



# MICROFINANCE IN IMPROVING OF NATIONAL ECONOMY ESPECIALLY IN INDIA

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## Abstract:

In a developing country and with 2<sup>nd</sup> largest populated country of the world (approx 1.38 billion population in 2022), out of that 65% are belonging from rural area and only 35% are belonging from urban area. More than 50% of the total populations are unemployed during 2012-2020. Highest unemployment rate found in the 2<sup>nd</sup> quarter of the year 2020 (approx 63.6%) due to COVID-19 pandemic.

Now, Microfinance (MF) is a backbone for improving of national economy of India as well as self-dependent by the way of providing financial inclusion to poor and low income groups. It works as a tool for socio-economic upliftment, empowering women and increasing the household income of rural part of India. In other word, it is a tool for development and reduces poverty.

*Reason behind to write this paper is that analysis of comparative growth of financial services in rural areas and growth of Microfinance Institutions (MFIs) as well as banking sectors in rural part of India.*

**Key Words:** MFI, COVID, MF, SEWA, SHG, NABARD, JLG, GDP, MFIN, NCAER, RFAS

## Introduction

Microfinance is a part of banking services, which provides financial services to low income group/people for their self dependent, who are beyond to access other financial services. MFIs are mainly found in developing nations like India.

In a developing country, financial services through formal channel do not meet the demand of the people who are belonging from rural areas. So, MF provides financial inclusion through sanctioning small amount of loans for short term period (usually less than one year). At the time of sanctioning of loans, microfinance institution did not retain any securities against the loan because MF is subject to Joint Liability Group (JLG).

## History of Microfinance

In 18<sup>th</sup> century, small operation of Microfinance is existed in Irish, introduced by Sir Jonathan Swift for improving economic condition of Irish citizens. In 1970s MF become popular on large scale, after receiving the attention by “Grameen Bank” of Bangladesh, which was started in 1976 by Prof. Muhammad Yunus.

MF introduces in India in 1980s as a tool to reducing poverty and empowers women. Self Employed Women Association (SEWA) Bank of Gujarat took first initiative to introduce MF in India by providing financial inclusion to poor, illiterate and lower section of the society. In 1992, National Bank for Agricultural and Rural Development (NABARD) started Self Help Group Bank Linkage Programme (SHG-BLP) as a pilot project for financial inclusion and economic development.

## Objective of Microfinance

MF plays a vital role of financial inclusion in India. Reducing poverty and empowering women is one of the most important objectives of MFIs. Promoting socio economic development at grassroots level by the way of providing various skill training like floriculture, horticulture, mushroom farming etc. and also grant the small loan for startup the business. Now MF becomes a backbone for socio economic development, upliftment standard of living of rural people and growth of national economy as well as Gross Domestic Product (GDP) of the country.

## Research Methodology

In my research paper, I used primary data as well secondary data for gathering relevant information/data. Primary data are collected by enquiry at branch office of different MFIs at various places and Govt. offices for enquiry about SHG. Secondary data is collected from internet previously published articles and yearly/quarterly report of NABARD and Microfinance Institution Network (MFIN).

## Growth of microfinance in India

Now there are broadly two models of MF found in India:

- Self Help Group (SHG) models
- Microfinance Institution (MFI) model

**Self Help Group (SHG) models:** SHGs are a voluntary association of 5-20 members (Specially Women) for achieving a collective goal. This concept first found in “Grameen Bank” of Bangladesh, which was started in 1976 by Prof, Muhammad Yunus.

In India, NABARD initiated in 1991-92 as a pilot project for the financial inclusion specially women members of SHG. There was only 225 SHG found in the year 1992. The ministry of Rural Development, Govt. of India, continuously work for the development of rural areas through various scheme/yojana, SHG is also one of the most important and successful yojana among others. Within two decades, around 112 lakh SHGs are found across the country in the financial year 2020-2021 (according to the NABARD report FY 2020-2021).

SHG provide different skill development training like horticulture, floriculture, advance agriculture process, Handicraft etc. as well as sanction small amount of loan through various banks for setup of business and self dependent.

**Microfinance Institution model:** In India basically Joint Liability Group (JLG), Grameen Bank model and Rural Cooperatives model are found. Some brief descriptions about MFIs model are as follows:

**Joint Liabilities Group (JLG):** It is an informal group consist 4-10 members in a group having mutual guarantee against the loan, that is, each and every members of the group are equally liable for such credit or loan. If one member of the group is unable or fail to pay installment, such installment must be pay within due date by others member of the group.

Basically, this type of loan or credit facilities offered by private finance companies like, Larsen and Turbo (popularly known as L&T), North east Finance Ltd., Bandhan Finance Ltd. etc.

As of may 2021, 94 NBFC had registered with RBI to run Microfinance. Among them, Bandhan Financial Service Pvt. Ltd (now Bandhan Bank Ltd.) is the largest MFI in India, which was started in 2001 as a MFI and registered in 2006 on NBFC and recognized as a bank in the year 2015.

Bharatya Samridhi Finance Ltd (BSFL) is the oldest NBFC-MFI of India, which was started in the year 1997 by Vijay Mahajan of Andra Pradesh. Now this MFI is collapsed due to high amount of bad loan.

**Grameen Bank Model:** This type of model introduce by Prof. Muhammad Yuns in the Grameen Bank of Bangladesh. In India, this model is also adopted in form of Regional Rural Bank (RRB), which was founded in 2<sup>nd</sup> October 1975. It comes under the ownership of Ministry of Finance, Govt. of India with 50% share, Nationalized Bank with 35% of share and State Govt. holds only 15% of total shares.

**Rural Cooperatives:** Rural Cooperatives provide short term as well as medium and long term agricultural loan. There are the three levels of mobilizing loan, that is, for the village-level, Primary Agricultural Credit Society (PACS), for the district-level, Central Cooperatives Banks (DCCBs) and for the state-level, State Cooperative Bank.

Rural Cooperative Banks of MFI model mainly focused on agricultural and agricultural related purpose only. This model is very unsuccessful model of Govt. of India in terms of financial inclusion, due to various limitations such as information gap between bank and public, high amount of Non Performing Assets (NPA), more competitive environment etc.

### **Product of Microfinance**

There are mainly three types of products found in Microfinance Industry of India, namely Micro-loans, Micro-savings and micro-insurance. Some brief description of those products as follows.

**Microloan:** Micro-loan is the main product of MFIs and it provides short term loans with no collateral, i.e without any security or mortgage against loan. If MFIs found that a person with good repayment record, MFIs allow for drawing loan with more amount than previous loan's amount. As of now, in India, more than 3000 MFIs (both registered and unregistered) provide microloans.

**Microsaving:** Usually microsaving product of MFIs related with Rural Bank and cooperative banks. Microsaving bank account allow to use saving account with no minimum balance (i.e Zero balance) to promote financial discipline and develop on interest in saving for future are the main objective of Microsaving account. "Pradhan Mantri Jan Dhan Yojana is the best example of Microsaving account, which is introduced by Honorable Prime Minister Narendra Damodardas Modi on the occasion of 68<sup>th</sup> independent day (15<sup>th</sup> August 2014).

**Microinsurance:** This type of insurance is cheaper than other insurance (i.e lower premium than traditional insurance premium). Protection of loan amount from borrower's mishap that might be taken place in future (eg: Accident, Chronic disease etc.) is the main objective of microinsurance.

### **Impact and contribution of microfinance in Indian Economy**

People use or draw loan from various financial institution including microfinance for business purpose or allied activity (including consumption purpose of the person) or for emergency requirement. But, according to Rural Finance Access Survey (RFAS) conducted by World Bank associated with National Council of Applied Economic Research (NCAER), there is some upward trending change in income level and standard of living of the person after receiving various facilities (including loan) from SHG and other MFIs.

Members of SHGs contribute a small amount fund at regular interval as a saving of group, it allow self-fund management and provide financial services among members, in addition to that, loan and other facilities are also there. According to NABARD report (FY 2021-22), there are total 13.8 crore household included in SHG with the loan disbursement of Rs. 2,01,118/- crore.

Microfinance industry's Gross Loan Portfolio (GLP) and as well as clients increases gradually Year-by-Year. GLP grew approx 15% from FY 2020-21 to FY 2021-22, that is from 3163 billion in 2020-21 to 3627 billion in 2021-22.

In microfinance industry more than 85 thousand employees engaged during the year 2016 and around 1.28 crore employees engaged during the financial year 2018-19 and more than 1.5 crore employee engaged during the financial year 2021-22.

Annual growth rate of the overall economy is measured by Gross Value Added (GVA) of the country. Financial services of the country contribute around 5.5% of GVA in the Indian economy and out of which microfinance sector contribute around 2.03%. There are some MFIs which play vital role for contribution of country's GDP but those institutions are no longer existence (according to report of NCAER).

### Challenges faced by Microfinance in India

In India, MFIs face various challenges during the business. Challenges vary different parts of the country, according to Geographical Demography, political Environment and Human Behavior etc. Some challenges are mainly faced by MFIs in almost all parts of the country are as follows:

- **Bad Loans:** In India, there is an upward trending graph line of bad loans and its lead Non Performing Assets (NPA) year after year. Hence, bad loan is main challenge faced by MFIs. For an example Indian's first MFI "Bharatya Samaradi Finance Ltd." was collapsed which was started by Vijay Mahajan in 1997 and followed by numbers of MFIs are available Indian.
- **Financer:** Bank usually have multiple product with an assured deposit structure, whereas MFIs deals with a single product , that is providing loan only and not deal with public deposit. Hence MFIs are highly dependent on market for funding or anchor investor. Without an anchor investor or financer, MFIs cannot grow independently and facing different obstacles during sanctioning and disbursement of loans.

- **High Rate of Intrest:** MFIs charge comparatively high rate of intrest with respect to bank's rate of intrest because MFIs did not asked for any securities or mortgage against loan. Hence there is high possibility of bad loan, that is high risk of non repayment of loan which leads NPA.

## Conclusion

Achieve full employment is one of the most important objective of fiscal policy of India. Other industries of the country are also focused for providing employment to unemployed youth and reducing unemployment and poverty. Apex institution like NABARD, SIDBI and other institution are engaged in infrastructure development through various channels. New opportunities and challenges are found in every field of business or other development projects. MF also cannot escape from new opportunities and challenges which are described in the above. With the passage of time, microfinance industry provided employment (directly and indirectly) in increasing trend. In the Financial year 2019-20, 128 .46 lakh employments are provided by Microfinance Industry (as per report of NCAER) along with the contribution of approx 2.03% of GVA of Indian economy.

From the analysis of this research paper, we can say that, contribution of Microfinance Industry play the important role towards the growth of Indian economy as well as GDP of the Country, through providing employment (directly and indirectly) and granting loans for starting small business for their self dependent and improvement of family income.

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