing Director of BASIX, the SHGs and Grameen models offer economies of transaction cost to MFIs, but at the cost of members time because the unit of dealing is "group" rather than individual. In contrast, MFIs offering individual loans incur higher transaction costs for serving their borrowers.

Growth and Outreach

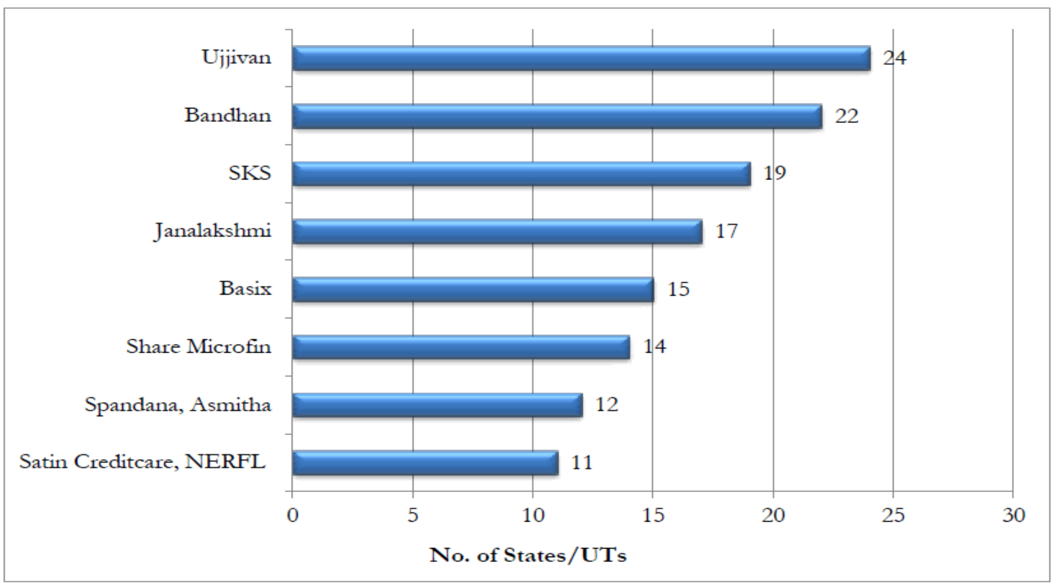
According to Sa-Dhan's(The Association of Community Development and Microfinance Institutions) "Bharat Microfinance Report – 2015" MFI's currently operate in 28 States, 5 Union Territories and 568 districts in India. The reported 156 MFI's with a branch network of 12,221 have reached out to an all-time high of 37 million clients with an outstanding loan portfolio of Rs 48,882 Crore. This includes a managed portfolio of Rs 9854 Crore. The average loan outstanding per borrower stood at Rs 13,162 and 80% of loans were used for income generation purposes.

Outreach grew by 13% and loan outstanding grew by 33% over the previous year. The Southern region continues to have the highest share of both outreach and loans outstanding, followed by East. However growth rates are higher in the North-eastern and Central regions. Outreach proportion of urban clientele is increasing year on year as against the rural population. The proportion of urban clientele which was 44% in 2013-14 increased to 67% in 2014-15. Women borrowers constitute 97% of the total clientele of MFI's, SC/ST borrowers constitute 28% and minorities 18%.

Of the total, NBFC-MFI's contribute to 85% of clients outreach and 88% of outstanding portfolio, while NGO MFI's contribute to the remaining. MFI's with portfolio size of more than Rs 500 Crore contribute significantly to the total outreach (82%) and loan outstanding (85%) of the sector.

Top 10 MFI's in India by Geographical Spread Ujjivan Financial Services has the largest geographical spread with operations across 24 states compared to 22 states for Bandhan Bank and 19 states for SKS Microfinance.

Top 10 MFIs Operating in Number of Indian States/Union Territories



Top 10 MFI's with Loan Portfolio Outstanding

Bandhan Bank is once again the leader followed by SKS Microfinance; Janalakshmi which is an urban focused MFI is placed third with Rs 3774 Crore outstanding.

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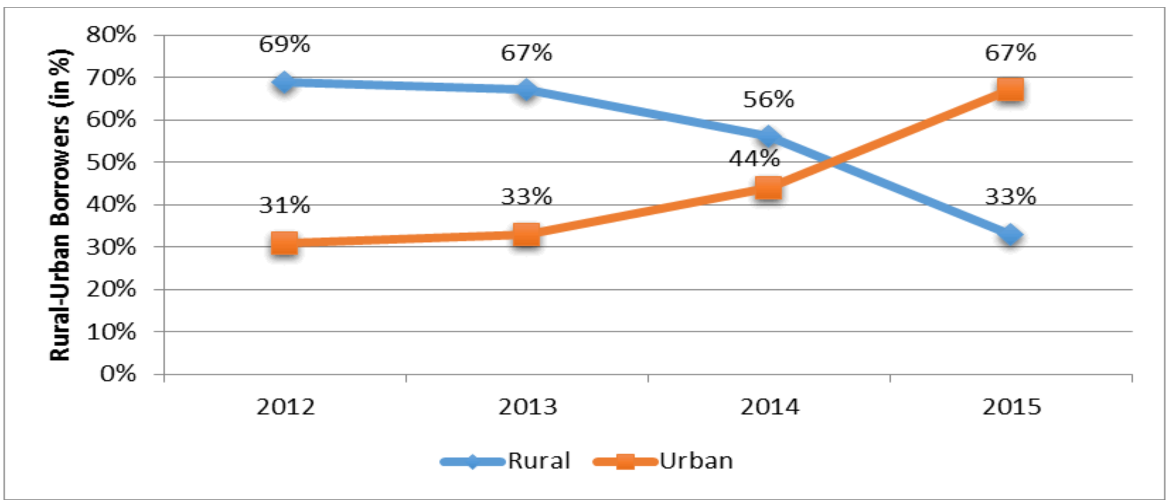
Table 2.4: List of Top MFIs with Loan Portfolio as of March 2015

S.No	Name of MFI	Gross Loan Portfolio (₹ in crore)
1	Bandhan	9524
2	SKS	4155
3	Janalakshmi	3774
4	SKDRDP	3570
5	Ujjivan	3274
6	Spandana	2665
7	Equitas	2144
8	Satin Creditcare	2141
9	Share Microfin	1603
10	Grameen Koota	1447

According to the Bharat Microfinance Report – 2015, 2014-15 can described as watershed year as far as the rural-urban divide in Indian microfinance is concerned. A very interesting trend is seen in the rural-urban focus of MFIs. The share of rural clientele which was 69 % in 2012 decreased to 56 % in 2014 and has drastically come down to 33 %.



Global Acceptance of Microfinance

It is claimed that this new paradigm of unsecured small scale financial service provision helps poor people take advantage of economic opportunities, expand their income, smoothen their consumption requirement, reduce vulnerability and also empowers them (CGAP,2003 ; ADB, 2004).

Former World Bank President James Wolfensohn said “Microfinance fits squarely into the Bank's overall strategy. As you know, the Bank's mission is to reduce poverty and improve living standards by promoting sustainable growth and investment in people through loans, technical assistance, and policy guidance. Microfinance contributes directly to this objective". The emphasis on microfinance is reflected in microfinance being a key feature in Poverty Reduction Strategy Papers (PRSPs).

Realizing the importance of microfinance, World Bank has also taken major steps in developing the sector. Formation of Consultative Group to Assist the Poor (CGAP) in 1995 as a consortium of 33 Public and private development agencies and establishment of Microfinance Management Institute (MAFMI) in 2003 are significant landmarks. CGAP acts as a "resource center for the entire microfinance industry, where it incubates and supports new ideas, innovative products, cutting-edge technology, novel mechanisms for delivering financial services, and concrete solutions to the challenges of expanding microfinance". MAFMI was established with support of CGAP and Open Society Institute for meeting the technical and managerial skills required for microfinance sector. CGAP has been instrumental in shaping the dominant theoretical orientation of microfinance.

Other Regional multilateral development banks like Asian Development Bank also champion the cause of commercial microfinance. ADB (2000, pg 1-2) outlining its policy for microfinance lends support to the logic by saying "to the poor, access to service is more important than the cost of services" and "the key to sustainable results seems to be the adoption of a financial-system development approach". The underlying logic offered in support of this is universally based on twin arguments i.e., a) subsidized funds are limited and cannot meet the vast unmet demand, hence private capital must flow to the sector and b) the ability of the poor to afford market rates. Though, various scholars like Morduch (2000) have brought out the flaws of this Win-Win proposition like belief in congruence between commercial microfinance and poverty outreach, this paper will limit itself to analyzing as to how the focus on commercialization has relegated impact assessment to backstage.

V. RECOMMENDATIONS

Proper Regulation

The regulation was not a major concern when the microfinance was in its initial stage and individual institutions were free to bring in new operational models. However, as the sector completes almost two decades with a considerable growth, a regulatory environment that protects interest of stakeholders as well as promotes growth, is required.

Field Supervision

In addition to proper regulation of the microfinance sector, field visits can be adopted as a medium for supervising the conditions on ground and taking corrective measures if required. This will keep a check on the performance of ground staff of various MFIs and their recovery practices. This will also encourage MFIs to follow proper code of conduct and work more efficiently. However, the problem of feasibility and cost involved in physical monitoring is huge which remains an issue.

Encourage rural penetration

It has been observed that instead of reducing the initial cost, MFIs are opening their branches in places which already have a few MFIs operating. Encouraging MFIs for opening new branches in areas of low microfinance penetration by providing financial assistance will increase the outreach of the microfinance in the state and check multiple lending. This will also increase rural penetration of microfinance in the state.

Complete range of Products

MFIs should provide complete range of products including credit, savings, remittance, financial advice and also non-financial services like training and support. As MFIs are acting as a substitute to banks in areas where people don't have access to banks, providing a complete range of products will enable the poor to avail all services.

Transparency of Interest rates

As it has been noticed that, MFIs are employing different patterns of charging interest rates and a few are also charging additional charges and interest free deposits (a part of the loan amount is kept as deposit on which no interest is paid). All this make the pricing very confusing and hence the borrower feels incompetent in terms of bargaining power. So a common practice for charging interest should be followed by all MFIs so that it makes the sector more competitive and the beneficiary gets the freedom to compare different financial products before buying.

Technology to reduce Operating Cost

MFIs should use new technologies and IT tools & applications to reduce their operating costs. Though most NBFCs are adopting such cost cutting measures, which is clearly evident from the low cost per unit money lent (9%-10%) of such institutions. NGOs and Section 25 companies are having a very high value of cost per unit money lent i.e. 15-35 percent and hence such institutions should be encouraged to adopt cost-cutting measures to reduce their operating costs. Also initiatives like development of common MIS and other software for all MFIs can be taken to make the operation more transparent and efficient.

Alternative sources of Fund

In absence of adequate funds the growth and the reach of MFIs become restricted and to overcome this problem MFIs should look for other sources for funding their loan portfolio. Most of the microfinance institutions are converting into NBFC MFIs in order to have easy access to funds from banks. This transformation is due to the profit motive of the microfinance institutions. The microfinance institutions should be given the access to raise funds from capital markets providing they are well rating in their performance.

Sufficient Repayment Time

Most of the micro-loans are given for the start of micro-enterprises and the loan should have to be repaid from the cash flows generated from the business. Hence, sufficient repayment time should be given by the microfinance institutions to the borrowers.

Regular Audits

Regular audits such as ACCION audit could be conducted by the regulatory authority to monitor the performance of MFIs. Subsidies could be provided for these audits as most of the MFIs do not undergo this audit as it is expensive.

VI. CONCLUSIONS

This paper examined the critical role of microfinance in developing the rural poor and substantially contributing to the national objective of poverty alleviation.The scope for growing micro finance institutions in India is very high. Major sections can benefit if this sector grows at a fastest pace. The loan outstanding will consequently grow from the present level of about 1600 crores to about 42000 crores Annual growth rate of about 20 % can be achieved during the next five years. Attaining financial viability and sustainability is the major institutional challenge. Deposit mobilization is the major means for microfinance institutions to expand outreach by leveraging equity (Sacay et al. 1996).

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