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An In-Depth Analysis of the Key Drivers and Influences of the Microfinance Institutions

Teesha Ahuja

Bharati College, University of Delhi

ABSTRACT

Microfinance development is crucial to financially disadvantaged individuals' upward mobility. Their contribution to enhancing financial inclusion demonstrates this, particularly in semi-urban and rural areas. Microfinance players have been working hard to balance social and commercial responsibilities. Customers of financial institutions and regulators are key stakeholders in this process. This article focuses on various aspects of the expansion of microfinance institutions in India that provide a wide range of services and have; as a result, significantly altered the lives of economically disadvantaged individuals and reduced the volatility of their income sources.

INTRODUCTION

Microfinance provides financial services to low-income clients, such as consumers and self-employed individuals, who traditionally need access to banking and other services related to banking. In a broader sense, the goal of this movement is "a world in which as many poor and near-poor households as possible have permanent access to an appropriate range of high-quality financial services, including not just credit but also savings, insurance, and fund transfers." Most people who advocate for microfinance think that having access to it will help the poor get out of poverty. Microcredit emphasizes providing credit services to customers with low incomes, typically in the form of small loans for micro businesses and activities that generate income. The term "microcredit" is frequently associated with low savings for the poor. Most of the time, "microcredit" schemes provide savings services by simply collecting mandatory deposit amounts only intended to serve as collateral for loans. Although the clients have restricted access to their enforced savings, additional voluntary savings may accumulate. The primary source of capital for financial institutions is now these savings. Microfinance is a one-of-a-kind economic development tool developed to evaluate low-income groups aiming to work their way out of poverty. As reported by India Today, a significant policy shift toward financial inclusion is underway. To provide financial services to underbanked and unbanked segments of the Indian population, microfinance has taken centre stage. Because of this, microfinance institutions make a better alternative to banks.

Problem Statement

Poverty is a defining feature of the Indian economy. Numerous programs to reduce poverty are run by the federal and state governments. Over the past few decades, the industry has grown steadily. In the early 1980s, India's microfinance institutions began as an informal self-help groups to gain access to crucial Savings and Credit services. Since then, the industry has grown to include many business models. The sustainable growth of a microfinance institution over time in terms of outreach and gross loan portfolio is one way to measure the achievement of financial inclusion goals.

CHANNELS OF MICROFINANCE

In India, microfinance operates through two channels:

1) Self-help group Linkage Programme (SBLP): This channel was started by NABARD in 1992. This model encourages women to form a group of 10 to 15 people. All women from economically disadvantaged backgrounds contribute by regularly donating their savings to the group. After that, group members receive loans through their contributions. Later on, self-help groups also offer loans for income-generating activities. In the past year, the Self

Help Group has had a lot of success and gained popularity for its contribution to women's empowerment. When these Self-Help Groups achieve stability, it has been observed that they operate almost entirely on their own with little assistance from NABARD, SIDBI, or other non-governmental organizations.

2) Microfinance Institutions (MFIs): These are financial institutions whose primary business is microfinance. They lend money using a joint liability group (JLG), i.e., an informal group of five to ten people who apply for loans together or individually.

A. The Contribution of Indian Microfinance Institutions to Financial Inclusion

Since its inception, microfinance has played a pivotal role in financial inclusion in India. It was established specifically to serve the population's smallest and most underserved segments. In layperson's terms, microcredit is a small loan given to rural self-employed people to help them live better and improve their conditions.

The basic goal of microcredit is to give people in rural areas willing to get out of poverty access to financial resources. Vendors of vegetables, artisans, farmers, rickshaw drivers, fishermen, and others are the most common occupations of those seeking microcredit. Microfinance Institutions (MFIs) have been one of the fastest-growing segments in recent years in reaching out to small borrowers, demonstrating the need for credit.

In 1992, the National Bank for Agriculture and Rural Development (NABARD) launched the Self-Help Group-Bank Linkage model in India to connect the unorganized sector to the formal banking sector. In 2019, this industry reached over 25% penetration in the total addressable market after two decades of development.

A "Committee on Financial Inclusion" headed by Dr C. Rangarajan, Chairman of the Economic Advisory Council to the Prime Minister, was established by the Indian government in 2006. They broadly defined financial inclusion as the process of ensuring that vulnerable groups, such as the poor and those with lower incomes, have access to affordable financial services and timely access to adequate credit when needed. This definition includes universal access to affordable insurance, risk management products, and banking services.

Dr C. Rangarajan identifies the following six methods for promoting financial inclusion:

1) Credit to marginal and sub-marginal farmers as well as other small borrowers

2) Going beyond credit and assisting rural areas

3) Commercial banks to open for granting loans to small branches in rural areas

4) Simplification of procedure Commercial banks to open for granting loans to small branches in rural areas borrowers

5) Strengthening the SHG-Bank business facilitator and Linkage program

6) Effective implementation of Strengthening the SHG-Bank business facilitator and Linkage program correspondent models

The regulators play an important role in driving responsible, inclusive formal credit while striking a balance between providing growth, managing risks, and not overburdening borrowers with debt. Microfinance contributes to all of these approaches and slowly but successfully accelerates financial inclusion.

Microfinance Institutional Network (MFIN) was recognized by the Reserve Bank of India (RBI), and Sa-Dhan was one of two Self-Regulatory Organizations (SROs) established to assist the microfinance industry. These member MFIs include an increase in SROs and the regulator working together to address some of the issues microfinance lenders face and provide prompt solutions based on feedback from NBFC-MFI members. The increase in lending caps for MFI borrowers is one recent change that may spur growth for these member MFIs.

Microfinance has been the key to reaching the last man on the ground, bringing millions of families into formalized credit over the past few decades. With the help of the Reserve Bank of India's policy support, the Self-Help Group-

Bank linkage model in India has developed into the hybrid Self-Help Group (SHG) and Joint Liability Group (JLG) models and has begun linking to banks. The core of this model was the shift from a paper-backed guarantee to a social support guarantee from a nearby group. Women account for approximately 99% of microcredit recipients in the nation, and the model social strata guarantee that the group repays the loans.

The microfinance industry has experienced rapid expansion over the past few years, supported by a steady influx of new clients. Over the past five years, the portfolio of microfinance companies has expanded at a CAGR of nearly 48%, reaching INR 26,200 crore. To 1,87,400 Cr INR in FY 19. At a CAGR of 20%, the number of customers increased from 180 million to 440 million in the same period. Various financial institutions, including but not limited to NBFCs, microfinance institutions, and banks, have contributed to this expansion. With a total loan outstanding of INR 68,868 Cr on March 31, 2019, 82 NBFC-MFIs held the largest share of the microcredit portfolio or 36.8% of the total microcredit universe. With an outstanding loan balance of INR 61,046 Cr, banks are the second largest microcredit provider representing 32.6% of the industry's total portfolio. MFIs are lending aggressively in 2016 with relatively low-interest rates. In the past three years, some MFIs' disbursements have increased at a CAGR of nearly 50%. Due to the enormous underlying growth potential, we will continue to observe similar trends in the coming years. This kind of growth has never been seen before.

To gain access to the low-income household market, MFIs in India hold the key. Players need to use differentiators to attract and retain customers in light of the growing prevalence of MFIs. In addition, microfinance lenders have been providing education loans for younger children with longer repayment terms and lower interest rates based on the loan amount to benefit the Community and raise literacy rates.

Corporate social responsibilities are also essential to the economic emancipation of the underprivileged section of society. We have evidence that microfinance lenders spend more than the statutory requirement to provide holistic empowerment to the Community, despite the regulators' mandate that lenders spend approximately 2% of their net profits over the past three years on CSR activities.

The following themes continue to be the focus of the CSR initiatives carried out by leading financial institutions in this sector:

B. The Role of Microfinance Institutions

1) Poverty Reduction Tool:

Better health and sanitation

Empowerment of Women

Social Welfare for the Community

As a key strategy for reducing poverty worldwide, microfinance has been developed as a means of providing those who are excluded from commercial, financial services with access to basic financial services like small credit, savings, insurance, and remittance.

2) Empowerment of Women:

In rural areas, where women suffer the most from illiteracy and social norms, microfinance aids in women's economic and social emancipation. Opportunities and basic amenities are unavailable to them. Through various programs run by the government and non-governmental organizations, microfinance is being promoted as a strategy for reducing poverty and empowering women. SHG bank's Linkage program, for instance.

3) The overall development of the financial system:

Through the integration of financial markets, microfinance can help develop the entire financial system. Small and medium-sized businesses can be at the centre of sustainable rural development at microfinance institutions (MFIs). Rural business growth is positively correlated with their development.

4) Working for oneself:

The poor can use their initiative through financial services, which could speed up generating incomes, assets, and economic security.

5) The SHG-bank program for linking:

Today, the SHG model connects a small group of women to the mainstream system and has the most customers worldwide. There are 15-20 members in the SHG. The group starts by saving money in a shared fund.

Instead of an apex cooperative bank, SHG is a cooperative society linked to a commercial bank. Additional credit delivery services for the unreached poor, mutual trust building between bankers and the poor, encouraging banking activity on both credit and thrift, and maintaining a straightforward formal mechanism of banking with the poor are the goals of the SHG bank linkage program. SHG contributes to the overall empowerment process by combining the formal financial sector's technical and administrative capabilities with the informal credit system's flexibility, sensitivity, and responsiveness. NABARD administers a variety of government of India schemes, including microcredit programs for agriculture and industry, service, and business (ISB). The program provides a total of Rs. 200 crores until December 31, 2003, 191 crores were approved, benefiting over 9 lakh beneficiaries. To obtain SIDBI financing, NGOs and MFIs are required to provide equity support under the program. To overcome the limitations of the current SIDBI program, which has a very limited reach, the office of the development commissioner (Small Scale Industries) within the Ministry of SSI is launching a new Micro Finance Programme. The government can play a crucial role in expanding the scheme's reach, ensuring the long-term viability of NGOs and MFIs, and developing intermediaries for project identification.

The Function of the Indian Government's Microfinance Program:

a) Setting up Fixed Deposits for MFIs and NGOs: Following this plan, the Indian government will provide microcredit to the poor through MFIs and NGOs like SIDBI.

b) Microfinance Program Training and Research: SIDBI would receive assistance from the Indian government to meet the training requirements of NGOs, SHGs, intermediaries, and entrepreneurs, as well as to raise awareness of the program. Establishment of institutions for "intermediaries" in the search for a viable project. In a variety of contexts, the SISIs would assist in the identification of such intermediaries.

c) Funding for the Program in the Tenth Plan: The tenth five-year plan included a budgetary provision, and the next plan anticipates additional funding.

d) Organizational Structure: A committee has been established to control and monitor MFI/NGOs' administrative arrangements.

CONCLUSION

The Indian government has recognized microfinance as a means of reducing economic poverty. India is currently undergoing a significant policy objective shift toward financial inclusion. To provide financial services to the underbanked and unbanked sections of the Indian population, microfinance has taken centre stage. Because of this, microfinance institutions work better as an alternative to banks. They provide not only microcredit but also allied services like savings, insurance, and remittance, as well as non-financial ones like training, individual counselling, and accessible support for activities that generate income.

Microfinance contributes to the healthy development of individual clients as well as the market and assists in promoting overall economic growth and development due to its proven access to credit and its effective provision in assisting the poor in meeting their needs, better managing their risk, gradually building their assets, developing microenterprises, and enhancing income-generating activities.

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