

Full Length Research Paper

Micro finance and poverty reduction in India (A comparative study with Asian Countries)

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The dynamic growth of the microfinance industry has been promoted not only by market forces but also by conscious actions of national governments, Non-Governmental Organizations (NGOs), and the donors who view microfinance as an effective tool for eradicating poverty. The powerful push behind this huge and increasing support for microfinance indicated that national economic and social impacts are significant and it needs to be examined more closely.

Key words: Micro finance, poverty, India.

INTRODUCTION

There are so many studies available on the characteristics of rural banking credit markets in India and the spread of in the post independence period. A number of studies begin with the All India Rural Credit Survey in 1954; found that the rural poor had high levels of indebtedness and very limited bank access. The State Bank of India was set up in 1955 as facilitator to provide banking services to poor population, the 14 large commercial banks were nationalized in 1969, and the National Bank for Agriculture and Rural Development (NABARD) was created in 1982. Each of the nationalized banks is deputed the role of lead banks in particular parts of the country and they are restricted to maintain justified ratios of urban and rural branches. A lot of cooperative banks and regional rural banks are created primarily to cater credit need of poor population in India. Total requirement of micro-credit in the country has been assessed at Rs. 50,000 crore. Micro-credit programme works through NGOs/ SHGs and the merit lies in weekly monitoring and refund of installments' (www.ssi.ac.in).

The credit policy for the poor involves many practical difficulties arises from operation followed by financial institutions and the economic characteristics and financing needs of low-income households. For example, commercial banking institutions require that borrowers have a stable source of income out of which principal and interest can be paid back according to the agreed terms. However, the income of many self employed households is not stable. A huge number of micro loans are needed to serve the poor, but banking institution prefers dealing with big loans in small numbers to minimize administration expenses. They also look for collateral with a clear title – which many

low-income households do not have. In addition bankers tend to consider low income households a bad risk imposing exceedingly high information monitoring costs on operation.

In this context, following questions are raised before us.

- i.) Is there a need for a new institution?
- ii.) Should it operate all India or in a state?
- iii.) What are methodological issues?
- iv.) Who will be its beneficiaries?

THE INDIAN MICROFINANCE CONTEXT

India has the one of the fast developing country in the world. India's 'first world' economy is oriented to the very highest standards of globalised consumption, and formal sector incomes and lifestyles reflect this. By contrast, the real incomes and 'lifestyles' of the very poor, particularly in rural areas, are comparable very low. Micro-finance is often advocated as a solution to multiple social problems in India. Poor Persons with access to credit can make investments in enterprises that bring them out of poverty. Over the last few years, savings and credit groups have also helped to manage some important social programs of the Indian government, such as the distribution of food grains and school meals in state primary schools.

Income in India is closely linked to social and economic status: whilst the upper and middle classes inhabit the 'formal' income from their formal ventures and employment, in other hand the poorest and low income status are largely 'informally' employed. Low income households are not usually involved in regular income occupa-

Table 1. Out reach by Asian counties (In terms of persons).

Bangladesh	Cambodia	Pakistan	Philippines	India 2004	India 2005
300,000 - 350,000	0 - 50,000	0 - 50,000	0 - 50,000	50,000 - 100,000	150,000 - 200,000

Source: Microfinance Information Exchange, Inc., 2005 Benchmarks. All observations are medians. India observations draw from panel data for MFIs in 2004-05 Benchmarks.[6]

tions and therefore waiting for job creation strategies to absorb them; they 'permanently inhabit' a dependent segment of the so called developing Indian economy, in which opportunities for jobs, or for independent and self-sustaining entrepreneurial capital accumulation, are minimal.

Though poverty reduction has long been a high priority for the Government of India, microfinance is a still experimental tool in its overall strategies. India's microfinance experiments are much differ from the more substantial microfinance institutions and programmes of its neighbors countries. The United Nations system was perhaps the first international partner to India's new experiments with small scale credit schemes.

Most of poor people manage to optimize resources over a time to develop their enterprises. Financial services could enable the poor to leverage their initiative, accelerating the process of generating incomes, assets and economic security. However, conventional finance institutions seldom lend down-market to serve the needs of low-income families and women-headed households. They are very often denied access to credit for any purpose, making the discussion of the level of interest rate and other terms of finance irrelevant. Therefore the fundamental problem is not so much of unaffordable terms of loan as the lack of access to credit itself.

The impact of microfinance on poverty reduction has been measured in terms of several dimensions, such as improved income, employment and household expenditure, and reduced vulnerability to economic and social crises. These measurements have tended to focus on a specific geographic area, an institution or a small client group and are difficult to generalize or draw conclusions that reach across borders, income levels, gender or socio-economic status. Even though many of these anecdotal studies clearly support a role for microfinance in achieving the Millennium Development Goals, a key challenge in measuring the impact of microfinance is obtaining reliable data. Sometimes clients are recipients of more than one product, which are provided by more than one microfinance institution (MFIs). MFIs, it becomes hard to obtain measures on the exact impact of their services and products on their clients' lives. We also do not have the answer to the question of what proportion of the population even has access to credit and savings (Patrick, 2004).

THE ASIAN MICRO FINANCE CONTEXT

Asian microfinance stands at the leading edge of the

industry's global drive to expand financial sector inclusion. According to the 2005 global survey of 446 microfinance institutions (MFIs) conducted by the Microfinance Information Exchange, Inc. (MIX), (Benchmarks, 2005) Asian institutions managed over 4 billion dollars in loans and served an impressive 22.5 million borrowers. While Asian institutions included here represent less than one fourth of the total global data set, they serve over two thirds of the total borrowers. Four colossal microfinance institutions take the limelight with an average outreach of four million borrowers each. These Asian giants – Grameen Bank, ASA, BRAC and BRI – stand unrivaled in scale of service. "Asia is the most developed continent in the world in terms of volume of MFI (microfinance institution) activities." (Lapenu and Zeller, 2001) This conclusion, drawn by Lapenu and Zeller (2001), is based on an analysis of over 1,500 institutions from 85 developing countries. Comparing MFIs in Asia with those in Africa and Latin America, the study found that in the 1990s Asia accounted for the majority of MFIs, retained the highest volume of savings and credit, and served more members than any other continent.

This generalization of course covers up some wide disparities within the region. East Asia is particularly well served by MFIs. The largest number of members served and the largest distribution of loans and mobilization of savings in terms of GNP is found in Bangladesh, Indonesia, Thailand and Viet Nam. In contrast, the two most populated countries in Asia, India and the China, have very low outreach, despite a high concentration of the regions poor. Countries such as Afghanistan, Myanmar and Pakistan also have low outreach due to a variety of factors. Despite these disparities within the region, overall it is said that MFIs have flourished in Asia and that compared to other regions they exhibit good outreach and high repayment rates (Meyer, 2002).

Table 1 below presents the most recent data from the Microfinance Information Exchange, Inc., 2005 Benchmarks , which gives a figure about outreach of MFIs in Asian countries. Asian MFIs demonstrate relatively good outreach. They account for the largest number of borrowers are belong to Bangladesh and are second Indian MFIs in terms of number of persons.

INDIAN MFI PERFORMANCE: 2005 - 2006

A 2005 - 2006 survey of India's leading 15 MFIs shows the industry's strength in both size and growth. While MFIs globally and within the region average less than 20,000 clients per institution, well managed Indian micro-

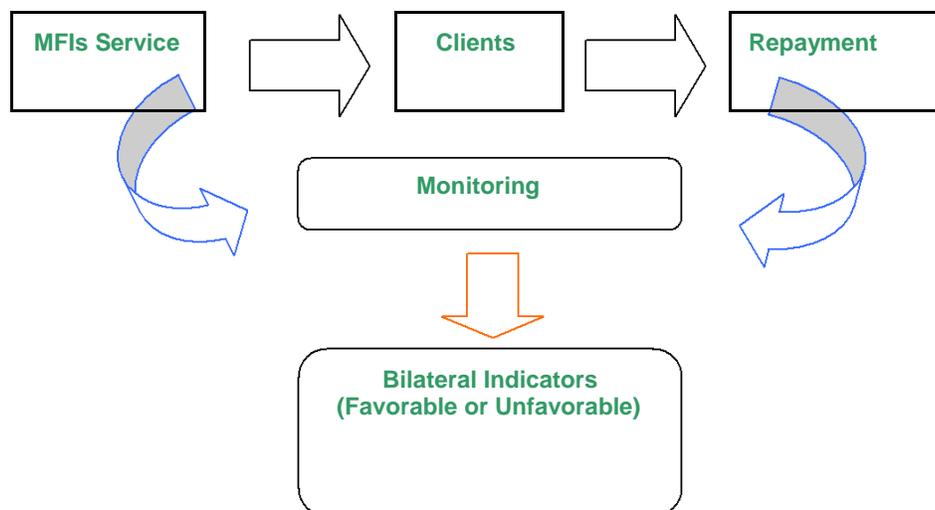


Figure 1. Bilateral function of MFIs and clients.

finance institutions already rank top in outreach, despite their relative young age; with nearly a decade more experience, only Bangladeshi institutions reach more borrowers. Not to be left behind, Indian institutions top the charts of all 78 countries surveyed in 2005 for their phenomenal growth rates, the median leading MFI doubling coverage in a single year. In fact, five of the top 20 fastest growing MFIs in 2005 were Indian, from a survey of nearly 450 institutions worldwide. While global microfinance talks about increasing commercial capital available to MFIs and of integrating with local financial markets, Indian microfinance defines the forward lines of this movement. Within Asia and around the globe, Indian MFIs are more leveraged than institutions in any other sector. Compared to other markets in South Asia, the importance of local financial institutions is readily apparent. Bangladeshi and Pakistani MFIs have built large institutions on the backs of soft money. Indian MFIs, on the other hand, deprived of shareholder capital or legal access to public deposits, have funded growth through commercial loans from local banks and development finance institutions. Tapping local financial markets leaves the sector well poised to continue its rapid growth. Loans to Indian MFIs fulfill more than priority sector lending requirements; they also fulfill the need for returns. Leading MFIs offer slim, but positive margins. Hardly the high returns presented in recent media coverage, leading institutions averaged just less than 1% return on assets (Figure 1) (Blaine and Hind, 2006).

UNITED NATIONS MANDATE FOR MICROFINANCE AND POVERTY ALLEVIATION

The World Summit for Social Development (WSSD) in March 1995 articulated a global commitment by Govern-

ments to eradicate poverty as an ethical, social, political and economic imperative. Poverty eradication was one of three core themes of WSSD. The Programme of Action affirmed the primacy of national responsibility for social development, including poverty eradication, but also called for international support to assist governments in developing strategies. The Programme of Action suggested ways to involve civil society in social development and to strengthen their capacities. It called on Governments to mobilize resources for social development, including poverty alleviation. The WSSD Programme of Action was to be implemented within the framework of international cooperation that integrated the follow-up to recent and planned UN conferences relating to social development, for example, the Children's Summit in 1990, the Environment and Development Conference in 1992, the Human Rights Conference in 1993, the Population and Development Conference in 1994 and the Women's Conference in 1995.

The United Nations System Conference Action Plan (UNSCAP) designated poverty alleviation as the integrating theme for follow-up to world conferences. It called for UN system action in five areas:

- i.) Jobs and sustainable livelihood.
- ii.) Regenerating the environmental issues.
- iii.) The enabling environment.
- iv.) Social service for all.
- v.) Arrangement of women and gender mainstreaming.

UNDP and UN Resident Coordinators were asked to coordinate UN system efforts in the five areas. UN development organizations have their own individual mandates.

Microfinance is one tool for poverty alleviation. The enabling environment influences the effectiveness of microfinance in the other four areas of poverty alleviation interventions. The UN organizations' mandates in the

area of microfinance primarily lie in the area of technical assistance and demonstration of models that contribute effectively to poverty alleviation. The responsibility for provision of capital rests with governments, with support from bilateral donors and international financial institutions (Report of United Nations, 1995).

FEW SCHEME OF A GOVERNMENT OF INDIA

There are so many schemes for the upliftment of poor in India. One of them Micro-credit programmes is run primarily by NABARD in the field of agriculture and SIDBI in the field of Industry, Service and Business (ISB). The success of Micro-credit programme lies in diversification of services. Micro Finance Scheme of SIDBI is under operation since January, 1999 with a corpus of Rs. 100 crore and a network of about 190 capacity assessed rated MFIs/NGOs. Under the programme, total amount of Rs. 191 crore have been sanctioned upto 31st December, 2003, benefiting over 9 lakh beneficiaries. Under the programme, NGOs/MFIs are supposed to provide equity support in order to avail SIDBI finance. But they find it difficult to manage the needed equity support because of their poor financial condition. The problem has got aggravated due to declining interest rate on deposits. The office of the development commissioner (Small Scale Industries) under Ministry of SSI is launching a new scheme of Micro Finance Programme to overcome the constraints in the existing scheme of SIDBI, whose reach is currently very low. It is felt that Government's role can be critical in expanding reach of the scheme, ensuring long term sustainability of NGOs / MFIs and development of Intermediaries for identification of viable projects.

SALIENT FEATURES OF MICRO-FINANCE PROGRAMME OF GOVERNMENT OF INDIA (www.laghuudyog.com/schemes/microfinance.htm)

Arranging fixed deposits for MFIs/NGOs: Under this scheme government of India arrange money to MFI/NGO like SIDBI for micro credit to poor.

Training and studies on micro-finance programme:

Government of India would help SIDBI in meeting the training needs of NGOs, SHGs, intermediaries and entrepreneurs and also in enhancing awareness about the programme.

Institution building for 'intermediaries' for identification of viable projects: The Government of India would help in institution building through identification and development of 'intermediary organization', which would help the NGOs/SHGs in identification of product, preparation of project report, working out forward and backward linkages and in fixing marketing/ technology tie-ups. The SISIs would help in the identification of such intermediaries in different areas.

Budgetary provision for the scheme during 10th plan:

There was a budgetary provision in 10th five year plan and hoping more funds in next plan.

Administrative arrangement: A committee has been formed to control and monitor the administrative arrangement of MFI/NGOs.

MICROFINANCE TERMINOLOGY

Micro credit: This is a small amount of money loaned to a client by a bank or other institution. Micro credit can be offered, often without collateral, to an individual or through group lending.

Microfinance: This refers to loans, savings, insurance, transfer services and other financial products targeted at low-income clients

Micro insurance: This is a system by which people, businesses and other organizations make payments to share risk. Access to insurance enables entrepreneurs to concentrate more on growing their businesses while mitigating other risks affecting property, health or the ability to work.

Remittances: These are transfer of funds from people in one place to people in another, usually across borders to family and friends. Compared with other sources of money that can fluctuate depending on the political or economic climate, remittances are a relatively steady source of funds.

Micro savings: These are deposit services that allow people to store small amounts of money for future use, often without minimum balance requirements. Savings accounts allow households to save small amounts of money to meet unexpected expenses and plan for future investments such as education and old age.

Inclusive financial sectors: It allows poor and low-income people to access credit, insurance, remittances and savings products. In many countries, the financial sectors do not provide these services to the lower income people. An inclusive financial sector will support the full participation of the lower income levels of the population.

Micro entrepreneurs: These are people who own small-scale businesses that are known as micro enterprises. These businesses usually employ less than 5 people and can be based out of the home. They can provide the sole source of family income or supplement other forms of income. Typical micro entrepreneur activities include retail kiosks sewing work shops, carpentry shops and market stalls.

Bankable: These people are those deemed eligible to obtain financial services that can lead to income generation, repayment of loans, savings, and the building of assets.

Unbanked: This describes people who have no access to financial services through any type of financial sector organization such as banks, non-bank financial institutions, financial cooperatives and credit unions, finance companies, and NGOs. Implicit in this definition is that financial services are usually available only to those individuals termed "economically active" or bankable.

Conclusion

Creating self employment opportunities is one way of attacking poverty and solving the problems of unemployment. There are over 24 crore people below the poverty line in our country. The Scheme of Micro-finance has been found as an effective instrument for lifting the poor above the level of poverty by providing them increased self-employment opportunities and making them credit worthy. A basic effort of last decade, the microfinance objectives in India has reached at top point similar to Bangladesh. With some effort substantial progress can be made in taking MFIs to the next orbit of significance and sustainability. There is a need of Designing financially sustainable models and increase outreach and scale up operations for poor in India. People belong to villages are still unaware about banking policies and credit system. So NGO should communicate to them and share their view with villagers. Banks should convert and build up professional system into social banking system for poor. Government of India and state governments should also provide support for capacity building initiatives and ensure transparency and enhance credibility through disclosures.

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