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MICROFINANCE: AN APPROACH FOR FINANCIAL INCLUSION IN INDIA

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ABSTRACT

Financial inclusion is the process of availing a range of required financial services, at a fair price, at the right place, form and time, through formal means and without any form of discrimination to the populace. Micro Finance has emerged as an effective approach for achieving financial inclusion in the country. It provides micro financial services to the poor (individual or group) at their doorsteps and enables them to raise their level of income and standard of living. Therefore, this paper is an attempt to study the concept and contribution of microfinance for achieving financial inclusion in India. The findings of the study reveal that microfinance plays an important role in achieving financial inclusion in India through its two programmes i.e. SHG-Bank Linkage Programme and MFI-Bank Linkage Programme. These programmes have been successful in providing financial services to a large number of the poor. However, the beneficiaries of the microfinance programmes need to be self-sustainable to have prolonged effect on their well-being and society as a whole.

Keywords: Microfinance, Financial Inclusion, India, Banks, Savings, Loans, SBLP, MFIs.

1. INTRODUCTION

Access to finance is a critical factor which enables people to engage in production and employment activities, and reduce poverty (Kumar & Mishra, 2011). Inclusion in the financial services brings positive and significant changes in general and economic condition of people (Uma & Rupa, 2013) and brings economic prosperity to region or state (Gupta, Chotia, & Muralidhar, 2014). Financial inclusion has been given a policy priority in many countries across the globe because of its contribution in building an inclusive financial system (Bawa, 2014). Building inclusive financial system can improve peoples' life, particularly of the poor (Chugh,

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2015). Financial Inclusion in simple terms is defined as the provision of banking services for the vast sections of disadvantaged and low income groups at an affordable cost (Leeladhar, 2006). It is the process that ensures the ease of access, availability and usage of the formal financial system for all members of an economy ((Sarma & Pais, 2008) and (Paramasivan & Ganeshkumar, 2013)). Thus, financial inclusion is the process of availing a range of required financial services, at a fair price, at the right place, form and time, through formal means and without any form of discrimination to the populace (Kalunda, 2014). There is a wide spread belief that viable financial inclusion in the rural areas or in the unorganized sector is better achieved through alternative channels such as Micro Finance (Ghosh, 2007).

Micro Finance in India has emerged as a powerful tool for Financial Inclusion. Micro Finance is a novel approach to "banking with the poor". Micro finance is a system of providing financial assistance to the poor, to free them from the clutches of local money lenders and enable them to undertake economically productive activities for attaining community development (Arputhamani & Prasannakumari, 2011). Microfinance is defined as "provision of thrift, credit, and other financial services and products of very small amounts to the poor in rural, semi-urban and urban areas for enabling them to raise their income levels and improve their living standards" (Thakral, Uppal, & Chawla, 2010). Its purpose is to provide door-step banking to the poor (individual or group) on one hand and contribute in building human capital through self-initiative of people on the other hand. It is a cost-effective tool for poverty alleviation, employment generation and financial inclusion. It is referred as banking through groups i.e. to provide financial services through the group of individuals formed either in joint liability or co-obligation mode (Kote & Honnakeri, 2012).

2. NEED, OBJECTIVES AND SCOPE OF THE STUDY

In India, a nation of 1.2 billion people, with around 6 lakh villages and 640 districts, a large proportion of population, especially in rural areas, still remain excluded from the formal financial system. This hampers people's ability to earn, protect themselves in times of crisis, and to build for the future (Chhabra, 2014). It is estimated that about 40 percent of Indians lack access even to the simplest kind of formal financial services (Maheswari, 2015). Therefore, this paper makes an attempt to study the concept and contribution of microfinance for financial inclusion in India. The specific objectives of the study are as under:

i. To study the concept of microfinance as an approach for financial inclusion in India.
ii. To analyze the contribution of microfinance for financial inclusion in India.

The study is based on the secondary data collected from various sources viz. reports of National Bank for Agricultural and Rural Development (NABARD), journals, magazines, newspapers,

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website portals etc. The analysis has been done for a period of 10 years i.e. from 2006-07 to 2015-16.

3. DISCUSSION AND RESULTS

3.1 Microfinance in India

In India, microfinance operates through two channels:

- **Self-Help Group (SHG) Bank Linkage Programme**
  Microfinance activities were initiated in India in 1992 with the commencement of Self-Help Group Bank Linkage Programme (SBLP) by National Bank for Agriculture and Rural Development (NABARD). The SBLP is a cost-effective mechanism to meet financial needs of the poor across vast geographic regions of the country through formation of self-help groups. According to the Reserve Bank of India (RBI), "a Self-Help Group (SHG) is a registered or unregistered group of micro-entrepreneurs having homogenous social and economic background, voluntarily coming together to save small amounts regularly, mutually agree to contribute to a common fund and to meet their emergency needs on mutual help basis" (Sudarshan, Narasamma, Krishna, & Himachalam, 2011). The main aim of SBLP is to provide banking facilities to the SHGs directly and/or through intermediaries for productive and consumption purposes. This approach replaced the need of collateral with group guarantee and peer pressure, making it a convenient model for both client and provider.

- **Micro Financing Institutions (MFIs) Bank Linkage Programme**
  Microfinance has also been accepted as a business opportunity. It has given birth to Micro Financing Institutions (MFIs) which play an important role of financial intermediaries to promote financial inclusion. The MFIs operate under various legal forms like Non-Government Organization (NGO) MFI, Co-operative MFI, Non-Banking Financial Corporation (NBFC) MFI incorporated under section 25 of Companies Act 1956 (not for profit) and NBFC MFI registered with RBI (for profit). They get financial assistance in the form of bulk loans from banks for on-lending to groups and other small borrowers.

3.2 Microfinance Delivery Models

Microfinance activities operate in India through three broad models:

a. ***Model I: Banks – SHGs Model***

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In this model, SHGs are promoted and financed by the banks. Banks form the groups, nurture them over a period of time, open their basic savings account and then provide them credit when they are eligible to absorb it (figure 1).

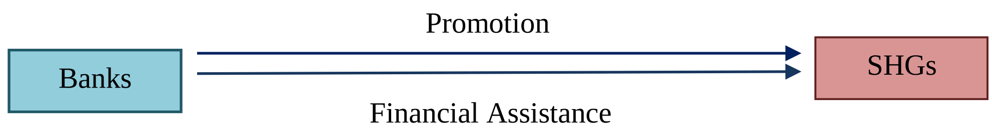

Figure 1

b. ***Model II: Banks – Facilitator Agencies – SHGs Model***

In this model, NGOs or formal agencies working in the field act as facilitators. They assist in organizing, forming, nurturing and training of SHGs. Banks provide loans directly to those SHGs after observing their operations and eligibility to absorb credit (figure 2).

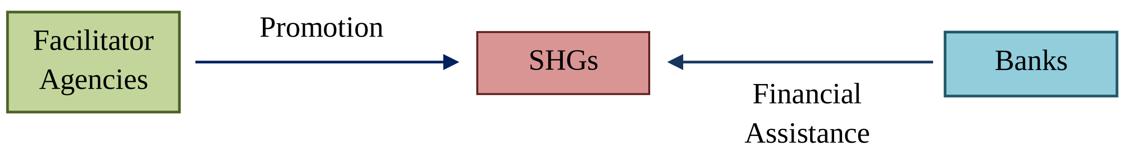

Figure 2

c. ***Model III: Banks – NGOs/MFIs – SHGs Model***

In this model, NGOs, SHG Federations or MFIs act both as facilitators and microfinance intermediaries, especially in the areas in which outreach of banks is low. They promote, nurture and train SHGs, and then approach banks for bulk loans for on-lending to SHGs.

Figure 3

(Source: (Grover & Singla, 2013))

3.3 Contribution of Microfinance

Microfinance has emerged as an effective strategy to serve the financial needs of the poor through various financial institutions like commercial banks, co-operative banks and regional

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rural banks (RRBs) in India. The analysis of the contribution of microfinance for financial inclusion in India has been shown in the Table 1 and Table 2.

The Table 1 highlights the year-wise analysis of SHG-Bank Linkage Model. The number of savings-linked SHGs with banks has increased from 41.60 million in 2006-07 to 79.03 million in 2015-16, registering an increase of 89.98 percent. The savings of these SHGs have increased tremendously by 289.76 percent i.e. from Rs. 3512.71 crore in 2006-07 to Rs. 13691.39 crore in 2015-16. Against these savings, bank loans are disbursed to the SHGs. The amount of bank loans disbursed to SHGs have increased from Rs. 6570.39 crore to 11.05 million SHGs in 2006-07 to Rs. 37286.90 crore to 18.32 million SHGs in 2015-16. The amount of bank loans disbursed has grown by 467.50 percent i.e. more than 1.5 times of the growth in the amount of savings during the span of 9 years. The results further indicate that the amount of savings and bank loans of SHGs has shown more growth than the number of savings and credit linked SHGs. The outstanding bank loans against SHGs have also increased both in terms of number of SHGs (61.47 percent) and amount of loans (361.89 percent) from 2006-07 to 2015-16. The bank loans worth Rs. 12366.50 crore had been outstanding against 28.94 million SHGs in 2006-07 which increased to Rs. 57119.20 crore against 46.73 million SHGs in 2015-16. More than 85 percent of the savings-linked and credit-linked SHGs belong to women. The average bank loan of Rs. 203495.24 has been disbursed to an SHG in 2015-16 while average bank loan worth Rs. 122242.39 has been outstanding per SHG as on 31 March 2016. The estimated number of families covered up to 31 March 2016 under microfinance is 1010 million (National Bank for Agriculture and Rural Development, 2016).

Table 1: SHG-Bank Linkage Model

(Units in Lakh, Amount in Rs. Crore)

Year		SHG Savings with Banks	Bank Loans Disbursed to SHGs	Bank Loans Outstanding against SHGs
2006-07	***Units***	41.60	11.05	28.94
	Amount	3512.71	6570.39	12366.50
2007-08	***Units***	50.09	12.27	36.25
	Amount	3785.39	8849.26	16999.90
2008-09	***Units***	61.21	16.09	42.24
	Amount	5545.62	12253.50	22679.80
2009-10	***Units***	69.53	15.87	48.51
	Amount	6198.71	14453.30	28038.30
2010-11	***Units***	74.62	11.96	47.87
	Amount	7016.30	14547.70	31221.20

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2011-12	***Units***	79.60	11.48	43.54
	Amount	6551.41	16534.80	36340.00
2012-13	***Units***	73.18	12.20	44.51
	Amount	8217.25	20585.40	39375.30
2013-14	***Units***	74.30	13.66	41.97
	Amount	9897.42	24017.40	42927.50
2014-15	***Units***	76.97	16.26	44.68
	Amount	11059.84	27582.30	51545.50
2015-16	***Units***	79.03	18.32	46.73
	Amount	13691.39	37286.90	57119.20

Source: Data Compiled from Status of Microfinance in India, National Bank for Agriculture and Rural Development (2009, 2011, 2014 and 2016)

The Table 2 displays the year-wise analysis of bank loans disbursed and outstanding under MFI-Bank Linkage Model. The amount of bank loans disbursed to MFIs has increased from Rs. 1151.56 crore to 334 MFIs in 2006-07 to Rs. 20795.60 crore to 647 MFIs in 2015-16, registering an overwhelming increase of 1705.86 percent. The amount of outstanding bank loans has also increased from Rs. 1584.48 crore against 550 MFIs in 2006-07 to Rs. 25580.80 crore against 2020 MFIs in 2015-16, recording an increase of 1514.46 percent. The amount of bank loans disbursed to MFIs and the outstanding bank loans against MFIs have increased every year except showing a decrease in the year 2011-12. This temporary decline had been due to the setback in the microfinance sector caused by the non-adherence to rules and going overboard by some of the MFIs. However, with the policy reforms to strengthen the microfinance sector including RBI guidelines on NBFC MFIs and inclusion of loans to MFIs by banks under priority sector has brought huge benefits to this sector. As a result, lending by MFIs exhibited a robust growth with 50 percent jump in loans disbursed consecutively during last three years (National Bank for Agriculture and Rural Development, 2016).

Table 2: MFI-Bank Linkage Model

(Amount in Rs. Crore)

Year		Bank Loans Disbursed to MFIs	Bank Loans Outstanding against MFIs
2006-07	***Units***	334	550
	Amount	1151.56	1584.48
2007-08	***Units***	518	1109
	Amount	1970.15	2748.84
2008-09	***Units***	581	1915
	Amount	3732.33	5009.09
2009-10	***Units***	691	1513
	Amount	8062.74	10147.50
2010-11	***Units***	471	2315
	Amount	8448.96	13730.60
2011-12	***Units***	465	1960
	Amount	5205.29	11450.40
2012-13	***Units***	426	2042
	Amount	7839.51	14425.80
2013-14	***Units***	545	2422
	Amount	10282.50	16517.40
2014-15	***Units***	589	4662
	Amount	15190.10	22500.50
2015-16	***Units***	647	2020
	Amount	20795.60	25580.80

Source: Data Compiled from Status of Microfinance in India, National Bank for Agriculture and Rural Development (2009, 2011, 2014 and 2016)

Note: Actual number of MFIs availing loans from banks would be less than the figures shown, as most of MFIs avail loans from more than one bank.

4. CONCLUSION

Microfinance is an important element of the Indian financial system as it plays a vital role in creating value for poor by providing access to financial services and means to generate income. It is evident from the analysis that the micro finance programmes have been successful in providing financial services to a large number of the poor. They have huge potential to satisfy the financial service needs of India's unbanked people in a sustainable way. The advent of MFIs has resulted in a significant increase in reach and credit availability. The success and outreach of large MFIs have enabled them to obtain approval to operate as mainstream banks/Small Finance banks which will lower their cost of funds, passing on the benefit to their clients. However, still there is a fear regarding overheating of the sector, multiple financing to the poor clients, poor financial literacy etc. While the growth of MFI sector has been phenomenal, driven mainly by

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corporate entities, the SHG-Bank Linkage Model has also been growing steadily (despite its slow growth in priority states) and contributes in terms of thrift and savings, financial literacy, community participation etc. However, it is crippled with concerns regarding book keeping, quality of groups and diminishing attention of banks (National Bank for Agriculture and Rural Development, 2016). Therefore, the beneficiaries of the microfinance programmes need to be self-sustainable to have prolonged effect on their well-being and society as a whole.

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