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Microfinance: A Robust Poverty Eradication Tool for India

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ABSTRACT

The ambitious India that H'blePrime Minister NarendraModi saw in 2019 would have a $5 trillion GDP and be a superpower in economic field. For this,increasedrate ofeconomic growth is an essential requirement. For sustainable growth it is important that it should be inclusive and broad-based.Inclusive growth is economic growth that is distributed fairly across society and creates opportunities for all.Here, microfinance is playing an important role in meeting the requirements of low-income aspirational households through delivering them financial services like deposit loans and insurance at their doorsteps and promoting financial literacy among the people of deprived section.Governments, businesses, banks, nonprofit organisations, civil society organisations, and philanthropists support microfinance, which is now becoming a global movement.The demand for financial help, particularly in microfinance, is rising as India's economy and supporting the growth of India's Gross Domestic Product (GDP). The less wealthy segments of society are making this demand along with businesses and other financially powerful groups.

Keywords: Economy, Microfinance, Financial Inclusion, SHG, NABARD, Commercial Banks.

INTRODUCTION

The Grameen Bank Model, an concept introduced by Dr. Mohammad Yunus in Bangladesh, has raised awareness in many nations, particularly India, to use it as a means of reducing poverty. The microfinance industry is currently undergoing enormous developments and positioning itself as an emergent industry, particularly as it relates to the idea of financial inclusion. financial inclusion, which may be defined as "The process of ensuring access to appropriate financial products and services needed by vulnerable groups such as weaker sections and low-income groups at an affordable cost in a fair and transparent manner by mainstream institutional players" (ChakrabartyCommitee, 2011).Financial inclusion includes a variety of financial services, such as payments, deposits and credit. The taskforce on Supportive Policy and Regulatory Framework for Microfinance constituted by NABARD defined microfinance as " *The provision of thrift, saving, credit and financial services and products of very small amount to the poor's in rural, semi urban and urban areas for enabling them to raise their income level and improve their standard of living."*NABARD has supported Financial Literacy efforts through various initiatives keeping in mind its importance to augment demand for financial services, especially for those offered

on the digital platform. Due to the extensive involvement of regulated entities, the Indian microfinance sector is distinguished from other countries, relying on semi-regulated or self-regulated MFIs.

In Emerging Economy like India, where a sizable portion of the populationstill lives in poverty and many individuals have notreach to formal banking services, the significance of microfinance cannot be ignored.Self Help Groups (SHGs) and Bank Linkage Program, which aims to provide a cost-effective framework for providing financial services to the unreached poor, dominate the microfinance industry in India.

The concept of micro finance in India took place in the early 1970s when the Self Employed Women's Association ("SEWA") of the state of Gujarat established an urban cooperative bank, known as the Shri Mahila SEWA Sahakari Bank, with the aim of supplying banking services to underprivileged women working in the unorganised sector in Ahmadabad, Gujarat. In the 1980s, the concept of SHGs—informal organisations that would offer their consumers much-needed loan and savings services—began to shape the development of the microfinance industry. With organisations like the Small Industries Development, Bank of India, and National Bank for Agriculture and Rural Development, the sector has evolved over time from modest beginnings to a multibillion dollar industry.

Micro Financial Sector (Development and Regulation) Bill, 2007 which highlights as

- Micro Financial Sector (Development and Regulation) Bill, 2007 seeks to promote the sector and regulate micro financial organisations (MFO).
- National Bank for Agriculture and Rural Development (NABARD) shall regulate the micro financial sector.
- Every MFO that accepts deposits needs to be registered with NABARD. Conditions for registration include (a) net owned funds of at least Rs 5 lakh; and (b) at least three years in existence as an MFO. All MFOs, whether registered or not, shall submit annual financial statements to NABARD.
- Every MFO that accepts deposits has to create a reserve fund by transferring a minimum of 15% of its net profit realised out of its thrift and micro finance services every year.
- The central government may establish a Micro Finance Development Council to advise NABARD on formulation of policies related to the micro financial sector.

  NABARD shall constitute a Micro Finance Development and Equity Fund to be utilised for the development of the sector.

Provides the guidelines for the financial and insurance services to an individual or an eligible client directly or through a group mechanism for an amount not exceeding INR 50,000 in aggregate per individual for small and marginal businesses, agricultural, and related activities or an amount not exceeding INR 1,25,000 in aggregate per individual for housing or other specified purposes.

As of June 30, 2022, a variety of regulated businesses, including NBFC-MFIs, Small Finance Banks, Banks, and NBFCs, were providing microfinance services to about 6 Cr individual clients.The microfinance sector distributed more than INR 4 lakhs credits during the Covid-19 crisis two years ago, despite problems with loan repayment on existing loans, and played a significant role in supporting the government's efforts to lessen the hardships brought on by the pandemic. This was the time when policy makers were focused on ensuring the liquidity through debt flows to the lowest section of the population.

Several studies suggest that microfinance model in India where a large untappeddeprived population still needs to be brought onto the financial bandwagon. It is estimated that microfinance will remain a ‘preferred’ policy vehicle for

both the policy framers and the practitioners formany upcoming years. It is also observed that in India, two types of microfinance institutions are workingat present time; 'non-profit' and 'for profit' institutions. Trusts and Societies come under the category of non-profit institutionswhichworks through the help of grants. These institutions are registered under the Societies Registration Act, 1860 or the Indian Trust Acts, 1882. On the other hand, Co-operative societies or Non-Banking Financial Companies are examples of 'for profit entities'.In India, numerous small financial institutions have recently changed their status to Non-Banking Financial Institutions (NBFCs) after getting the license from the Reserve Bank of India.

OBJECTIVES OF THE STUDY

The objectives of the study are to understand the concept and analyze the challenges of microfinance in India. This paper throws light on:

• Microfinance concept and its mechanism

•Structure of NBFCs

• MFIs contribution and potential to the economy

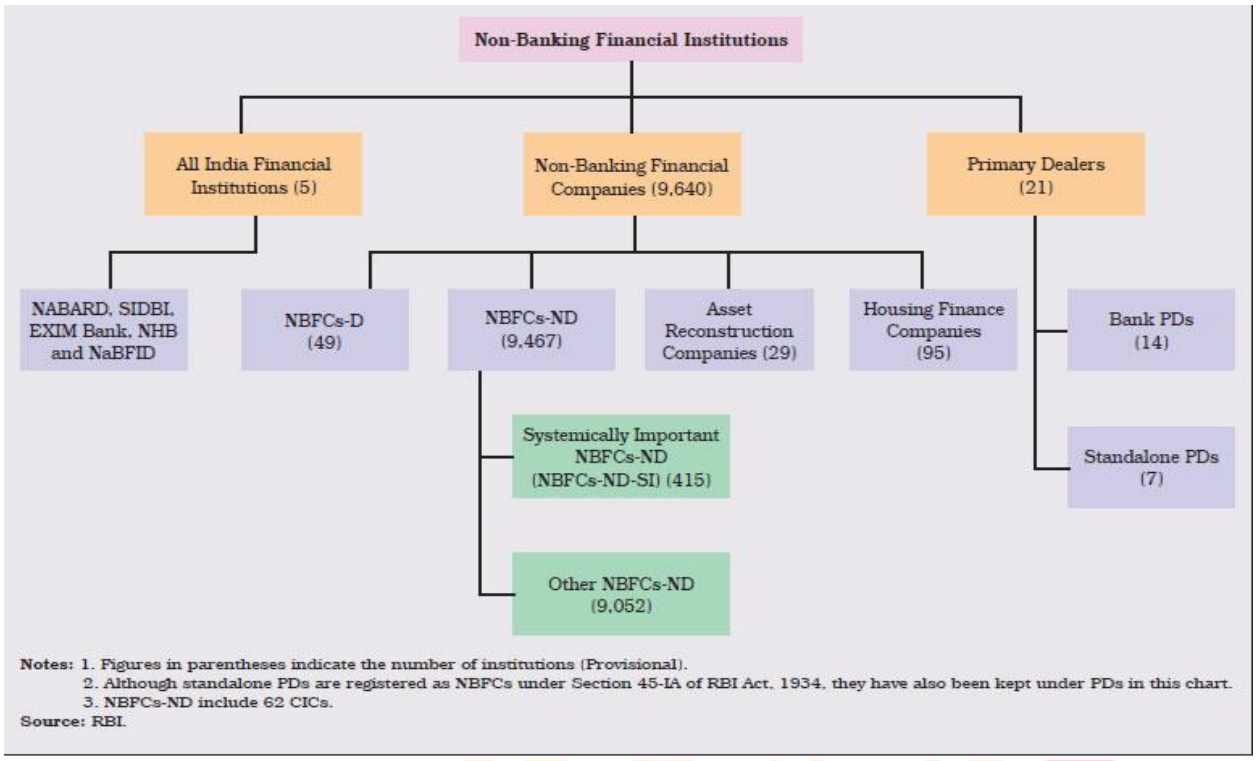
RESEARCH METHODOLOGY

This conceptual study is based on secondary data. The secondary data is utilised to highlight the conceptual analysis and literature review. The reports, books, essays and journals related to microfinance in India are used as the sources of secondary data for the study.

Findings and Analysis

Structure of NBFCs in India

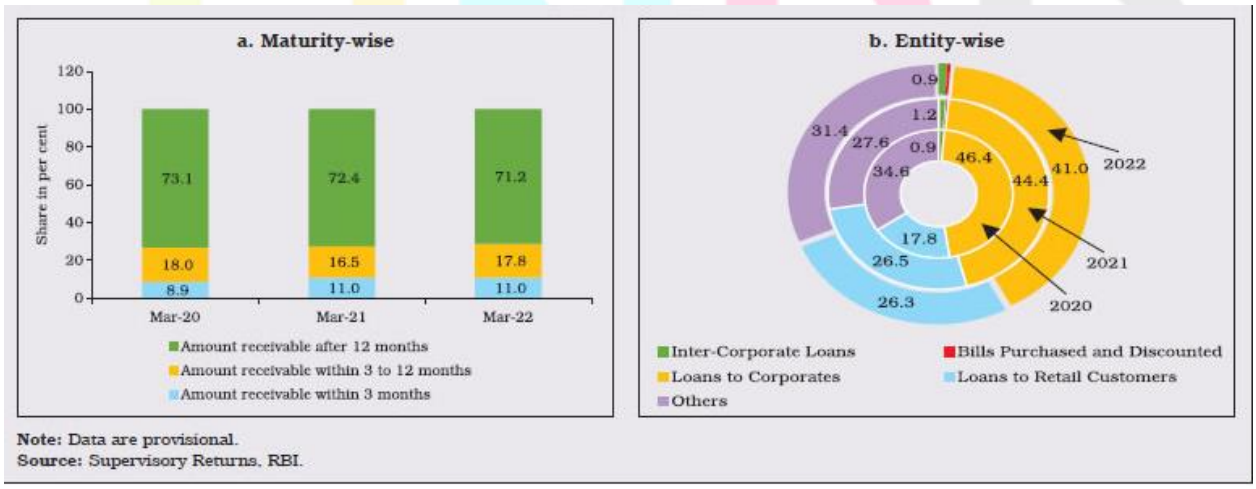
The structure of Non-Banking Financial Companies (NBFCs) can be clearly understand through following flow chart. This chart examines the operations and performance of the Non-Banking Financial Companies (NBFCs), Housing Finance Companies (HFCs), All India Financial Institutions(AIFIs) and Primary Dealers (PDs) that fall within the Reserve Bank's regulatory purview. In order to augment bank credit, NBFCs are made up of government, public, and private limited companies that offer specialised financing to a variety of economic sectors, from real estate, infrastructure to agriculture and microloans. HFCs are specialised in offering home financing to private persons,co-operative societies, and corporate entities to promote the nation's housing market.



The Export Import Bank of India (EXIM Bank), the Small Industries Development Bank of India (SIDBI), the National Bank for Agriculture and Rural Development (NABARD), and the National Bank for The premier financial institutions, Financing Infrastructure and Development (NaBFID), respectively provide long-term funding for infrastructure, small businesses, overseas commerce, agricultural, and housing finance enterprises. In addition to serving as market makers in the government securities market, PDs ensure subscription to primary issuances of government sectors.

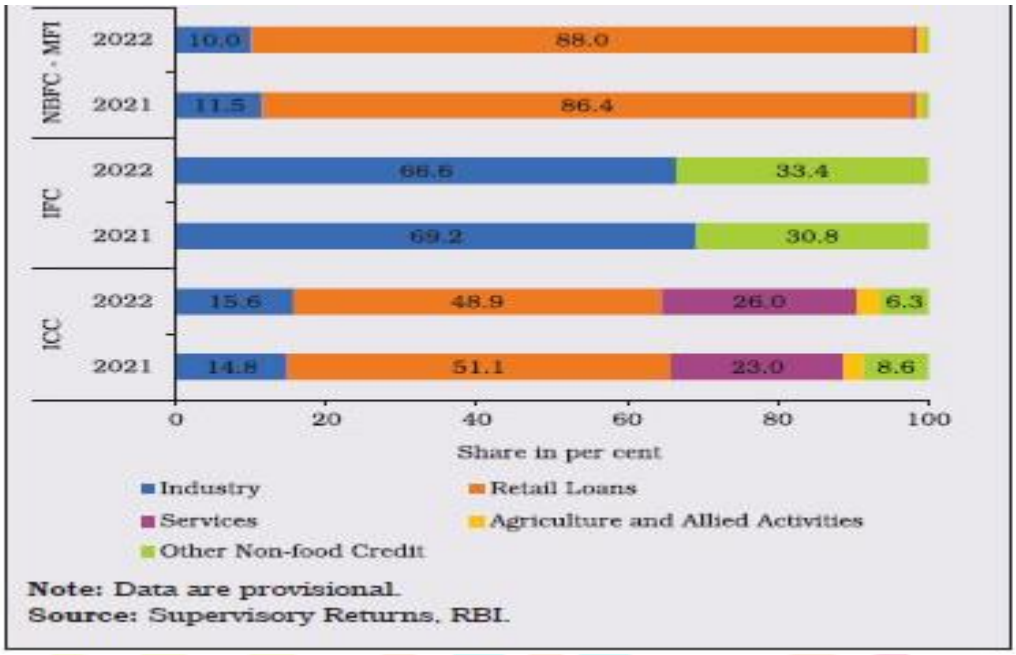
Classification of NBFCs Loans and Advances

In the following chart, thecomparison among different NBFC's loans and advances between 2020 to 2022 years is shown:



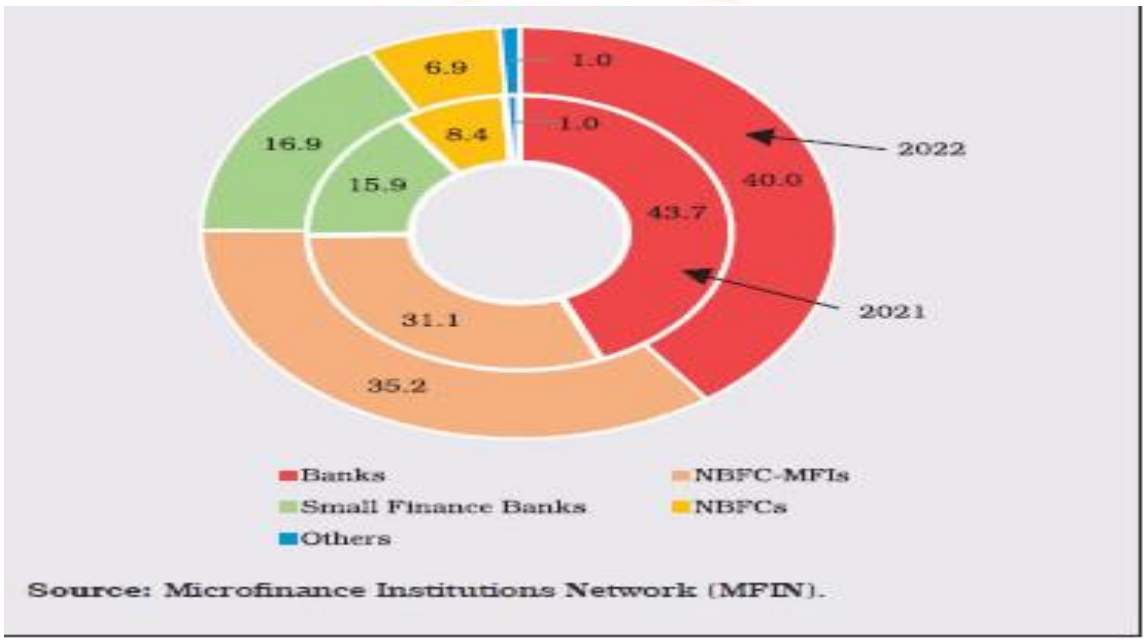
The diagrams show that over two-thirds of NBFCs' loans are receivable after 12 months as per their credit maturity profile. It is also observed that the pandemic did cause a slight shift in favour of loans with shorter terms shown in figure 4a. The two groups that benefited from NBFC credit the most are corporations and retail customers. In spite

of weak demand, the proportion of wholesale loans in NBFCs' loan book decreased between 2020 and 2022. On the other hand, the proportion of retail loans increased significantly as discretionary expenditure increased as shown in figure 4b.



Share of Microloans Provided by NBFC-MFIs

The share of microloans provided by NBFC-MFIs increased significantly in 2021–2022 as seen in the accompanying chart. In March 2022, the Reserve Bank established a uniform regulatory framework for microloans that all Regulated Enterprises (REs) must adhere to. RBI initiatives like the lifting of the interest rate limitation and the increase in the income level up to 3 lakhs should make it easier to expand credit flows.

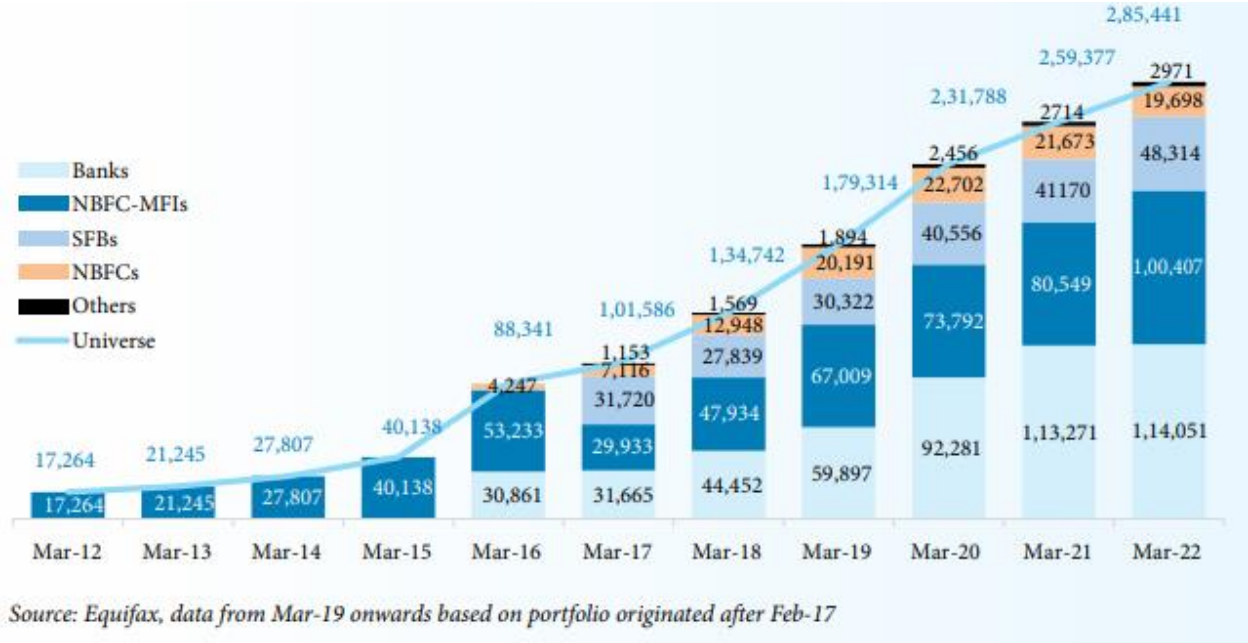


Progress of Microfinance over the Last Ten Years

As per India Microfinance Review FY 2021-22, after 2012, NBFC-MFIs were the only regulated organisation providing microfinance to their clients/borrowers. As of March 31, 2012, the sector's portfolio was at Rs. 17,264 Cr.

It shows that how the sector's size will increase 16.5 times over the following 10 years to Rs 2,85,441 Cr as of March 31, 2022. The only organisations offering microfinance to borrowers up until March 2015 were NBFC-MFIs. Banks and NBFCs also started offering microloans in 2016, and SFBs were added in 2017.

Microcredit Portfolio (Rs Cr)

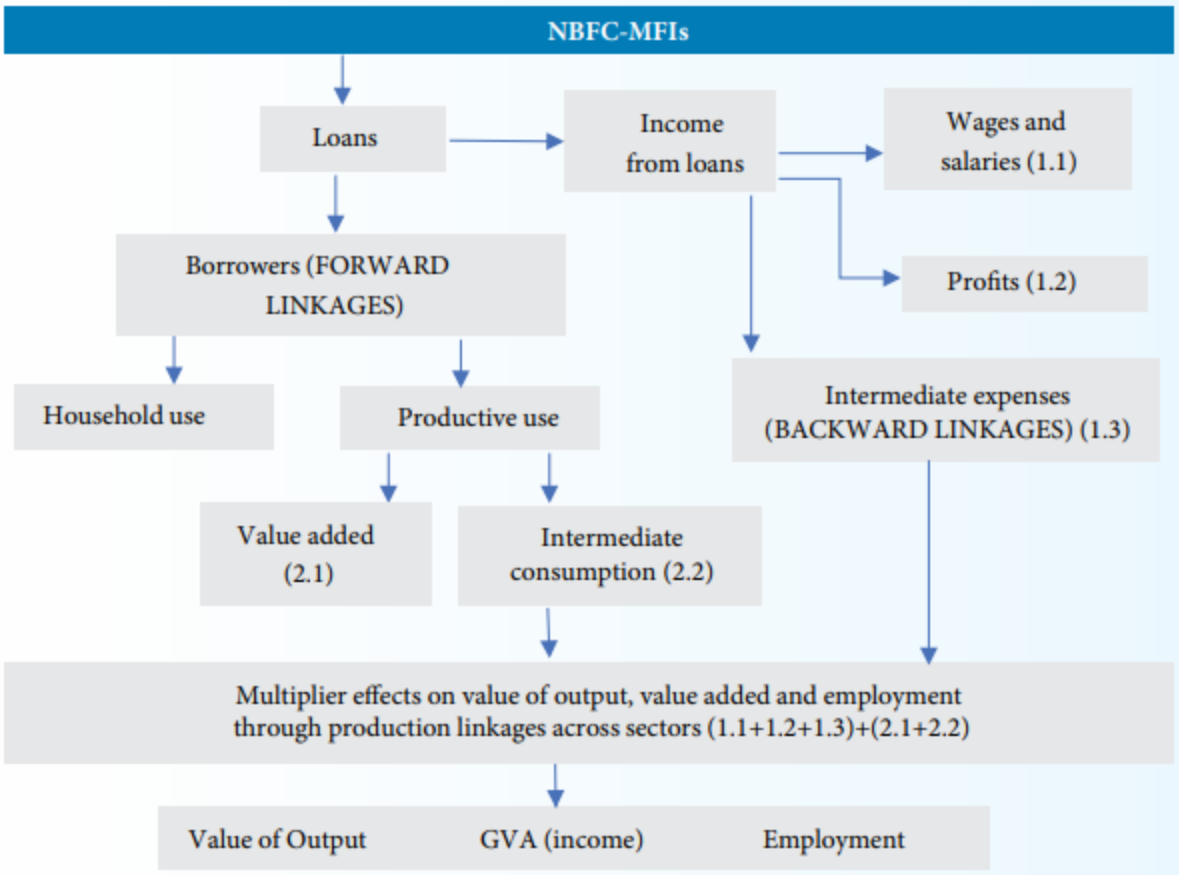


Source: Equifax, data from Mar-19 onwards based on portfolio originated after Feb-17

The above figure shows that about 202 differentorganisations were operating in the microfinance sector as of March 2022. Banks (12) hold the biggest portion of the portfolio, accounting for 40.0% of the total universe of microcredit and having a total loan outstanding of Rs 1,14,051 Cr with a loan balance of Rs 1,00,407Cr and a 35.2% share of the industry portfolio, NBFC-MFIs (84) are the second-largest providers of microcredit. SFBs (9) currently own a combined Rs 48,314 Cr in loans, accounting for 16.9% of the total. Additional NBFCs (58) make up 6.9% of the total, and Other MFIs (39) make up 1.0%.Two models of microfinance are dominating in the market, are the Joint Liability Groups (JLG) and Self Help Groups (SHGs).

The Contribution of Microfinance to the Economy

The contribution through the consumption of intermediate inputs causes multiplier effects on the value of output, value added, and employment which are calculated through the input output system.



Source: 2021, NCAER. "Present and Potential Contribution of Microfinance to India's Economy"

The figure dipicts that the NBFC-MFIs supply loans, derive income from loans to pay for wages & salaries ofemployees (1.1), profits to owners (1.2) and other expenses (1.3). The item no.(1.1) and (1.2) account for value added by the NBFCs directly. The intermediate consumption, such as offices, ICT services (1.3), lead to multiplier effects estimated through input-output system. The multipliers are estimated first for value of output and then for value added and employment.

Potential of Microfinance

		Past CAGR*	Actual	Extrapolated*			
			21-22	22-23	23-24	24-25	25-26
A	Potential HHs, Cr	2.5%	20.32	20.83	21.37	21.91	22.48
B	Unique borrowers reached, Cr	5.5%	5.80	6.12	6.46	6.82	7.20
C	Av. loan O/s per UB, Rs	10.7%	49,249	54,797	60,969	67,837	75,478
D=A*C	GLP demand, Rs Lk Cr		10.01	11.42	13.03	14.87	16.96
E=B*C	GLP of the sector, Rs Lk Cr		2.85	3.35	3.94	4.63	5.43
F=E/D	% of demand covered	2.9%	28.5%	29.4%	30.2%	31.1%	32.0%

** Using CAGR for the period 2018-19 to 2021-22*

MFIN estimates that the total microfinance market size in terms of GLP Rs 10 Lakhs Cr. as of March 2022. Considering the same CAGR of increasein No. of potential HHs, average loan outstanding per UB and depth of outreach, the potential market size will reach Rs 16.96 Lakhs Cr by March 2026.Therefore, if the essential parameters continue to increase at their current rate, microfinance would reach around 32% of its potential size by 2025–2026.

CONCLUSION

Financial inclusion is a goal of microfinance, and the outstanding support and supportive policy environment provided by the RBI is helpful in advancing this goal. This sector has been given a separate category under the wider NBFC category of the RBI. It is a distinct identity and solid legitimacy by having the nation's first RBI-recognized Self Regulatory Organization (SRO). According to chairperson of Microfinance that the key pillars of MFIN's work have been customer protection, industry code of conduct and policy advocacy, all of which contribute towards building of a Responsible Finance ecosystem. He added that various studies reveal that development of microfinance and overall inclusive economic growth are interdependent. MFIN sector has a vital role to play in making sure that both India and Bharat progress together towards becoming a Global Powerhouse as it is the second largest asset class after mortgages.

To improve the future microfinance operations for the betterment of each segment of the poor and society, organisations like NABARD and SIDBI have called for coordination of efforts. The microfinance industry has improved now.Thanks to NABARD and SIDBI asmajor resources are now going for helping the underprivileged for getting the loans, they need.The development of the credit bureau ecosystem for microfinance in India, the promotion of cashless disbursement and repayment collections, the creation of an industry code of conduct, a code for responsible lending and other initiatives were all undertaken in the past by MFIN.This is definitely a good sign for microfinance institutions in India. It is needed that Government should support and regulate microfinance in effective manner so that it may prove to be a robust tool for poverty eradication in developing countries like India.

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