RESEARCH PAPER | Accountancy | Volume : 2 | Issue : 1 | October 2012 | ISSN - 2249-555X

Micro Finance : A Bird View

Prof. Dr. D. M. Parmar
Shreea. R. S. Sakhida Arts & Shree C.C.Gediwala Commerce College, Limbdi

Prof. Dr. Kishor V. Bhesaniya
Shreea. R. S. Sakhida Arts & Shree C.C.Gediwala Commerce College, Limbdi

Introduction
Microfinance is the practice of extending small longs to the poor for income-generating activities often coupled with other financial

Services such as savings and insurance.
During the 1970's, social innovators revolutionized the banking industry. They created microfinance institutions (MFIs) that lent money at reasonable interest rates to poor women who could not offer collateral. Not only did the borrowers expand their businesses and increase their incomes, but their high repayment rates demonstrated that the working poor are capable of transforming their own lives given the chance. This model of lending disproved all conventional thinking. Microfinance was born.

More than a quarter century later, MFIs serve more than 80 million poor people in developing countries with over $7 billion in outstanding microcredit loans. They exist in many forms – credit unions, commercial banks and, most often, non-governmental organizations (NGOs). Repayment rates average higher than 95 percent while commercial loan repayments from large businesses often fall below 50 percent. The high repayment rates demonstrate that the working poor are willing and able to repay their loans, and that they are capable of transforming their own lives given the chance. Microcredit promotes self-reliance and empowers the poor to lift themselves out of poverty.

What is microfinance?
Microfinance was started with the practice of extending small microcredit loans (usually $50 to $150) to the poor for income-generating activities, and has now grown to encompass other financial services such as savings and insurance products. Access to credit and savings has proven to be an effective poverty alleviation strategy by providing the poor with opportunities for self-reliance through self-employment and asset accumulation.

How Microfinance Works
Microfinance products such as savings accounts, microcredit loans (usually $50 to $150), and health insurance empower the poor to lift themselves out of poverty. Through microfinance, they can secure better nutrition, education, healthcare and housing for their families. Microfinance has helped millions in developing countries raise their standards of living and protect themselves from economic setbacks. The tragedy is that the vast majority of the world's poorest people still lack access to these basic financial services.

The traditional banking system requires that a borrower have collateral in order to receive a loan. The world's poorest people have no such collateral. Further, traditional banks are not generally interested in issuing small loans - $50 to $150 - as the interest benefits do not exceed the transaction costs. So how exactly does microfinance work?

First, many microfinance institutions (MFIs) utilize social collateral in the form of peer groups to ensure loan repayment. Borrowers take out loans in groups of five to eight individuals. If a borrower defaults on her loan, the entire group typically is penalized and sometimes barred altogether from taking further loans. This peer pressure encourages borrowers to repay loans in full and on time, resulting in the higher than 95 percent repayment retas. Among the few who default, the most common reason is an illness in the family, which disrupts their lives, rendering them unable to continue their business and repay their loans. The second most frequent reason is natural disaster or unanticipated crisis.

Microcredit loan cycles are usually shorter than traditional commercial loans-typically six months to a year with payments plus interest, due weekly. Shorter loan cycles and weekly payments help the borrowers stay current and not become overwhelmed by large payments.

Clearly the transaction-intense nature of weekly payment collections, often in rural areas, is more expensive than running a bank branch that provides large loans to economically secure borrowers in a metropolitan area. As a result, MFIs must charge interest rates that may sound high-often 30 percent annually – in order to cover their costs. These interest rates are still significantly lower than the 300 percent to 3,000 percent annual rates the borrowers were previously paying money lenders and are typical of the local credit interest rates.

Why Target Women?
There are many reasons why women become the primary target of microfinance services. At a macro level, it is because 70% of the world's poor are women. Women have a higher unemployment rate than men in virtually every country and make up the majority of the informal sector of most economies. They constitute the bulk of those needing microfinance services.

Women are usually the primary or only sole family caretakers in many developing countries. Helping them gain additional daily income improves the condition of their entire household. Putting extra income in women's hands is often the most efficient way to impact an entire family, as they typically put their children's needs before their own. Children are more likely to complete their education and escape the poverty trap than their parents. Giving women access to microcredit loans therefore a multiplier effect that increases the impact of a microfinance institution's activities, benefiting multiple generations.

What is a "microfinance institution"?
A microfinance institution (MFI) is generally a nonprofit, non-government organization that extends loans to the poor for income generating activities. There are thousands of MFIs worldwide making loans to millions of poor, self-employed borrowers.

Whom does microfinance serve?
Microfinance serves poor people who do not have access to commercial finance institution. They are typically self-employed in sales. Production or agricultural activities. Women are most frequently served as they constitute 70% of the world's poor.

Terms
- **Microcredit**

The practice of extending small loans to poor people for in-

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come generating self-employment projects, allowing them to improve their standard of living.

- **Microcredit Loan**

A small loan, typically $50 - $150, depending on the geographic location. These loans are made to the poor for income generating self-employment projects, allowing them to meet their basic needs, improve their standard of living and become economically self-sufficient.

- **Microenterprise**

A self –employment project or very small business run by a poor borrower. Types of business vary widely by geographic location and may include shining shoes, selling items as a street vendor, selling agricultural products, weaving, sewing or banking.

- **Microfinance**

A general term describing the practice of extending small ("micro") loans and other financial services, such as savings accounts and insurance, to poor borrowers for income generating self-employment projects.

- **Microfinance Institution (MFI)**

An organization engaged in extending microcredit loans-and often other financial services – to poor borrowers for income generating self-employment activities.

- **Non-government Organization (NGO)**

In the microfinance industry, this term is generally used to describe an entity that usually works with the poor but is not formally administered by the government. Many NGOs, however, receive portions of their funding from government sources. Microfinance institutions are an example of an NGO.

- **Poor Group or Solidarity Circle**

A group of 5-8 borrowers who have received individual microcredit loans to finance their collective or individual income-generating activity. The peer group is designed to encourage solidarity among members who co-guarantee each other's loans. Often, if one borrower defaults on her loan, the entire peer group is penalized.

- **Poverty**

A state of being in which one is unable to provide for basic human needs, including food, shelter, medicine and clothing.

- **Sustainability**

Refers to the ability of a microfinance institution to develop a methodology that ensures loans successfully reach the poor while covering all of its costs without subsidy.

- **Transformation**

The term "transformation", or commercialization, of a microfinance institution (MFI) refers to a change in legal status from an unregulated nonprofit or non-governmental organization (NGO) into a regulated, for-profit institution.

- **Unitus Donor-Investor**

An individual or organization who contributes money to Unitus, investing in our ability to most efficiently leverage resources to accelerate MFI growth, empowering exponentially more poor borrowers to improve their standard of living.

Can microfinance really help alleviate poverty?

Yes. Research shows that access to small amounts of credit-with reasonable interest rates instead of the exorbitant rates charged by traditional money lenders-helps the poor to create or grow their own self-employment projects, which in turns help them to build their income. By providing the poor credit and a chance to save, microfinance helps empower families to work their way out of poverty.

What is Unitus?

Headquartered in Redmond, Washington, with a regional office at the Unitus India Microfinance Center in Banglore, India, Unitus is a global microfinance accelerator. Unitus is a 501(c)(3) nonprofit organization led by Mike Murray (Board chairman) and Geoff Davis (President & CEO). Our mission is to alleviate global poverty by increasing access to microfinance. The Unitus Board of Directors is composed of business-minded professionals with expertise in finance, venture capital and management. 100% of your contribution goes directly to our program work thanks to a committed group of supporters covering our 2006 operating costs. All contribution are tax-deductible to the extent allowed by law.

What do you mean by "microfinance accelerator"?

Unitus focuses on "supersizing" MFIs that have already clearly demonstrated an ability to design, implement and grow a successful microfinance program. Unitus aims to exponentially increase the number of loans made by their MFI partners.

What is your methodology?

Using our own evaluation methods, Unitus selects and partners with MFIs that have demonstrated an ability to design, implement and grow a successful microfinance program. Unitus provides capital funding and organization capacity-building consulting to these MFIs with the aim of dramatically accelerating the number of microcredit loans that can be made to poor borrowers in developing countries.

Who is behind Unitus?

The Unitus Board of Directors is composed of business-minded professionals with expertise in finance, venture capital and management. Operationally and strategically, Unitus is run by Geoff Davis, a leading scholar, lecturer and practitioner in the field of microfinance and the economics of poverty.

How can I get involved in Unitus ?

Unitus welcomes inquiries from similar –minded individuals Families and foundations who would like to become involved unitus to Fulfill its mission.