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Current scenario of microfinance industry in India

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Abstract: The present paper highlights the microfinance & evaluates the position of micro-finance. The concept of microfinance is not new in India. Traditionally, people have saved with and taken small loans from individuals and groups within the context of self-help to start businesses or farming ventures. Majority of poor are excluded from financial services. Microfinance is a programme to support the poor rural people to pay its debt and maintain social and economic status in the villages. Microfinance is an important tool for improving the standard of living of poor. In spite of many organizations of microfinance, microfinance is not sufficient in India. The study explores some suggestions to make microfinance more effective. The potential for growing micro finance institutions in India is very high. Microfinance market in India is expected to grow rapidly, supported by government of India's initiatives to achieve greater financial inclusion, and growth in the country's unorganized but priority sector. Microfinance has evolved rapidly into a global movement dedicated to providing access to a range of financial services to poor and nearpoor households. Major Cross-section can have benefit if this sector will grow in its fastest pace. On the basis of growth and evolution related to microfinance, the study predicts the new agenda for future. The microfinance industry being very small in terms of value added to the Indian financial sector. It examines the experience, of India, which has one of the largest microfinance sectors in the world. Globally, over a billion poor people are still without access to formal financial services. Some 200 million of these people live in India. The Indian Government should find an avenue for creation of awareness on how microfinance can benefit from loans and monitors closely to ensure disbursement of loans and grants to entrepreneurs.

Keywords: Microfinance Institutions, Self Help Groups, Microcredit, MUDRA Bank.

INTRODUCTION

In 1976, a small experiment was conducted in the poverty-stricken and flood ravaged Bangladeshi village of Jobra. Professor Muhammad Yunus, a lecturer of Economics at Chittagong University visited the village and upon seeing the desperate poverty there he decided to lend about \$27 (free of interest) as working capital to a few women he met there. To his surprise, the women used the money productively in their modest commercial enterprises and repaid the loan with thanks. This small experiment was to become the basis for a global revolution popularly known as microfinance. As the new millennium arrived, micro credit had come to be recognised as the ultimate panacea for endemic poverty. In 2005 the UN Secretary General Kofi Annan said it was a

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critical anti-poverty tool, emancipating women and empowering the poor and their communities. Yunus claimed that thanks to micro credit the next generation will only find poverty in museums.

OBJECTIVES OF THE STUDY

- To understand the need and evolution of Microfinance Industry in India
- To evaluate the success of Microfinance in providing microcredit to poor population.
- The changing scenario of microfinance industry in India
- The steps taken up by the government to promote microfinance sector.

MATERIALS AND METHODS

It is mainly concerned with peculiar sources of secondary data collection are tapped. Secondary data are collected from the research papers, dissertations of the scholars, books of references, standard publication and reports by institutes and organizations, magazines, periodicals, internet etc.

EVOLUTION OF MFI'S INDUSTRY

Microfinance has built a solid track record as a critical tool in the fight against poverty and has entered the financial mainstream. The rapid growth of the industry over the past 15 years has reached approximately 130 million clients according to recent estimates. Yet microfinance still reaches less than 20 percent of its potential market among the world's three billion or more poor. Nearly three billion people in developing countries have little or no access to formal financial services. Financial services for poor people are a powerful instrument for reducing poverty, enabling them to build assets, increase incomes, and reduce their vulnerability to economic stress. Formal financial services such as savings, loans, and money transfers enable poor families to invest in enterprises, better nutrition, improved living conditions, and the health and education of their children. Microfinance has also been a powerful catalyst for empowering women. The evolution of the industry has been driven by many factors which include the transformation of microfinance providers, the sizable supply gap for basic financial services, the expansion of funding sources supporting the industry and the use of technology. As the industry has developed, there has been a shift from specialized NGOs to an increasing number of regulated and licensed MFIs which stress that sustainability and impact go hand in hand. Furthermore, The World Bank Group is working with private microfinance institutions and stakeholders to incorporate responsible finance practices into all aspects of business operations. Since pioneering commercial microfinance in the early 1990s, IFC has continued to lead innovation in microfinance, using developments in technology, financial products, and policy to help financial institutions reach a greater number of people in a more cost-effective way. IFC's goal for microfinance is to scale up access to a range of high quality



financial services for underserved populations, maximizing development impact and ensuring institutional sustainability. IFC achieves this goal by effectively combining investment and advisory services to a range of financial intermediaries. IFC is the World Bank Group's lead investor in microfinance, and is one of the leading multilateral investors in terms of outreach to microfinance institutions, working with more than 100 institutions in over 60 countries. Within the microfinance industry, the majority of MFIs are subsidized, either by governments or by NGOs. According to the World Bank, although there are over 10,000 microfinance institutions (MFIs), serving over 150 million poor people in developing countries, they only reached 4 percent of the potential market. In the recent years there has been a tremendous growth in the number of microfinance borrowers, growing over the past five years, between 25 and 30 percent annually and it is expected a similar growth in the coming years¹⁸ Microfinance industry is segmented, ranging from very small NGOs with few clients to large institutions with millions of clients and it is a highly concentrated industry.

One need only consider that the median share of the largest MFI in a country is one third of the entire market and the median share of the top ten MFIs is about 95 percent of the all industry¹⁹. The microfinance investment market is also growing in size and maturity and it is increasing the need of investors for transparency through market research, data provider and analysis of MIFs. Transparency is encouraged by the launch of open data for microfinance such as MIXMarket²⁰, which publishes data on more than 1,500 microfinance institutions (MFIs) in more than 190 countries, and helps to build the information infrastructures needed in developing countries.

MICROFINANCE HISTORICAL EVOLUTION WORLDWIDE

Traditionally, people have saved with and taken small loans from individuals and groups within the context of self-help to start businesses or farming ventures. These stages are described below: The evolution of Microfinance sector can be broadly divided into four distinct phases:

Phase 1: The cooperative movement (1900-1960)

During this phase, credit cooperatives were vehicles to extend subsidized credit to villages under government sponsorship.

Phase 2: Subsidized social banking (1960s – 1990)

With failure of cooperatives, the government focused on measures such as nationalization of Banks, expansion of rural branch networks, establishment of Regional Rural Banks (RRBs) and the setting up of apex institutions such as the National Bank for Agriculture and Rural Development (NABARD) and the Small Scale Industries Development Bank of India (SIDBI), including initiation of a government sponsored Integrated Rural Development Programme (IRDP). While these steps led to reaching a large population, the period was characterized by large-scale misuse of credit,



creating a negative perception about the credibility of micro borrowers among bankers, thus further hindering access to banking services for the low-income people.

Phase 3: SHG-Bank linkage program and growth of NGO-MFIs (1990 – 2000)

The failure of subsidized social banking triggered a paradigm shift in delivery of rural credit with NABARD initiating the Self Help Group (SHG) Bank Linkage Programme (SBLP), aiming to link informal women's groups to formal banks. The program helped increase banking system outreach to otherwise unreached people and initiate a change in the bank's outlook towards low-income families from 'beneficiaries' to 'customers'. This period was thus marked by the extension of credit at market rates. The model generated a lot of interest among newly emerging Microfinance Institutions (MFIs), largely of non-profit origin, to collaborate with NABARD under this program. The macroeconomic crisis in the early 1990s that led to introduction of the Economic Reforms of 1991 resulted in greater autonomy to the financial sector. This also led to emergence of new generation private sector banks that would become important players in the microfinance sector a decade later.

Phase 4: Commercialization of Microfinance: The first decade of the new millennium

Post reforms, rural markets emerged as the new growth drivers for MFIs and banks, the latter taking interest in the sector not only as part of their corporate social responsibility but also as a new business line. On the demand side, NGO-MFIs increasingly began transforming themselves into more regulated legal entities such as Non Banking Finance Companies (NBFCs) to attract commercial investment. MFIs set up after 2000 saw themselves less in the developmental mould and more as businesses in the financial services space, catering to an untapped market segment while creating value for their shareholders.

Historical Evolution of Microfinance in India

1960 to 1980 Phase 1: Social Banking	1990 Phase2: Financial Systems Approach	2000 Phase:3 Financial Inclusion
1. Nationalization of private commercial Banks 2. Expansion of rural branch network 3. Establishment of	1. Peer-pressure 2. Establishment of MFIs, typically of nonprofit origins	1. NGO-MFIs and SHGs gaining more egitimacy. 2. MFIs emerging as strategic partners to diverse entities interested



rural regional banks 4. Establishment of apex institutions such as national bank for agriculture and rural development and small industries development bank of <i>India</i>		in the low income Segments 3. Consumer finance emerged as high growth area Increased policy Regulation Increasing Commercialization
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Source: Report on "Status of Microfinance sector 2010"

This overriding shift brought about changes in institutions' legal forms, capital structures, sources of funds, growth strategies and strategic alliances. Microfinance in India, as elsewhere, originally began as part of a developmental and poverty-reduction project, led by NGOs who thought this would be an effective way of allowing the poor to lift themselves out of poverty by their own efforts. Many NGOs began the process of group lending based on self-help groups (SHGs) and the linkage with commercial banks (whereby banks were allowed to lend to groups with a proven track record of repayment) further enlarged its scope.

Table1. Microfinance penetration by country (and region) in 2008

Global Ranking	Country	Population
1.	Bangladesh	25%
2.	Andhra Pradesh State (India)	17%
3.	Bosnia and Herzegovina	15%
4.	Mongolia	15%
5.	Cambodia	13%
6.	Nicaragua	11%
7.	Srilanka	10%
8.	Montenegro	10%
9.	Vietnam	10%
10.	Peru	10%
11.	Armenia	9%
12.	Bolivia	9%
13.	Thailand	8%
14.	India	7%
15.	Paraguay	6%
16.	El Salvador	6%
17.	Burkina Faso	5%



18.	Kyrgystan	5%
19.	Ecuador	5%
20.	Guatemala	5%
21.	Mexico	5%
22.	Colombia	5%
23.	Morocco	4%

Sources: Gonzalez, 2010. Rozas and Sinha, 2010

SHGs and their federations became the intermediaries between individual clients (who were mostly women) and the commercial banking system through the SHG–Bank Linkage Programme (SBLP). The basic methodology being used in commercial microfinance in India was broadly along the lines innovated by Grameen Bank and later adapted by several players. These involved three steps: (i) identifying potential customers, typically on the basis of some measure of poverty, which also ensured significant homogeneity among customers; (ii) organising them into groups (SHGs) that effectively dealt with the problems of information asymmetry described earlier; and (iii) offering standardised products based on standardised operating systems, with strict enforcement of discipline.

RECENT DEVELOPMENTS IN INDIA

The Government of India will setup Micro Units Development and Refinance Agency (MUDRA) Bank with a capital of Rs 20,000 crore which would regulate and refinance all microfinance institutions. The government proposes to set up MUDRA Bank through a statutory enactment. This Bank would be responsible for regulating and refinancing all Microfinance Institutions (MFI) which are in the business of lending to micro/small business entities engaged in manufacturing, trading and services activities, The Bank would partner with state level/regional level coordinators to provide finance to Last Mile Financer of small/micro business enterprises. The MUDRA Bank would primarily be responsible for laying down policy guidelines for micro/small enterprise financing business, registration of MFI entities, regulation of MFI entities, accreditation /rating of MFI entities, laying down responsible financing practices to ward off indebtedness and ensure proper client protection principles and methods of recovery. It would also be responsible for development of standardised set of covenants governing last mile lending to micro/small enterprises, promoting right technology solutions for the last mile, formulating and running a Credit Guarantee scheme for providing guarantees to the loans which are being extended to micro enterprises and creating a good architecture of Last Mile Credit Delivery to micro businesses under the scheme of Pradhan Mantri Mudra Yojana, A sum of Rs 20,000 crore would be allocated to the MUDRA Bank from the money available from shortfalls of priority sector lending for creating a refinance fund to provide refinance to the last mile financiers. Another Rs 3,000 crore



would be provided to the MUDRA Bank from the budget to create a Credit Guarantee corpus for guaranteeing loans being provided to the micro enterprises. The no of people microfinance borrowers have been reduced in the wake of the Andhra Pradesh (AP) microfinance crisis of 2009-10, triggered by a series of borrower suicides, allegedly on account of unscrupulous MFI (microfinance institutions)

TABLE 2. NUMBER OF PEOPLE SERVED BY MICROCREDIT

	Minimum number of MFIs Reporting	Customers Serves (millions)	Number of poorest in first loan(millions)	Number of women among the poorest(millions)	Percentage of women among the poorest
31 December 2003	2,931	81	55	45	82.5
31 December 2009	3,589	190	128	105	81.7
31 December 2010	3,652	205	138	113	81.9
31 December 2011	3,703	195	124		

Source: State of the Microcredit Summit Campaign Report 2004, 2011, and 2012 (Daley-Harris 2004, 2011; Maes and Reed 2012; Reed 2013).

TABLE 3. NUMBER OF ACTIVE BORROWERS OF MICROCREDIT

Number of Microcredit Institutions Actives Borrowers(millions)		
Regions		
Sub-Saharan Africa	1,009	12.7
Asia and the Pacific	1,746	129.1
Latin America and the Caribbean	647	13.8
Middle East and North Africa	91	4.3
Eastern Europe and Central Asia	73	5.2
North America and Western Europe	86	0.2

Source: State of the Microcredit Summit Report 2012(Maes and Reed 2012) Astha et al



Practices of charging high interest rates and excessive lending, leading to increased indebtedness among poor borrowers, and turning to coercion to recover those loans. The industry itself took some hard knocks. Asset under management (outstanding loans or gross loan portfolio) fell Rs 3,000 crore to close at Rs 20,500 crore in 2011-12. MFIs that had large-scale operations in AP suffered the most. Non-repayment of loans by borrowers (at the behest of politicians and other community leaders) resulted in AP portfolios of most MFIs declining by 35%. The AP State Government Ordinance imposed stringent operating guidelines mainly tightening screws around lending rates and collection mechanisms employed by MFIs till then. Meanwhile, the RBI was waiting for the 'Malegam Committee Report on Microfinance' before listing out its own set of guidelines.

The regulator turned in its first set of regulations in 2011 deeming for-profit MFIs as NBFC-MFIs (a new category of nonbanking finance companies). It also directed all MFIs to maintain sufficient 'net owned funds' and structure portfolios with 85% of lending to "qualifying assets." In subsequent amendments, the regulator put in place lending limits per borrower, capped interest rates, employed measures to reduce excessive indebtedness, explicitly stated tenure of loans and worked out loan repayment schedules. These moves seemed like a bitter pill then, but were the ideal remedy for the industry's ills. "Prior to the AP crisis, there were no rules governing microfinance industry. Micro loans are set to become cheaper with SKS Microfinance, the listed lender to poor individuals, taking the lead among small lenders to cut lending rates. SKS, which caters to about 50 lakh small borrowers and has Rs 6,177 crore of outstanding loans at the end of December last, is the only MFI to lend at sub-20% rate of 19.75%. With borrowing cost set to fall, other MFIs are expected to lower lending rates by 25-50 basis points in the next three to six months. Bank loans are becoming cheaper as they moved to marginal cost-based pricing. MFIs rely on bank loans for on-lending MFIs' outstanding borrowings now stands at Rs 36,439 crore, representing an 86% growth, according to Microfinance Institutions Network (MFIN). In the third quarter of 2015-16, micro lenders received a total of Rs 9,121 crore debt funding from banks as well as other financial institutions. MFI loans grew 84% in the third quarter to Rs 42,331 crore, MFIN said.

The number of beneficiaries grew by a third to 2.88 crore with an average loan size rising to Rs 17,917 at the end of December from Rs 14,409 a year ago. Microfinance player Ujjivan Financial Services opened its Rs 885-crore initial public float on April 28 and has fixed the price band at Rs 207-210 per share. Ujjivan, which will become the second microlender to go public, is a recipient of an in-principal approval to set up a small finance bank. The IPO, involves fresh issuance of shares worth Rs 358 crore by the company and a Rs 527-crore offer-for-sale by its overseas investors who are exiting or paring their stakes in the company. The company has raised Rs 292 crore through a pre-IPO placement.



MICROFINANCE HAS BEEN A HUGE DISAPPOINTMENT AROUND THE WORLD

World leaders cheered in unison, overjoyed at the discovery of a market-based mechanism for eradicating poverty. Thousands of NGOs took up micro-lending to poor communities with billions of dollars in development aid flowing through them. The microfinance revolution had well and truly arrived. The UN declared 2005 as the year of microfinance and next year a Nobel Peace Prize was awarded to Yunus and Grameen Bank for “efforts to create economic and social development from below.” Within five years, however, the gloss has started to come off. Long-standing claims of poverty alleviation and female empowerment came to be challenged. Reports of usurious interest rates being charged to desperate borrowers came to light amidst mounting criticism of the high-handed tactics employed by loan officers to collect monthly installments. Collective defaults by entire villages were reported around the world. Most disturbingly, in the Indian state of Andhra Pradesh, a hotbed of microfinance lending, dozens of suicides occurred among borrowers under pressure from large micro-lenders, forcing the state to clamp down on the exorbitant interest rates. Microfinance has been found to have had zero impact on poverty alleviation. While it still has a big presence in the developing world, and undoubtedly helps some entrepreneurs find their feet, the hopes and aspirations that it once aroused are no more. Yes, many grassroots organisations are doing a world of good through embedding themselves deeply within the communities they hope to serve. But the myth surrounding the minimalist model of microfinance favoured by international agencies and private investors, which involves only lending at the “true cost of capital” with no other “intervention” has exploded rather spectacularly.

CONCLUSION

Micro-credit could indeed provide a lifeline for desperate borrowers, if it operated at a small scale and with subsidized interest rates. To some borrowers it could provide a crutch even at relatively high interest rates, saving them from the clutches of moneylenders. But given the huge increases in living costs and the reduced role of governments, especially with respect to healthcare and education, micro credit was never going to be able to stem the tide of poverty. Healthcare is perhaps the number one route to bankruptcy among the poor in many developing countries and education takes an everincreasing proportion of their income. Painting all the women in the world as heroic entrepreneurs doesn't actually make them so. They are heroic all right, given the struggle they lead against brutal poverty – but entrepreneurial ventures have always had a high mortality rate. And there aren't that many which can deliver the kind of returns one requires to be able to pay back interest rates in excess of 40%. Given that much of the loaned money is actually used for consumption, the chances of getting into debt are always high. Realising that poverty alleviation was an unsustainable and unachievable goal, the micro-credit industry shifted the goal posts. “Financial inclusion” was the new aspiration, which in practice meant access to credit, insurance and other financial products. The term micro-credit became microfinance and poverty alleviation quietly moved out of the spotlight. The fact that most borrowers were using the loans for consumption rather than production was not taken as a failure



to achieve the original goal either. Instead, this “consumption smoothing” was celebrated as another achievement. Microfinance then had two different realities. One was the global celebration of this market-based model for poverty alleviation. The other was the cruel reality of many borrowers caught up in debt cycles and struggling against an oppressive neoliberal world order where the proportion of incomes spent on health, education and food kept going up. Either way, it presented an opportunity for investors to “do well by doing good”. Once development agencies and multilateral institutions had paved the way, global investors piled in. Sitting far away in New York and other capitals of the financial world, they were attracted by the tales woven by microfinance providers looking to tap into global equity markets, tales of helping the poor and making a buck at the same time. With international capital, however, came unprecedented pressure for growth and quarterly profits. Those providers who tapped into the equity markets responded by seeking out more borrowers, and then when defaults loomed they tightened the screws to keep things on track. They devised elaborate public shaming rituals and used these ruthlessly to destroy borrowers’ social capital. Even Yunus disapproved, accusing them of making profits off the back of the poorest, neediest members of society. If the minimalist model, fuelled by global capital, survives today it is thanks primarily to desperate poverty that engulfs the world and to bigger loans that target the not-so-poor. Growing polarisation of society that raises the cost of living for the poor, along with wholesale privatisation of social welfare institutions, is putting increasing pressure on the poor. At best, minimalist microfinance provides a bandage where a major operation is needed, and at worst, it deepens the wounds. Socially embedded microfinance institutions that organise entrepreneurs, provide them with training and then deploy them in larger ventures are much more effective though high cost propositions. Interest-free microfinance, based on charity, similarly offers much greater relief. Ultimately, however, both are largely helpless in face of the neoliberal onslaught.

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