



## Microfinance : Emerging Role, Issues and Challenges in India

### KEYWORDS

Microfinance, MIF's, RBI

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**ABSTRACT** *This present paper highlights the meaning of microfinance, emerging role, issues and challenges being faced in India. The paper represents the micro finance meaning and definition provided by the authors. This paper explains the need and challenges that are faced by the poor people in India and providing them financial helps, in way of microcredit to start their own small businesses, so they can generate income and provide for their families. The study explores some glaring issues, challenges and offers some suggestion to make micro finance more effective. Hence, Government, RBI and various MFI's have to face various challenges and to overcome with these challenges and issues some preventive measures are also taken by these financial bodies so that to provide benefits to the poor people and social class of the society. On the basis of need, issues and challenges related to microfinance, the study predicts the new agenda for future.*

### Introduction:

Form few decades microfinance sector has grown rapidly, many Indian economies, experimented with subsidised credit for the poor people. But only the tangible outcome perhaps was the increases in Non- Performing assets (NPA). Then come the realisation that the core issue for the poor people was to access credit rather than the cost of credit. Finance is very essential for every economic activity. Microfinance is the provision of financial services to low income people and self employed who are lack accesses to banking and related services. It covered a wide range of services like insurance, credit, remittance and also non financial services like training, counselling etc. Finance is also required by the every section of the society. But from the beginning of the civilization, only the financial needs of the upper section of the society were catered.

### Literature Review:

Review of literature on microfinance has revealed the emerging issues, need and challenges that are earlier taken by the microfinance institution for the development and growth for the country. There have been numerous researchers that analyzed these emerging factors. Sekhi.V (2007) proposed a view that micro finance has been proved to be powerful tool in poverty alleviations. It is one of the only development tools with the potential to be financially self-sustaining. After that, certain microfinance programmes have gained prominence in the drive field and beyond. However, after more than 30 years of industry effort 80 pc of the working poor is still without access to microfinance services. According to Singh B and Chawla.S (2007) analyzed that major hindrance in the development of the poor is not lack of opportunities, but the availability of credit and related financial support services that helps in promoting sustainable livelihood activities. During later years, the concept of microfinance gained popularity to meet the credit requirements of poor through and with the help of SHG's groups.

### Research Methodology

This study is basically exploratory in nature and entire discussion has been made on the basis of secondary data. The secondary data are collected from various reports of

RRB's publish by NABARD, books, magazines and journals etc.

### Objectives

**To be specifics, the main objectives of this study are:**

- To defines the meaning and role of microfinance
- To explains the need of microfinance institutions and their components.
- To examine the glaring challenges of microfinance in India.

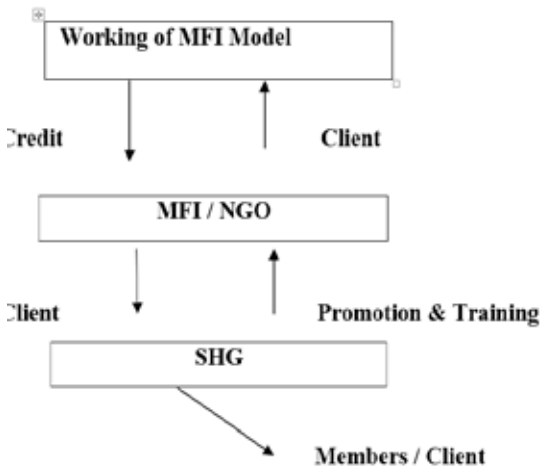
### Microfinance Meaning:

Microfinance refers to a variety of financial services that target low income people, particularly women. Since the clients of microfinance institutions (MIF's) have lower incomes and often limited access to other financial services, microfinance products trend to be for smaller monetary amounts than traditional financial services.

### Microfinance Defines:

A good definition of Microfinance given by **Robinson** is "Microfinance defines as a small –scale financial services for both credits and deposits that provided to people who farm or fish or herd; operate small or microenterprises where goods are produced and recycled, repaired, or traded.

Microfinance is a type of banking service that is provided to unemployed or low income individuals or groups of people who would otherwise have no other means of gaining financial services. Ultimately, the aim of microfinance is to give low income people provide them an opportunity to become self- sufficient by providing a means of saving their money, borrowing money and insurance.



Source: Status of Microfinance in India - 2012 NABARD

### Role of Microfinance

Microfinance played a vital role in the mobilization of savings and promoting economic development. In the past financial sector reforms in India (1991) phase, the performance and strength of the banking structure improved perceptibly. The financial soundness of the Indian commercial banking system compares favourably with most of the advanced and emerging countries. From 1991, the size of the Indian economy in terms of Gross Domestic Product (GDP) at market prices has increased by almost fifteen times, whereas the household financial savings have expanded up to sixteen times and the gross domestic saving by almost seventeen times during the same period but in this growth the contribution of Rural India is negligible.

### Need of Microfinance

India is agriculture based rural economy and more than 60 percent of total population still lived in villages. Villages are heart of India. The main occupation of rural people is agriculture and usually they take agriculture as their way of life. India's repaid development depends on the developments of rural sector. Micro finance need has increased after reading the report of NSSO. According to NSSO "the income of rural farmer is Rs 2115 per month in 2007". In this family of a farmer consists 5 members and 2 animals? So microfinance becomes essential for rural India.

### Components of Microfinance

The following components of the microfinance which are mostly discussed are:

- 1. Micro credit:** Micro credit is the extension of very small loans (which are known as microcredit) to improve borrowers who typically lack collateral, steady employment and verifiable credit history. It is designed not only to support entrepreneurship and alleviate poverty but also in many cases to empower women and uplifting the social class by extension. Micro credit has emerged as an idea that appeals to various sections of poor people.
- 2. Micro insurance:** It is the insurance with low premiums and low caps / coverage. In this micro refers to the small financial transaction that each insurance policy generates. Products in micro insurance are:
  - Health insurance contract
  - Personal accident contract
  - Contract covering belonging Hurt, livestock, Tolls or instruments, hut etc.

- 3. Micro saving:** Micro finance branch of small deposits accounts recommended as an incentive to those with lower incomes for saving money. They are similar to saving accounts, but designed for small deposits. There are either low or minimum deposits and typically no services charge. Micro finance accounts are designed for small and in some cases very small deposits into a savings accounts that has minimum balance.

### Micro Finance Institutions

Those institutions which have microfinance as their operation are known as micro finance institutions. A large number of organisations with varied size and legal forms offer microfinance services. These institutions lend through the concept of Joint Liability Group (JLG) act as an informal group comprising of 5 to 10 members who come together for the purpose of availing bank loans. The reasons for existence of separate institutions i.e. MFIs for offering micro finance are as follows :

- High transaction cost – generally micro credit fall below the break-even point of providing loans by banks
- Loans are generally taken for very short duration periods.
- High frequency of repayment of instalments and higher rate of default
- Absence of collaterals – poor are not in a state to offer collaterals to secure the credit

### Challenges faced by Micro finance

There are over 10,000 microfinance institutions serving in excess of 150m customers, 100m of them being the poorest families. Microfinance is gathering momentum to become a significant force in India. Some challenges faced by micro finance in India are:

- **Financial illiteracy:** One the major challenge in India towards the growth of the microfinance sector i.e. illiteracy of the people. This makes it difficult in creating awareness of microfinance and even more difficult to serve them as microfinance clients.
- **Inability to generate funds:** MFIs have inability to raise sufficient fund in the microfinance sector which is again an important concerning challenge. Through NBFCs are able to raise funds through private equity investment because of the for profit motive, such MFIs are restricted from taking public deposits.
- **Heavy dependence on banks & FIS:** MIF's are dependent on borrowing from banks & FIS. For most of the MFI's funding sources are restricted to private banks & apex MFI's. In these available banks funds are typically short term i.e. maximum 2 years period. Also there is a tendency among some lending banks to sanction and disburse loans to MFI,s around the end of the accounting year in pursuit of their targets.
- **Weak governance:** Many MFI's are not willing to convert to a corporate structure; hence they trend to remain closed to transparency and improved governance, thus unable to attract capital. MFI's also facing a challenge to strike a balance between social and business goals. Managements need to adapt business models based on changing scenarios & increased transparency; this will enable attracting capital infusion and private equity funds.
- **Competition:** India's microfinance sector is fragmented, having more than 3000 MFI's, NGO-MFI are present. Top 10 microfinance companies in India account for 74 percent of the total loans are outstanding and about more than 17 MFI's have more than Rs. 1mn

outstanding loans. Also, entries of commercial banks present to be a key competitor to MFIs.

- **Political sensitivity of interest rates:** Interest rates charged by MFIs are primarily to the poor people; thereby it can become a political sensitive issue. Over the past few decades, MFIs in Southern part of Indian states were accused of excessively charging high rate of interest and have been targets by local administrations. The states of India include Andhra Pradesh, Tamil Nadu, and Karnataka etc.
- **Need to resist the current trend:** The pressure being applied by MFIs to resist should be seen in this context. The political influence is reflected in the fact that the Andhra Pradesh MFIs (Regulation act passed on December 2010) has caps on interest rates. This once again shows that the government is willing to let the micro finance institutions do business as usual and larger fight against neo-liberal policies and the increased social security for the rural and urban poor people.
- **Operational issues while aggressive growth**
- **Perspectives on the SHGs**
- **Build professional system and process**
- **Design financially sustainable models**
- **Steady access to capital**

## FINDINGS

The paper found that in India there are large numbers of populations and rural poor households who do not have access to banking and other financial services. Therefore, to provide access to these services to them RBI and government of India has taken various initiatives. In taking all these initiatives government found out some issues and challenges. Many hindrance and obstacles are there in the path of promoting and achieving financial activities. It should not be taken as an obligation by these intuitions and banks but seen as future prospect and opportunity for growth and targeting untapped and unorganized market.

## CONCLUSION

This study concludes that microfinance is an important tool for improving standard of living of people. In India micro finance has succeeded with repayment rates upto 98 per cent reported in all across the country which consists states like Andhra Pradesh, Tamil Nadu, west Bengal, Karnataka, and Orissa etc. This tells us that micro finance has certainly has the capacity to reduce poverty by a great margin. The challenging issue in microfinance helps to reduce the financial problems faced by poor people. Inability of MFIs in getting sufficient funds is a major challenge in the microfinance growth and so these institutions should look for alternative source of funds. The impact of microfinance is appreciable in bringing confidence, courage skill development among poor people. Thus external factors such as microfinance institutions are needed to help fix these problems.

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