

SUCCESS OF MICROFINANCE ORGANIZATIONS IN INDIA A STRATEGIC VIEW**Dr. MANOJ PANDEY**

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Abstract: Formal financial sector institutions in India have been mainly serving the needs of commercial sectors and people belonging to middle and upper income groups. The needs of the lower income groups and poor are not catered by formal financial institutions because of many factors. This paper tries to explore all those factors that contribute towards the development of microfinance organizations in India. A careful research on demand for financing and saving behavior of the potential borrowers and their participation in determining the mix of multipurpose loans are essential in making the concept work. For microfinance institutions to be successful in our country they have to increase the credit worthiness of the poor and they have to be made more "bankable" so that we are able to create a stronger society with a balanced economy having less disparity between the rich and the poor.

Keywords: Microfinance, Multipurpose loans, Credit, Financial Sector

Introduction: Microfinance organizations intend to help poor and deprived class by integrating their efforts/initiatives with the help of credit money to improve their economic status in a small entrepreneurial way but normally they are deprived credit by the microfinance organizations and financial institutions because of so many reasons. Therefore the fundamental problem is not so much of unaffordable terms of loan as the lack of access to credit itself (Kim 1995).

The lack of accessibility of credit to poor is attributed to practical difficulties arising because of the operational procedures of financial institutions and the other economic factors & characteristics. To understand this let us take a small example. Financial institutions require that the borrower must have a financial asset and a stable income so that the interest and principal amount can be repaid as per the agreed terms & conditions. But large number of borrowers lack either of these two or both. Another example is that the strategic requirement is that small loans should be rendered to more and more people but financial institutions prefer to give bigger loan to lesser people to minimize the administrative load and cost. Because of these problems these people go to the informal lenders (Sahukars) and pay a much higher interest rate and fall prey to

them. Despite the so called success of microfinance organizations in India only about 2% of world's 500 million small entrepreneurs have access to financial services (Barry et al. 1996)

Now this statistics poses a huge challenge & opportunity for microfinance and other financial institutions. Now what microfinance and other financial institutions can do is

1. Reaching the potential borrowers or making themselves accessible to the potential borrowers.
2. Making the process people friendly ie simple, easy and less time consuming. Decentralization can be an effective way.
3. Reducing their administrative cost.
4. Ensuring that the interest and principle amount are recovered in stipulated time period.
5. Disbursing group loans on the account of one person (leader). This can be a good model for joint families and friends (partnership)
6. Government should provide a feasible legal and regulatory framework that encourages the development of microfinance and financial institutions and promotes them as recognized financial institutions engaged in the upliftment of poor and deprived class.

Now there are few questions that have to be answered before we proceed as these questions give a strategic view to the theme of the paper.

1. What is the success of microfinance companies and other financial institutions compared to the global counterparts?
2. Can the efforts of all the microfinance and financial institutions engaged in the common cause be integrated to bring about a synergy so that collectively a huge success can be achieved?
3. Is there uniformity in the operational process, interest rates and support system in all the financial institutions and microfinance organizations across the country engaged in the similar course?
4. Is there a need for new institution? If yes what kind of? should it be a national level institution or state level institution and who would be the beneficiaries?
5. Is there a need for corporate financial organization like nationalized bank to get involved, if yes what would be their role?
6. What would be the role of donor agencies and how the communities can be involved?
7. What is the role of the government for all the above issues and how should government go out of the way to help the poor and deprived in developing a healthy economic society with less disparity.

Formal financial sector institutions

Formal financial sector institutions in India have been mainly serving the needs of commercial sectors and people belonging to middle and upper income groups. The needs of the lower income groups and poor are not catered by formal financial institutions because of many factors. Few of the factors are

- ✓ Risk of recovery of interest and principle amount
- ✓ High service and transaction cost
- ✓ Irregular flow of income of the borrower
- ✓ Lack of documents and proof for the assessment of income
- ✓ Unacceptable assets like crops, utensils, trees and jewellery
- ✓ Cumbersome and complex process

The formal financial sectors are commercial banks, housing finance institutions, rural development banks, NABARD and cooperative banks. Government has taken lot of steps in developing and strengthening rural banks but these banks are not highly successful in empowering the lower income group and poor as their major problem is penetration and reach.

Informal financial sources

Informal financial sources include funds from family members or local money lenders. The local money lenders normally charge a huge interest that ranges from 30 – 60%. The poor borrows and spends his entire life in the payment of interest and the principle amount. Chit fund is another form of credit system operated by a group of people for their mutual interest /benefits and it has its own limitations.

NGO's/ SHG's

Another category is non government, not for profit organizations. Now these NGO's also operate in different manners. Many NGO's directly lend the money to individuals/groups, help and empower them and ensure to get the interest and principle amount back ensuring the financial upliftment of the person.

The other NGO's work with the help of self help groups (SHG's). Thus we can categorize the organizations engaged in providing credits to the needy as

- Wholesalers – NABARD, Rastriya Mahila Kosh (New Delhi)
- NGO's – directly providing credits (SHARE Hyderabad/ASA – Trichy/RDO – Loyalam Bank – Manipur)
- NGO's – providing credits with the help of SHG's & SHG federation. (MYRADA – Bangalore/SEWA – Ahmadabad/ PRADAN – Tamilnadu)

Measures taken by other South Asian Nations for low income groups & deprived class.

➤ **The Grameen Bank (Bangladesh)**

This concept is the brain child of Prof. (Dr.) Mohammad Yunus of Chittagong University who reasoned that women after a hard day

labor earn a very little amount and he thought about a model to uplift their economic and social status with this concept he established Grameen Bank in Bangladesh. The bank has more than 1000 branches, covering 28000 villages and 12 Lakh borrowers (more than 90% are women). One branch covers 25-30 villages, 240 groups and around 1200 borrowers. The most important features of this bank is that the recovery of loans is as high as 98% and on top of that it provides credit without any "collateral security". The system followed by Grameen bank is simple yet effective. In order to get loans, potential borrowers have to form a group of five and conduct weekly meetings for loan repayment. At the start of the weekly meeting they chant "16 Decisions". In fact these decisions are a part of the basic code of conduct that the members will follow in their day today life.

These decisions are focused towards production of fruits and vegetables in kitchen garden, improvement of the education of children, not to support dowry in marriages, use of safe drinking water among others. The group members are encouraged to take risk and new initiatives and they are provided different kind of help and support. The loan repayment is on weekly basis spread over 12 months and a simple interest is charged @20% at the end of the year. An interesting feature in this model is that it is mandatory for every member to save one taka/week which is collected in the group fund.

Amount collected on account of indiscipline by a members of the group is also collected in the group fund and this amount is then deposited in the Grameen Bank. A member can borrow money from this account for sickness, social ceremony or contingency. Normally these loans are provided without interest. Factors behind the success of Grameen Bank are trust, peer pressure, ensuring regular income, weekly collection is small amounts, weekly meetings and compulsion in savings.

➤ **Linking banks with self help groups (Indonesia)**

During the era of financial liberalization in Indonesia during 1988, the Central Bank supported a pilot project involving 13 Banks, 12 NGO's and 420 Self Help Groups (SHG). In this program the self help groups were supported to lend 60% of their funds to the borrowers and 40% was to be deposited in Bank. The members were encouraged to do some savings as this would become a base for furthering borrowing. Interest to be charged to borrowers would be at market rate and will be decided by the SHG's. There will be incentives for timely repayments or early repayments.

➤ **Pag IBIG fund (Philippines)**

Pag IBIG fund is a government owned, controlled and highly stable financial fund. Pag stands for Pagtulongan sa Kinabukasan (partnership for future) Ikaw (you), Banko (Bank), Industriya (Industry) Gobyerno (government). As on now it has over 1.2 million members with huge fund base of US \$ 800 million. The fund is in the form of provident saving fund and housing credit system for wage earners. To empower the fund a National shelter program was started and a home development mutual fund (HDMF) was started as a separate entity to provide fund for housing. The membership to this fund was compulsory but exemptions were granted to employees who already were members to any program offering similar or superior benefits.

Members were allowed to withdraw their savings after 20 year membership on certain grounds. Thus Pag IBIG helped people in a great way by pooling the funds of people of the country and helping the needy for housing.

The case of Pag IBIG is discussed in this paper to understand the success model of pooling the funds/resources of society and passing the benefits to the deprived class.

Now to develop a better mechanism for India we need to understand the strength of the informal sector and the weakness of formal sector so that if these two sectors come

together and they can utilize the strength of each other to create an economic balance.

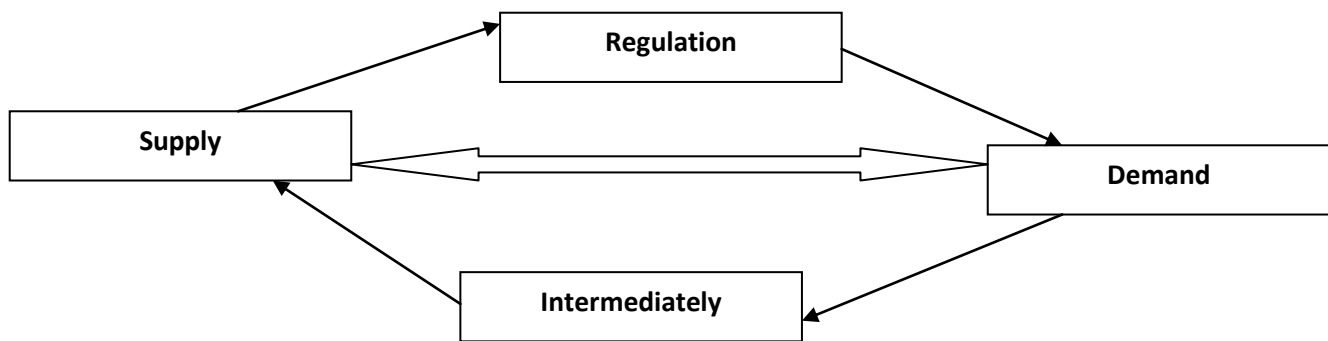
• **Strength of informal sector**

- a. A better knowledge of local need and geography
- b. In touch with the borrowers in a better manner
- c. Have the funds
- d. Better monitoring mechanism

• **weakness of informal sector**

- a. Higher rate of interest
- b. No standard polity for all
- c. No support or empowerment program
- d. Unorganized way of dealing

A good system with reference to financial institutions has to be based on demand & supply balance, strong regulation and a dedicated & a reliable intermediately.



Conclusion

Now a better mechanism has to be developed to utilize the strength of informal sector and the strength of the existing financial institutions. This can be done by involving informal sector people like Sahukars and local operators into the system of organized financial institutions and microfinance organizations. This can be done effectively by taking the help of the government Financial institutions, NGO’s & other bodies by designing a flexible yet highly effective mechanism. The learning can be taken by the highly successful financial bodies of the world engaged in similar cause like the Grameen Bank of Bangladesh, the linking banks & the self help groups of Indonesia and the Pag IBIG fund of Philippines and can be incorporated in our system. Above learning also prove that funding/financial/banking on poor can surely be a profitable business. A careful research on demand for financing and saving behavior of the potential borrowers and their participation in determining the mix of multipurpose loans are essential in making the concept work (tall 1996). For microfinance institutions to be successful in our country they have to increase the credit worthiness of the poor and they have to be made more “bankable” so that

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