

MICRO-FINANCE: IS IT A MYTH OR REALITY?

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Abstract

Micro-finance is the promising alternative that offered funds at the doorstep of the poor. There has been a lot of debate on the nature, concept, regulations and practices of micro-finance in India. Many development economists believe that economic prosperity can not come without financial inclusion and micro-finance is being considered as a vehicle for financial inclusion in Indian economy especially in rural economy. This is true. But as of today, micro-finance has not made any significant contribution in financial inclusion and economic prosperity especially in rural India. To my mind micro-finance is a myth as cooperatives have failed in bringing or attaining financial inclusion and economic emancipation. Much has been left on the part of micro-finance institution and their regulations. For this system to work it had to have very low defaults. The present paper is a modest attempt in this direction. The paper explores the issues which have made the nature, concept, regulations and practices of micro-finance as a myth rather than a reality.

Key words: financial inclusion, economic prosperity, money lenders, and financial access. agent of development; bureaucratic hurdles; rural indebtedness, usurious interest rates.

Introduction:

In India, the majority of the population lives in rural areas and hence, their overall development is the need of the hour. Development process requires financial access. Micro-finance could be most convenient way or method of attaining financial inclusion and inclusive growth. It is an undisputed fact that financial inclusion and inclusive growth have to go hand-in-hand.

The concept of micro-finance was the outcome of an inspiration got from the success of the concept and practice in Bangladesh wherein the pioneer Mr. Yunus got the Nobel Prize for his outstanding contribution in the field of micro-finance

resulting into financial inclusion in the rural areas of the Bangladesh economy. The enormous success in Bangladesh has become an eye opener for Indian planners and policy makers and accordingly, transformed the idea into practice in a different way namely-self-help groups (SHGs) in India especially in rural India.

Basic Aims:

The business of micro-finance was commenced in the middle of the decade of 1980s. The Government of India, which was vying for the affordable and available loaning option for the poor and weaker section of society, encouraged the idea. The very aim of transforming the idea of micro finance was to take out rural people from the clutches of the traditional money lenders on the one hand and on the other hand to extend easy, convenient and affordable loans to facilitate the much needed economic empowerment of the rural people, particularly women and youths.

Scenario in Developing Economies:

World's financial crisis has reduced investment opportunities in different continents of the globe, lending to India's poor has come up as a good option for private firms or equity funds from the developed economies. In many developing nations, access to financial services is greatly confined due to a number of institutional weaknesses and other reasons that prevent people from achieving their respective economic potential and opportunities, resulting into a limited economic growth. Inadequate availability of financial services has further raised the sense of equality, as it does affect disproportionately the poor and people living in rural areas.

In developing world, the size and scope of the micro-finance institutions have been increased rapidly, and it is expected to growth further since the demand for financial services by poor person's remains largely unmet. There are estimates that the potential and opportunities of micro-finance i.e. financial services world over stood at 500 to 700 million people and less than 1/9th of theme are being covered by MFIs. {1}

The basic objective of initiating the idea of micro-finance in developing nations was to promote much needed financial sector as a part of the Monterrey Consensus on financing for development. Accordingly, micro-finance schemes have also been inducted or introduced in developed economies to serve people living in disadvantaged areas such as inner cities.

Can micro-finance attain Sustainable Development?

In case of India, micro-finance has relevance as bulk of the population lives in rural areas and hence, development economist call "rural India the real India" therefore, its sustainable development is of paramount significance.

Among different poverty eradication schemes that are being carried out through micro-finance are being considered as the spring boards for sustainable development. The very first step in this direction was taken as back as 1980 when the Integrated Rural Development programme was initiated which was called as IRDP. The main objective of introducing IRDP was to generate self-employment among the poor in the rural areas through micro-credit extended by the commercial banks. This micro-credit was meant for purchasing productive assets and supported with subsidies given by the Central Government.

The magnitude of poverty and disparities among various social groups had called for planned State intervention to give succor and relief especially disadvantaged and marginalized groups' namely -Schedule Caste, Schedule Tribes, and women. Keeping this in mind as well as having regard to the positive facets and deficiencies, the earlier

Self-employment schemes such as TRYSEM, SITRA, GKY, DWCRA, IRDP and MWS were amalgamated and got a shape of SGSY on April 1, 1999 to attain sustainable development which is still considered as the dream of developing economies.

The SGSY is being considered as a holistic scheme of micro-institutions concentrating all facets of self-employment and creating effective and efficient links between the different ingredients namely- organization of the rural poor into Self Help Groups, their respective capacity and ability building, planning of operation clusters, infrastructure build up, technology, credit and marketing etc.

MFIs and Inclusive Growth:

Micro finance enterprises are being considered as a promising alternative for expanding the base of financial services to the poor and weaker sections especially in developing economies. The following arguments may go a long way in achieving inclusive growth through micro-finance.

a) Micro-credit has been established as a spring board for empowerment of people, taking out from poverty and extending helping hand in the economic progress sine-quo-non for inclusive growth;

b) Micro finance enterprises extend credit as well as other financial services to low income persons, weaker sections and informal business;

c) Micro-finance institutions create a effective and efficient mechanism for poor people to absorb the affects of income shocks on consumption, explore safe and affordable repositories for their savings, share advantage of profitable investment potential and opportunities and minimize risk;

d) Micro-finance enterprises have created a variety of innovative tools namely-weak legal creditor protection, ineffective and inefficient enforcement of laws and rules, lack of usable collateral, poor means of communication facilities and weak prudential oversight over saving enterprises;

e) Micro-finance institutions have extended their range of financial services beyond micro-credit. These institutions are now covering transfer of funds and insurance.

f) Micro-credit has been accepted as a major instrument in the attainment of MDGs by the end of 2015.

Working:

After a considerable gap of 19 years, another step was taken in the name of Swarnajayant Gram Swarojagar Yojana by the Central Government in 1999 as a replacement of IRDP and its allied schemes. Under the then scheme namely- IRDP nearly 5.4 million families of rural areas were assisted with bank loan amounted to Rs. 2, 30,000 million along with subsidies amounting to Rs. 1,45, 000 million.

The Indian model of micro-finance known as Self Help Group Bank Linkage Programmed; Kisan Credit Card (KCC) scheme, Rashtriya Swasthya Bima Yojana (RSBY); financing Regional Rural Banks (RRBs), Cooperatives and Public Sector

Banks that are lending to rural population are the existing instances of financial access or financial inclusion. This is also true that these agencies have contributed significantly and positively in creating financial access to rural population. But there has been left much to be attained as the performances of these agencies are more politics based rather than economics based. This is true as financial services are more effective in reaching electorate. These services are being used by the politicians to intact vote bank rather than enhancing quality of life, purchasing power and over all welfare of the rural population.

Keeping in mind the very basic aims of evolving and practicing the concept of micro-finance, Micro-Finance Institutions were established and they got enormous success in the attainment of financial inclusion. This very fact could be tested from the fact that in the year 2003 these agencies have lent an amount of Rs. 12 million and in 2010 this figure has touched upon an impressive amount of Rs. 17 billion. {2}

Within a short-span of five years, Indian micro-finance segment which was build around carefully nurtured affinities and an appropriate rate of increase depends upon the capacities, has resulted into a chaotic marketplace wherein there are very little regulations to regulate in the right perspective and spirit. As a result there has been a diverse offering from multiple players and scant regard for proper group formation (Sine-Quo-Non) for the success of the concept and practices of micro-finance. According to an estimate, nearly Rs. 30,000 crore is chasing the poor and being collected from them, whether they are ready for it or not {3}.

Thirty million or three crore poor women in Indian villages have acquired small amount in loans and started productive ventures. With these loans they buy a cow to supplement their respective income by selling milk. Some of them invest these loans in purchasing a sewing machine to sell cloths. Others have preferred to open a kirana shops to enhance their purchasing power. What is the most interesting, astonishing and worth mentioning is the transformation of charity work carried out by Non-Governmental Organizations (NGOs) into a self-sustaining business due to the entry of Micro-Finance Institution (MFIs). These organizations are replacing the village money lenders and bringing out rural people from the clutches of money lenders. {4}

The most heartening fact that has come up is emerging out is in Southern India micro-credit is as common as panwala or cell phones. The MFIs have been providing **dignity to the people especially women to raise their heads in the society on the one hand and on the other bringing the most wanted segment ‘financial inclusion’**. There is a true saying that success always created envy. Accordingly, in October 2010 the issue of micro-finance was politicized and as a result, politicians started accusing MFIs that these institutions have sharking loans and are also responsible for farmers’ suicides because of the exorbitant rate of interest charged by MFIs.

In India MFIs charge interest between 24 per cent and 32 per cent which is being considered on a high side. But if we compare these interest rates with the interest rates charged on credit cards (30 per cent) and village money lenders (65 per cent) then this rate of interests is normal. Even in Bangladesh the rate of interest charged by MFIs is 20 per cent (based on subsidized credit). The most impractical issue that has been affecting the working of micro-finance in India especially in many States of the country is that the State Government of Andhra Pradesh has issued an Ordinance wherein it is specifically given that Micro-finance Intuitions have to take

permission from the State Government for every loan. It is practically not possible for MFIs to undertake. Even in Andhra more than a crore people are the consumer of micro-finance. If this is carried out then what would happen in case of Uttar Pradesh and Bihar States. This is a sort of License Raj which is beyond imagination in the present globalize scenario. Added to this, the evil of bribery would be rampant in micro-finance agencies.

In Bangladesh, the truth is that it is relatively expensive to deliver and collect loans weekly in the villages. Users of micro-finance does not think it unfair because these people are earning far more from the business which they started by taking micro-finance. It is really strange that why in India the concept has not been getting its due and the people started believing that micro-finance, nature, contents, philosophy and practices are becoming the myth.

The SGSY is being considered as a holistic scheme of micro-institutions concentrating all facets of self-employment and creating effective and efficient links between the different ingredients namely- organization of the rural poor into Self Help Groups, their respective capacity and ability building, planning of operation clusters, infrastructure build up, technology, credit and marketing etc.

The main purpose of the scheme is to bring up the existing poor families above poverty line. It is a credit cum subsidy program with the involvement of banking and financial enterprises. The expenditure under SGSY is shared by the Central Government and the State Governments with ratio of 3:1 or 75: 25. Subsidy would be given 30 per cent of the project cost subject to a maximum of Rs. 7,500 and 50 per cent for SC/ST subject to a maximum of Rs. 10,000. For groups, the rate of subsidy is 50 per cent subject to a maximum ceiling of Rs. 1.25 lakh. Under SGSY scheme nearly 29 lakh. SHGs have been formed since inception of the scheme till the end of 2008-09. {5}

According to an estimate nearly 7 lakh SHGs or 70 lakh beneficiaries have been covered for taking up the economic operations. So far more than 110 lakh swarozgaries or 40 lakh individual have been assisted. Total investment is amounted to Rs 23000 crore consist of credit mobilized Rs. 15,500 crore and subsidy disbursed Rs 7500 crore. Per capita investment has increased from Rs. 17000 in 1999-2000 to Rs. 28700 in 2008-09 showing a rise of about 70 per cent over the same period.

What's wrong with Micro-Credit/Finance?

In rural India [the real India], the rural indebtedness "a child is born in debt; lives in debt and die in debt" is not the off-shoot of micro-finance intuitions, but in reality, the major chunk of rural debt among households is non-micro-finance credit. The major contributors are unregulated local moneylenders who extend financial services which are fast and flexible and in return they charge usurious interest rates ranging between 60 and 120 per cent per year. {6}

There reports in regard to debt-related suicide in different parts of the India. According to Micro-finance Institutions Network (MFIN), 40 MFI's are accounted for Rs 30,000 crore as loan outstanding with 3 crore poor people. There are certain vital arguments against MFIs which demand immediate attention and solution by the planners and policy makers:

- 1) Micro-finance institutions are charging exorbitant rates of interest;

2) Micro-finance enterprises are carrying out unethical practices in their lending and recovering of loans;

3) Micro-finance institutions are aggressively poaching from Government and banks to capture their borrowers.

4) Micro-finance enterprises lack in transparency with regard to practices in respect of their interest rates structure.\

5) Micro-finance institutions are adopting and practicing multiple financing mode which is against their spirit and aim.

Keeping in mind the above arguments, micro-credit requires different treatment from normal banking especially due to the fact that microfinance assets consist of many small, uncollateralized loans which are un-guaranteed both in terms of nature and contents.

Myth:

The following are the myths on which the working and performance of micro-finance institutions are based on:

a) The very purpose of financial inclusion through micro-finance was not to give loans only. But it does include mobilizing deposits and providing basic banking services to the rural masses making it as mass banking. These are the missing links in existing contents of the MFIs.

b) MFIs are supposed to reach to those people in rural areas who have not access to banks. This is not true. These agencies concentrate on tapping into established SHGs for making loans resulting into two fold problems namely- duplication or multiple lending and excessive debt burdens.

c) MFIs are also being considered as an instrument for poverty reduction. But the biggest issue is that the loans are going for consumption purpose rather than productive purpose i.e. income supplementation which is the need of the hour for enhancing the purchasing power of the rural masses. Added to this, these loans are also used in agricultural operation wherein the rate of return is very low and it is become difficult for the loanee to bear 24 per cent rate of interest.

d) MFIs were created for replacing traditional money lenders in providing access to credit in the rural areas. This is also a myth. Still money lenders are dominating the rural credit scene. MFIs are marketing their credit instead the rural masses come to them. The most astonishing trend is that most of the traditional money lenders have established MFIs and making use of this facility for their own benefits. This means old wine in new bottle.

e) Operational cost is high and hence, high rate of interest i.e. 24 per cent is being charged. How sanctioning and disbursing loans are economically viable for poor, marginal and weaker section of the society to afford such rate of interest. Therefore, the very aim of easy and convenient loans to rural masses has been defeated.

g) Capacity building among borrowers is another myth. Rural masses have failed on this count also.

h) As in India, agriculture is till dominant sector and is responsible for rural poverty, micro-finance can not making much needed breakthrough in poverty eradication.

Reality:

The following are the harsh truths in respect of micro-finance availability to the poor and marginal farmers as well as weaker section of the society.

- 1) MFIs have emerged as profit-driven agencies.
- 2) MFIs are not different from private banks as these agencies are undertaking marketing of loans. They are running on the lines the US banks are marketing sub prime loans.
- 3) From a vision of creating slow and steady small fortune for the bottom of the pyramid, some micro-finance institutions moved to sell selling glittering story of quick and large fortunes from the bottom of the pyramid.
- 4) In India micro-finance sector, built around carefully nurtured affinities and an appropriate pace of scaling up based on capacities, has turned into a chaotic market places with little regulation.
- 5) The movement of micro-finance which was come up with the hope that poor, marginal farmers and weaker section of the society could create for all of them some economic and social value is over running by the idea that loose coalitions of joint liability groups could enable individuals to escape poverty.
- 6) Astonishingly high salaries of top management.
- 7) Bureaucratic interference leads to reduce the degree of flexibility which is essential for the success of micro-credit concept.
- 8) Bureaucratic hurdles also leads to corruption and hence, administrative cost goes up appreciably.

How to get MFI's back on track?

Keeping in mind the relevance, significance and contribution of micro-finance enterprises in rural areas, the need for better, effective, and efficient regulation of these institutions has become difficult to neglect. But on the other side of it, the moral edge these institutions are enjoying through extending loans to the poor and weaker sections of the population is being rapidly eroding.

The borrowers often needed to pay over a third of what they borrow as interest every year. This is because of the rising operational; costs which include very high salary to the managers. {7} This is why; the for-profit facet of these institutions is rapidly overwhelming the not-for-profit players.

In order to reap out the real fruits of micro-finance as a means of eradication of poverty on the one hand and on the other hand to bring economic emancipation to rural population, the concept and practices must eventually move into enterprises which are licensed and supervised by nation's financial authorities. These units could also be brought together in a large network and must control by their respective representatives. The functioning of each local unit could then be dominated by the local borrowers and savers.

Formidable Challenges:

The existing concept, structure and practices have to face tough challenges in years to come: They are given as under:

- a) To ensure quality of Self-helping-group and effective links between these groups and the banks;

- b) Even distribution of micro-credit and keep balance between savings and lending;
- c) Extension in the tenure of micro-finance products;
- d) How to make conscious the illiterate member of SHG in respect of maintaining records and accounts;
- e) Lack of perennial job opportunities to SHGs.

Conclusion:

From the foregoing discussion and analysis, it is clear that micro-finance is a promising alternative which offers funds at the doorstep of the poor and weaker section of the population in rural areas. For this system to operate upon, it has to have very low defaults. The success of micro-finance is based upon local mechanism that offers a great deal of flexibility that allows for lending decisions based on knowledge about specific individuals. What immediately required is to strengthen the voice of borrowers and curb that of national and global capital?

As the global recession hits investment potential and opportunities elsewhere in the world, lending to India's poor population could be extremely attractive options for private firms from the developed economies.

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