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Micro finance and financial inclusion

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Abstract

Micro Finance is a type of banking service that is provided to unemployed or low income individual, or groups who otherwise have no other access to financial services. The main goal of micro finance is to empower under- privileged class of society, women and poor. The idea of micro finance was developed as survival strategy for the poor. Ela Bhatt in India and Professor Muhammad Yunus of Bangladesh are the pioneers in this field. For the development of under developed countries, a strong finance system is required. The goal of inclusive growth can be achieved by financial inclusion. Financial inclusion is delivery of financial services; at affordable cost to section of disadvantage and low income groups and weaker sections. Micro finance has significant role in bridging the gap between formal financial institution and rural poor. This paper aims to study the concept of microfinance and microfinance institution. This paper also describes the impact of micro finance on financial inclusion with special focus on poverty eradication. The paper also discusses the type of MFIs, its working and geographical spread, branch network, and client outreach and portfolio size of micro finance institution.

Keywords: micro finance institution, financial inclusion, poverty eradication

Introduction

Micro Finance is a form of financial services for entrepreneurs and small business lacking access to banking and related services. Two main mechanisms for the delivery of financial services to such either are:

1. Relationship- based banking for individual entrepreneurs and small business
2. Group- based models, where several entrepreneurs come together to apply for loans and other services as a group.

Micro Finance is a way to promote economic development, employment and growth through the support of micro entrepreneurs and small business. Mohammad Yunus, a Nobel Prize winner introduced the concept of Micro Finance in Bangladesh in the form of the "Grameen Bank". NABARD took this idea and started concept of micro finance in India.

Micro finance services are aimed at the poor clients, who do not have access to formal financial sources. Micro finance has its unique characteristics, which are as follows:

- Mostly it is collateral free.
- MFI's goes to the client rather than clients go to MFIs.
- Simplified saving and loan procedure.
- Small size of loans and savings.
- Repeat loans.
- Free use of loans.
- Repayment considers income from business as well as other sources.
- Interest rate is usually in between money lender and formal banks.
- Member of SGHs enjoy micro finance.

History of Micro Finance

In the early days the service of banks and the financial institutions are exclusively for those people who are financially strong. However the person from the weaker section of economy was unable to avail these services. There comes the concept of micro finance. The history of micro finance can be traced back as long to the middle of the 1800 when the theorist Lysander Spooner was writing over the benefits from small credits to entrepreneurs and farmers as a way getting the people out of poverty. Starting late 1960, India was home to one of the largest state intervention in rural credit market. It saw nationalization of existing private commercial banks, massive expansion of branches in rural area, creation of new set of rural banks at district level and an Apex bank for agriculture and rural development. In India, micro finance revolution begins in the 1980 with the formation of SGHs. India's first micro finance institution was 'Shri Mahila Seva Sahkari bank" and it was an urban cooperative bank leading financial institution as SIDBI, NABARD and Rashtriya Mahila Kosh and few NGOs like PRADAN, MRYADA and SEWA have played a significant role in promoting micro credit.

Objective of the study

- To study the concept of micro finance and micro finance institutions.
- To study the current status of MFIs in India.
- To highlight how the micro finance models are useful to achieve financial inclusion.

Conceptual Framework

Microfinance is buzzing word, used when financing for micro entrepreneurs. Concept of micro finance is emerged in need of meeting Special goal to empower under-privileged class of society, women and poor, downtrodden by natural reasons or men made; caste, Creed, religion or otherwise. The principles of Micro Finance are founded on the philosophy of cooperation and its central values of Equality, Equity and Mutual Self-help. At the heart of these principles are the concept of human development and the brotherhood of man expressed through people working together to achieve a better life for themselves and their children. Micro credit is the most common product offering. Micro-finance in India is synonymous with micro credit; because savings, thrift and micro-insurance constitute a miniscule segment of the micro finance space. The motherland for Indian Microfinance is Andhra Pradesh, mainly because of the state government's critical efforts in the late 1980s in building SHG-bank linkage models with loans from NABARD (National Bank of Agriculture and Rural Development) which built up a strong Micro-finance portfolio.

i) Microfinance Institution

A MFI is an organization that acts as an interface between the formal credit delivery institutions and credit seekers, with an aim to assist for the socio economic development of poor and marginalized people. MFIs are essential to encourage micro enterprises and empower local people including women. The geographical distribution of MFIs is very much concentrated in the Southern India where the rural branch network of formal bank is excellent.

ii) Types of MFI

By taking into account legal structures, MFIs may be classified as follows:

a) Not For profit MFIs

1. Societies (e.g. such as Bandhan, Rashtriya Seva Samithi and Gram Utthan.)
2. Public trusts (such as Shri Khetra Dharmasthala Rural Development Project, and community development centre.)
3. Non-profit companies (such as Indian Association for savings and credit, and cash per micro credit).

b) Mutual benefit MFIs

1. Co-operatives registered under state or National Acts (such as Pustikar Lagh Vyaparik Pratisthan Bachat and sakh Sahkari Samiti Limited)
2. Mutually-aided Co-operative societies (MACS, such as Sewa Mutually Aided Co-operative Thrift Societies Federation Ltd.)

c) For –Profit MFIs

1. Non-banking financial Companies (NBFCs, such as Bharatiya Samruddhi Finance Ltd, Share Micro fin Ltd, SKS Microfinance Ltd and Spandan Sphoorthy Finance Ltd.)
2. Producer Companies (such as Sri Vijaya Visakha Milk Producers Co. Ltd.)
3. Local area banks (the only such MFI is Krishna Bhima Samruddhi Local Area Bank.)

iii) Working of Microfinance Institutions

The Microfinance Institutions (MFIs) take little or no collateral security for the credit extended. The people covered are mostly those who cannot avail loans from banks and other such financial institutions due to the lack of ability to provide guarantee or collateral security against the money borrowed. Although the amount of finance provided individually is less (say around 5-10 thousand), they aggregate to a substantial amount when the entire financial year is considered (most cases running to crore). Banks failing to extend loans to the poor section of people is the high default risk for repayment of interest and in some cases, the principle amount itself. So the question arises as to how the MFIs are able to thrive and perhaps record a staggering growth rate over the years and how they almost nullify the risk of default of repayment. It is pertinent to note that the individuals availing loans are divided into groups (each group consisting of say 5 members) headed by one leader from the group. The amount to be repaid by every individual member is guaranteed by the remaining members of the group. 4-5 groups from one particular locality form a batch, again headed by a leader from amongst the members of different groups. A field officer, who is the employee of MFI, is put in-charge of each batch, who conducts meetings periodically (say every week) where the collections are made. It is quite clear that the mutuality concept is used here to the extent that, groups of persons with a common objective and mutual interest are involved. The default risk is further reduced by applying more conditions. A few of them are:-

a. An individual can avail his/her initial loan, only after attending certain number of batch meetings
b. Subsequent loans can be availed depending on the history of repayments made towards earlier loans.
c. Size of loans will be increased gradually.
d. Interest on a single loan will be reduced gradually during each collection period.

Growth, Outreach and Loan Portfolio

Client outreach and loan portfolio are two key indicators of a MFIs contribution to financial inclusion as well as the depth and breadth of financial deepening achieved by it. This paper aims to provide an overview of MFIs outreach in terms of client coverage and loan portfolio, based on the data received from 166 MFIs.

1. Geographical Spread of Microfinance

MFIs currently operate in 29 States, 4 Union Territories and 588 districts in India. Table 2.2 shows the distribution of MFIs by state. In particular, it shows the number of MFIs operating in each state, their total number of branches in the state and the number of districts with microfinance operations. Annexure1 indicates the state wise presence of different MFIs. Twenty five MFIs with a large outreach and portfolio have operations in more than five states, out of which five leading MFIs are operating in more than fifteen states. A total of 62 MFIs (38%) are operating in two to five states, while 79 MFIs (48%) have confined their operations to only one state. The details of States/ Union Territories wise operation of 165 MFIs are given in Table.

No. of MFIs in Indian States/UTs

Table 1

No. of States/UTs	No. of MFI
1	79
2 to 5	62
6 to 10	16
11 to 15	4
> 15	5
Total	166

MFIs with a smaller scale or regional focus have concentrated their operations in 1-2 states only whereas other MFIs have spread across a higher number of states in order to increase their size, scale and simultaneously mitigate concentration risk. MFIs operating in multiple states, in general, are typically larger in size and follow the legal form of an NBFC-MFI. The geographical expansion of bigger MFIs is illustrated by the fact that while in 2013 -14 only 15 MFIs had operations in more than 5 states, that number increased to 25 in 2015 -16.

2. Branch Network

The MFIs in India had been consolidating their operations to cope with the effects of transition taking place in the sector. While 2012 and 2013 witnessed a decline in the branch network, the trend was arrested in 2014. In 2014 -15, MFIs have expanded their branches, posting a marginal growth of 4.57 %. In 2015 -16, total branch network of the MFIs excluding Bandhan was 11644. In 2014 -15, Bandhan alone had 2022 branches out of total branch network of 12221. Number wise branch network in 2015-16 has declined to 11644 from 12221 but actually there is a growth of 14% (factoring in Bandhan's exit as an MFI).

3. Client Outreach

The total number of clients served by MFIs stood at 399 lakhs as on 31 March, 2016. Client outreach of MFIs had grown substantially from 2005 to 2011, reaching a level of 317 lakhs. This trend slowed down during 2012 and 2013 and the number of clients slumped to 275 lakhs. The trend reversed in 2014 with a growth and reached a level of 330 lakhs. This trend continues in 2016 with a huge rise in clients/borrowers to an all time high of 399 lakhs. Majority of these clients are being served by NBFC-MFIs (84.94%), primarily the larger ones. MFIs with outstanding portfolio above 500 crore are responsible for reaching out to 85.41% of the clients in the industry. Client Outreach grew by 8% 2016 relative to 2015 without Bandhan which indicates a sound growth of MFIs in 2015-16. This rise in the number of borrowers is positively correlated with an increase in fund flow from banks, MUDRA and financial institutions to MFIs.

4. Loan Portfolio of MFIs

As per the NSS data of various years, including the latest one of 2013, majority of the population is still dependent largely on informal and expensive sources, including money lenders to meet their credit needs. Credit needs for such a population range from emergency loans, consumption loans, business loans, working capital loans, housing etc. Credit is the flagship service offered by MFIs to clients outside the net of formal financial services. For MFIs, loan portfolio is the primary revenue generating asset. It also gives details about the health of MFIs through financial performance, as the financial performance is a function of revenue and cost. Loan portfolio of the MFIs and its trends are analyzed below to understand the performance of the institutions and their contribution to the goal of financial inclusion. As of March 2016, the total loan portfolio of MFIs has reached an all time high of over 63,853 which is a 31% growth over last year that also includes a managed portfolio of nearly 16,914 crore. Total managed portfolio also includes a BC portfolio of `7984 crore which is 13% of total loan portfolio. The net loan portfolio owned portfolio on the books of the MFIs stood at `46939 crore, which is an increase of 20% over the last year.

List of Top MFIs with Loan Portfolio as of March 2016

Table 2

S. No	Name of MFIs	Gross Loan Portfolio (in crore)
1	Janalakshmi Financial Services Ltd.	10983
2	SKS Microfinance Ltd.	7682
3	Ujjivan Financial Services Ltd.	5389
4	SKDRDP	4994
5	Equitas Micro Finance Ltd.	3283
6	Satin Credit care Network Ltd.	3271
7	Grameen Koota Financial Services Pvt. Ltd.	2539
8	Spandana Sphoorty Financial Ltd.	2282
9	ESAF Microfinance & Investments Pvt. Ltd.	1925
10	Share Micro fin Ltd.	1540

Micro Finance and Financial Inclusion

Micro finance is one of the most effective tools of reducing poverty. Micro finance has a significant role in bridging the gap between the formal financial institution and the rural poor. The MFIs accesses financial resources from the bank and other main stream of financial institution and financial services to the poor. MFIs play a significant role in financial inclusion as they are uniquely positioned in reaching out to the rural poor. To achieve the economic growth the participation of all section of society is required, but the lack of access to financial for weaker section of society, small farmer has become a serious threat to economic progress. Financial inclusion is the main object of many developing countries as there is direct correlation between financial exclusion and poverty. According to World Report, "Financial Inclusion or broad access to financial services is defined as absence of price or non price barriers in the use of financial services."

The Bharat Micro Finance 2016 reveals that

- The reported 166 MFIs with branch network of 12,221 employees have reached out to an all time high of 39 million clients with an outstanding loan portfolio of Rs. 63,853 crore.
- Outreach grew by 31% over the 2014-15.
- Average loan distributed per SHG for 2015-16 is reported at Rs. 203,526.

- Total no of SGHs credit linked during 2015-16 is 18.32 lakhs.
- MFIs offered products ranging from micro credits, micro insurance, savings and remittance.

Conclusion

Access to financial services such as savings, insurance and remittances are extremely important for poverty alleviation and development. In order to achieve goal of total financial inclusion, policymakers, banks MFIs, NGOs and regulators have to work together. Financial Inclusion is a win- win situation for the financially excluded, the corporate, the government and the banks. Financial Inclusion is the path for inclusive growth. As a complementary to financial inclusion, micro finance can work as a powerful tool to fight poverty. Micro Credit, Micro Finance Institutions such as SHGs has a strong footing in India. Micro Finance plays a significant role to achieve financial inclusion but as rules and regulations of micro finance institutions are not regulated properly, so there would be high case of risk and defaults.

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