AN ANALYSIS OF ROLE OF MICRO FINANCE IN PROMOTING FINANCIAL INCLUSION

HAILLY KUMARI

(Research Scholar)

University Department of Commerce & Business Management, Ranchi University, Ranchi

DR. ASHISH MOHAN
Research Scholar (D.Litt.)
University Department of Commerce & Business Management, Ranchi University, Ranchi

ABSTRACT

This paper focuses on the role of micro finance in the empowerment of people and the realization of financial inclusion in India. India is a large segment of the society, which has particularly low-income people, have very little access to formal financial services. Micro finance is emerging as new paradigm for promoting financial inclusion plays prominent role in eradicating the poverty from country. The Indian government and RBI has been making proactive steps in promoting 'Financial Inclusion' reaching out to the un-banked and under-banked populace in partnership with MFIs and/or Pvt. Ltd. Cos. The two manifold mechanisms for promoting such financial services are: (1) Developing relationship-based banking for entrepreneurs and small businesses; and (2) group-based models, for promoting entrepreneurs to apply against loans and other services as a group. MFIs contribute in bringing up of the society leading to economic benefit of the country as a whole.

Keywords:

Financial inclusion, Microfinance, Poverty reduction & inequality elimination, Self Helped Groups(SHGs)

INTRODUCTION

"The poor stay poor, not because they are lazy but because they have no access to capital" - Milton Friedman

Since the beginning microfinance has played a key role in financial Inclusion in India, as it came into existence mainly to serve the smaller and overlooked sections of society. Microfinance companies can play a vital role in providing financial services in remote areas, as per Reserve Bank of India. "There is no banking facility present in remote areas and therefore, these companies can play a major role in providing financial services in these areas and to the last man in the society," said Reserve Bank of India (RBI) Regional Manager Murali Ramkrishna. They caters to the financial needs of people of the lowest strata by providing small loans without any guarantees, despite of it, their loan recovery rate is 98 per cent, which is of great surprise. Microfinance Institutions (MFIs) is one of the fastest growing segments in the recent years in terms of reaching out to small borrowers. Microfinance institutions act as supplement and supporter to the services offered by banks. It not only offers micro credit but also provides financial services such as insurance, savings, and remittance. Non-financial services such as training, checking, and supporting borrowers are made available in the most convenient manner as well. Microfinance is a way in which loans, credit, insurance, access to savings accounts, and money transfers are provided to small business owners and entrepreneurs in the underdeveloped parts of India. Micro finance aims at easy access to finance, especially by the poor and un-banked groups is a prerequisite for employment, economic growth, poverty reduction and social cohesion. Microfinance is a wide category of services, which includes microcredit. That aims at delivering of banking services to masses including privileged and disadvantaged people at an affordable terms and conditions. The initial success of Grameen Bank in alleviating poverty brought the concept of microfinance into the global limelight and led to form a group of bankable individuals. Micro finance promote loans granted to the poor and low-income households for their microenterprises and small businesses in order to raise income levels and as a result raising their living standards. Micro financing loans are small loans granted to the basic sectors. The main aspect of micro credit is that the loan is given without the requirement of any collateral security.

DEFINITION OF MICROFINANCE

Microfinance is a kind of financial services that targets individuals and small businesses who lack access to promote conventional banking and other related services. Microfinance services are designed to reach customers mainly to the poorer segments of population and also possibly socially marginalized, or geographically isolated in order to help them become self-sufficient. Microfinance consists of microcredit to provide provisions of promoting small loans, mobilizing savings and checking accounts to poor clients and also to provide the facility of micro insurance; and other payment systems. Microfinance initially promotes the provision of issuing microloans to entrepreneurs who are poor and to small businesses lacking an access to credit. The two manifold mechanisms for issuing of financial services to such type of clients are: (1) Establishing relationship-based banking for individual entrepreneurs and small businesses; (2) group-based models, so as to enable several entrepreneurs to apply against loans and other services as a whole. Microfinance has emerged as a mass movement whose subject is "a world that as everyone, mainly the poor and socially marginalized people and households to promote access to a large range of affordable, high quality financial products and services that not only includes credit but also promotes and accesses savings, insurance, payment services, and fund transfers." So as to have an access poor people to get rid of poverty. Microfinance promotes economic development, economic growth and also helps to generate employment by supporting micro-entrepreneurs and small businesses in a way to manage their finances more efficiently and effectively and also to tap up with the new opportunities and advantages of economic environment along with mitigating the risks.

TYPES OF MICROFINANCE

Microfinance includes the following:

- **Microloans** - Microfinance loans are loans made available to borrowers with no collateral. The result of microloans should outgrow the recipients of small loans and also to prepare for traditional bank loans.
- **Micro-savings** – Micro-savings allows entrepreneurs to operate savings accounts with no minimum balance. These accounts help users in inculcating financial discipline and also to develop an interest in saving.
- **Micro-insurance** – Micro-insurance is a form of coverage provided to borrowers of microloans. These insurance plans have lower premiums than traditional insurance policies.

OBJECTIVES

Role and importance of micro finance in Indian Financial System:

- To introspect the role of micro finance as promoting financial inclusion.
- To examine benefits of financial institutions in extending micro finance services.
- To enumerate the achievements and problems of SHG microfinance in including the excluded section of the society.
- Providing the poor with access to financial services an opportunity for them to build their financial capacity ability to grow to financial self-sufficiency.

- Providing women with the easy opportunity to access the financial activity to start their own businesses and a chance to actively participate in the economy.

BENEFITS AND LIMITATIONS

Microfinance concept started with the idea of providing financial services to the poor who are otherwise considered un-bankable or poor bankable or credit-unworthy.Micro financing promotes many benefits to poverty stricken and low-income households. One of the benefits is easy accessibility to Banks for small size loans. In general banks don't extend loans to ones having little or no assets. Micro financing is based on the theory that even small amounts of credit can help to end the cycle of poverty. Another benefit produced from the micro financing initiative is tapping against the present opportunities, such as extending education of their children, enhancing job opportunities, promoting entrepreneurial activities, raising standard of living by opening small businesses that will aid in creating of new job opportunity. Overall, the benefits outline that the micro financing initiative is set to improve the standard of living amongst impoverished communities. Micro finance promotes protection against risk. There are many social and financial challenges faced by microfinance initiatives too, more articulate and better-off community members may cheat upon poorer ones or less-educated folks. It may happen intentionally or inadvertently by loosely run organizations. Microfinance initiatives require a large amount of social capital or trust in order to work effectively. The ability of poor people to save may fluctuate from time to time from saving little to none. Rates of inflation may create lose their value of funds, as a result financially harming the saver and not benefiting the collector.

CHANNELS OF MICROFINANCE

Microfinance in India operates primarily through two channels:

- SHG-Bank Linkage Programme (SBLP) – SBLP was initiated by NABARD in the year 1992. This channel encourages financially backward women to come together to form groups of 10-15 members and contribute their individual savings to the group at regular intervals. Loans are provided from these contributions to members of the group. SHG also offers bank loans at later stages, and these loans can be used for funding incomes. This channel has achieved a lot of success in the past and has also gained a lot of popularity for contributing to the empowerment of women in the country. Once these self-sustaining groups reach the stage of stability, they function almost independently with minimal support from NABARD, SIDBI, and NGOs.

- Microfinance Institutions (MFIs) - These institutions promote microfinance as primary operation. They lend through the concept of Joint Liability Group (JLG), i.e., an informal group that consists of 5-10 members who seek loans either jointly or individually.

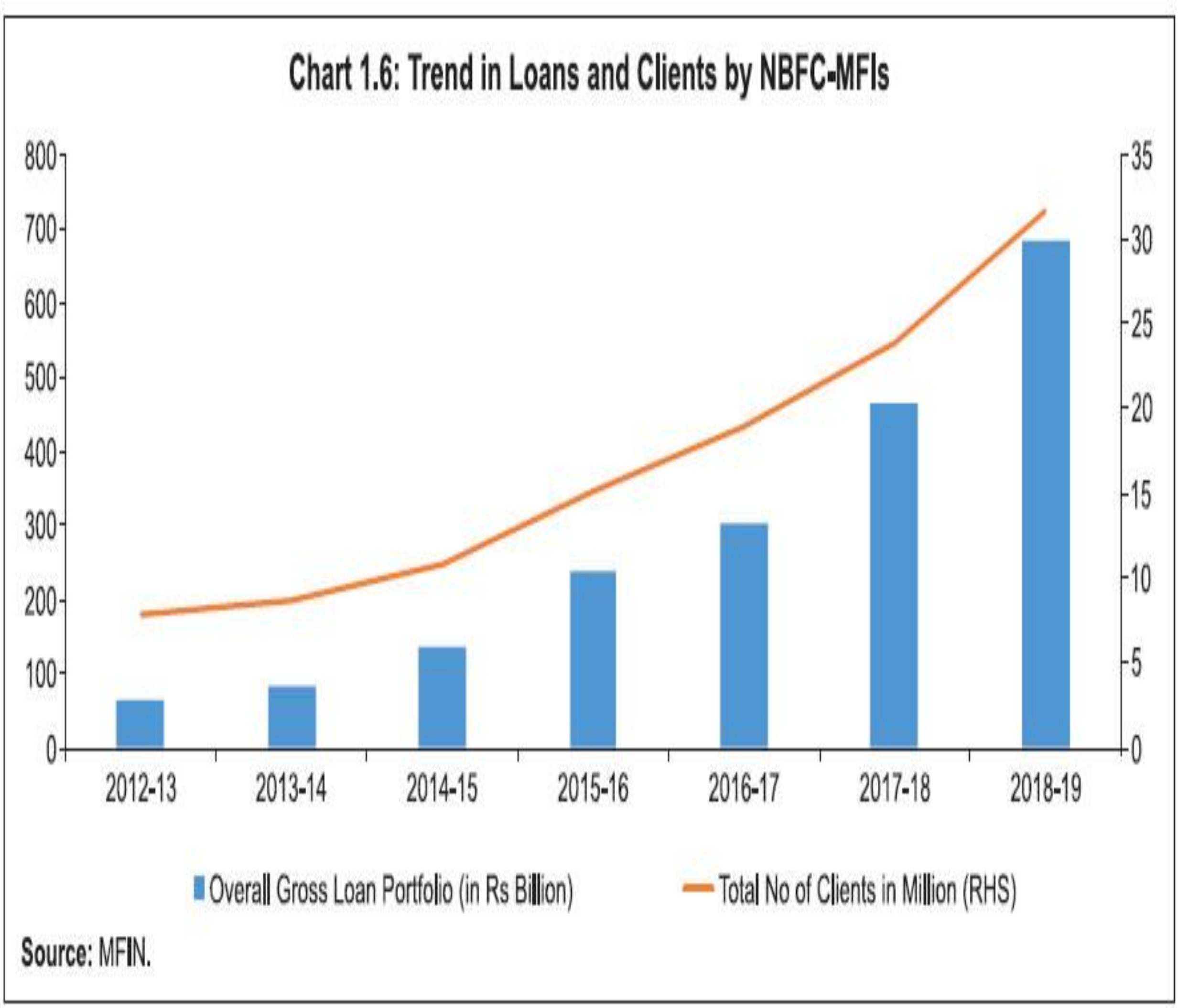
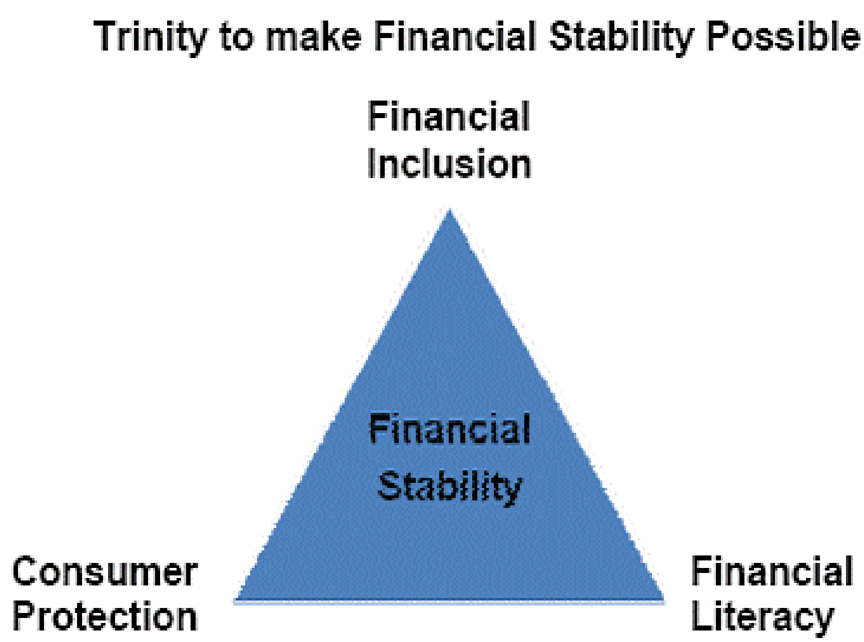


Chart 1.6: Trend in Loans and Clients by NBFC-MFIs
800
700
600
500
400
300
200
100
0
35
30
25
20
15
10
5
0
2012-13
2013-14
2014-15
2015-16
2016-17
2017-18
2018-19
Overall Gross Loan Portfolio (in Rs Billion)
Total No of Clients in Million (RHS)
Source: MFIN.

Financial inclusion-meaning, growth and challenges

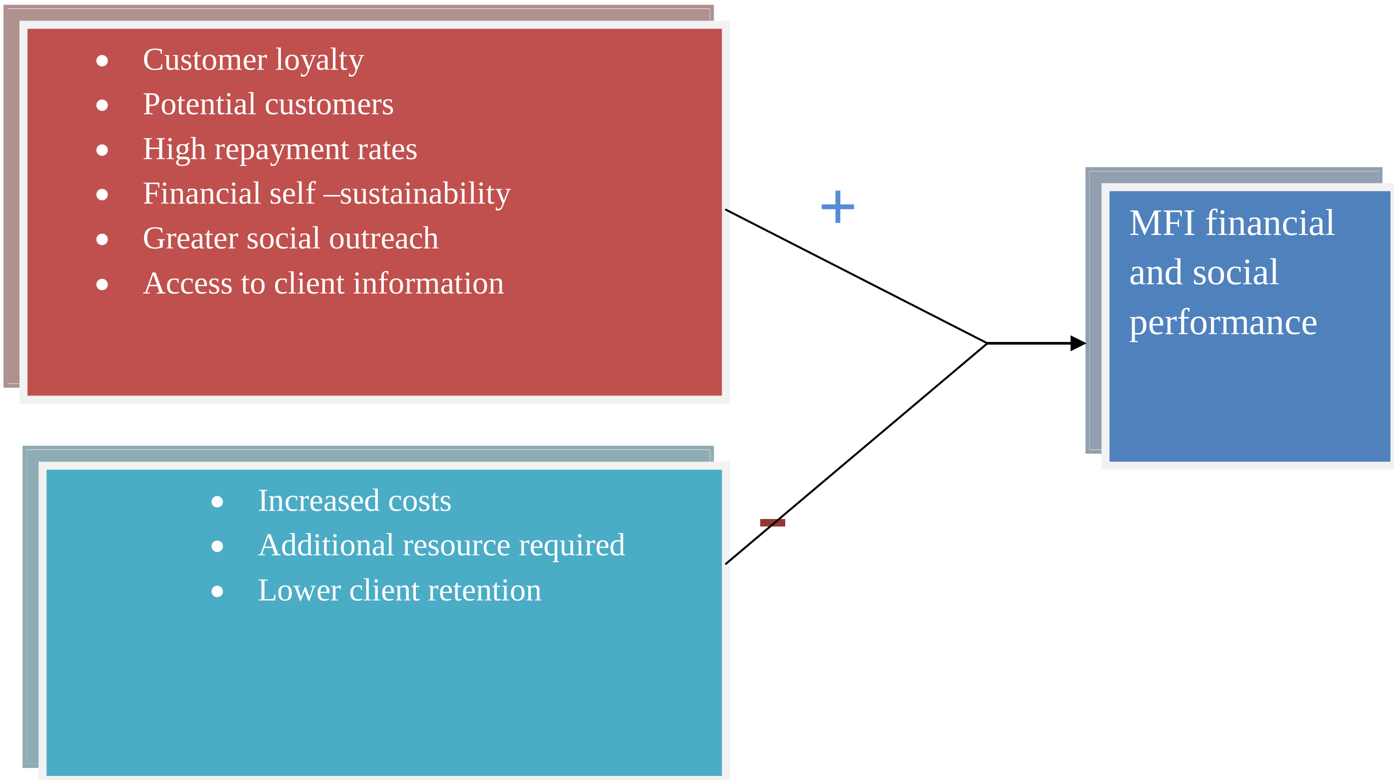
Financial inclusion is a set of measures that placed to combat banking and financial exclusion. It consists of a range of financial and non-financial products and services made available to the poor. Micro insurance with all possible variants related to insurance (climate risk, death, etc.), Different credit products, Pension, Savings products, Money transfer etc are some of the financial services. Training(in business management, risk management, governance, etc.), Decision support software, Advice and technical expertise, Financial education and awareness are some of the Non-financial services. Financial inclusion helps poor ones to finance their activities, save, support their families and protect themselves against risks. Microfinance institutions (MFIs), cooperatives, micro insurance providers, banks, etc are some financial institutions which signify their distribution on market. To fight against poverty it is important for distributors to be socially responsible in order to achieve the main objective of financial inclusion. Financial inclusion is an important priority of the country in terms of economic growth and advancement of society.

Financial inclusion aims at widening the access to affordable and responsible (non-banking) and (non-financial) products and services for populations excluded from the traditional banking system. To ensure benefits for population, a range of products and services have been developed with, appropriate banking services, the best known being microcredit. Nowadays various financial services, far beyond the microcredit have been promoted such as: money transfers, micro-savings, micro insurance, micro-pension. These have enormous potential for development.



IMPACT OF MICROFINANCE ACTIVITIES

The figure below represents: Microfinance ‘plus’ outcomes.



Source: KPMG in India analysis 2019

RECENT RBI REGULATORY UPDATES

In response to cater against the request of the micro finance lenders and to promote MFI growth, RBI increased the lending cap for borrowers and semi-urban areas recently during October 2019:

1. The annual household income eligibility in rural areas increased from INR 1 lakh to 1.25 lakhs and in urban/semi-urban areas from INR 1.6 lakhs to 2 lakhs.

2. The lending limit per borrower has also increased manifold from the first cycle from INR60k to INR75k and for subsequent cycle INR1 lakh to 1.25lakh.

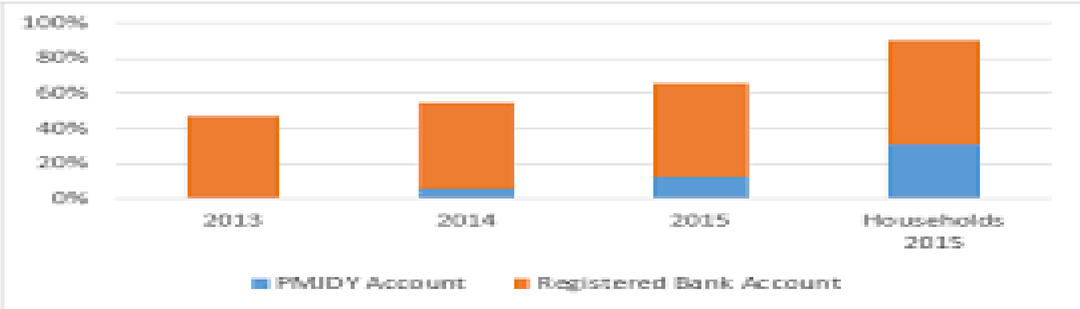
Role of microfinance in promoter of financial inclusion in the economy

This is quite opportune and timely that NBFCs, microfinance institutions (MFIs) and other financial institutions have played a significant role in taking up as an effort for promoting financial inclusion. Now we are at a peak point needing to unleash the next set of financial inclusion interventions for converting a large part of our population to efficient consumers of financial services. For this various technological transformation is taking place in associated areas by the microfinance industry which is playing a prominent role in identifying, enabling and handholding a sizeable set of the population to consume financial services rationally, and also to grow out of poverty and become productive citizens of the country. Microfinance involves promotion of small loans and other financial services to low income groups as an important economic conduit designed to facilitate financial inclusion and help the poor to get rid out of poverty. Microfinance aims to facilitate the achievement of national policies that is target of the nation as poverty reduction, empowerment of women, assisting vulnerable groups, and improving standards of living.

Two decades ago, the absence of technology and infrastructure was a major challenge restricting the growth and expansion of banking services to far-flung areas of the country consisting of over 600 thousand villages. Institutionalization of the framework of Business Correspondents (BCs) is a major step towards enhancing access to banking services. The RBI promoted a combination of ‘Brick and Mortar’ structure along with technology for extending financial inclusion in the geographically dispersed areas. These measures led to an increase in number of banking outlets in villages significantly.

The journey of financial inclusion in the past two decades has been taken an intensive efforts and incremental experimentation. The extraordinary jump came when Pradhan Mantri Jan Dhan Yojana (PMJDY) was launched in 2014 that promoted the achievement of aim of providing bank accounts to adult population in almost every household. The access of mobile phones and e-KYC has ensured that these accounts are accessible to all who have been included in the financial services. The Reserve Bank of India is taking sustained efforts to increase the penetration of formal financial services in unbanked areas and at the same time continuing with its existing and new policy of ensuring adequate flow of credit to productive sectors of the economy and also ensuring the availability of banking services for all sections of society and people in the country as a whole.

Figure 1: Bank Account Ownership in India (2013-2015)



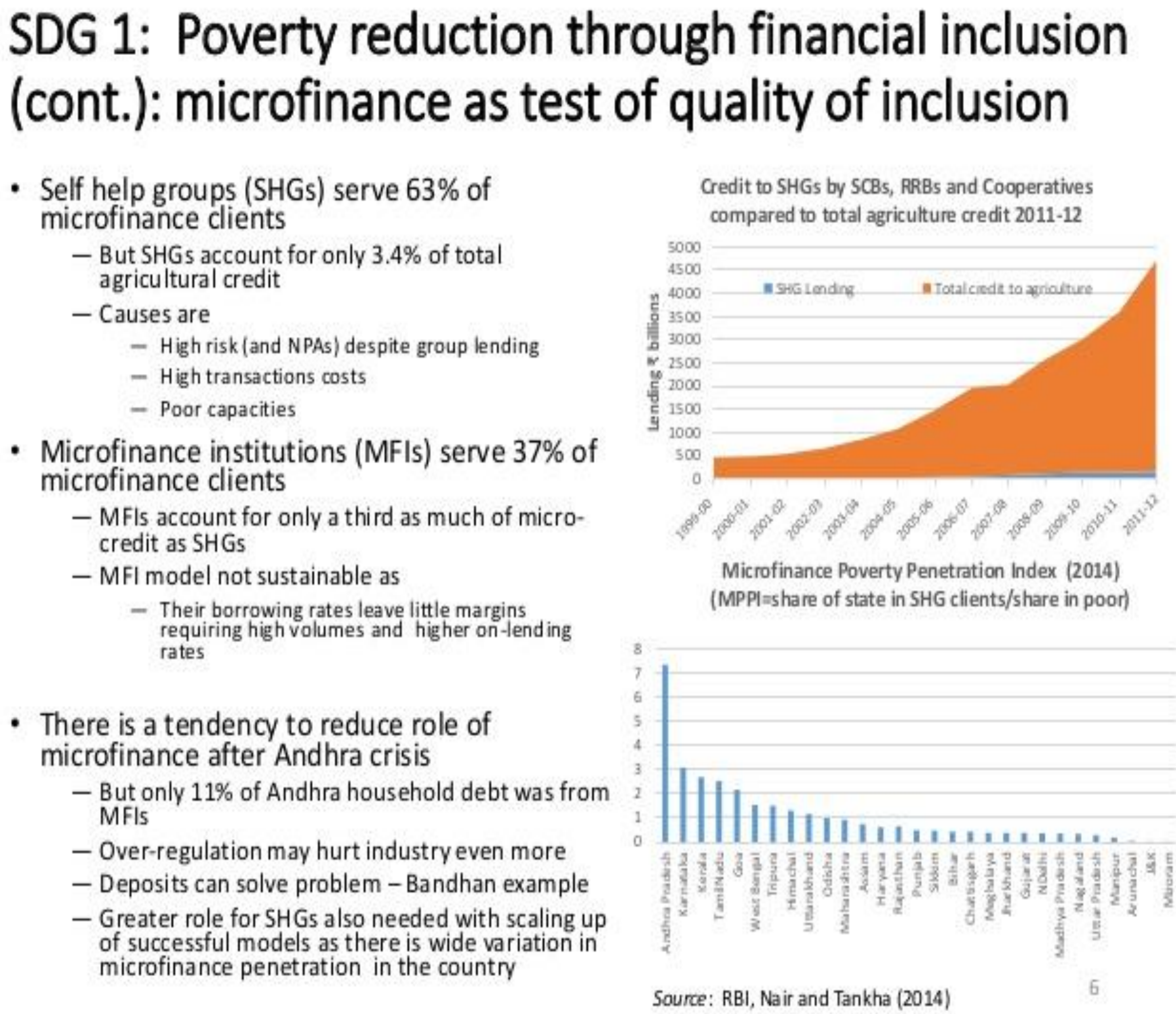
Source: Financial Inclusion Insights Surveys (n=135,147) & FinScope India (n=16,000)

The new banking entities considered the strong link between financial inclusion and payment systems by country taking several steps like encouraging use of mobile banking, pre-paid instruments such as digital and mobile wallets so as to promote in the financial inclusion. Financial inclusion is becoming a focus area for banks, NBFCs, Financial Technology and other financial entities. Banks work hard to sustain the momentum for achieving the objective of financial inclusion. Small Finance Banks have been set up with a client base comprising mainly of migrant workforce, low income households, small businesses and other unorganized sector entities to further promote financial inclusion. There are several channels like universal banks, small finance banks, micro finance institutions, BCs that determines universal financial inclusion at affordable cost as a defining moment for financial inclusion and microfinance. Several innovative measures have been undertaken by the RBI, for the country to facilitate the formation of convenient environment and increasing the penetration level of the banking system to promote access and aid to un-served and underserved population in order to attain the objective of sustainable and inclusive economic growth. Co-origination model enables the scheduled commercial banks (excluding Regional Rural Banks and Small Finance Banks) to co-ordinate loans with the non-deposit systemically taking important NBFCs that has been moved out for credit delivery to the priority sector. It is expected to boost lending to micro enterprises, small and marginal farmers, Self Help Groups (SHGs), etc. The Reserve Bank has suggested all Scheduled Commercial Banks (excluding Regional Rural Banks and Small Finance Banks) that bank should credit for registered NBFCs (other than MFIs) for on-lending which will be eligible for classification as priority sector under certain conditions for respective categories for boosting credit to needy segment of borrowers.

The Committee made various recommendations in areas like legislative and institutional framework, access to finance, capacity building and new technological interventions for lending to MSME sector and the same has been recommended. The Micro, Small and Medium Enterprises play a vital role in contributing towards employment generation, inclusive growth, promoting exports, innovation activity for the economy. In light of this, the Reserve Bank had constituted an 'Expert Committee on Micro, Small and Medium Enterprises' (Chairman: Shri U. K. Sinha) to identify causes and remedy of long-term solutions for the economic and financial sustainability of the MSME sector. The RBI adopted a planned and structured approach to address against the issues of financial inclusion by establishing a focus on both the demand and supply. With the development of formalized form of financial services, we should intensify efforts on the demand side as a result enhancing capabilities so that individuals with low income groups are in a position to not only to avail the offered services, but also capable of demanding preferred products and services. The importance of the microfinance sector in our economy has also been steadily growing. The MFIs are also expanding into newer territories for reducing their concentration risk. According to The Bharat Microfinance Report 2019 prepared by Sa-Dhan, MFIs operate in 29 States, 5 Union Territories and 570 districts in India. Tailored products provide credit to those who don't have a credit score, entrepreneurial and consumption credit, handholding, financial literacy, social occasion credits and insurance. The RBI defines Financial Inclusion as the "process of ensuring access to appropriate financial products and services needed by all sections of the society in general and vulnerable groups such as weaker sections and low income groups in particular, at an affordable cost in a fair and transparent manner by regulated, mainstream institutional players". It gives the Vision to make financial services available, accessible, and affordable to all citizens in a safe and transparent manner to support inclusive and resilient multi-stakeholder led growth.

The Indian microfinance sector has witnessed a significant amount of phenomenal growth over the past two decades. It is to note that both the number of institutions providing microfinance as well as the quantum of credit made available to the financially excluded clients have increased manifold during this period. It is equally important to discuss the way forward at this point of time. Therefore one must consider emerging concerns / issues faced due to major changes in the sector in recent years; strategic drivers, trends and possible solutions for stimulating industry growth, innovative, futuristic and high-impact business models being taken up across the sector for technological transformation in the industry. The National Strategy for Financial Inclusion (NSFI) 2019-24 has been framed.

ISSN: 2278-4632
Vol-10 Issue-7 No. 7 July 2020



CONCLUSION

Financial exclusion is a manifestation of social exclusion Microfinance sector is subject to significant changes amidst of growing competition, rising expectations of masses, technological up gradation and an evolving regulatory landscape. The sector expects to transform the livelihoods of the borrowers by widening micro credit beyond certain platform. The sector should continue to pursue the adoption of innovative, futuristic and high-impact business models as Digital Microfinance. In light of increasing transparency, the financing institutions should safeguard the interests of low-income customers, lay interest on their clients first and implement the Code for Responsible Lending, redressing grievances of consumer complaints quickly and effectively as an agenda for MFIs and the Self Regulatory Organisations (SROs). Banks, NBFCs and financial institutions are placed to innovate in cutting-edge technologies so as to lend to the micro and small enterprises and broaden their client outreach to reduce concentration risk. Financial Inclusion is a vital component of the inclusive growth viewed as a tool for the overall development of the economy. Micro finance promotes Micro insurance and remittance facilities looked as variety of schemes to alleviate poverty and empower rural people. SHGs are the main medium for rural employment generation, encouragement and support by the Government will solve the problem of rural unemployment. Microfinance helps to build empowerment among the poor or less or un-served sections of society. Financial inclusion establishes a negative relationship with poverty & inequality.

REFERENCES

1. https://www.igi-global.com/chapter/role-of-microfinance-in-financial-inclusion-in-india/206386
2. https://economictimes.indiatimes.com/industry/banking/finance/microfinance-firms-can-play-role-in-financial-inclusion-rbi/articleshow/48348803.cms
3. https://www.adb.org/sectors/finance/issues/financial-inclusion-microfinance
4. https://home.kpmg/in/en/home/insights/2019/12/mfi-microfinance-contributions-to-financial-inclusion.html
5. https://shodhganga.inflibnet.ac.in/bitstream/10603/152211/2/11.%20chapter-4.pdf
6. https://www.researchgate.net/publication/311203640_Financial_Inclusion_and_Micro-Finance_in_India_An_Overview
7. https://www.sciencedirect.com/science/article/abs/pii/S0160791X16300811
8. https://www.ada-microfinance.org/en/about-ada/definition-financial-inclusion
9. https://en.wikipedia.org/wiki/Financial_inclusion
10. https://en.wikipedia.org/wiki/Microfinance
11. https://www.reliancemoney.co.in/microfinance
12. https://financialservices.gov.in/financial-inclusion
13. https://www.sciencedirect.com/science/article/pii/S0186104217300104