MICROFINANCE: THE PATH TO POVERTY ERADICATION IN RURAL INDIA

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Abstract : Microfinance stands as one of the most promising and cost- effective tools in the fight against global poverty. Microfinance is being practiced as a tool to assault poverty the world over. Microfinance is the provision of financial services to low – income clients, including consumers, and the self- employed, who traditionally lack access to banking and related services. Microfinance Institution (MFIs) are those, which provide thrift, credit and other financial services and products of very small amounts chiefly to the poor in rural, semi urban or urban areas for enabling them to raise their income. The poor can also obtain essential entrepreneurship and risk management skills through training and information sessions provided by microfinance institutions, foremost to an overall improvement in their human capital.

Key words: Micro finance, Poverty eradication, India, Microfinance Institutions, Rural Finance

INTRODUCTION

In the developing country like India, wherever greater part population resides in rural areas, rural development becomes vital for the economic development of that nation and rural development, poverty diminution needs to be the focus of each and every one development programs. During, the government of India has been imitating varies poverty alleviation programs since independence but not to a great extent development has been manifest. The basis reason of the problem of poverty has been the fund to be economic dependence and lack of access to the credit. Poor have been considered to be non bank able. They are depriving of the fundamental financial services in the lack of saving and collateral to be offered to the financial poverty, specially the banking sector. Therefore, the poor have to be depending upon the casual channels of finance like private moneylenders who usually, exploit them in the name of financial assist and frequently, lead to life time indebtedness among the borrowers. Micro finance is one such intrusion that aims a poverty diminution by providing fundamental financial service to the underserved section of the society at affordable. Microfinance is also considered as a tool for socio-economic development.

Numerous studies available on the characteristics of rural banking credit markets in India and the spread of in the post independence period. Numerals of studies start with the all India Rural Credit Survey in 1954; found that the rural poor had high levels of indebtedness and very limited bank access. The state bank of India was set up in 1955 as facilitator to provide banking services to poor population, the 14 large commercial banks were nationalized in 1969, and the National Bank for Agriculture and Rural Development (NABARD) was created in 1982. All of the nationalized banks is deputed the role of lead banks in particular parts of the country and they are limited to uphold justified ratios of urban and rural branches. Many cooperative banks and regional rural banks are created first and foremost to cater credit require of poor population in India.

The credit policy for the poor involves a lot of practical difficulties arises from operation followed by financial institutions and the economic characteristics and financing requirements of low-income households. For example, commercial banking institutions need that borrowers have a steady source of income out of which principle and interest can be paid back according to the agreed stipulations. Nevertheless, the income of a lot of self employed households is not steady. An enormous number of micro loans are needed to serve the poor, however banking institution prefers dealing with big loans in small numbers to minimize administrative expenses. They also look for collateral with a clear title- which numerous low-income households do not have. In addition bankers tend to consider low income households an awful risk imposing extremely high information monitoring costs on operation. In this context, following questions are raise previous to us.

- Is there necessitate for a new institution?
- Should it operate all India or in a state?
- What are methodological issues?
- Who will be its beneficiaries?

Microfinance operates through two channels in India

- Microfinance Institutions (MFIs)
- NABARD's SHGs bank linkage programme (SBLP) – a partnership model between SHGs, banks and NGOs

Prominent Features of Micro-Finance Programme of Government of India

- **Arranging Fixed Deposits for MFIs/NGOs:** In this scheme government of India arrange money to MFI/ NGO like SIDBI for micro credit to poor.
- **Training and Studies on Micro-Finance Programme:** Government of India would assist SIDBI in assembly the training needs of NGOs, SHGs, intermediaries and entrepreneurs and also in enhancing consciousness about the programme. Institution building for 'intermediaries' for identification of viable projects: The government of India would assist in institution building through identification and development of 'intermediary organization', which would assist the NGOs/SHGs in identification of product, preparation of project report, working out frontward and rearward linkages and in fixing marketing/ technology tie-ups. The SISIs would assist in the identification of such intermediaries in dissimilar areas.
- **Budgetary provisions For the Scheme through 10th plan:** There was a budgetary provision in 10th five year plan and hoping more funds in next plan.
- **Administrative arrangement:** A committee has been formed to manage and monitor the administrative arrangement of MFI/NGOs.

Microfinance Terminology

- **Micro credit:** This is a little amount of money loaned to a client by a bank or other institution. Micro credit can be offered, frequently with no collateral, to an individual or during group lending.
- **Microfinance:** This refers to insurance, saving, loans, transfer service and other financial products targeted at low- income clients.
- **Micro insurance:** This is a system via which people, businesses and other organizations make payment to share risk. Entrance to insurance enable entrepreneurs to concentrate more on increasing their business whereas mitigating other risks affecting correctly, health or the capability to work.
- **Remittances:** These are transfer of funds from people in one place to people in another, generally across borders to family and friends. Compared with other sources of money that can vary depending on the political or economic climate, remittances are a relatively stable basis of fund.
- **Micro saving:** These are deposit services that permit people to store small amounts of money for future use, frequently without minimum balance necessities. Saving accounts permit households to save small amounts of money to meet unanticipated expenses and plan for future savings such as old age and education. Comprehensive financial sectors: It allows poor and low-income people to access credit, remittances, insurance and saving products. In numerous countries, the financial sectors do not provide these services to the lower income people. A comprehensive financial sector will support the full contribution of the lower income levels of the population.
- **Micro entrepreneurs:** These are people who personal small scale business that is identified as micro enterprises. These businesses generally employ less than 5 people and can be based out of the home. They can give the sole source of family income or supplement other forms of income. Distinctive micro entrepreneur activities include retail kiosks sewing workshops, market stalls and carpentry shops.
- **Bankable:** These people are those deemed eligible to acquire financial services that can lead to income generation, saving, building of assets and the reimbursement of loans.

- **Unbanked:** This describes people who have no access to financial services through any type of financial sector organization such as banks, non- bank financial institution, financial cooperatives and credit unions, finance companies, and NGOs. Implicit in this definition is that financial services are generally obtainable only to those individuals termed "economically active" or bankable.

Microfinance Institutions usually have the following characteristics

- Providing small loans for the working capital necessities of the rural people.
- Minimal appraisal of borrowers and savings as compared to commercial bank.
- No collateral demanded; nevertheless, these institutions impose compulsory saving and group guarantees.
- Based on loan reimbursement history of the members, microfinance institution extend large loan to the members.

Microfinance Provides are classified into Three Categories as follows

- **Formal Sector:** It covers the whole banking industry including all public, private, regional rural banks, RBI and NABARD.
- **Semi-formal Sector**: It covers each and every one exclusive micro financing institution, varies self help groups (SHGS) and NGOs.
- **Informal Sector**: It covers family friends, relatives, moneylenders, pawnbrokers, traders and landlords etc.

Usually, microfinance products are categorized under three heads- micro saving, micro credit and micro insurance. The term micro credit is frequently used in place of micro finance itself. However micro credit is just one facet of micro financing concept which means to provide micro loans to the low income group people, it covers a extensive variety of loans for consumption as well as production such as housing loans, agricultural loans, education loans, loans for small and medium enterprises, it is just the credit and saving facet of the microfinance that has developed in the current years. Micro insurance is immobile in the process of development. Micro insurance products include health insurance, life insurance and crop insurance.

Role of Microcredit in Poverty Eradication in India

Microfinance is about providing financial services to the poor who are not served by the conservative formal financial institutions – it is about extending the frontiers of financial service provision. The provision of such financial services requires innovative delivery channels and methodologies.

The requirements for financial services that permit people to both obtain benefit of opportunities and better management of their resources. Microfinance may be one effectual tool among numerous for poverty mitigation. Nevertheless, it must be used with caution – in spite of recent claims, the equation among microfinance and poverty alleviation is not straight – frontward, because poverty is a multifaceted phenomenon and numerous constraints that the poor in common have to cope with. There are need to understand when and in what form microfinance is apposite for the poorest; the delivery channel, methodology and products offered are each and every one inter- linked and in turn affect the prospect and promise of poverty mitigation. Access to formal banking services is complicated for the poor. The major problem the poor have to take when trying to obtain loans from formal financial institution is the demand for collateral asked by these institutions. In addition, the process of acquiring a loan entails a lot of bureaucratic procedures, which lead to additional transaction costs for the poor. Formal financial institutions are not aggravated to lend money to them. In general, formal financial institutions demonstrate a preference for urban over rural sectors, large- scale over small scale transactions, and non- agricultural over agricultural loans.

Formal financial institutions have small incentives to lend to the rural poor for the following reasons:

- **Administrable difficulties:** Small rural farmers frequently live geologically scattered, in areas with poor communiqué facilities, making loan administrative not easy.
- **Systematic risks:** Agricultural Production is connected with few systematic risks, such as floods and drought, which is reflected in a high covariance of local incomes.
- **Lack of Information:** The nonappearance of standardized information, standard lending tools, such as credit histories or financial statements, does not exist in these areas.

· **Reimbursement problems:** The reimbursement of working capital may be necessary merely once a year for example through the harvest season. On the other hand, access to informal loans is comparatively simple, available and convenient locally to low income households for the following reasons:

· Informal moneylenders use interlinked credit contracts to diminish default risk such as development of business relationship with the clients.

· Informal moneylenders have local information which helps them to appraise credit requirements and credit worthiness of the client.

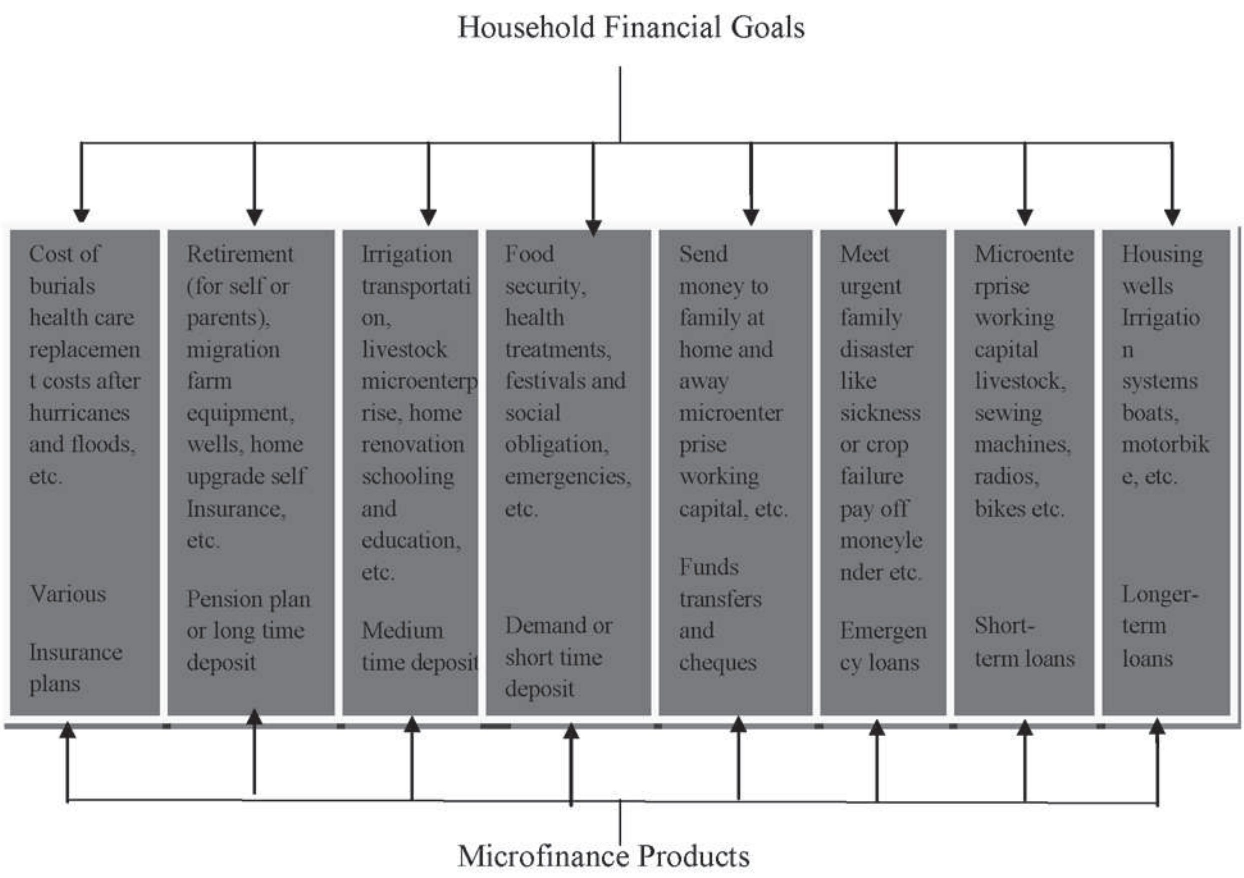
· Informal moneylenders are considering the requirements and necessities of clients even for small amount of loan.

· Informal moneylenders will profit from social sanctions such as those that may exist among members of a family. These sanctions can serve as a substitute for legal enforcement.

· Informal moneylenders utilize specific incentives to stimulate reimbursement, such as repeat lending to borrowers who pay back promptly, with progressively rising loan size.

In spite of the fact that a lot of rural poor obtain their loans from the informal financial sector in rural areas of developing countries; the sector has some basic confines. An ordinary feature of numerous rural communities is that much of the local information does not flow freely; it tends to be segmented and circulates merely within specific groups. Generally the informal credit market is based on local economies and is thus limited by local wealth constraints and the covariant risks of the local surroundings. Since the majority of the world's poor do not have access to fundamental financial services that would assist them manage their assets and generate income. To conquer poverty, they require being able to borrow, save and invest, and to defend their families against adversity.

Types of Microfinance used by poor people



Source: Brett Matthews, Mathwood Consulting Company

Few Schemes of a Government of India

There are a lot of schemes for the upliftment of poor in India. One of them Micro- credit programmes is sprint first and foremost by and SIDBI in the field of Industry, Service and Business (ISB) and NABARD in the field of agriculture. The success of Micro - credit programme lies in diversification of services. Micro Finance Scheme of SIDBI is under operation since January, 1999 with a corpus of Rs. 100 crore and a network of about 190 capacity assessed rated MFIs/NGOs. Under the programme, whole amount of Rs. 191 crore have been sanctioned upto 31st December, 2003, benefiting over 9 lakh beneficiaries. Under the programme, MFIs /NGOs are supposed to give equity support in order to avail SIDBI finance. However they find it complicated to manage the required equity support because of their poor financial situation. The problem has got provoked due to moribund interest rate on deposits. The office of the development commissioner the constraints (Small Scale Industries) under Ministry of SSI is launching a new scheme of Micro Finance Programme to conquer the constraints in the existing scheme of SIDBI, whose reach are at present extremely low. It is felt that Government's role can be critical in expanding reach of the scheme, ensuring long term sustainability of MFIs /NGOs and development of Intermediaries for recognition of feasible projects.

CONCLUSION

Microfinance and microcredit have received widespread acknowledgment as a strategy for poverty eradication and for economic empowerment. Microfinance is a way for fighting poverty, particularly in rural areas, where the majority of the world's poorest people live. The scheme of Micro - finance has been found as an effectual instrument for lifting the poor above the level of poverty by providing them increased self- employment opportunities and making them credit worthy. Accessing small amounts of credit at sensible interest rates provide poor people an opportunity to set up their own small business. There is a necessitate of Designing financially sustainable models and increase outreach and scale up operations for poor in India. People belongs to villages are still uninformed about banking policies and credit system. So NGO should converse to them and share their view with villagers. Banks must convert and build up professional system into social banking system for poor. Government of India and state governments must also provide support for capability building initiatives and make sure transparency and augment credibility during disclosures.

It shows that access and efficient provision of microcredit can enable the poor to smooth their consumption, gradually build their assets, develop their micro enterprises, better manage their risks, enhance their income earning capacity and enjoy an improved quality of life. Microfinance services can also contribute to the enhancement of resource allocation, promotion of markets, and adoption of improved technology; consequently, microfinance helps to promote economic growth and development.

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