Research Paper Management

Micro Finance- Risk Scenario and Remedies

*Dr. P. Subramanyachary

* Associate Professor, Department of MBA, Siddharth Institute of Engineering and Technology, Narayanavanam Road, Puttur-517583,Chittor District, Andhra Pradesh

ABSTRACT

This paper discusses the role of Micro Finance in the development of a country and also discusses different types of risks occur in the operations of Micro finance activities. Though Micro finance sector started with small beginning, it has grown significantly with efforts of forming informal Self Help Groups to provided access too much needed saving and credit services. For strengthen Micro finance sector in India, NGOs must be permitted to invest in the equity of Micro Finance Organizations (MFOs) like Bolivia and some African Countries. In the course of providing their services to the poor Micro finance institutions are facing the different types of risks like political risk, economic risk, currency risk, geographical limits, unhealthy competitions etc. To remove these risks steps to be taken for strengthening of MFOs. In addition to this, terms for setting up of MFOs to be eased. As per the changes take place in the economic scenario of global economy changes to be adapted for smooth running of Micro finance sector. Regulations should ensure to help genuine MFOs which encourages Micro finance sector for well performance.

Keywords : Micro Finance, Self Help Groups, Risk

Introduction:
Micro finance is probably the first concept based on the credit delivery systems aimed mainly at the poor. The in-built flexibility of choice for the purpose of credit without the formalities of collaterals and sanction conditions has made the concept popular among the people all over the world cutting across race, religion and political status of nations. Micro finance refers to credit extended by:

Formal institutions to individuals.
Formal institutions to informal groups.
Informal groups to its individual members.
Formal institutions through voluntary association to Informal groups

Micro credit is defined as a system of credit delivery and savings mobilizing scheme especially designed to meet the unique financial requirements of the poor. The financing schemes allow the recipients to improve the status of their living through access to additional capital without collateral. A borrower of micro credit must belong to a group to qualify for a loan. The original micro credit model requires that the group of individuals apply for a loan on behalf of one member. The group guaranteed repayment of a loan offered to one member at a time. Once a group member has paid off a loan, another member of group may qualify for a new loan or a repeat loan may be granted to a non- defaulting client. The original model has gone through many transformations. In most countries micro finance clients are typically self-employed and low income entrepreneurs in both urban and rural areas.

II Need for Micro Finance:
Micro finance accelerates the growth of domestic deposits and mobilizes micro savings which will be given for investments for encouraging self-employment. It becomes ad good financial mechanism in the informal economy. Women participate in economic activities through this sector which made them self sufficient and empowerment. Micro finance facilitates national and international remittance flow of investments as well as development of local private sector and investment in innovations. Broadly the micro finance activities improve slum conditions, develop rural areas, interest in agricultural and allied activities and also improve health services.

III Role of micro finance sector in undeveloped countries:
Over the last twenty years micro credit is one of the most effective tools to fight poverty in under developed countries. It is an investment to reduce poverty in the world. In third world countries many statistics have shown them like Dominican Republic, Srilanka, Poland. Sub-Sahara African countries, Bangladesh etc. micro finance made better life to the poor people.

When the observe examples in Brazil Casas Bahia has significant contribution in retail sector. In Mexico micro finance sector achieved success in cement sector by Cemex Company which is largest cement company Mexico. In cellular network sector, Gram Phone Company in Bangladesh brought significant change. In India ICICI brought recognized change lending issue. In Sub- Sahara in African Countries there is a prospect for the growth of micro- entrepreneurship in at least 13 countries of the region where the size of the loan may allow the borrowers to assume a certain degree of risk. The micro credit operation in Sub- Sahara Africa can be a successful experience if reforms a company the growth of the micro credit programmers paying a way for the growth of micro- entrepreneurship

Poverty alleviation in the common and overriding objectives of the developing world. United Nations Millennium Declaration committing their nations to a new global partnership to reduce extreme poverty and setting out a series of tune-bound goals with target deadline of 2015. These goals have become known as the Millennium Developed Goals (MDG's). While income was considered as the major factor of the poverty, other factors such as hunger, disease, lack of adequate shelter, gender equality, education and environmental sustainability were also included in these goals there as follows.

Eradicate extreme poverty and hunger.
Achieve universal primary education.
Promote gender equality and empower women.

Reduce child mortality.
Improve maternal health.
Combat HIV AIDS, Malaria and other diseases.
Ensure environmental sustainability.
Develop a global partnership for development.

These goals are also known as indicators of micro finance to achieve the mentioned goals micro credit has to play a key role.

IV Role of micro credit in India:
In India micro finance started in the early 1980's by forming self-help-groups which aimed at accessing saving and credit services. National Institute like NABARD, SIDBI etc is also contributions resources to micro finance. In Indian context there is an opinion on micro credit that

Micro finance is providing with the interest of the lender.
It is something done predominantly with the poor.
It is also considered as alternative commercial sector.

India has learnt so many experiments from the world countries especially from Bangladesh, Indonesia, Bolivia and some other African countries. Since micro credit is positioned as a development strategy for anti- poverty programmers, micro finance is considered as financing for the poor. Similarly the credit delivery systems through informal channel self-help-groups. Self help groups refer to involve people who have similar needs and are operated on informal and non-profit basics. Generally governmental or non-governmental organizations will form and guide these groups with emphasis on body thrift and credit activities. Through a consensual approach the group finalizes all the financial decisions. Once the groups show the maturity of financial behavior, banks are encouraged to make loans of the SHG's in certain multiples of the accumulated savings on the SHG's.

Best practices in micro finance through SHG's:
India has been trying to reduce the poverty and other problems of rural poor through SHG's by following credit practices.

Effectiveness which refers degree of the delivery services for achieving the intended objectives
Equity which refers fair distribution of benefits and opportunities
Efficiency which refer favorable ratio of costs of outputs
Stability which refers should not confront with the structured barriers of inequity in the growth in communities and local power structures

Transparency which refer through systems, procedures and rewards

Some other practices are positive interest rates of loan, community monitoring of the utilization of credit, pressure the member to repayment, overdue less than 10% etc. Ratio of SHG will facilitate the banks to take taster decision on distributing the loans to the groups; Ratio is given on the basics pf several aspects like operations, punctuality of repayment and size, education, participation of members. Ratio's also increases competitiveness among SHG's in providing finance to poor and their performance.

The following are the various Indian micro finance institutions that are active at present

The Activities for Social Alternatives (ASA) – Tamil Nadu

Bharat Integrated Social Welfare Agency (BISWA) – Orissa

Grameen Koota – Karnataka

Gram Vikar – Orissa

ICICI Bank – through out India

Kas Foundation – Orissa & Chattisgarh

SEWA Bank – Gujarat

Spandana – Andhra Pradesh

Basic – Throughout India

Mysore Resettlement & Development Agency (MYRADA) – Karnataka

Mutually Aided Cooperative Societies (MACS) – Andhra Pradesh

For strengthening micro finance sector in India NGO's must be permitted to invest in the equity of micro finance organization in the countries like Bolivia and African Countries.

V Risk Scenario:
Like all the other sectors micro finance sector is facing different types of risk as follows;

Political risk:
In the micro finance sector present greater risk in the interference of government by improving interest rates in addition to this RBI confirmed in august 2004 that " The interest rate applicable to loans given by……………micro credit organization's to self-help-groups / member beneficiaries would be left to their discretion". Some state is not supportive due to political pressure. In some states a weak rule of law may present riskier operations environmental for both MFI's and micro enterprises.

Economic risk:
India's new government is not expected to make any radical shifts in economic policy. However the goal is likely to increase social spending, which some analysis believe could hamper India's ability to service in foreign debt and pressure interest rates upward.

Currency risk:
India's exchange rate can be character as managed float in relation to the US dollar. RBI intervener in foreign exchange markets to keep the exchange rate stable. In addition as it is possible to purchase on one year forward contract on Indian currency in liquid markets, it is possible to hedge against currency risk during this period.

Geographic concentration:
Indian micro finance activity is located in south, with anywhere between 50 & 70% alone in Andhra Pradesh. So some MFI's have begun to encourage their clients to engage in diverse livelihood activities and provide micro insurance as a way to minimize the covariant risks that they themselves face due to geographical concentration.

Unhealthy competition:
Many in industry feel the level and nature of MFI competition in Andhra Pradesh and Tamil Nadu is unhealthy and could potentially lead to unsound lending and reduced portfolio quality due to clients borrowing from more than one institutions.

Institutional risk:
When we come to institution risk, there will be lack of sound governance policies at the board level. Besides thus, there is lack of skills in managerial staff and accounting and financial reporting are not proper.

Some other risk perception are most borrowers are without desired entrepreneurial skills, costly exercise and small loans for many, unorganized scatter groups , low capital and low skill base, limited prospects, insufficient infrastructure, vicious financial cycle, low investment-low income-low profit, weak accounting practices, unsecured credit exposure etc.

Steps to remove risks:
The success of micro finance institutions depends on the following factors and risk can be removed by providing some facilities.

Visionary Leadership

Supportive Policy Environment

Effective Donors

Physical & Social environment

Management with political economy.

Institutional process bearing

Conclusion:
Many of the countries in the world have adapted some form of micro credit model with a goal to reducing poverty. In the course of operating its activities micro finance sector is facing different types of risk. By removing risk the sector can be strengthened and make it the best tool for reducing poverty in the world. By making changes related micro finance sector as per needed in the global economy, it can be made as sustainable model to reduce poverty and other problems in the world.

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