

Microfinance in India: Issues and Challenges

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Abstract: Indian Government has taken different steps for alleviating poverty since Independence. However, in spite of the various efforts, almost one-third of total population in India is still below the poverty line. It has been observed that the majority of the poor are in the rural areas. Further, along with this poverty scenario, no adequate employment has been generated in the labour market in India. Credit can help the poor in taking up income generation activities which will in turn improve their standard of living. “Microfinance is the provision of financial services to low-income clients or solidarity lending groups including consumers and the self-employed, who traditionally lack access to banking and related services.” Microfinance is considered to be revolutionary because it aims at servicing the poorest of the poor, who were up till now considered unfit for financing of any kind except charity. It acts as a catalyst to organize the unorganized for social change. But the outreach is too small as compared to the requirement and potential. Currently India is considered to be the largest emerging market for microfinance. It has been growing in India at a steady pace over the past decade. Apart from this growth there are some issues and challenges concerned with it. This lays emphasis on the problems, issues and challenges prevailing in India regarding the Microfinance. An attempt is made through the paper to evolve strategies to solve these problems and issues.

Key Words: Microfinance, Self Help Groups, MFIs, Poverty Alleviation

Introduction:

Government of India has taken various steps for alleviating poverty since Independence. However, in spite of the various efforts, almost 27 percent of total population in India still continues to be below the poverty line. It is identified that most of the poor are in the rural areas. Further, along with this poverty scenario, no adequate employment has been generated in the labour market in India. This may be one of the reasons for the persistence of poverty. Poor adopt various coping strategies to surmount their poverty situation. Credit, Asset Selling and Migration are some of the popular coping strategies adopted by the poor in India. Development Economists have over the years proposed that credit is one of the best strategies to overcome the problem of poverty. Credit can help the poor in taking up income generation activities

which will in turn improve their standard of living. Microfinance is considered to be revolutionary because it aims at servicing the poorest of the poor, who were up till now considered unfit for financing of any kind except charity. Microfinance is one of the products of new developmental thinking and policy-making. It is a unique amalgamation of industrial (including financial) and institutional reforms in the present scenario of development economics.

Microfinance and Microfinance Institutions

Micro-Finance is an innovative word and is very much part of the vocabulary today. It constitutes two words: Micro and finance, which could mean small credit or “microcredit”. However, the concept of micro-finance goes far beyond small credit and it is to be noted that not all small credit is Microfinance. Microfinance is an emerging

phenomenon that opens access to capital for individuals previously shut out from financial services. Microfinance constitutes various financial services, which mostly includes savings and credit. It also includes other services like insurance, directed to ultimately benefit the poor or disadvantaged section of the population, especially those who are economically poor. This is often backed up with a variety of support services such as encouraging and organizing the poor and helping them build backward and forward linkages with other supporting institutions. The purpose is to provide capital to help the poor to achieve self-reliance.

Microfinance institutions are not a specific legal institutional form - typically, microfinance is considered a line of business. Among the Indian institutions offering microfinance services, there are Non-Government Organizations (NGOs), Private Foundations/Trusts, Cooperatives, Commercial Banks, Regional Rural Banks (RRBs), Local Area Banks (LABS) as well as specialized Non-Banking Financial Institutions (NBFCs). Currently India is considered to be the largest emerging market for microfinance. It has been growing in India at a steady pace over the past decade. At present Reserve Bank of India is focusing on priority sector lending and hence banks have become more aggressive in lending to rural clients.

Review of Literature

According to Dr. Siddharth G. Das et al.(2013) have focused on Strategies to Counter Microfinance Delivery Challenges. The major hurdles in successful delivery of microfinance can be overcome through innovation in operational strategies to handle these macro and micro challenges. According to Report of India Brand

Equity foundation (2013) by the Use of IT for monitoring, increasing productivity and efficiency, Internet-based funding model Microfinance challenges can be overcome. As asserted by Medatwal Chandan(2013) progress of SHGs is not up to the mark. It should be improved through various schemes and programmes and there is need to find the factors in SHGs programmes, which have greater impact on the empowerment of women. Sibhatullah Nasir (2013) found the contemporary issues and challenges in microfinance. Padamcholans Mahanta et al. (2012) has described the current status of Microfinance in India. The paper has focused on the factors and theoretical position associated with evolution of microfinance and its role in global scenario. He discovered the prevailing gap in the functioning of MFIs. According to D Bansal (2011) there is the need of technical innovations to improve the quality of microfinance services. A number of electronic devices are being used in different countries to expand the outreach and to improve the microfinance functioning. Some of these devices are mobile phones, ATMs, processor cards, computers etc. but there is enough scope to use such innovative techniques in microfinance sector in India. M.L.Chhipa(2011) emphasized on various measures initiated in the state to bring about women empowerment through microfinance in Rajasthan. He focused on various opportunities, developments and challenges in its way and gave recommendations for improving the situations. T.S. Anand et al. (2011) highlighted the Institutional Challenges in Micro Finance Sector. To be successful, in the market the Micro Finance Institutions marketing strategy must meet the customer's requirements. He concluded that the MFIs should consider the Five Fold Factors like Challenges in Interest Rate, Win Over, Marketing Strategies, Customer Feedback and Analysis and

Marketing Audit as institutional challenges for catering to the needs of the rural customer need thereby sustaining the credit operations by Micro Finance Institutions.

Objectives

Through this research, an endeavor has been made to identify the latest issues, problems and challenges. The objectives of this research are:

1. To study the various issues, challenges and problems in effective implementation of various Microfinance programmes.
2. To explore the strategies to be implemented to overcome issues and challenges.

Microfinance Issues and Challenges

Microfinance institutions are not flawless, they do possess some drawbacks. Despite significant progress of various microfinance programmes and development schemes there are some issues:

1. Risk of failure to pay

There is uncertainty regarding the lending to economically weaker section of society. The rural poor have irregularity/volatility in income streams and expenditure patterns, and there is possibility of systemic risks such as crop failures or a fall in commodity prices, and therefore, may face real difficulties servicing loans. So banks have genuine concerns while dealing with the rural poor, and tend to identify such loans as risky.

Table 1: Loans outstanding against SHGs as on 31st March (Amt. in crore)

Particulars		2010-11		2011-12		2012-13	
		No. of SHGs (lakh)	Amount	No. of SHGs (lakh)	Amount	No. of SHGs (lakh)	Amount
Loans Outstanding against SHGs as on 31 March	Total SHGs	47.87	31221.2	43.54	36340	44.51	39375.3
	Of which SGSY Groups	12.86	7829.39	12.16	8054.83	11.93	8597.09
	Groups to Total	26.9	25.1	27.9	22.2	26.8	21.8
	All Women SHGs	39.84	26123.8	36.49	30465.3	37.57	32840
	% of Women Groups to Total	83.2	83.7	83.8	83.8	84.4	83.3

Source: Status of Microfinance (NABARD)

2. Lack of information

There are various sources of credit information in India, but none of these focuses on small, rural borrowers. Credit information on such borrowers is

difficult to obtain because the majority of the rural poor rely on moneylenders and other informal lenders, and it is not in the interest of such lenders to pass on a borrower's good credit repayment record to other providers of finance.

3. Weak regulatory framework

Government has not been able to develop and enforce a legal and regulatory framework conducive to rural finance, so that contract design, contract renegotiation, and contract enforcement remain weak, making it even more difficult for financiers to provide borrowers with the right incentives for repayment.

4. Lack of elastic services and products

Rural banks do not provide flexible products and services to meet the income and expenditure patterns of small rural borrowers. As noted above,

small rural borrowers have irregular/volatile income streams and expenditure needs, and therefore, prefer to borrow frequently, and repay in small installments, but most banks do not offer such products.

5. Interest Rate

MFIs are charging very high interest rates, which the poor find difficult to pay. MFIs are private institutions and therefore require being economically sustainable. They do not get any subsidized credit for their lending activities and that is why they need to recover their operational costs from borrowers.

Table 2: Interest Rates of different MFIs

S.No.	Name of MFIs Purpose of Loan	Interest Rate
1.	SHARE Production / Housing	15 %
2.	Nari Nidhi Production	12 %
3.	WWF Production	18 %
4.	RDI Production / Consumption	24 %
5.	Shanti Dhan Production / Consumption	13 %
6.	MYRADA Production / Consumption	24-36 %
7.	SPMS Production / Consumption and Marriage	24-60 %

(Source – Studying by EDA Rural System, Gurgaon2)

6. Low Outreach

In India, MFI outreach is very low as compared with its requirement and potential. It is only 8% as compared to 65% in Bangladesh. It has been observed that MF programmes focus a great deal of attention on women.

7. Education Level

The level of education of the clients is low. So it creates a problem in the growth and expansion of the organization because its percentage is around

70% in MFIs. Target population of MFIs is people of rural areas and they have no or less education level. As the percentage of people who have very less education.

8. Unequal distribution

There is unequal geographical growth of Microfinance institutions and SHGs in India. Most of institutions and SHGs are located in southern states. Main reason for this is the state government support, NGO concentration and public awareness.

Table 3: Regional spread of SHG federations in India in 2007 and 2013

Region	No. of primary Federations		No. of secondary federations		No. of tertiary federations		Total	
	2007	2013	2007	2013	2007	2013	2007	2013
Northern	126	371	21	24	–	14	147	409
North Eastern	122	369	10	18	–	0	132	387
Eastern	5,745	62,189	105	2,940	–	56	5,852	65,185
Central	487	5,459	334	180	–	2	821	5,641
Western	663	8,629	1	11	–	1	664	8,641
Southern	59,172	83,268	2,093	3,185	22	25	61,287	86,478
Union Territories	–	1	–	0	–	0	–	1
All India	66,310	160,286	2,571	6,358	22	98	68,903	166,742

Source: APMAS Hyderabad.

9. Gap in Demand and Supply of Microfinance

Various initiatives taken by authorities and financial institutions have not helped the rural poor to improve their living standards and create welfare. Looking at the provision of rural credit, there appears to be a big gap between the needs of rural people related to savings and credit options, and the receipt of the same from various financing institutions.

10. Improper usage of Loan

Loan raised through microfinance is mainly used for consumption purpose not for productive purpose. It does not serve the real purpose of Micro-credit.

11. Language difficulty

Language barrier makes communication with the clients (verbal and written) is an issue that creates a problem in growth and expansion of the organization because around 54% language barrier has been identified in MFIs. As the education level of clients is low so it is difficult to communicate with them. For this reason it is also difficult for the MFIs employees to make the clients to understand the policy and related details.

12. Negligence of Urban Poor

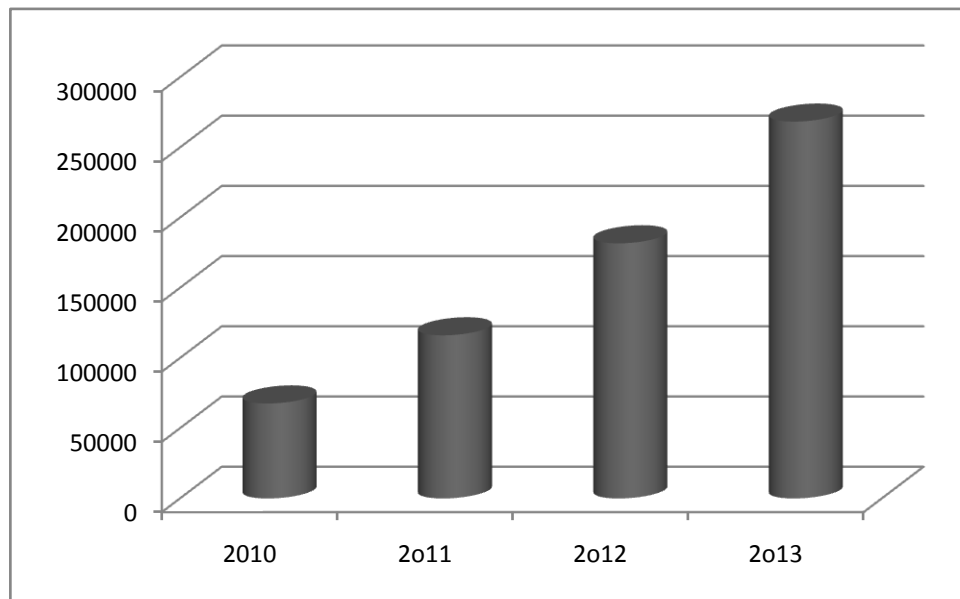
It has been noted that MFIs pay more attention to rural areas and largely neglect the urban poor. However, the population of the urban poor is quite urbanization, this number is expected to rise rapidly in the coming years. In this situation, MFIs need to pay equal attention to the urban poor because they too need financial assistance for various activities.

Table 4

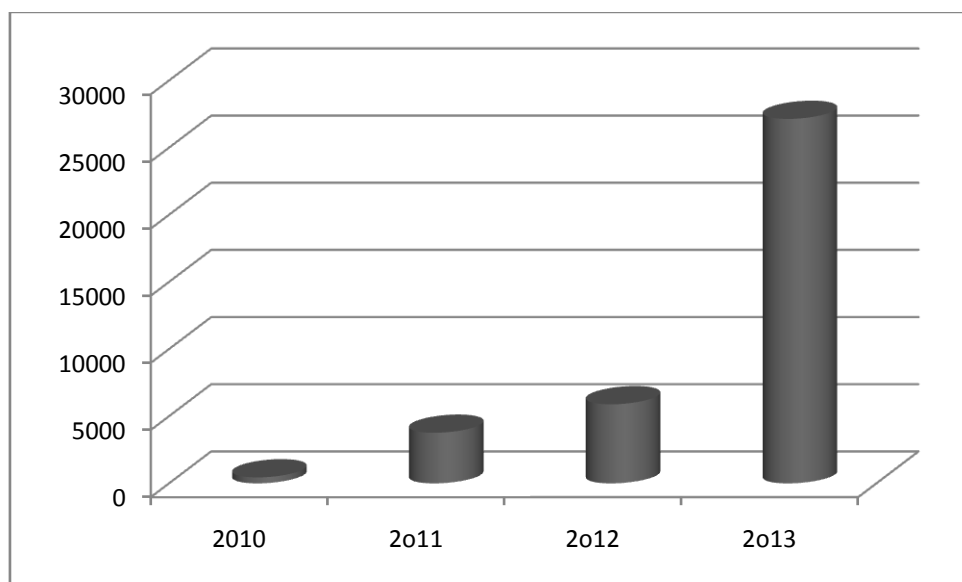
Years	2010	2011	2012	2013
No of MFIs in rural areas	67694	116208	181753	268454
Years	2010	2011	2012	2013

Urban Locations Covered	447	3771	5891	27143
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(Source: www.rbi.org)



No of MFIs in Rural Areas



Urban Locations Covered

13. Lack of access to Funding

Another factor contributing to the lack of growth in MFIs is that requisite financial support has not been

provided to MFIs by concerned agencies. Around 68% of MFIs response was in favour of that government don't support them to meet the funds

requirement as MFIs cannot alone remove the poverty from the country.

14. High operational cost

High transaction cost is a big challenge for microfinance institution. The volume of transactions is very small, whereas the fixed cost of those transactions is very high. It cannot vary with the size of the loan.

15. Lack of Insurance Services

Poor people are exposed to monetary shocks but, the current Microfinance programme in India is just focused on regular saving and micro-credit. However, some of the MFIs have started providing insurance services but the efforts are still at an experimental stage.

Strategies to face Issues and Challenges

Microfinance provides the best platform for the weaker sections of society. Taking into consideration the issues and challenges, we can make some recommendations.

1. Microfinance programmes and group formation should be handled by trained personnel in a professional manner.
2. Leading banks and industry developments must be taken into consideration for district-wise and block-wise economic opportunities and resource mapping.
3. The skills should be imparted through various training programmes to rural poor for capacity building.

4. New help groups should be formed and quality standard should be focused for new as well as reorganized groups.
5. Co-ordination committees should be formed for better linkage/association among different SHGs working in different areas.
6. The microfinance programs should not be restricted only for meeting the financial needs of women but also include entitlements and status of women.
7. Substantial financial investments are required for the promotion of different self-help groups. These financial resources must be planned as per a concrete, long-term action plan.
8. For control of interest rates of microcredit institutions, regulatory framework should be established, based on transparency and avoiding hidden cost.
9. Special federations must be established to cater the equity needs of MFIs.
10. There should awareness building among poor through various media programs.
11. Ensure the uniform distribution of micro financing in both rural and urban areas of each states of India.
12. Involving Microfinance into sector-wide approaches (SWAPs) to enhance

the contribution of Microfinance to wider economic growth and poverty reduction.

13. Surveys should be conducted by NSSO and State govt. to collect information and statistics about progress of Microfinance programs.
14. Micro insurance services should be provided to protect the poor from financial shocks.
15. Information and Communication Technology should be adopted for implementation of various credit programs.

Conclusion

Microfinance is very necessary in India to achieve financial inclusion of the poor in the rural and urban areas. Lending to the poor population if handled in an effective manner it can be a miracle for the development of the country and alleviation of Poverty. If government and MFIs act together then microcredit can play a great role in poverty alleviation. MFIs are the foundation institutions offering financial services to low income people. They have been proactive in the process of comprehensive growth in India by their novel approaches. They have enthused with the passage of time. They are varying for the better. With the provision of financial and social services and helping the members put into practice repayment ethics and social unity they can be solution for rural poverty and backwardness. They have huge potential not only as a system of peer-to peer (p2p) lending but also as an opportunity of social bonding. The Micro Finance Institutions will henceforth have to bear in mind that they will not merely compete with themselves but also with

other significant actors in the whole industry. Their real success will depend on the potential, reach and transparency, both from the financial side and from the social side. Accessibility, accountability and sustainability in all their operations will help the MFIs to lift themselves as social engineers, effectively.

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