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A STUDY ON MICROFINANCE AS A POTENT TOOL TO COMBAT POVERTY IN RURAL INDIA

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Abstract:

Microfinance initiatives are widely acknowledged globally as an efficient means of reducing poverty and enhancing the socio-economic conditions of rural populations. In India, microfinance is also gaining momentum in its endeavor to alleviate poverty and empower women in rural areas. The need for microfinance emerges due to financial resources in rural India for poverty reduction and the acquisition of agricultural and farming inputs. Microfinance is a scheme designed to assist impoverished rural individuals in repaying their debts and preserving their social and economic standing within their communities. Given that India's economy relies heavily on agriculture, microfinance may serve as a means "to empower farmers and rural populations to make agriculture more lucrative. This research paper presents a developing perspective on rural India as a market segment for microfinance institutions."

Keywords: Market, Micro-finance, Poverty, Rural finance, Socio-economic conditions

Introduction:

Microfinance is a widely used phrase across several fields to combat poverty. Microfinance is a well-established idea. It originated in "the 19th century when moneylenders were unofficially fulfilling the function established financial organizations currently carry out. The informal financial institutions include village banks, co-operative credit unions, state-owned banks, and social venture capital funds, all of which aim to assist the impoverished."[1] These banks are dedicated to providing financial services, such as savings and lending, specifically tailored "for small and medium-sized firms." They facilitate the mobilization of savings from rural areas, using a plain and uncomplicated technique that stems from local customs and is readily understandable to the public. "These funds provide financial support to small and medium-sized enterprises (SMEs) in the informal sector of developing nations. It is well-established that these SMEs have a higher likelihood of experiencing failure."[2]

Establishing small and medium-sized enterprises (SMEs) leads to job creation. However, these businesses have a limited lifespan and are likely to cease operations within a short period. As a result, individuals who have obtained work in these enterprises may lose their jobs and experience a decline in their financial status. Financial institutions refrain from extending credit to these individuals due to their failure to meet the necessary criteria for loan approval or access to

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banking services. The absence of economic leverage is a significant determinant of most social issues. These issues derive from poverty, which is recognized to result in several adverse outcomes such as inadequate healthcare, education, and nutrition and disproving the effectiveness of microfinance. Their focus is on impoverished individuals considered high-risk, although the repayment rate proves to be favorable compared to traditional commercial banks.[3]

Review of Literature:

Microfinance has been examined from several perspectives by researchers. "Microfinance empowers individuals by providing them with access to financial resources, enabling them to level the playing field and control their destinies." Singh, S (2010)[4] states that it enhances people's living situations by expanding their perspectives and fulfilling economic and social functions. Roy, A. (2010)[5] stated that the UN Millennium objective of reducing poverty by 2015 remains elusive despite the significant efforts made by microfinance institutions to help in this area. Bateman, M. (2010)[6] stated that the primary obstacle for those living in poverty is acquiring financial resources to enhance their capacity to generate revenue.

"Objectives of the Study:"

1. "To assess the expansion of the microfinance industry in India and evaluate the opportunities available to microfinance institutions, non-governmental organizations (NGOs), and self-help groups (SHGs) in the market.
2. To evaluate the savings of Self-Help Groups with Banks.
3. To evaluate the allocation of bank loans to self-help groups (SHGs) in the rural market.
4. To assess the amount of unpaid bank loans held by Self-Help Groups (SHGs) in rural areas."

"Research Methodology:"

"Data Collection:"

This research study provides a comprehensive analysis that relies on secondary data. The data has been gathered from books, numerous websites, and current research articles published on "different websites" and periodicals.

Research Tool:

"Percent Growth Rate:"

"A percent growth rate, also known as percent change, growth rate, or rate of change," is a valuable statistic for assessing the extent to which "a population, product, or instrument" is experiencing growth or decline in a specific region or year. "The rate of change," often known as the percent change or growth rate, is determined by the following formula: The formula for calculating percent change is as follows: "Percent Change = (final value - initial value) / initial value * 100"

Profile of Rural India

Micro-finance assists socioeconomically marginalized sectors of society in increasing their income levels, making it the second biggest in terms "of population, behind China. India's GDP is ranked among the top 15 economies globally." Approximately 300 million individuals, or roughly 80 million families, live below the poverty threshold, defined as earning "less than $2 per day," as reported by "the World Bank." The most needy individuals make a mere $1 per day. Additionally, it is projected that only around 20% of these families can get loans from the official sector. Among "these 80 million households, 80% get loans from informal sources like local landlords and chit funds." Around 80 million families fall under Microfinance Institutions (MFIs), which include various entities such as "non-governmental organizations (NGOs), credit unions, non-banking financial intermediaries, & a small number of commercial banks."[7]

- There are 50 million individuals living below the poverty line.
- Ninety-five percent of the population needs access to microfinance.
- 56% of individuals continue to get loans from informal sources.
- Seventy percent of individuals do not own any deposit account.
- 87% need access to credit via official channels.
- The annual credit demand amounts to around Rs. 70,000 crores.
- Ninety-five percent of families lack insurance coverage.
- Informal microfinance has been a long-standing practice.

Historically, the primary sources of credit were individuals engaged in money lending, such as affluent farmers, merchants, or community members whose customary profession included lending money. Following government involvement, "RRBs and NABARD were established to provide refinancing for all rural credit and developmental funds." Despite the government's intervention and the development of financial institutions, several forms of loan providers continue to flourish in rural areas. While banks, co-operative organizations, "and government institutions serve as the primary sources of credit in rural areas, private moneylenders still play a significant role as loan providers."

Rural India and Microfinance:

The significance of micro-funding has increased. To thrive in India, the agribusiness sector must empower farmers by ensuring that agriculture is viable rather than exploiting them for a specific agenda. It is crucial to provide financial support to farmers for their essential and modest requirements. "The use of microfinance is anticipated to have a substantial impact on the reduction of poverty and the advancement of development."[8] Hence, it is essential to exchange experiences and resources, which will facilitate the comprehension of achievements and setbacks and provide expertise and principles to enhance and broaden microfinance initiatives. The ultimate objective is to achieve economic and social empowerment. The success of intervention relies on the meticulous handling of each stage and the implementing organizations' abilities to attain the ultimate objective. For instance, if credit delivery occurs without consolidating self-help groups (SHGs), it may encounter issues regarding self-sustainability and recovery. Several initiatives by banks and federal "and state governments provide direct loans to people without requiring them to join Self-Help Groups (SHGs)." The communication items in the directory are compiled and classified according to this development method.

"The Constructive Role of NABARD:"

"National Bank for Rural & Agricultural Development (Nabard) actively facilitates effective coordination between the States and the institutions engaged in rural development to achieve seamless and outcome-driven outcomes. Nabard employs a targeted and distinct strategy for each State to identify the discrepancies, shortcomings, and issues in advancing agricultural and rural industries." [9] It then offers the necessary coordination, assistance, advice, and motivation to the relevant authorities engaged in these sectors.

The organization has a robust presence in business and infrastructure and has shown unwavering dedication to serving the populace. Commercial banks should progressively be replaced by regional rural banks (whenever possible), robust co-operative banks, local area banks, and microfinance organizations.[10]

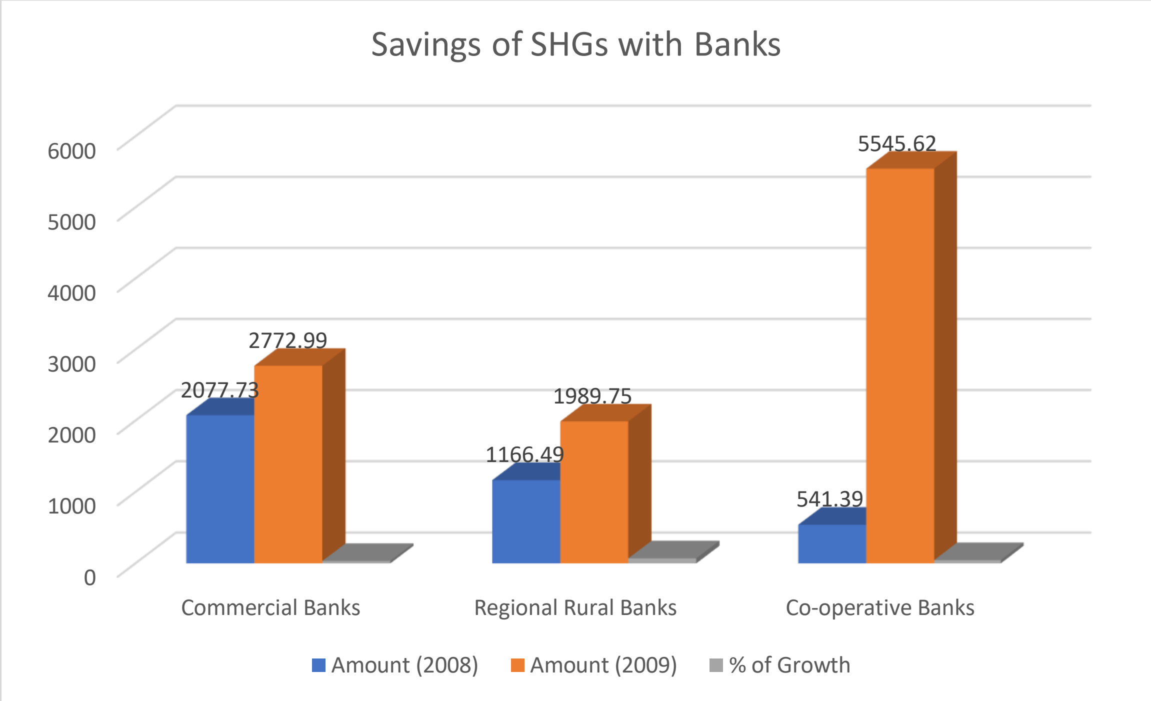
"The State Government and NABARD must collaborate to transform the rural landscape by implementing incentives and rewards" to encourage continued involvement in agricultural and rural activities for those who offer credit and those who borrow. Using information technology, in conjunction with implementing the planned Unique Identity Card, can significantly enhance the efficiency of credit distribution and facilitate financial inclusion.

"Data Analysis & Interpretation"

"Table-1: Savings of Self-Help Groups with Banks (Rs in crores)"

"Agency	Amount (2008)	Amount (2009)	% of growth
Commercial Banks	2077.73	2772.99	33.5
Regional Rural Banks	1166.49	1989.75	70.6
Co-operative Banks	541.17	782.88	44.7
Total	3785.39	5545.62	46.5"

"Source: Status of Micro Finance in India 2008 -09 (NABARD)"

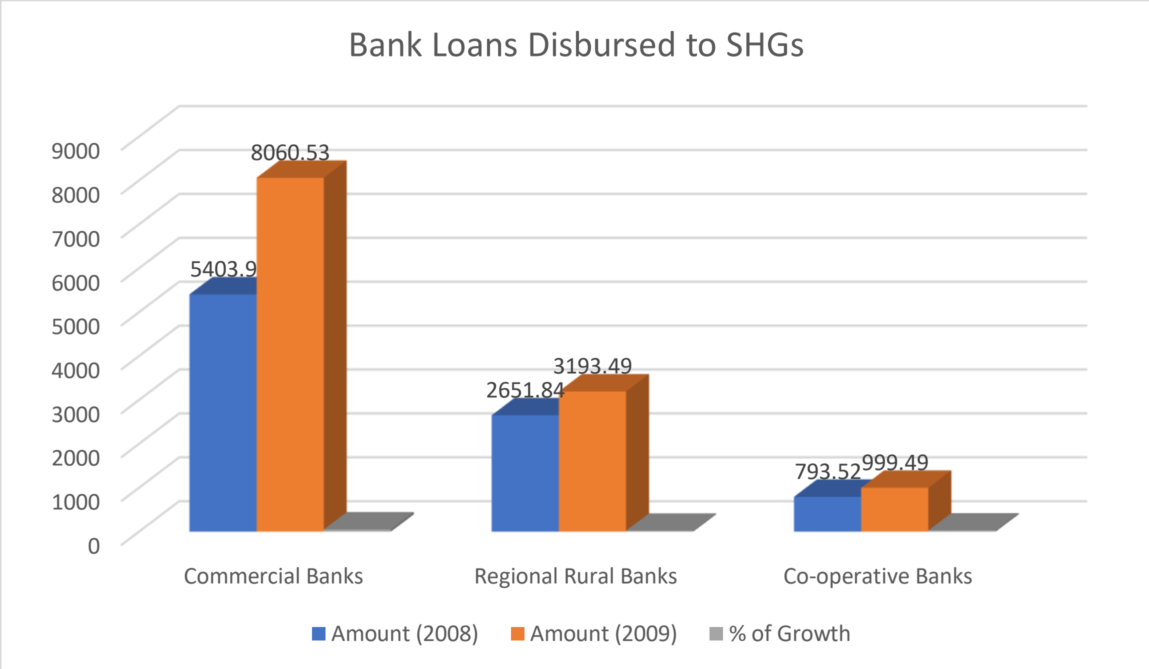


According to the table, "the savings of Self-Help Groups (SHGs)" with all banks grew by 46.5% as of March 31, 2009. The percentage ranges from a maximum "of 70.6% with Regional Rural Banks to a minimum of 33.5% with commercial banks."

"Table-2: Bank Loan Disbursed to SHG (Rs in crore)"

"Agency	Amount (2008)	Amount (2009)	% of growth
Commercial Banks	5403.90	8060.53	49.2
Regional Rural Banks	2651.84	3193.49	20.4
Co-operative Banks	793.52	999.49	26.0
Total	8849.26	12253.51	38.5"

"Source: Status of Micro Finance in India 2008 -09 (NABARD)"



According to the data, commercial banks were the primary lenders to SHGs in 2008-2009, accounting for 49.2% of the loans. "Co-operative banks followed with a share of 26%, while Regional Rural Banks had a stake of 20.4%."

"Table-3: Bank Loan Outstanding Against SHGs (Rs in crore)"

"Agency	Amount (2008)	Amount (2009)	% of growth
Commercial Banks	11475.47	16149.43	40.7
Regional Rural Banks	4421.04	5224.42	18.2
Co-operative Banks	1103.39	1306.00	18.4
Total	16999.90	22679.85	33.4"

"Source: Status of Micro Finance in India 2008 -09 (NABARD)"

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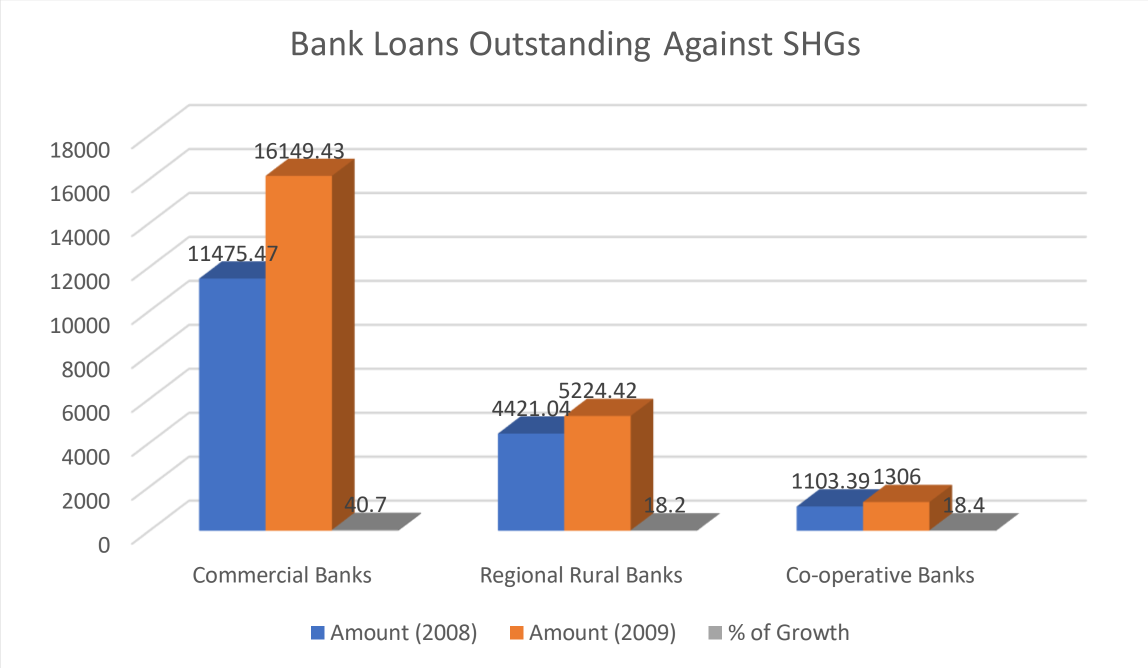

Based on the provided figure, it is evident that commercial banks had the largest portion of outstanding bank loans to SHGs, accounting for 40.7% of the total. Co-operative banks followed with a share of 18.4%, while Regional Rural Banks held a part of 18.2%.

Crucial factors that influence the success of microfinance in rural India:

Recent evidence from the last decade shows that offering financial services to small business owners and producers has been effective in helping impoverished individuals. By providing them with accessible and prompt financial services at competitive interest rates, these individuals can "repay their loans and use the funds to enhance their income and assets." This is unsurprising since their only viable option is to seek loans from the informal market, where the interest rates are far higher than those in the legal market. Microfinance is a very successful strategy for alleviating poverty, as demonstrated by the success of community banks, NGOs, grassroots savings, and credit organizations worldwide. These organizations have proved that "microenterprise loans can be lucrative for borrowers and lenders."

A. For non-governmental organizations (NGOs)

The field of development undergoes continual expansion and adjustments in focus. NGOs are often more inclined to embrace new ideas, mainly when the necessary resources are few, the process of becoming involved is uncomplicated, the jobs are viewed as straightforward, and there is a high level of acceptability from the public. These are all qualities associated with microfinance, whether actual or assumed.

Canvassing by multiple entities, such as “the National Bank for Agriculture and Rural Development (NABARD), Small Industries Development Bank of India (SIDBI), Friends of Women’s World Banking (FWWB), Rashtriya Mahila Kosh (RMK), Council for Advancement of People’s Action and Rural Technologies (CAPART), Rashtriya Gramin Vikas Nidhi (RGVN),” “various donor-funded programs, particularly by the International Fund for Agricultural Development (IFAD), United Nations Development Programme (UNDP), World Bank, and Department for International Development, UK (DFID), and more recently commercial banks, has significantly contributed to the generation of innovative ideas.” As a result of the global attention on microfinance, donor non-governmental organizations (NGOs) have also begun providing financial support for microfinance initiatives. It might be referred to as the supply push.[11]

Microfinance stands out among initiatives, such as Khadi spinning, Nadep compost, and Balwadis, in terms of its ability to generate tangible outcomes and long-term engagement among its beneficiaries. Most microfinance initiatives undertaken by non-governmental organizations (NGOs) primarily target impoverished women. These women greatly benefit from the availability of modest loans, which they may use to address urgent financial needs. Hence, the rapid and substantial “customer satisfaction” is the unique selling proposition (USP) that has enticed non-governmental organizations (NGOs) to engage in this business.

B. For Financial Institutions & banks

The lending agencies have been drawn to microfinance due to its sustainability and minimal operational expenses. Institutions such as SIDBI and NABARD are pragmatic financial institutions that would only consider a proposal if they see a long-term commitment, which is only possible via sustainability, i.e., economic viability. From the supply perspective, it is evident that this entity has all the characteristics of a commercial venture. Its production is visible and can be readily comprehended by the majority. This also seems favourable to the government, which, after liberalization, is endeavouring to justify the rationale behind every penny spent. Microfinance has garnered significant attention from mainstream organizations, surpassing other socio-economic projects. The primary catalyst that prompted banks to become engaged in “the policy push. Since most of our banks are under public ownership, public policy influences their actions and decisions.” In this instance, NABARD diligently adhered to the established guidelines and carried out promotional activities, although indirectly. A seven-page memorandum issued by NABARD initially implemented the policy change made by RBI roughly ten years ago, which permitted banks to provide loans to Self-Help Groups (SHGs). This policy shift was subsequently reinforced via nationwide awareness and training initiatives for bank personnel.[12] NGOs performed several programs, totalling several hundred, with each session engaging 15 to 20 bank workers. NABARD covered all expenses for these programs. The NABARD refinancing plan enhances the policy push by providing more advantageous conditions (such as 100% refinance and more extensive spread) compared to other rural lending options banks offer. NABARD has recently undertaken system configuration tasks, and banks have also been assigned goals. NABARD's canvassing, training, refinancing, and diligent follow-up have led to extensive participation of banks.

Findings:

1. There is a significant disparity between the demand and supply of financial services, and most impoverished individuals cannot access these "services" [Source: Status of Micro Finance in India 2008-09 (NABARD)].
2. Self-Help Groups "(SHGs) savings significantly grew by 46.5% from 2008 to 2009. The rise in bank deposits reflects shifting patterns in rural savings," with farmers aiming to maintain liquidity in their holdings.
3. Rural residents often favor Regional Rural Banks as a secure location for depositing their savings. It has garnered around 70.6% of savings from Self-Help Groups (SHGs). Rural consumers have seen increased liquidity in recent years due to the investment shift towards formal financial institutions.
4. From 2008 to 2009, commercial banks were the primary lenders to Self-Help Groups (SHGs), accounting for 49.2% of loan disbursements. "Co-operative banks followed with a share of 26%, while Regional Rural Banks had a stake of 20.4%."
5. Bankers see financing individuals with low socio-economic status as dangerous due to their lack of "creditworthiness."
6. "Commercial banks held the most significant portion of outstanding bank loans to Self Help Groups (SHGs)," accounting for 40.7%. They were followed by co-operative banks, which accounted for 18.4% of the loans, and regional rural banks, which accounted for 18.2%. The outstanding bank loan to Self-Help Groups (SHGs) is the elevated transaction expenses, as stated in the report "Status of Micro Finance in India 2008-09" by NABARD.

Conclusion:

India has a significant potential for the expansion of microfinance organizations. The central cross-section might be advantageous if this industry experiences rapid growth. Financial institutions must educate communities on the simplicity of lending processes and the availability of loans at favourable interest rates. The repayment period must be tailored to accommodate the cyclical nature of rural income, such as "the availability of funds after the harvest season. Nationalized banks have hesitated to provide loans to self-help groups (SHGs) due to their perceived lack of trustworthiness." However, these banks have extensive access to SHGs, presenting a promising economic opportunity they should actively pursue.

Similarly, nationalized banks may engage the many Self-Help Groups (SHGs) to promote regular monthly savings among their members. NABARD is dedicated to fostering comprehensive development in rural India. NABARD offers comprehensive support to rural India and has established itself as an organization that embodies "Growth with Social Justice."

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