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A Case Study on Micro Financial Institutions – Effective Tool for Alleviating Rural Poverty in India

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Abstract:

Micro financial (MFI's) are extremely important in helping the underprivileged and low-income people in a nation like India, where 70% of people reside in rural areas and 60% of people are employed in agriculture according to the data of World Bank. The case study aims to highlights significance of microfinance in developing nations like India, where a sizable portion of the populace lives in poverty and lacks access to regular banking services. The Self Help Groups (SHGs)-Bank Linkage Program and Microfinance Institutions (MFIs) are the two main techniques that define the microfinance sector in India. The Self Help Groups (SHGs)-Bank linkage initiative, which aims to give the unreached poor a cost-effective way to receive financial services, is the main player in microfinance in India. The purpose of this case study is to assess the current state and contribution of microfinance to India's growth by elevating the economic conditions of rural population.

Keywords: MFI's, SHGs (Self Help Groups), Poverty Alleviation.

Introduction:

In India, the microfinance sector was established in 1970s to give the underprivileged access to loans. It is now expected to meet the basic financial necessities of the majority of the population who live under poverty bracket in rural India. This industry has successfully broken through long-standing societal conventions of social seclusion and brought people closer to the mainstream. The goal of microfinance is to expand the boundaries of financial service delivery by offering financial services to the underprivileged who are not catered to by traditional formal financial institutions. Such financial services must be provided, and this calls for creative delivery strategies and channels. The requirement for financial services that enable consumers to manage their resources more wisely and to seize opportunities.

In India the numerous useful instruments available for reducing poverty, microfinance can be one. It should be utilized cautiously, though, as the relationship between microfinance and reducing poverty is not simple due to the complexity of the problem and the numerous obstacles that the impoverished face generally. Understanding the right time and manner of microfinance for the poorest is crucial, as the goods, delivery system, and technique all have an impact on the possibility and promise of reducing poverty. Although, in Indian economy microfinance is a crucial tactic for meeting rural residents' needs and including them in the socioeconomic development process in order to significantly raise their standard of living Approximately 350 million people are estimated to be living below the poverty level throughout India. If social investment went toward building hospitals or schools, toward developing and supporting local businesses that employ people year-round and give them a stable income, or toward social movements that advocate for fair and equitable access to land for farming, better social and economic outcomes could be realized.

The primary obstacle faced by the impoverished when attempting to obtain loans from official financial institutions is the requirement for collateral that these organizations make. Furthermore, obtaining a loan involves numerous bureaucratic processes that result in additional transaction expenses for the underprivileged. There is no incentive for formal banking institutions to lend them money. Formal financial institutions typically favor large-scale transactions over small-scale ones, loans for non-agricultural purposes over those for agricultural purposes, and urban over rural areas. For the following reasons, formal financial institutions are not very motivated to lend to the impoverished in rural areas.

Whereas, microfinance is becoming a significant credit partner for the impoverished in developing countries and is thought to be able to lessen the aforementioned shortcomings of formal and informal financial institutions. Microfinance has improved clients' lives and given impoverished people more capacity to improve their circumstances. Some have even reported that impoverished people have used their additional income to enhance their level of consumption, maintain better health, and accumulate assets. [1] When it comes to reaching out to the rural poor through efficient distribution channels, MFIs are more proactive and creative than the traditional banking system.

Microfinance has been shown to be one of the most successful methods for reducing poverty because community banks, non-governmental organizations, grassroots savings and credit groups, and others around the world have shown that these microenterprise loans are profitable for both lenders and borrowers.

Review of Literature:

Microfinance is characterized as an economic development instrument in the Indian context, with the aim of helping the impoverished overcome their poverty. It encompasses a wide range of services, including lending as well as numerous other services including savings, insurance, money transfers, counseling, etc. Microfinance is the practice of giving very low-income families little loans, or micro-credit, to support their small enterprises or productive endeavors. As all parties involved have realized, microfinance has expanded over time to include a wider range of services (credit, savings, insurance, etc.) because the poor and extremely poor do not have access to traditional formal financial institutions and need a variety of financial products that are tailored to their specific needs. The microcredit interventions were crucial in lowering vulnerability by promoting responsible consumption, accumulating assets, offering emergency support, and empowering women in India.

Self-help groups' microfinance program is helping to reduce poverty in a sustainable way, and rural women's standards of living have significantly improved in terms of their ability to borrow money, accumulate assets, save money, and engage in income-generating activities. [2]

As previously mentioned, the majority of research on the effects of microfinance in India has concentrated on the country's west and south. These Indian regions saw a lot of microfinance and scholarly research on the socioeconomic upliftment of those living below the poverty line.

Economic measures of poverty may highlight its structural elements, but they fail to account for its cultural, social, and psychological components. More significantly, they deny the impoverished any agency by disregarding their means of resistance, social networks, and survival tactics. [3]

Microfinance institutions differ greatly from charities, despite having as their sole goal reducing poverty in poor nations. Higher interest rates are associated with the repayment of loans by borrowers. [4]

Microfinance provides financial assistance to low-income individuals, including those living in rural areas, low-income clientele, and small company owners with little capital to operate their enterprises. In this approach, microfinance helps those who struggle to get funding expand their businesses by giving them financial support. Increasing employment through microfinance-supported small business operations in India is unquestionably a positive step in the fight against poverty. [5]

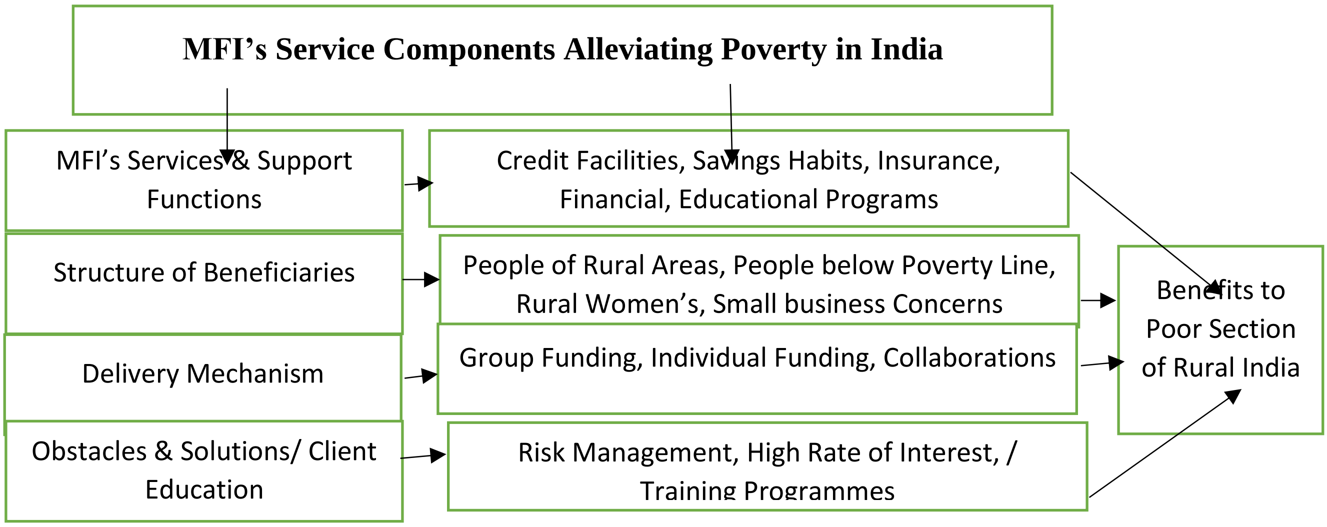
In India, there are numerous government and non-government microfinance organizations that operate and meet the requirements of the populace. Numerous cooperative societies also strive to offer the public microfinance. The emergence of several organizations in the form of microfinance institutions has narrowed the gap between the supply and demand of those in need. The biggest MFIs in India are SHARE, SPANDANA, CDF, MYRADA, SKS, and PREM; they offer low-income individuals financial services.

An examination of the microfinance institutions' performance in India. An Indian study sheds light on a number of microfinance initiatives. The many microfinance models used in India, as well as the function and significance of microfinance in reducing poverty, empowering women, promoting social welfare, etc. According to the study's findings, microfinance plays a significant role in reducing poverty in India, and the RBI and Central Government frequently intervene to support the sector's growth. [6]

This research paper provides an overview of microfinance in India. It draws attention to the development of inclusive financial systems, the history of microfinance, microfinance in India, and the issue of microcredit in developing nations. Finally, the author highlights that while microfinance may seem appealing to investors, there are a number of warning signs. For example, while MFIs might be successful investments, they also carry a number of hazards, and the field of microfinance has received little research. [7]

Conceptual Frame Work of MFI’s in Alleviating Poverty in India

By offering financial services that help low-income people better their economic situation, their quality of life, and their ability to contribute to larger social and economic growth, microfinance institutions play a critical role in reducing poverty in India. MFIs empower vulnerable people, encourage entrepreneurship, and support sustainable development by providing access to loans, savings, insurance, and financial education. But in order to ensure their ongoing success and influence, they must handle issues including high default risk, operating expenses, and regulatory compliance.



MFI's Services & Support Functions:

- **Credit:** Small loans to promote income-producing endeavors and entrepreneurship,
- **Savings:** Using bank accounts to promote and facilitate saving behaviors.
- **Insurance**: The offering of risk-reduction goods like life or health insurance.
- **Financial education** is the study of money management and financial literacy.

Structure of Beneficiaries:

- **Low-income** families are made up of people who make less than the federal poverty threshold.
- **Women:** Because of their ability to contribute economically and their role in managing households, women are frequently the main emphasis.
- **Micro- and small-scale** business owners are known as small business owners.

Delivery Mechanism:

- **Groups:** Providing loans through cooperative models or self-help groups to improve support among members and lower risk.
- **Individual Loans:** Outright loans given to borrowers who have demonstrated their creditworthiness.
- **Collaborations:** Working together with regional NGOs, authorities, and civic groups.

Obstacles & Solutions/ Client Education:

- **Elevated Chance of Default:** Risk management involves putting creditworthiness assessments and risk assessment processes into practice.
- **Group Lending**: Reducing defaults by mutual guarantees and peer pressure.
- **Costs of Operations**: Efficiency Gains: Cutting expenses by using technology and simplifying processes.
- **Funding:** Obtaining financial support for operating expenses via investors, grants, and subsidies. **Instruction for Clients:** Ongoing Financial Education and Assistance: Ensuring that clients are able to handle their finances well requires constant training.

- **Policy and Regulatory Environment:** Compliance: Following rules and pushing for laws that support the operations of microfinance.

Failures of MFI's:

When viewed from the outside, the microfinance sector seems to be a useful tool for promoting economic opportunity and combating injustice. Actually, there are a number of shortcomings that have diminished numerous investigations. Whether microloans truly assist borrowers in escaping poverty has emerged as the central query. In certain regions where there is a significant economic divide, providing basic necessities such as food and medicine is the most important first step in helping the underprivileged society. Even while it's critical that these economically distressed communities have access to financial assistance, others have questioned if microfinance initiatives will be sufficient to address the pervasive poverty that exists in these emerging nations. [7]. Microfinance institutions differ greatly from charities, despite having as their sole goal reducing poverty in poor nations. Higher interest rates are associated with the loan repayment that borrowers are required to make. These borrowers frequently get temporary relief, but when their payments increase, they are left with considerably more debt and more financial strain. Furthermore, increased regulation is required by the business to guarantee that borrowers are receiving the proper help. Employees of MFIs are frequently given sales incentives, which frequently results in overlanding to people who cannot afford the loans.

Growing Establishment of IMF's in Rural India:

Table 1: MFIs in India States/UTs and No. of Districts with MFI Operation- Year 2020

Name of the States /UTs	No. of MFIs operating in the state (including those having Head Quarters outside)	No. of districts of the state where MFIs operate	No. of Branches
Andaman Nicobar Islands	3	1	1
Andhra Pradesh	3	12	66
Arunachal Pradesh	4	4	11
Assam	21	28	344
Bihar	33	37	692
Chandigarh	3	1	4
Chhattisgarh	20	22	306
Delhi	10	6	33
Goa	4	2	10
Gujarat	18	24	257
Haryana	17	19	190
Himachal Pradesh	4	4	9
Jammu & Kashmir	1	1	1
Jharkhand	20	24	263
Karnataka	23	30	1218
Kerala	16	12	261
Madhya Pradesh	34	48	907
Maharashtra	41	36	808
Manipur	5	10	38

Meghalaya	8	5	18
Mizoram	4	8	26
Nagaland	3	2	3
Odisha	28	30	744
Puducherry	7	2	10
Punjab	10	22	173
Rajasthan	22	29	352
Sikkim	2	3	8
Tamil Nadu	35	34	1152
Telangana	5	6	11
Tripura	9	6	39
Uttarakhand	20	6	117
Uttar Pradesh	28	68	1067
West Bengal	41	21	1097
Total		**563**	**10,233**

Table-2: Rural and Urban Share of MFI Borrowers

Year	**Rural**	**Urban**	**Total**
2016	184 (67)	91 (33)	275 (100)
2017	185 (56)	145 (44)	330 (100)
2018	122 (33)	249 (67)	371 (100)
2019	152 (38)	247 (62)	399(100)
2020	180(61)	115(39)	295(100)

Table 2 display the distribution of MFI borrowers by rural and urban areas. Indian microfinance was mostly thought to be a phenomena found in rural areas. Rural clients accounted for 67% of the total in 2016, down from 56% in 2014 and 33% in the most recent year.
In the year 2018. The percentage of rural clients grew slightly to 38% in the following year, or 2017. Urban clientele has surpassed rural clientele for the first time. But in the upcoming year
i.e., the percentage of rural clients climbed to 61% in 2017, indicating a notable improvement. Due to the removal of six, the shift from rural to urban in 2017 is the opposite of that from 2016.

Table-3 Performance indicator of MFIs Model in India

Particular	**2019**	**2020**
Client outreach (Lakhs)	399	295
Women client (%)	97%	96%
Gross O/S Portfolio (crore)	63853	46842
Average loan per borrower (crore)	11425	12751
Income generation loan (%)	94%	85%
Margin (%)	10%	8.08%
ROA (%)	2.20%	2.4%
ROE (%)	11.60%	13.31%

OSS (%)	113%	114%
CAR (%)	19.39%	21.13%
NPA(%)	0.15%	0.69%

An overview of microfinance institutions' overall performance in 2019 and 2020 was provided in Table 3. According to the table, there was a 26% decrease in client outreach in 2019 compared to 2020. Nevertheless, the outreach to women fell from 97% to 96% of the total. The average loan per borrower has increased by 11.60 per cent during this period in 2019, while the gross outstanding portfolio has decreased from Rs. 63,853, crore to Rs. 46,842, crore, or by roughly 27%, during this period in 2018 over 2019. In 2016, 94% of all loans were income-generating loans; by 2017, that percentage had dropped to 85%. The corresponding indicators

Conclusion:

It is impossible to overstate the significance of microfinance in developing nations like India; it is essential to the socioeconomic advancement of the underprivileged. Reducing poverty has become a top focus at the national and international development levels since the 1990s. The government has undertaken a number of projects under this framework. The effectiveness of microfinance as a strategy for socioeconomic development and poverty reduction has drawn attention.

Any nation's potential to thrive economically is greatly impacted by its financial services availability. A wide range of financial services, including deposits, loans, payment processing, money transfers, insurance, savings accounts, microcredit, and more, are provided to the underprivileged and low-income population through microfinance. An economy with a strong financial system has more investment options. Thus, in order to guarantee inclusive and sustainable growth, the Indian government must concentrate on providing financial services to both rural and urban areas. Over the past twenty years, the functioning of microfinance banks in India has been crucial for rural communities. The RBI and the national government should take the appropriate action to maintain the expansion of India's microfinance industry. The concerned state governments also take the appropriate actions to educate the public about the benefits of using microfinance organizations to raise one's economic standing and standard of living.

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