Volume : 2 | Issue : 7 | July 2013 • ISSN No 2277 - 8160

Research Paper | Entrepreneurship

Financial Inclusion: A Study on Opportunities and Challenges of Microfinance

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ABSTRACT

Financial Inclusion has been well recognized as the effective tool for ensuring equitable economic growth especially among the rural poor. Microfinance Institutions are expected to play a significant role in social upliftment and poverty alleviation. Microfinance is the fastest growing non-institutional channel for financial inclusion in developing economies. The initiatives of NABARD and RBI made India a home to the extensive microfinance programmes in the world, there is yet to have a substantial impact on outreach to the excluded population. The objective of maximizing financial inclusion is constrained by number of socio, economic and administrative factors. The formal banking system in India is still struggling to balance the dual objectives of outreach and financial performance. In this process an important issue is the ability of Microfinance Institutions to raise finance. An attempt is made in this research paper to examine the opportunities and challenges in Indian microfinance sector.

KEYWORDS: Microcredit, Self Help Group, Poverty alleviation

I. Introduction:

Financial inclusion objective is to extend the facilities of the organized financial system to include people with low incomes. Through credit facilities the poor can be lifted from one stage to another so that they come out of poverty. Financial inclusion has been acknowledged as the effective tool for ensuring equitable economic growth especially among the rural poor. The Reserve Bank of India has a policy priority of moving towards universal financial inclusion for the past decade. The Government of India, RBI, IRDA, have developed regulations and guidelines for strengthening financial inclusion. The banks have been advised by the RBI to integrate their financial inclusion plans with their normal business plans. India has for a long time recognized the social and economic imperatives for broader financial inclusion and has made enormous contribution to economic development by finding innovative ways to empower the poor. Over its entire life the formal rural banking system in India has struggled to balance the dual objectives of outreach and financial performance. Inclusive growth will act a source of empowerment and all people to participate more effectively in the economic and social process. The role of microfinance is well known for social upliftment and Microfinance Institutions (MFIs) are expected to play a pivotal role in poverty alleviation.

Microfinance is the fastest growing non-institutional channel for financial inclusion in developing economies. There have definitely been significant advances in microfinance operations across the global and NABARD initiatives made India as a home to one of the largest microfinance programmes in the world. But there is yet to have a substantial impact on outreach to the excluded population. The task of increasing and maximizing financial inclusion faces major challenges. The future growth of microfinance is constrained by a number of factors. An important issue is the ability of MFIs to raise finance. It covers a wide range of issues embracing social exclusion of low income families, widespread illiteracy, inhibition and poor physical access, high cost of operations and slow adoption of mechanisms. Given the largest estimated demand for microcredit, MFIs need multiple sources of financing, apart from the traditional loan financing from banks. The question remain whether the banks see business potential in the delivery financially inclusive services. The engagement of banks with low income families has been essentially in response to directed programmes such as Integrated Rural Development Programme. In the light of these developments, this research paper aims to examine the opportunities and challenges for Financial Inclusion by Self Help Groups of Microfinance.

II. Review of Literature:

Several studies have revealed that microfinance can help poor in coping with vulnerable situations, enhance the opportunities for savings and reduce the dependency on money lenders. Microfinance promotes women empowerment, individual growth, decision making and economic activities. While many studies have explored into the connection between microfinance and poverty alleviation in general, others have brought out the significance of Self Help Groups as a vehicle of microfinance delivery systems. Several researchers on financial inclusion have more concerned with socio-economic and socio-political empowerment of beneficiaries, especially women SHGs. Bank linkage system and problems, role of bankers and non-governmental organizations have no less been a subject of intensive research and researchers occasionally come up with alternative models of SHG Bank Linkage Programmes.

III. Need for the Study:

Rural people contribution to the economy is quite significant. Over 70 per cent of the people in the country live in rural areas and engaged in agriculture and allied activities. Eventhough microfinance has been successful in encouraging savings, the point of concern is about the continued stability and integrity of the movement. In the financial inclusion success lies in the regularity in the flow of finance on the one hand and availability of ready markets for their productions on the other. Given the large estimated demand for microcredit, Microfinance Institutions need multiple sources of Financing, apart from the traditional loan financing from banks. As part of the renewed emphasis on financial inclusion, six lakh villages have been allocated to various banks for coverage by 2012-15. With a view to promote awareness and closer cooperation among key stakeholders handling this issue, an attempt is made in this paper to highlight the opportunities and challenges for financial inclusion.

IV. Objectives of the Study:

Keeping in view of the importance of the study, the objectives of the present research paper are set as follows.

1. to examine the Microfinance role in financial inclusion.
2. to analyze the role of SHG – Bank Linkage Programme in microfinance.
3. To portrait the opportunities and challenges in financial inclusion
4. To offer suggestions based on the study for more effective financial inclusion.

V. Data Sources and Methodology:

The relevant information and data on which this research paper is prepared was extracted from primary as well as secondary data sources. Primary data was compiled on the responses obtained from selected Self Help Group members in the Krishna district of Andhra Pradesh. The secondary data sources include Research papers published, Reports of Banks, Previous research works and CRISIL grading of MFI sector. The primary data was thoroughly analysed using statistical techniques for arriving meaningful analysis. The conclusions drawn were also framed on the extensive literature available on the study area.

VI. Analyses and Interpretation:

Growth in the microfinance sector has been driven by an increase in investor interest in Micro Finance Institutions which is evident from growth in equity investments resulted in significant growth in the size of MFI balance sheets. "It is indefinitely not a high-risk sector, but it won't be a high-return sector either", said Mahendra Swarup, President of Indian Venture Capital Association. The Reserve Bank of India has now recognized Micro Finance Institutions as a special category NBFC and issued clear cut guidelines. Investors have got back their confidence as RBI regularly monitoring the sector. But most of the companies from Andhra, which fall under the CDR scheme, continue to brave the crisis as they cannot take advantage of the revival of the industry as they have to make provisions for the bad loans.

Financial inclusion makes growth broadbased and sustainable by progressively encompassing the hitherto excluded population. Inspite of the efforts of Government and RBI, the extent of financial inclusion is staggering as only about 40 per cent, of the Indian population have bank accounts. At the same time the proportion of people with life insurance cover is below 10 per cent. The growth under the MFI Linkage programmes was much higher than the growth under SHG Bank Linkage Programme. The progress of Micro Finance Programmes during the past five years period is presented in Table I.

Table – I
Growth of Micro Finance in India

	Number (million)		Amount (Rs. Million)	
	2008-09	2011-12	2008-09	2011-12
I.Self Help Groups				
Loans dispursed by banks	1.61	1.37	122,540	152,314
Savings with banks	6.12	7.57	55,460	75,120
II.Micro Finance Institutions:				
Loans disbursed by banks	581	5.64	373,200	780,430
Loans outstanding with banks	1915	2069	50,090	111,685

Source: Compiled from Trends and Progress of Banking in India 2011-12.

It can be known from Table – 1 that as per the opinion of majority respondents it MFIs and SHG Bank Linkage Programme help in promoting financial inclusion. In 2011-12 about 1.27 million new SHGs were credit linked with banks and 7.84 million SHGs maintained savings accounts with banks. It has been strongly believed that SHGs have the capacity to meet the financial requirements of unbanked people. NABARD is making all the needed efforts to make the approach more friendly and according to the ever changing requirements of the borrowers. Among the three models of micro financing in India i.e., SHG Bank Linkage Model, Grameen Model and Individual Banking Model, the first one is more popular as nearly 90 per cent of micro-credit is disbursed through it.

In Andhra Pradesh about 70 per cent of the fresh loan applications of MFIs have existing multiple loans ranging from 4 to 12, even though the A.P. MFI Regulation Act prohibits lending of fresh loans to people with existing loans. After February 2011 collections by banks have dropped to 20 per cent as A.P. MFIs (Regulation of Money Lending) Act, 2010 permits repayment of loans only at Panchayat offices. Prior to Octobe 2010, MFI Agents could visit the borrowers at their homes to make recoveries.

Bankers tend to consider low income households a bad risk imposing exceedingly high information monitoring costs on operations. Although there is demand for credit by poor and women at market interest rates, the volume of financial operation becomes self sustaining. Although microfinance offers a promising institutional structure to provide acess to credit to the poor, the scale problems needs to be resolved so that it can reach vast majority of potential customers who demand access to credit at market rates.

Financial Inclusion necessitates MFIs to broaden their resource base by mobilizing savings, accessing capital markets and effective institutional development. On the other hand, studies also reveal that the poor operating in the informal sector do save, although not in financial assets, and hence value access to client-friendly savings service at least as much access to credit. One way of expanding the successful operation of financial inclusion in the informal sector is through strengthened linkage of microfinance institutions with their formal sector counterparts. In this concern several strategic, institutional and connectivity issues of microfinance will arise.

Most MFIs that struggled to survive until last year, the loan portfolios are swelling, with investors and lenders deciding not to shy away anymore. In the words of Dilli Raj, CEO, SKS Microfinance all the descriptions were mainly because of a shock on the supply side and not on demand side. With regulatory clarity the survivors shall make use of it and address the huge market, so that there is a huge potential for growth.

The Reserve Bank of India has now recognized MFIs as a special category NBFC and regularly monitoring the sector by issuing clear-cut guidelines. Investors have got back their confidence, said Chandra Sekhar Ghosh, CMD, Bandhan.

Andhra Pradesh at the peak of the business in 2008 and contributed around 35 per cent of the total MFI portfolio, lost the portfolio due to government regulatory measures. Now most of the companies from A.P., which fall under the CDR scheme continue to brave the crisis. They include Share, Asmitha, Spandana and Trident. They cannot take advantage of the revival that the industry in general is going through as they have to make provisions for the bad loans. As expressed by Alok Prasad, CEO of Microfinance Institution Network (MFIN) "Investors confidence in microfinance had dried up almost entirely post the Andhra Pradesh Ordinance of 2010 but returning gradually. The gross loan portfolio has also seen a surge and that was the key driver of funding to the sector.

Financial Inclusion through Microfinance faces several challenges in India. The formation of Self Help Groups emphasize the inclusion of the poorest of the poor. The inconsistency arises on account of their failure to drew members from the poorest section of the rural society. Most of the members have seen to come from financially well-to-do families. The exclusion is mainly because of illiteracy, prejudices, blind belief and poverty.

Another major hurdle for the financial inclusion is lack of physical, social and technological infrastructure and also lack of understanding of products and services suited to the needs of low income families.

From the study it was noticed that majority of the members joined in Groups are motivated by themselves and about one third of sample respondents joined SHGs for saving money and the remaining for benefitting from the government programmes.

Group leaders without proper education, group conflicts, lack of effective participation in the meetings, lack of management approaches for conflict management, lack of periodical appraisal of the performance of the groups, variations in the amount of investment from one income generating activity to another, dependence of the SHG members upon moneylenders for investment, bank loan amount and marketing problems have been the major challenges posing to financial inclusion.

The study of strengths, weaknesses, threats and opportunities of members of SHGs revealed certain important factors on the prospects of microfinance management. Strengths of the sample respondents are shown in Table – 2.

Table – 2 Strengths of SHG Members

S.No.	Strengths	% of Respondents
1.	Proper Rationale behind joining SHGs	100%
2.	Group Leader is acceptable to all members	100%
3.	Holding meeting whenever necessary	100%
4.	Unanimous decisions	100%

5.	Providing chance to every member to raise their voice	100%
6.	Flexibility in Group management in terms of disbursement of bank loan etc.	100%
7.	Regular payment of thrift amount	100%
8.	Proper utilization of interest accrued on savings amount	100%
9.	Having awareness of Rules and Regulations	98%
10.	Regular updating of SGH pars book	95%
11.	Regular repayment of internal group loan installment amount	87%
12.	Selection of Income generating activity	87%
13.	Periodical appraisal of performance of the group	84%
14.	Unity among group member	76%
15.	Regular attendance of the members to the group meetings	72%
16.	Marketing on own	55%
17.	Support from the family members to provide capital in case loan amount is not sufficient	12%

Source: Computed from the primary data

For any collective entity or organization to survive, it is necessary for the members to have the capacity to identify threat factors and take steps to ensure that these threats do not affect sustainability. Threats of sample respondents of SGH are shown in Table – 3.

Table – 3
Threats of Sample Respondents of SHG

S.No.	Threats	% of Respondents
1.	Lack of training to the SHGs on conflict management	100%
2.	Dependence on others for marketing	45%
3.	Dependence on money lenders for insufficient capital amount	44%
4.	Group conflicts	24%
5.	Lack of support from the family members to group members	24%
6.	Problem of raw materials	17%

Source: Computed from the primary data

SWOT analysis of sample SHGs reveals that strengths and opportunities are found to be in higher degree when compared to weakness and threats. Women in the SHGs are confident of overcoming the minor weaknesses and threats utilizing the major strengths and opportunities that they possess.

VII. Conclusion:

Financial Inclusion improved from 2010-11 as a result of the efforts of RBI and NABARD. Based on the recommendations of the C.Ranga Rajan Committee, has set up two funds namely Financial Inclusion Fund (FIF) and Financial Inclusion Technology Fund. Simultaneous efforts have been made by banks and several schemes were also introduced by Government of India towards the direction of financial inclusion viz., General Purpose Credit Card, Government to Person (G2P) Know Your Customer (KYC) etc. The Government need to intensify its efforts towards financial inclusion as the progress towards the target of covering all villages with a population of over 2000 by the year 2012. It requires a comprehensive approach by banks towards creating awareness on financial services, debt counseling, encouraging savings through proper linkages with MFIs. The banks shall capitalize on the growing aspirations of the poor as a result of growing incomes and educational level towards financial inclusion.

CRISIL in its recent study of Top 50 Microfinance Institutions revealed that growth in the microfinance sector has been driven by an increase in investor interest in MFIs over the past couple of years. Strong business growth, improving geographic diversity, growing earnings, and healthy asset quality are the key strengths of India's MFIs. On the other hand, dependence of financial institutions for funds, political sensitivity of matters relating to interest rates, pressure on processes and controls and weak governance architecture are also the major challenges in the sector.

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