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Operation, Issues and Challenges of Microfinance in India

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Abstract

Objective: The main objective this paper is to understand the concept of microfinance, the operation and to identify the latest issues, problems and challenges in effective implementation of various Microfinance programmes.
Method: Secondary data forms the basis for this paper as the study is descriptive in nature. Books, various websites, magazines, newspapers, and publications of recent research papers available in different websites are the sources of data.
Findings: The study reveals that While Micro Finance Sector seems to be growing fast with no road blockages, it has also brought to fore several challenges and issues. Some of such issues are: providing varietal savings avenues to the micro finance beneficiaries, and mobilization of such savings by MFIs, creating regulatory frame work for MFIs, provision of finance to MFIs as a regular channel of finance/refinance, reduction in cost of resources/management resulting in lending rates for micro finance beneficiaries, safety and precautions for MFIs entering into new financial services like micro leasing, insurance, housing, medical services etc.
Applications: This paper provides a platform for researchers to understand the problems and challenges in effective implementation of various Microfinance programmes.

Keywords: Challenges, Issues, Micro Finance, Mutual Financial Institutions'. Poverty alleviation, SHGs, Women Empowerment.

1. Introduction

Micro Finance can trace its origin back to the early in 1970s when the self-employed women association (SEWA) of the state of Gujarat formed an urban Co-operative Bank called Sri Mahila Seva Sahakara Bank to meet the banking needs of the deprived women employed in Ahmadabad city, Gujarat[1].Microfinance was present in India for a very long time in informal formats such informal money lending, chit-funds or rotating savings, etc.Microfinance sector is a sub-stream of Finance sector. It covers a lot of services such as, pension plans, cheques and fund transfers for the poor people. Those people who were traditionally not provided access to financial services can have these services with the help of microfinance. Microfinance industry was present in India from the early 1970s; it came into prominence very recently. Since the beginning of 21st century, it came into prominence and its growth has accelerated in a very rapid rate [1].Unemployment and poverty constitute the two key challenges faced by India since independence. Lack of adequate credit facilities for the deprived and unemployed is the main reason for unemployment and poverty. To achieve sustainable development of the nation, unemployment and poverty are the main barricades. The space between the have and have not's has been widening due to the acceleration in the opening of the economy[2]. The foundation for microfinance movement has been laid with the establishment of Self Help Group (SHG) – Bank Linkage Programme (SBLP) started as a pilot project in 1992 by NABARD. The programme became successful and also developed as the most well-liked model of microfinance in India. Thus, microfinance has become important buzzword in India [3].

Microfinance – A Concept

Microfinance being practiced as a tool to attack poverty the world over. The term "microfinance" is an amazingly simple approach that has proven to empower very poor people around the world to pull themselves out of poverty. Relying on their traditional skills and entrepreneurial instincts, very poor people, mostly women, use small loans, other financial services and support from local organizations called micro financial institutions to start, establish, sustain, or expand very small, self supporting businesses. A key to microfinance is the recycling of loan dollars[4]. As

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each loan repaid usually within six months to a year-the money is recycled as another loan, thus multiplying the value of each dollar in defeating global poverty and changing lives and communities.

FUNCTIONING OF INDIAN MICRO FINANCE;
The following models govern the functioning of Indian microfinance [5]:

1. Self Help Group Model (SHG)
2. Joint Liability Group Model (JLG)
3. Individual Lending Model (IL)

Self Help Groups: are self-governing social bodies consisting of of 10 to 20 members which mobilize a fund through its members or from a bank; They advance loans to its members or others keeping in mind their requirements after taking the united opinion of the group. While advancing the loans, the borrower's community standing acts as the security rather than the corporeal property. The group members exercise their influence for the refund of the loans. The formation of SHG takes place by the election of executive body by the group members [5].
Joint Liability Group: In this model, there is a collective dependability. Centers are formed with the help of groups and the group formation is with the help of members.05 members per group and 08 groups per centre constitute the most preferential grouping. Its focus is concerned only with the financial matters and not with the social issues. The group takes the responsibility for the repayment of the loan in case member fails to repay the loan if it has funds. Otherwise, the onus is on the centre to repay from its funds; the credit risks are overcome by holding repeated group meetings[5].
Individual lending Microfinance Institutions (MFIs) lend money to individuals. The verification of individual's capacity to repay the loan is done. Substantial loans sanctioning needs security[5].

Issues/challenges:

ISSUES:-
Sustainability: - MFIs model is comparatively costlier in terms of delivery of financial services. Cost of supervision of credit is high, the loan volumes and loan seize is low. MFIs pass on the higher cost of credit to their clients who are interest insensitive for small loans but may not be so as loan seize increase. So, high cost involved in MFIs Question arises on sustainability of small MFIs [6].
Lack of Capital: Lack of owned funds is the challenge of this sector. Presently, to meet this challenge of MFIs, no trustworthy machinery is available in the country. Fund availability is necessary for MFIs to operate but due to various obligations and regulation imposed by the government and banks, MFIs are not getting funds easily from the banks [6].
Lack of Modern Technology: - MFIs have no efficient software to deal with the information. Reason can be of high cost. All MFIs facing the problem of multiple lending and they are trying to fulfill regulation announced by RBI but no one has strong software to cope up this problem [6].
Lack Of good Management: - Small MFIs have no effective management in middle level & upper middle level. Due to this operational function is not implementing effectively.
Borrowings: - Earlier years, MFIs are now finding it relatively easier to raise loan funds from banks. They know very well about need of MFIs. Banks are trying to find exact risk about MFIs. They are trying to use right technology to assessment of right risk. So, they can make innovative & suitable product for MFIs [7].
Insurance In MFIs: - Some MFIs use product of insurance for security of portfolio. Clients do not get benefit of insurance. Claim ratio is high so premium of insurance is high. Small MFIs are facing problem to implement other life & general insurance product. Still, insurance companies are not making product as per need of MFIs. MFI shave no right approach to find risk about prospects death clients. So, claim ratio is high. Many death clients are husband of clients. Many MFIs are using group term life insurance product. Some MFIs violate the regulation regarding group insurance micro insurance of IRDA.

CHALLENGEs
From Credit to Enterprise: - MFIs always linked to the banks, how they can be induced to matured level of enterprises, how they can be induced to factor in livelihood diversification, how they can be increasing their access to the supply chain linkage to the capital market. So, MFIs are facing different type of problems, how they can be matured as good enterprise[7].

Mixing Charity with Business Activity: - To run a business activity a marginal profit is needed. In the absence of this no organization or institution will run but often microfinance business is connected with charity have problem arises on operational stages.

Difficulty In Measuring the Social Performance of MFIs: - there is no specific tool to measure the performance with proves that is working in positive direction and where it lack, what more initiative is needed.

Lack of Customized Solution for the Poor People: - Many poor and rural people are illiterate and not able to easily understand about the rule, policies, and features of products. Thus proper channel must be set up for the customer satisfaction and solution of problem [4].

Dual responsibility of MFIS to be financially sustainable, Sound and development oriented: MFIs have dual responsibility to be financially sound and work for socioeconomic development of in rural, semi rural or urban areas.

Human resource challenges in MFIs: - Due to low salary, low growth rate, lack of resources, and lack of good human resource policies, employee' resignation rate is high. Lacuna of good employees in small MFIs. That effect on growth and operational functions of MFIs.

Challenge regarding clarity of regulation about MFIs: - Still, microfinance bill is pending. How to make clear regulation and policies about MFIs is a big challenge.

2. Conclusion

Over the last thirty years, Microfinance has become one of the most important national development policies. Huge amounts of national development and philanthropic investment and commercial funding have been committed in its direction. Most of all, the savings of ordinary people, have increasingly been intermediated through MFIs. The intentions appeared to be just and ambitions were bold. It all looked so optimistic at start. The initial progress looked even better. Reports began to emerge from the pioneering MFIs that they were creating and sustaining large number of jobs and income flows, local women were being empowered as never before and a 'bottom up' development process was emerging that would see the typical local economy finally shake itself free of poverty and underdevelopment.

While Micro Finance Sector seems to be growing fast with no road blockages, it has also brought to fore several challenges and issues. Some of such issues are: providing varietal saving avenues to the microfinance beneficiaries, and mobilization of such savings by MFIs, creating regulatory frame work for MFIs, provision of finance to MFIs as a regular channel of finance/refinance, reduction in cost of resources/management resulting in lending rates for microfinance beneficiaries, safety and precautions for MFIs entering into new financial services like micro leasing, insurance, housing, medical services etc. MFIs' increasing involvement will happen through improving financial inclusion, owners'(institutional) oriented vs. clients' oriented and reconciling conflict of interest in profit and social motives, bringing social agenda back in the fold of MFIs without sacrificing sustainability, enhanced emphasis on livelihood finance and concentrating on target family as a unit for empowerment, switch over from single product to multi product basket, built in effective and transparent self regulation with watch dogs and establishing microfinance beneficiaries' protection mechanism and grievance redress, removing regional imbalances in microfinance lending, increased transparency, accountability, responsibility and quality corporate governance, growth with quality and verification of credentials of new MFIs and their registration before commencement of business. Rating of MFIs will go high with increasing use of IT by MFIs and development of common software, mobile banking for improving outreach and reducing cost of operations, improving financial literacy among Microfinance beneficiaries, recording and propagating success stories and innovative methods of financial intermediation and addressing other emerging issues during the course of microfinance journey.

In the context of mobile phone connectivity in rural /semi urban and far flung areas rapidly expanding and once the mobile banking is introduced through mobile service providers either directly or as agents/Business Correspondents of the banks, and /or banks themselves coming forward to provide mobile banking in a more aggressive manner so as to expedite the process of financial inclusion. It is feared in certain quarters that MFIs may become redundant unless they re - invent their role to continue to be relevant to the poor[8].

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