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ROLE OF MICROFINANCE INSTITUTIONS IN FINANCIAL INCLUSION IN INDIA

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Abstract
Financial inclusion is emerging as a new paradigm of economic growth that plays major role in driving away the poverty from the country. Banking services are making accessible to masses including privileged and disadvantaged people at an affordable terms and conditions. But a section of the society in developing economy still deprived of financial services. Microfinance institutions plays a very significant role in bridging the gap. Financial inclusion is important priority of the country in terms of economic growth and advanceness of society. It enables to reduce the gap between rich and poor population. In the current scenario financial institutions are the robust pillars of progress, economic growth and development of the economy. The present study aims to examine Microfinance impact on financial inclusion in the economy. Secondary data has been taken for analysing the impact of microfinance institutions in India. Results of the study found positive and there is significant impact of Microfinance institutions on financial inclusion aspect.
Keywords: Financial inclusion; Microfinance Institutions, Indian Economy, Micro Credit, Financial Independence

Introduction:

Microfinance began in India way back in 1921 with the establishment of Syndicate Bank in the private sector. In its initial years, the Syndicate Bank concentrated on raising micro deposits in the form of daily/weekly basis and sanctioned micro loans to its clients for shorter periods. But microfinance came to be well known only when Dr Mohammad Yunus made it a mass movement in the form of Grameen Bank experiment in Bangladesh. Microfinance can be called a novel approach to provide savings and investment facility to the poor around world. The modern economy depends on the availability of an array of financial products to support individuals in times of economic need. Microfinance is the provision of these financial services to people who either are poor or very poor. This concept, which now covers a broad range of financial products, was initially just one service - Micro Credit, a form of targeted development lending that became widespread in the 1980s. The aim of microfinance is to provide an alternative and economically beneficial form of lending to the poor and very poor communities that have no other viable financial option (Sarah Gettings and Rajni Thakur feasibility Study of Microfinance programme, Chhatarpur, 2007).

Role of MFIs and Commercial Banks:

There is a wide array of institutions and classifications that overlap in the India microfinance sector, making analysis difficult and identification of appropriate regulators confusing.

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Furthermore, the scope and reach of microfinance in India is hard to capture because direct bank lending is usually not included in microfinance analysis. Commercial banks in India are required to make a certain percentage of loans to designated "priority sectors." Microfinance is one of the priority sectors banks may choose from, and loans are made to institutions as well as individuals in order to fulfill the requirement. As of April 2011, microfinance loans must meet certain prudential requirements in order to qualify for priority sector status. The majority of microfinance is provided by commercial banks, regional rural banks (RRBs), self-help groups (SHGs) (with special linkage programs to banks), cooperative societies, and microfinance institutions (MFIs) that take a variety of forms, including NGOs (registered as societies, trusts or Section 25 companies) and non-bank financial companies (NBFCs).

Review of Literature:

Sivasankar.P.R, Ekambaram. K (2015), concluded that commercial banks continue to play an important role in financing small scale industrial sectors. The growth rate of bank credit has been low as compared to the growth rate of production from small scale industrial sector.

Rajan Kumar, Subhash chander (2013), focused that most of the small scale industries in Punjab depended heavily on the owner's capitals for financing fixed capital. They resorted to long — term borrowings under compulsion and not as a matter of policy or convenience to take advantage of favourable financial leverage. Commercial banks are the most prominent institutions approached by the units for long — term borrowings followed by Punjab Financial Corporation, Punjab Small Industries Development Corporation of India and District Industrial Center.

Ramana Reddy. K.V, Krishna Reddy. B, Maddileti.K (2016), concluded that State Financial Corporation contributed to the emergence of 903 units in Mahaboob Nagar district with the credit disbursement of Rs.45 crores over the period of 40 years. This led to the capital formation of Rs. 57 crores and generated employment to 8251 persons.

Sindhu Vijayalcumar (2017) noted that commercial banks sanction loans to industries but their focus is generally on large — scale units. They hesitate to provide large funds to small — scale units because of two reasons. First, small — scale units generally need small amount of finance. Second credit worthiness of small — scale entrepreneurs is doubtful. So small scale entrepreneurs especially women entrepreneurs, largely depend on financial institutions other than commercial banks.

Ram Chandra Rao.K.S, Abhiman Das, aravidn Kumar Singh. (2016), viewed that the definition and coverage of the small scale industrial sector is being revised from time to time by excluding more and more commodities from the reserved small -scale industries list and also through liberalizing the credit delivery mechanism of the banking industry. Despite increase in the coverage of the small-scale industrial sector, its share in bank credit decreased and growth fluctuated.

Thingalaya.N.K (2006), described that new generation banks are normally not interested in small amounts of credit. They have ventured in to this only after the upward revision is made in the definition of small and medium sector, and with a narrow base of advances made; their progress in credit disbursements appears impreMFIve.

Prasain. G.P, Nixon singh. E.N, Sharat Singh. N (2006), concluded that there was a severe

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lack of capital as well as credit, largely because of low productivity in many branches of small scale industries. The commercial banks and financial agencies may establish more small scale industrial specialized branches at least one in every district headquarters to cater to the financial needs of small entrepreneurs

Srivasta. R. (2005) concluded that the operating feature of the State Financial Corporations is that they have provided three fourths of their MFI stance to small-scale sector. He also concluded that the state financial corporations existing resources are too limited to cater to the growing needs of smaller enterprises.

Research Methodology:

Objectives of the Study:

The study covers the following objectives:

1. Study of Microfinance institutions providing access to banking services in Indian economy.
2. Analysis of impact of microfinance institutions in Indian economy.

Microfinance & Indian Economy:

One of the guiding principles of the planning process in India has always been poverty alleviation. The allocation for the provision of education, health, sanitation and other facilities has been considerable. Allocation for these is supposed to promote capacity building and well being of the poor. The Indian government puts emphasis on providing financial services to the poor and underprivileged since independence. Commercial banks were nationalized in 1969 and were directed to lend 40% of their loans at concessional rates to the priority sector. The priority sector included agriculture and other rural activities and weaker sections of the society in general. The aim was to provide resources to help the poor start their micro enterprise and attain self sufficiency.

The government also launched various poverty alleviation programs like Small Farmers Development Scheme (SFDS) 1974-75, Twenty Point Programme (TPP) 1975, National Rural Development Programme (NRDP) 1980, Integrated Rural Development Programme (IRDP) 1980, Rural Landless Employment Guarantee Programme (RLEGP) 1983, Jawahar Rozgar Yojana (JRY) 1989, Swarna Jayanti Gram Swarojgar Yojana (SGSY) 1999 and many other programs. But most of these programs failed to achieve their desired goal due to poor execution and malpractices on the part of government officials. Funds meant for the welfare of the poor were misappropriated or diverted by powerful and corrupt manipulators at the local level (Mehta, 1996). To supplement the efforts of micro credit, the government started a very good scheme – the Integrated Rural Development Programme (IRDP) in 1980. But this supply side program (ignoring demand side of economy) hardly achieved anything. It involved the commercial banks in giving loans of less than Rs 15,000 to people of socially weaker sections. The total investment, within 20 years, was around Rs 250 billion to roughly 55 million families. But that was far from realizing its desired goal.

The design of IRDP incorporated a substantial element of subsidies (25-50% of each family's project cost), which became a problem, as this allowed extensive misuse of funds and malpractices. This situation led to bankers viewing the IRDP loan as a motivated handout and they largely failed to follow up with borrowers. The estimates of repayment rates in IRDP ranged from 25-33%. The two decades of IRDP experience in the 1980s and 1990s affected the credibility of micro borrowers in the view of bankers and, ultimately, hindered access of

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the less literate poor to banking services. This act of the government had a serious long-term impact on the development of micro entrepreneurship among the underprivileged. The program, which was claimed to be *"the world's largest microfinance program"* during its launch, failed due to poor execution and political interference. The mid-term appraisal of the ninth plan had indicated that these programs presented a matrix of multiple programs without desired linkages. The programs suffered from critical investments, lack of bank credit, over-crowding in certain projects and lack of market linkages. And the reason was that the programs were basically subsidy driven. They completely ignored the process of social intermediation, which is critical for the success of self-employment programs. A one-time provision of credit without a follow up action and lack of continued relationship between borrowers and lenders also contributed to the failure of these programs.
In the year 1997 a committee was constituted by the planning commission to review the effectiveness of self-employment and wage employment programs. The committee, in its report, recommended that all self employment programs be merged. It also recommended a shift of importance from individual beneficiary approach to a group-based approach. It emphasized identification of activity clusters in specific areas and strong training and marketing linkages. The government accepted the recommendations of the committee. On April 1, 1999, a new program called Swarnajayanti Gram Swarojgar Yojana (SGSY) was launched. This was basically an amalgamation of programs such as IRDP (the Integrated Rural Development Programme) and a number of allied programs such as TRYSEM (Training of Rural Youth for Self Employment), DWCRA (Development of Women and Children in Rural Areas), SITRA (Supply of Improved Toolkits to Rural Artisans), GKY (Ganga Kalyan Yojana) and MWS (Million Wells Schemes). This has been a holistic program covering all aspects of self-employment such as formation of Self-Help Groups (SHGs), training, credit, technology, infrastructure and marketing. The program aims at establishing many micro-enterprises in rural areas. SGSY is a credit-cum-subsidy program. It lays emphasis on activity clusters.

The Swarnajayanti Gram Swarojgar Yojana got tremendous response from its beneficiaries. While the number of SHGs under this program is about 2.25 million, an investment of Rs 14,403 crore goes into it, profiting over 6,697million people (Wikipedia).

Another effort that proved to be a colossal failure was the entire network of primary cooperatives and RRBs. It was established to meet the need of the rural sector in general and poor. Saddled with the burden of directed credit and a restrictive interest regime, the position of RRBs deteriorated quickly. The cooperatives suffered from the malaise of mismanagement, privileged leadership and corruption born from excessive state patronage (Sinha, 2003).
The microfinance initiative in the private sector in India can be traced back to an initiative undertaken by Shri Mahila SEWA (Self Employed Women's Association) Sahakari Bank in 1974. This was started to provide banking services to poor women of Gujarat's Ahmedabad. This bank was established at the initiative of 4,000 self employed women workers who put in shares of Rs10 each. The objective of the bank was to provide credit to these women to empower them and free them from the vicious circle of debt. Currently SEWA Bank has over 318,594 account holders with a total working capital of Rs 1291.89 million (March 09).

Another NGO which fostered the process of change in the lives of the poor was MYRADA (Mysore Rehabilitation and Development Agency) of Karnataka. The year was 1968. While the objective was to help the poor help themselves, MYRADA achieved this by forming Self

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Help Affinity Groups (SHAGs) and through partnership with NGOs and other organizations in 1984-85. At present it is managing 18 projects in 20 backward districts of Karnataka, Tamil Nadu and Andhra Pradesh. These initial initiatives had a much-localized operation and were limited to their members only. The result was that they failed to take the shape of a mass movement. In India, initially many non-government microfinance institutions (MFIs) were funded by donor support in the form of revolving funds and operating grants.

The entry of NABARD, the National Bank for Agriculture and Rural Development, in 1992 brought a boom in the field of microcredit. The whole movement of microfinance in India got a boost. Around 70% of landless and marginal farmers in India did not have a bank account and 87% of poor had no access to credit from a formal source (NCAER Rural Financial Access Survey 2003).The share of formal financial sector in total rural credit was 56.6% compared to informal finance at 39.6% and unspecified source at 3.8%(RBI Report 1992). There is a huge potential for microcredit in rural India. The Reserve Bank of India (RBI) has advocated for financial inclusion of majority of population for economic development of our country. Access to affordable financial services, especially credit and insurance, enlarges livelihood opportunities for the poor. Apart from social and political empowerment, financial inclusion imparts formal identity and provides access to the payment system and to saving safety net like deposit insurance. Hence financial inclusion is considered to be critical for achieving inclusive growth (U Thorat, 2007).

A simple definition of financial inclusion given by RBI Governor Y.V. Reddy (2007) is: *"Ensuring bank account to all families which want them"*. He said it would be the first step towards reaching the goal of bank credit as a human right as advocated by Nobel laureate Professor Mohammed Yunus.

Now the microfinance service providers include apex institutions like National Bank for Agriculture and Rural Development (NABARD), Small Industries Development Bank of India (SIDBI) and Rashtriya MahilaKosh (RMK). At the lower level we have commercial Banks, Regional Rural Banks and cooperatives to provide microfinance services. The private institutions that undertake microfinance services as their main activity are generally referred to as Microfinance Institutions (MFIs) in Indian context. There are also some NGOs which lend credit to Self Help Groups (SHGs). The NGOs that support the SHGs include MYRADA in Bangalore, Self Help Women's Association (SEWA) in Ahmadabad, PRADAN in Tamil Nadu and Bihar, ADITHI in Patna, SPARC in Mumbai. The NGOs directly providing credit to the borrowers include SHARE in Hyderabad, ASA in Trichy, RDO Loyalam Bank in Manipur (Tiwari, 2004).

Microfinance Delivery Models:

The leading models of microfinance are:

- Grameen banking, perhaps the most widespread, with characteristic forms of small group organization and strict procedure
- Self Help Groups, with larger and more autonomous groups and a mixture of social and financial intermediation
- Regulated financial institutions, usually small and operating in favorable regulatory environments
- Credit cooperatives, some of which, as in Sri Lanka, have made an effort to include the poor

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An important model in India, among the array of microfinance models, is the Self-Help Groups (SHGs). These are larger and much more autonomous than borrower groups in the Grameen Model. SHGs are based primarily on the principle of lending the savings of their members. They also seek external funding to augment their resources. A number of non government organizations (NGOs) specialize in promoting and motivating SHGs with an important distinction between NGOs, which operate as financial intermediaries, and those, which confine themselves to social intermediation. About 400 to 500 NGOs are said to have been engaged in microfinance, but the total outreach is estimated to be less than 1.5 million households. This is very small as compared to the number of poor households in the country. While some NGOs emphasize sustainability, in many cases interest margins are far too low for these to be achieved and the institutions remain heavily dependent on donor assistance.

A group of people, who have personally faced an issue or experienced a life situation, either directly or have seen it closely happening to their family or friends, comprises a self-help group or a mutual aid group. Sharing experiences enables them to empathise with each other and give mutual support and to pool practical information and ways of coping with it. Some groups hold regular meetings – on a weekly, monthly, or quarterly basis. Meetings may be at public venues, such as community centers, or group members' homes. Other groups maintain support through letter writing, or through a network of telephone, internet, news groups and e-mails. In India, about 90% of SHGs are women's groups where each SHG has 10-20 members. An SHG is linked to a commercial bank, regional rural bank or cooperative bank for its credit needs. Before a loan is granted to any SHG, it must prove its ability to save, learn book-keeping skills, and commit to continue as a cohesive group. Usually 6-12 months observation period is kept to comply with the above conditions.

Conclusion:

Microfinance institutions (MFIs) play a crucial role in promoting financial inclusion, especially in underserved and economically disadvantaged communities. Financial inclusion refers to the access and usage of financial services by individuals and businesses, regardless of their income level or social status. MFIs contribute to this goal by providing a range of financial services tailored to the needs of low-income individuals who have limited or no access to traditional banking services. Here are some key roles played by MFIs in achieving financial inclusion:

MFIs are known for providing microcredit or small loans to entrepreneurs, small business owners, and individuals who lack collateral or credit history. These loans help them start or expand their businesses, generate income, and improve their living standards. By offering accessible credit options, MFIs empower individuals to become financially self-sufficient and contribute to local economic development.

MFIs encourage savings habits among low-income individuals by offering safe and convenient savings accounts. These accounts provide a secure place to deposit money, earn interest, and build financial resilience. By promoting savings, MFIs enable individuals to accumulate funds for emergencies, future investments, or long-term goals, thereby fostering economic stability. MFIs often collaborate with insurance providers to offer microinsurance products to their clients. Microinsurance provides coverage for risks such as illness, accidents, crop failures, and natural disasters. By accessing affordable insurance options, low-income individuals can protect themselves and their assets from unexpected events, reducing their vulnerability and enabling them to recover more quickly from setbacks

Many MFIs prioritize financial literacy and education programs alongside their financial services. They provide training and workshops to help clients understand basic financial

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concepts, develop money management skills, and make informed financial decisions. By improving financial knowledge, MFIs empower individuals to utilize financial services effectively, avoid predatory practices, and plan for their future.

MFIs often have a social mission and aim to address broader development goals beyond financial inclusion. They may support initiatives related to women's empowerment, rural development, healthcare, education, and environmental sustainability. By integrating social and environmental objectives into their operations, MFIs contribute to inclusive growth and the well-being of the communities they serve.

As of September 2021, the microfinance sector in India had a total loan portfolio outstanding of around INR 2.48 trillion (approximately USD 33.9 billion).The sector witnessed significant growth over the years, with the loan portfolio increasing from around INR 1.79 trillion in March 2019 to INR 2.48 trillion in September 2021.India has a large number of microfinance institutions operating across the country, ranging from small NGOs to larger specialized institutions. As of September 2021, there were over 1,000 registered microfinance institutions in India. The microfinance sector in India has reached millions of borrowers, predominantly consisting of low-income individuals, women, and small businesses.As of September 2021, the sector had around 42 million active borrowers.

Overall, MFIs act as catalysts in expanding financial services to marginalized populations, empowering them economically, and breaking the cycle of poverty. Through their inclusive and tailored approach, they contribute significantly to achieving financial inclusion and fostering sustainable development.

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