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MICROFINANCE – A WAY OUT FOR POOR

Introduction

Microfinance is a very popular term in today's financial market scenario. As the name suggests, Microfinance refers to the microcredit or micro- loan. Microfinance refers to banking or financial services offered by banks or other financial institutions to the low income or under privileged section of the society. Microfinance can be in the form of loans, insurance and savings deposits.

What is Microfinance?

Microfinance refers to financial services – most commonly loans, savings, and insurance – delivered in small denominations to poor clients who lack the collateral, credit history, or other assets to enter the formal financial system. The MFI industry has long viewed its primary role as delivering loans to poor clients. If clients are able to pay back their loans and take out new ones, they must be getting economic and social benefits from them. Indeed, MFIs routinely report repayment rates of over 95 percent. And today, there are 100 million people receiving microcredit loans from more than 3,000 institutions.

Micro Finance is defined as, financial services such as Saving Account, Insurance Fund and credit provided to poor and low income clients so as to help them to raise their income and there by improve their standard of living.

Definition of Micro financing

Micro financing is defined as the process of providing loans, credit, saving and other necessary financial services and products to individuals who are extremely poor to get access to the regular sources of finance such as banks or other financial institutions.

Features

- Microfinance has easy and quick loan application process.
- Loans are given without security.
- The interest rates of microfinance are very low.
- Microfinance is also offered to people below poverty line (BPL) since they do not have access to other form of finance.
- Generally, microfinance institutions approach clients instead of waiting for clients to approach them. They want impoverish people to be aware that there are inexpensive forms of financing.

- Microfinance also intends to assist individuals in securing good medical treatment when they have health issues.
- Some microfinance options come with micro insurance. Micro insurance is offered as helps the borrower in protecting to his own life.
- Microfinance focus on offering financial transparency by offering loans to individual without any hidden costs or charges.
- Microfinance aims at developing financial sustainability among economically downtrodden people.
- Microfinance institution aims to eliminate interest rate ceiling as they believe that these ceiling can restrict poor people from securing finance.

Objectives

- It aims to bring a financial change among the poor people with the help of a community based approach.
- It intends to organise and conduct simple training programmes for unemployed people so that they have some means of livelihood.
- Microfinance also intends to assist disabled people who are economically underprivileged.
- It aims to help them find some source of employment or artistry so that they can fend for themselves.
- Microfinance aims to help women of poor families. Institutions that offer microfinance believe that women are more responsible with money and hence, they have exclusive microfinance loan options specially designed for women borrowers.
- Microfinance intends to bring gender equality by encouraging women to equally take part in household decision making, financial decision making, and also earn money independently by engaging in any form of employment.
- It intends to enhance operations and activities at the grass root level.
- Microfinance lays emphasis on optimum utilisation of local resources available in nearby areas and villages in order to minimise transportation costs for bringing resources, etc.
- Microfinance aims to raise the wages of the underprivileged people so that their lives can be improved at least a little.
- Microfinance aims at attaining socio-economic development at the most basic level of the society.

- It serves as a great instrument to eradicate poverty.

History

The history of micro financing can be traced back as long to the middle of the 1800s 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. But it was at the end of World War II with the Marshall plan the concept had a big impact. The today use of the expression micro financing has its roots in the 1970s. A new wave of microfinance initiatives introduced many new innovations into the sector. Many pioneering enterprises began experimenting with loaning to the underserved people. The main reason why microfinance is dated to the 1970s is that the programs could show that people can be relied on to repay their loans and that it´s possible to provide financial services to poor people through market based enterprises without subsidy. Shore bank was the first microfinance and community development bank founded 1974 in Chicago.

The origins of microfinance in India can be traced back to the early 1970's when the Self Employed Women's Association ("SEWA") of the state of Gujarat formed an urban cooperative bank, called the Shri Mahila SEWA Sahakari Bank, with the objective of providing banking services to poor women employed in the unorganized sector in Ahmadabad City, Gujarat. The microfinance sector went on to evolve in the 1980s around the concept of SHGs, informal bodies that would provide their clients with much-needed savings and credit services. From humble beginnings, the sector has grown significantly over the years to become a multi-billion dollar industry, with bodies such as the Small Industries Development Bank of India and the National Bank for Agriculture and Rural Development devoting significant financial resources to microfinance. Today, the top five private sector MFIs reach more than 20 million clients in nearly every state in India and many Indian MFIs have been recognized as global leaders in the industry. According to recent RBI estimates, there are over 450 million "unbanked people" in India, most of who live in rural areas. The term "unbanked" refers to people who have no access to formal financial services, but rather must rely on either family, or informal providers of finance, such as the village moneylender.

Significance:

- Microfinance allows people to provide better for their families through added level of resilience in the developing world. By allowing entrepreneurs to become more resilient through their own efforts gives them the opportunity to make it through times of economic difficulty.
- It gives easy and quick access to credit. Most banks will not extend loans to someone with any collateral or credit because of the high level of risk. By extending microfinance to these people they have access to small amount of credit which can stop poverty at rapid pace.
- Microfinance serves those who are often overlooked in society. Most users of such microfinance are women. Such microfinance helps these people to take control of their lives.
- It offers better loan repayment rate than traditional banking rates. Therefore microfinance institutions see total repayment rates higher than banks.
- It provides families with an opportunity to provide an education to their children. By receiving microfinance products, there is a lesser threat of going without funding for school and that would mean more opportunities for children to stay at school.
- Microfinance creates the possibility of future investments wherein when basic needs of families are met they can move onto the next level of investing into better means.
- It can create real jobs by letting entrepreneurs in developing countries to be able to create new employment opportunities for others.
- Microloans is an important component of microfinance but it also encourages the prospect of savings by allowing for small improvements and changes in their lives and when enough of these improvements occur then there are better chances of savings.

- Microfinance offers for significant economic gains even if the income levels remain the same as there are higher levels of consumption and consumption smoothing. There is also an immeasurable effect which occurs when women are empowered as they also contribute. As spending occurs these benefits also extend outward to those who may not be participating in the program so that the entire community benefits.

WHO ARE THE CLIENTS OF MICROFINANCE INSTITUTIONS?

Low – income population having their own business, in most of the cases not having the access to other formal financial institutions, are the typical clients of micro - credit institutions. These are usually self – employed entrepreneurs, performing their activities at their household. Their small business is focused on retail stores, street sale, handcraft production, agriculture, animal husbandry or the provision of all sorts of services.

There are trends indicating that the majority of micro – financing beneficiaries is on the edge, above and below the poverty threshold. Financial services, particularly loans, are not always suitable to everyone. They are tailored to persons who have recognized the economic opportunity for generating profits, provided that they have the access to a satisfactory amount of money. Regardless of the way of using the loan, MFI may provide a long - term and stable access to money only if the clients are ready and able to adhere to the repayment schedules.

Most vulnerable households, around 10% of them, including also the poor ones, are not the traditional clients of micro – financing organizations since they do not have a stable cash inflow required for servicing the loan. They need grants or other public funding sources for the improvement of their economic situation. This is also the most efficient form of supporting this category of population, since the majority is not able to timely service the loans.

Supporters of microfinance contend that small loans fuel economic self-sufficiency. They point to the billions of dollars that microfinance institutions (MFIs) such as Grameen Bank, Accion International, and Opportunity International (OI) have given to millions of small-time, impoverished entrepreneurs. They cite research showing that microloans increase household consumption, give women more clout in their communities, encourage the use of contraceptives, and improve the nutrition of young children.

MFIs usually operate in places where it is difficult to conduct research – places that are geographically isolated, politically unstable, technologically backward, and educationally disadvantaged. But the largest barrier to understanding whether microfinance works is that few MFIs have clearly articulated what it would mean for microfinance to work – let alone how it could work, for whom it could work, where it could work, or when it could work.

For most MFIs, that ultimate goal is to alleviate poverty. Many MFIs do not explicitly state this. Instead, they say that their goal is to give poor people access to credit. But their donors, staff, and beneficiaries draw the last two links in the chain of logic: Access to credit will help beneficiaries establish profitable businesses that will, in turn, make them economically self-sufficient. We call these organizations institution-centred MFIs, because their theory of change – often implicit – is that building financial institutions for poor clients will eventually help lift these clients out of poverty. In keeping with this theory of change, institution centred MFIs aim to serve as many clients as possible by offering a few basic, high-quality, low-cost services. They assume that their clients will be able to use these services to improve their businesses and, in turn, their socioeconomic standing. And like banks, they track financial outcomes such as loan repayment rates, loan sizes, and number of clients.

Adopting the practices of commercial banks can allow MFIs to serve more clients and therefore can increase their social impact. But the pressure to instil more financial discipline often shifts organizations' focus away from their original mission. As a result, many firms can recite their portfolio at risk (PAR) percentages to two decimal places, but few have even rough estimates of the percentages of their clients who eventually move out of poverty.

Beyond financial services, most MFIs offer basic loan repayment training. Generally the training is limited to emphasizing the importance of repaying the loan and of applying the loan to the business, rather than spending it on personal needs. Yet clients often face health emergencies and family crises, and also want to spend some of the loan proceeds on education. And so MFIs need to give clients more training in financial literacy and money management so that they can better meet both their business and personal needs. At present, MFIs do very little of this.

Moreover, mastering loan management does not lead to generating profits. Just because clients use a loan to stock more inventories, for example, does not mean that they will be able to sell the goods at a profit. And just because they sell goods at a profit does not mean that they can generate enough profits to support household needs, business reinvestments, and loan repayments – sometimes at interest rates as high as 60 percent per year. Yet that is exactly what most MFIs and clients presume.

To make businesses even more productive, some MFIs have targeted the health and happiness of the clients themselves, offering training in areas such as nutrition, health care, and domestic problem solving. These social services not only help clients profit from their loans, but also aid in the development of human capital – an important contributor to the alleviation of poverty.

To make microfinance work for more people, more often, in more places, MFIs need to think clearly about how their practices will bring about the changes they seek. This may mean making fewer microfinance loans and incurring more costs to support the loans they've already made. The benefit, of course, is the building of sustainable businesses. The challenge is finding ways to provide these additional services efficiently. In our current research, we are designing and testing these client-centred practices. We hope that our results will ultimately lead to the broader application of effective and cost-efficient client-centred microfinance programs.

WHY DO POOR PEOPLE NEED MICROFINANCE?

- The idea of microfinance is to provide extremely poor people with small loans so they can start and operate a business. The borrowers are able to save money and pay back the loan over time. Microfinance helps support financial security because it is not just a donation.
- Through the increased income generated by their businesses as well as the ability to save and obtain loans, microfinance allows poor people to build their assets, for example by acquiring land, constructing or improving their homes and purchasing livestock and poultry.
- The microfinance is an effective tool for reducing poverty in most emerging and developing countries. It enables the poor to engage in self-employment and income-

generating activities, which helps the poor people to become financially independent and better able to break out of poverty.

- Poor people in rural areas often cannot get banking services. Also, banks generally do not provide very small loans because administrative costs are too high. Microfinance provides poor people with a way to build savings and work toward becoming part of a country's official financial system.
- Many organizations provide microcredit mainly for poor women. This is partly because women are often more excluded from financial services and educational opportunities than men. Women usually spend their money in ways that improve their families' nutrition, health and education. Also, studies have shown that women are better than men in repaying their loans on time.
- Microfinance can lead to improved access to clean water and better sanitation whicle also providing better access to health care.
- Microfinance can also help to create new employment opportunities to poor people, which has a beneficial impact on the local economy.
- Microfinance provides poor families with an opportunity to provide an education to their children- Children who are living in poverty are more likely to have missed school days or to not even be enrolled in school at all. This is because the majority of families who live in poverty are working in the agricultural sector. The families need the children to be working and productive so their financial needs can be met. By receiving micro financing products, there is less of a threat of going without funding, and that means more opportunities for children to stay in school.
- It gives poor people access to credit- By extending microfinance opportunities; poor people have access to small amounts of credit, which can then stop poverty at a rapid pace.

MERITS AND DEMERITS OF MICROFINANCE

Merits:

- Accompanying non financial services for the poor.
- Continued access to funding low income clients.

- Fast and easy procedure for the poor to get the loan.
- Helps in women empowerment.
- Promotes entrepreneurship.
- Direct contact with clients, which gives less chances of default.
- It helps in the alleviating the poverty.
- Helps in the creation of demand as a whole.
- Helps in the development of the country.
- Contribute in the prosperity of the nation.
- Product tailored to clients needs.
- It provides a long-term increase in income and consumption of poor families.
- Credit makes it easier to manage shocks like sickness of a wage earner, theft, or natural disasters.
- It provides support to micro enterprises
- It offers a better overall loan repayment rate than traditional banking products.
- It provides families with an opportunity to provide an education to their children.
- It creates the possibility of future investments.
- It is a sustainable process.
- It can create real jobs.
- It encourages people to save.
- It offers significant economic gains even if income levels remain the same.

Demerits:

- To the bank the borrowers are few for the problem of reaching out to the people

- A main disadvantage to micro-finance is that the deal is too small for the lender to devote ample time and money to doing proper due diligence
- As the capital is low the profits are also low.
- Borrowers seldom if ever give lenders the full story on their situation and with a small amount at risk; it does not make sense for lenders to spend a lot of money to check out the story. When lenders get burned, they decide to stop lending and the next round of lending must be done by greenhorns who have no idea what they are getting into.
- To some extent micro lending depends on an ever-increasing number of lenders in order to be successful.
- The inability to reach the poorest of the poor is a problem that plagues most poverty alleviation programs.
- Some criticize that microfinance programs benefit the moderately poor more than the destitute, and thus impact can vary by income group.
- Most microfinance programs target women, which may result in men requiring wife to get loans for them.
- Vicious cycle of debt, microcredit dependency, increased workloads, and domestic violence associated with participation in microfinance programs.
- Low repayment rates in comparison with traditional financial institutions.
- Use of harsh and coercive methods to push for repayment and excessive interest rates.
- Concerns have been raised that the reliance on microfinance programs to aid the poor may result in a reduction of government and charitable assistance.

PRODUCT AND SERVICES OF MICROFINANCE

Microfinance Products:

Product	Purpose	Terms	Interest Rate

Income Generation Loan (IGL)	Income generation, asset development	50 weeks loan paid weekly	12.5% (flat) 24% (effective)
Mid-Term Loan (MTL)	Same as IGL, available at middle (week 25) of IGL	50 weeks loan paid weekly	12.5% (flat) 24% (effective)
Emergency Loan (EL)	All emergencies such as health, funerals, hospitalization	20 weeks loan	0% Interest free
Individual Loan (IL)	Income generation, asset development	1-2 years loan repaid monthly	11% (flat) 23% (effective)

1. The **Income Generating Loan** is used for a variety of activities that generate income for their families. Clients submit a loan application and based on approval receive the loan after one week. Loans are paid in 50 equal, weekly instalments. After completion of a loan cycle, the client can submit a loan application for a future loan. The approach with smaller short-term loan is to avoid long-term economic problems with bigger loans.

2. The **Mid Term Loan** is available to clients after 25 weeks of repaying their IGL loan. A client is eligible for a MTL if the client has not taken the maximum amount of the IGL. The residual amount can be taken as a MTL. The terms and conditions of the MTL are otherwise exactly the same as IGL.

3. The **Emergency Loan** is available to all clients over the course of a fiscal year. The loan is interest free and the amount and repayment terms are agreed upon by the MFI and the client on a case by case basis. The amount is small compared to the income generating products and is only given in times of dire need to meet expenses such as funerals, hospital admissions, prenatal care and other crisis situations.

4. The **Individual Loan** is designed for clients and non clients that have specific needs beyond the group lending model. Loans are given to an individual outside of the group lending process. Amounts are typically higher than that of the income generating loan and repayments are less frequent. Applicants must complete a strict business appraisal process and have both collateral and a guarantor.

In the microfinance sector there are other services expanding as well. The poor need, like all of us, a secure place to save their money and access to insurance for their homes, businesses and health. Microfinance institutions are now innovating new products to help meet these needs, empowering the world's poor to improve their own lives. Products common used in the microfinance sector today is:

1. **Micro savings** – A possibility to save money without any minimum balance. Allows people to retain money for future use or for unexpected costs. In SHGs the members save small amounts of money, as little as a few rupees a month in a group fund. Members may borrow from the group fund for a variety of purposes ranging from household emergencies to school fees. As SHGs prove capable of managing their funds well, they may borrow from a local bank to invest in small business or farm activities. Banks typically lend up to four rupees for every rupee in the group fund.

2. **Micro insurance** – Gives the entrepreneurs the chance to focus more on their core business which drastically reduces the risk affecting their property, health or working possibilities. The is different types of insurance services like life insurance, property insurance, health insurance and disability insurance. The spectrum of services in this sphere is constantly expanded, as schemes and terms of providing insurance services are determined by each company individually.

3. **Micro leasing** – For entrepreneurs or small businesses who can't afford to buy at full cost they can instead lease equipment, agricultural machinery or vehicles. Often no limitations of minimum cost of the leased object.

4. **Money transfer** – A service for transferring money, mainly overseas to family or friends. Money transfers without opening current accounts are performed by a number of commercial banks through international money transfer systems such as Western Union, Money Gram etc. On the surface they may seem like small money transfers, but when one considers that such transactions take place millions of times around the world each week, the numbers start to become impressive. According to the World Bank, the annual global market for remittances – money transferred home from migrant workers – is around 167 billion US dollars. The estimated total is closer to 230 billion dollars if one counts unregulated transactions. Remittances are also an important source of income for many

developing countries including India, China and Mexico, all of which receive over 20 billion dollars each year in remittances from abroad.

MICROFINANCE INSTITUTIONS IN INDIA

Nowadays, it is very easy for anyone to take a small loan to open a business or self-employment. All thanks to Microfinance Institutions. You need not be rich, own assets or pay taxes to avail these small loans: these loans, called microfinance, are specially given for people to rise above the poverty line and earn a decent living.

List of 10 Best Microfinance Institutions in India (March 2018):

1**. State Bank of India**

The topmost state-owned lender, State Bank of India is the country's largest microfinance company in India. It does not operate as an NBFC but is yet is by far the biggest player in the country's microfinance sector.SBI conducts training programs for financial inclusion in rural India, offers microfinance of up to Rs. 50,000 for home building and development for villagers.SBI also provides finances to women's Self Help Groups (SHGs) as part of the country's poverty alleviation drive, funds farm equipment and machinery for small entrepreneurs and a host of other microfinance solutions.

2. **Ujjivan Financial Services Ltd.**

Bangalore-based Ujjivan Financial Services began operating as a Non-Banking Financial Company in 2005 to offer a wide range of financial services targeting the economically active poor population of India.UFS currently operates in 24 states and Union Territories. Its services are available in some a209 districts across India, which makes it the largest MFI in India. The company serves over 2.77 million active customers through its 469 branches and 7,786 employees, states the company website. In February 2017, this MFI set up the Ujjivan Small Finance Bank to offer microfinance and other banking services to economically underprivileged sections of the society.

3. Equitas Small Finance Bank Ltd

Equitas Small Finance Bank Ltd is one of the most popular microfinance institutions which commenced operations on September 5, 2016, from Tamil Nadu. It is a division of Equitas

Holdings- an NBFC operating as Non-Deposit Taking- Systematically Important-Core Investment Company. Equitas SFB offers small loans and microfinance to women who strive for financial empowerment, persons with special needs, youth and others who aspire to open a small business or find ways of self-employment by providing various services. The bank has helped tens of thousands of people come out of poverty.

4. **M&M Financial Services**

Mahindra and Mahindra Financial Services is one of the most reputed MFI in India. It has helped millions of aspiring Indian women and youth to fulfil their dreams of becoming financially self-dependent and stable by offering microfinance. The company offers "personalized finance for a wide range of vehicles, home development requirements and many other diverse endeavors," states its website. M&M Financial Services is a company listed on the BSE. It ranks as the topmost financer for farm tractors in India. The company has served over four million customers in India with microfinance through over 1,200 branches that hire about 20,000 employees.

5. **Sundaram Finance Ltd**

Sundaram Finance Ltd provides microfinance loans for people to buy commercial vehicles, cars, multi-utility vehicles, construction equipment, tractors and working capital finance. It is also a leading NBFC of India and is listed on the BSE. Sundaram Finance Ltd was launched by the Chennai-based corporate major, TVS Group. The company offers various microfinance products such as car finance, farming equipment finance, tyre finance, equipment finance and home finance through its offices spread across India.

6**. Bandhan Financial Services**

Bandhan Financial Services was established in 2001 with the dual objective of poverty alleviation and women empowerment. It is registered as an NBFC with the Reserve Bank of India. Bandhan Financial Services Pvt. Ltd has operations in 22 states and Union Territories. According to the company's website, Bandhan has some 2,022 branches and has served about 6.8 million borrowers. In 2011, US-based International Finance Corporation pumped US$ 600 million into Bandhan, to help boost its microfinance segment. BFSPL also operates the Bandhan Bank Ltd.

7**. Bharat Financial Inclusion Ltd**

The next microfinance institution to feature in this list is Bharat Financial Inclusion Ltd which was incorporated as an NBFC on January 20, 2005. It was formerly known as SKS Microfinance. “BFIL distributes small loans that begin at Rs. 2,000 to Rs. 12,000 to poor women so they can start and expand simple businesses and increase their incomes. Their micro-enterprises range from raising cows and goats in order to sell their milk, to opening a village tea stall. BFIL uses the group lending model where poor women guarantee each other’s loans,” states the company website. BFIL offers free financial literacy training and all microfinance applicants have to pass an exam following this training. “BFIL also offers micro-insurance to the poor as well as financing for other goods and services that can help them combat poverty,” the company states.

8. **Muthoot Microfin Ltd**

Muthoot Microfin Ltd was formed in 2015 and is one of the most reputed NBFCs in the microfinance sector of India. It is a division of the Muthoot Pappachan group (MPG that was established in Kerala in 1887. “Muthoot Microfin’s microfinance products are “designed to promote entrepreneurship among women and inclusive growth. The institution provides financial assistance through micro loans to women engaged in small income-generating activities. The company also facilitates entrepreneurship development and harnesses entrepreneurship skills through skill development workshops and financial literacy classes for its clients,” states the company website.

9. **Madura Microfinance Ltd**

Madura Microfinance was founded in 2006. The company focuses on promoting financial literacy among rural women and economically underprivileged sections of the society. It has over 200 branches in India. MML provides microfinance for Self Help Groups (SHGs) and individual entrepreneurs who wish to start their own small retail businesses.

A majority of microfinance products of MML are targeted at women SHGs. However, retail microfinance up to a maximum of Rs. 100,000 is available for individuals who are engaged in retail business. The company has partnered with several banks for offering microfinance products.

10. **Janalakshmi Financial Services**

Janalakshmi Financial Services is an emerging microfinance company of India in NBFC sector. However, Reserve Bank of India has licensed JFS to open an autonomous microfinance bank under the brand Jana Small Finance Bank. Currently, JFS offers microfinance from Rs. 15,000 to Rs. 50,000 with a maximum tenure of 24 months to open small businesses and generate self-employment. It also provides loans for the Micro, Small and Medium Enterprises (MSME) sector of India, of Rs. 100,000 and upwards, depending upon the scale of the industry.

THE LOAN PROCESS

Once a Micro finance institution has been selected and integrated on MicroWorld.org, it will be possible to post some loans on the website. To minimize the impact on the MFI, the institutions are committed to remain flexible and able to adapt the processes to suit the MFI.

1. Loan application

A prospective borrower applies for a loan with one of the MFIs partners. The person may already be a client of the MFI who is applying for a new loan, or may be applying for their first loan.

2. Application evaluation

A loan officer, employed by the MFI, visits the client to assess their application. This will involve an assessment of the client's wealth, character, business plan, and credit history. The loan officer explains to the client about Micro World and asks if they would like to be a Micro World borrower. If they agree, in addition to normal requirements, the loan officer will ask some additional questions for the website, and take a photograph of the client using provided cameras or even their mobile phone if it is easier.

3. Loan approval

Loan officer submits the loan application to the branch manager. Small loans can be approved by another loan officer, or sometimes by the branch manager. Larger loans must

be approved by the head office only. At the same time as submitting the application, the loan officer uploads the client photo, and a photo of their application form, to the Micro World system.

4. Disbursal and Loan Posting on the Micro World Website

If the loan is approved, the loan is disbursed to the client within 48 hours. The process is fast to enable the MFI to remain competitive among rival MFIs. Once the loan has been approved, the Micro World correspondent uses the information sent by the loan officer to create a loan profile in the Micro World system. This can then be published on the website which is ready to be funded.

5. Funding

Once the loan has been published on the website, it can be funded by Micro World members. Although the loan has been pre-disbursed, a contractual agreement is entered between the lender and the MFI that their money will be used to backfill the account of the borrower. The loan will remain on the website for a limited period which will vary between MFIs. If a loan reaches expiry before it has been fully funded, we will send the amount that has been raised to the MFI.

6. Fund transfer

To reduce transaction costs, payments between the platform and the MFI take place monthly on a net billing system, which means that the net of loans less loan repayments will be transferred between the two parties.

7. Repayment

The loan officer visits the client on a regular basis, weekly or monthly, to collect repayments. Once the loan is completely repaid, the full amount will be transferred back to the institution and it will be showed in the lenders' Micro World accounts.

ROLE OF GOVERNMENT IN MICROFINANCE

Over the last few decades, Indian economy has been at the forefront of world trade & industry. The opening up of the economy to encourage foreign investors, financial

services providers & global corporations has transformed modern day India into a bustling world power & brought in state-of-the-art technology & wealth across different sectors.

This has however not been transferred to a sizeable section of the population, which continues to remain excluded from the most basic opportunities and services provided by the traditional financial system. Thus, the idea behind Microfinance is to provide financial services to the low-income proletariat who traditionally lack access to banking and other monetary services.

During the last two decades, substantial work has been done in developing and experimenting with different concepts and approaches to reach financial services to the poor, by the Government, Non-Governmental Organizations (NGOs) and banking institutions in various parts of the country.

Microfinance encompasses a variety of financial instruments. The only common factor amongst the available services is the low amount of capital involved. Most Microfinance programmes provide multiple services like lending, savings, life insurance, crop insurance etc. Such financial services are important for the uplift of the economically weak sections of the society who are not able to avail financial services from the traditional sector. The lack of access to credit for the poor can be attributed to practical difficulties arising from the discrepancy between the mode of operation followed by financial institutions and the economic characteristics and financing needs of low-income households

Microfinance in India

Microfinance based credit delivery mechanism ensures viable financial services to address issues like actualizing equitable gains from development activities on a sustained basis, and plays a vital role in fighting poverty.

National Bank of Agriculture and Rural Development- External website that opens in a new window (NABARD) has taken the lead in promoting microfinance in India. Its Self Help Group- External website that opens in a new window (SHG) model has created opportunities for commercial banks to lend to the poor. It has been encouraging voluntary agencies, bankers, and socially spirited individuals, other formal and informal entities and also government functionaries to promote and nurture SHGs & Microfinance Institutions (MFIs)).

Due to the Government's active promotion & special schemes, Commercial banks have actively started lending capital to SHGs & MFIs, which then further lend to their members overcoming the information asymmetries that the bank would normally have faced. Thus engaging a dormant source of financing for the needy, as in lending to the poor, banks face high risks and transaction costs, while the lack of borrower information and of collateral make it unattractive for the formal financial sector to lend to the very poor.

Dominant Models of Microfinance in India

SHG-Bank Linkage Model: This model involves Self Help Groups (SHGs) which are financed directly by the Commercial Banks (Public Sector and Private Sector), Regional Rural Banks (RRBs) or Co-operative Banks.

Microfinance programmes focus on organization at the grassroots level through a process of social mobilization that enables the poor to build Self Help Groups (SHGs) amongst themselves, consisting of 10-20 persons. They participate fully and directly and take decisions independently in such organizations.

These groups are formed, developed and strengthened to evolve into self-managed people's organizations which provide internal loans to its members from the group corpus. The group corpus is supplemented with Revolving Fund sanctioned as cash credit limit by the banks.

MFI-Bank Linkage Model: This model covers financing of Microfinance Institutions (MFIs) by banking agencies for on-lending to SHGs and other small borrowers covered under microfinance sector.

MFIs combine flexibility, sensitivity and responsiveness of the informal credit system with technical and administrative capabilities and financial resources of the formal

financial sector which rely heavily on collective strength and closeness of social groups for effective social mobilization to enable financial empowerment.

MFIs have adapted themselves to circle around the shortcomings of traditional financial organizations, by forming a partnership between socially focused NGOs, which invest in human and social capital at the grass roots, and economically sensitive banking institutions, experienced in mobilizing funds for graduating and enabling rural communities.

MFIs enable commercial banks to overcome the formal requirements of paper-work to support transaction costs, information asymmetries and risk, making lending to the poor a commercially attractive proposition. The role of the MFIs therefore is to act as the guarantor to the bank, to support the credit worthiness of the poor.

National Bank for Agriculture and Rural Development - (NABARD)

NABARD is a development bank which facilitates credit flow for promotion and development of agriculture, small-scale industries, cottage and village industries, handicrafts and other rural crafts. Its Financial Inclusion Department (FID) is the nodal agency which oversees the Financial Inclusion Fund (FIF) and Financial Inclusion Technology Fund (FITF) which promote microfinance initiatives.

Rashtriya Mahila Kosh

The National Credit Fund for Women or the Rashtriya Mahila Kosh (RMK) has a large number of grant and subsidy based poverty alleviation programmes comprising micro-credit & micro-savings schemes with a focus on poor women across the country. RMK takes active initiatives in channelizing funds, market development social advocacy.

Small Industries Development Bank of India (SIDBI)

SIDBI's Foundation for Micro Credit is the apex wholesaler for micro finance in India. It provides a range of financial and non-financial services such as loan funds, grant support, equity and institution building support to the retailing Micro Finance Institutions (MFIs) including two-tier MFIs so as to facilitate their development into financially sustainable entities, besides developing a network of service providers for the sector.

Tamil Nadu Women's' Development Corporation

The Tamil Nadu Corporation for Development of Women, in partnership with Non-Governmental Organizations (NGOs) and Community based organizations, supports 'Mahalir Thittam' or Self Help Groups (SHGs) which inculcate sound habits of thrift, savings and banking amongst the volunteer members of the scheme

IMPACT / EFFECT OF MICROFINANCE IN INDIA

- Due to microfinance the borrowing base has increased from 83.6 to 93.9 million.
- People got self-employed and started earning which result in increase in personal income and GDP (Gross Domestic Product) of the nation.
- Pressure on banking institutions to improve because of microfinance the bank services (like saving, depositing, lending loan and etc.) are used by more and more people.
- Empowerment of women has increased as they have become self-dependent women and have jobs.
- Micro finance promotes child education by providing education loan to the public.
- Microfinance reduced the problem of poverty by providing loans to the poor people, to start their own business.
- Microfinance provides certain financial services like- Saving, Credit, Money transfer, insurance and etc. for the poor to enable them to raise their income level and improve living.
- Shares, SKS and Spandana serve more than 1.5 million families most of them are very poor when they started accessing micro- financial services.

- MFI's achieved an overall growth of customer base by 10.8%.

1. **Microfinance and Social Empowerment** - SHG-BLP itself has had a profound social impact. A number of studies conducted on the effectiveness of the programme, have highlighted its impact on the social empowerment process. Important findings with respect to the SHG programme are:

- It has enabled households to spend much more on education than non-client households. Families participating in the programme have reported better school attendance and lower dropout rates.
- It has empowered women by enhancing their contribution to household income, increasing the value of their assets and generally by giving them better control over decisions that affect their lives.
- In certain areas, microfinance has reduced child mortality, improved maternal health and the ability of the poor to combat disease through better nutrition, housing and health – especially among women and children.
- It has contributed to reduced dependency on informal moneylenders and other non-institutional lenders in rural areas.

2. **Microfinance and Economic Growth** - Economic growth requires many things from relatively stable governments to alleviation of poverty to the creation of a formal business sector to access to clean water, education, and healthcare. Long term growth can be achieved by:

- Putting an emphasis placed on improving overall quality of life, Public goods are missing from many of the small villages and poor slums in which microcredit is extended. Lack of safe wells, paved roads, and so on, limits the growth that successful and entrepreneurial microcredit borrowers can experience.
- A focus on real businesses (which very possibly means not lending to the poorest of the poor, but lending to the better off who can create real enterprises and employ

their less able neighbors) is necessary to create self-sustaining small companies, and to make the push toward a formal sector. Because MFIs have maintained their strong reputation and their ability to reach millions of people, they possess the necessary qualities to bring change. While projects of this caliber may sound too lofty, it is absolutely necessary to consider using microfinance on a slightly larger, more innovative scale. There is no accessible data to say that these types of projects in conjunction with MFIs have been tested or tried, therefore it cannot be stated that microfinance used in other ways would not lead to more successful, and developed towns, villages and cities. Because microfinance is still a relatively new idea, MFIs are not eager to switch practices.

3. **The SHG system -** The launching of pilot phase of SHG programme in February 1992 was a landmark development in banking with poor. SHG informal thrift and credit groups of poor came to be recognized as the bank clients under the Pilot phase.
According to NABARD, almost 3 million SHGs have linked to nearly 500 banks since the program started, reaching over 11 million households across.

The members form a group of around twenty members. The group formation process may be facilitated by an NGO or by the MFI or bank itself, or it may evolve from a traditional rotating savings and credit group (ROSCA) or other locally initiated grouping. The process of formal 'linkage' to an MFI or bank usually goes through the following stages, which may be spread over many years or which may take place within a few month.

- The SHG members decide to make regular savings contributions. These may be kept by their elected head, in cash, or in kind, or they may be banked.
- The members start to borrow individually from the SHG, for purposes, on terms and at interest rates decided by the group themselves.
- The SHG opens a savings account, in the group's name, with the bank or MFI, for such funds as may not be needed by members, or in order to qualify for a loan from the bank.

- The bank or MFI makes a loan to the SHG, in the name of the Group, which is then used by the Group to supplement its own funds for on-lending to it members. The SHG carries out all the same functions as those required by the Grameen system, but they do this on their own behalf, since the SHG is effectively a micro-bank, carrying out all the familiar intermediation tasks of savings mobilization and lending. The MFI or bank may assist the SHG in record keeping, and they may also demand to know who are the members and impose certain conditions as to the uses of the loan which they make to the SHG, but the SHG is an autonomous financial institution in its own right. The SHG system is mainly found in India, where it is used by both MFIs and banks. The SHG system in India was initiated by NGOs, and is used for financial intermediation both by commercial banks and by MFIs.

4. **Illusive socio-economic impacts** - SHGs form a critical link for poor women to access a variety of financial services. They are effective platforms for women to participate in politics through awareness campaigns and community action. SHGs have also emerged as "last mile" channels for government to distribute financial benefits and for corporations to retail their products through member-entrepreneurs.

CONCLUSION

Microcredit or microfinance is banking the un bankables, bringing credit, savings and other essential financial services within the reach of millions of people who are too poor to be served by regular banks in most cases because they are unable to offer sufficient collateral. In general, banks are for people with money not for people without.

In focusing on microfinance, emphasis has been laid on the need that poor people have for a wide range of financial services. These needs are evidenced by the uses made of financial services that already exist but which are usually informal in nature. This shift in emphasis away from the provision of credit solely for income generation towards a range of financial services is consistent with an understanding of poverty which looks beyond low incomes to vulnerability and powerlessness. Providing microfinance can give poor people the means to protect their livelihoods against shocks as well as to build up and diversify-also a means of protecting their livelihood activities by investing loan capital.

The role of credit in promoting incomes has been the rationale for NGO programmes in this sector in the past. However, obtaining one or two loans has rarely resulted in sustained improvements in income for poor people. Moreover, even if very poor people are able to invest successfully, unexpected shocks can undo any gains very quickly. Thus, the poorest are likely to need to build up a degree of security before investment and growth become possible.

Micro finance institutions can reduce the interest rate because the poor are more favourable to micro-financing due to they can't get the amount at minimum range of 25000 at banks and the process of banks system take much longer to provide them loan after they fill all formalities, As they will not be proper securities to present at bank so they approach microfinance institutions to get loan for full filling their need but again due to interest they are facing the same poverty and falling into debt.

Although there are merits and demerits of microfinance, it is more helpful in reducing poverty in country and also due to this many women are getting empowered setting up their own business and getting loans without individual securities. Overall, microfinance has largely contributed to the growth and development of the country.

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