

Microfinance and Rural Development in India

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Abstract

It is an established fact that the main problem of the rural world is poverty which made to be evaluated for social justice and development. In the developing countries of the world, 40% of the population lives in absolute poverty. Improvement in the living condition of the rural areas can be achieved by enlarging employment opportunity, extending public services and through these means improving the levels of living and enhancing the quality of life. Rural development is driving force of the entire development process and lies at the heart of the National development. Rural development thus involves improving the living standards of subsistence level population, ensuring participation in development, activities and making the development process self-sustaining.

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I. Introduction of Microfinance

The term "Microfinance," can be referred as financial service that provides small loans as well as other related financial services to poor and low-income households in a consistent and legitimate way. It is an economic tool designed to promote financial inclusion, which enables marginal and low-income households to overcome poverty, increase their family income, and improve their overall living standards. It can facilitate the achievement of national policies that target poverty reduction, women's empowerment, assistance to vulnerable groups, and an improvement in the standard of living. Microfinance can play as one of the tool to reduce the rural poverty not only in India but also in the other developing nations of the world. As we are also a developing nation and penetration of financial system at micro level will act as is vital for rural development.

Microfinance can also be defined as substitute assistance of formal bank for underprivileged with low income and unemployed fraction of population with services such as lending, setting up bank accounts and providing micro-insurance products. As we know that credit plays a pivotal role in increasing production, income and fostering and equitable, distribution of increasing rural income. In developing countries like India, financial services through formal channel do not meet the demands of rural poor, so microfinance can provide flexibility to underprivileged.

The definition of microfinance with respect to amount varies between countries. In India, generally all loans that are below 1 lakh can be considered under micro-finance. Microfinance enables economically disadvantaged individuals to obtain the small-scale capital they are need to start up viable income earning business.

Broadly, two different approaches are followed in India for extending microfinance services:

- The bank-led approach, Self-Help Groups-Bank Linkage Program (SHG-BLG),
- The Micro Finance Institution (MFI)-led approach

II. Historical Background

Microfinance started as a global movement in the early 1980s to provide credit access to underprivileged population with low income. From then to now this industry has shown significant transformation with the creation of self-regulatory organisations, formulation of structured guidelines, digital advancements and redefined customer service approach. This led to a significant boost in the loan portfolio and consequently number of borrowers. This industry has grown tremendously and today, the global microfinance industry is worth over INR 8.90 trillion with the loan disbursed amount growing at an average annual rate of 11.5% over the last five years. This industry has impacted the lives of 139.9 million borrowers worldwide, 80% whom are women and 65% from rural population.

The initial phase of Micro-financing can be traced back as long as to the middle of the 1800s. Lysander Spooner, a theorist wrote about the benefits for small credits to entrepreneurs and farmers as a way getting people out of the poverty. At the end of World War 2 with the Marshall plan the concept became bigger.

The word microfinance has started its roots in Asia in 1970s when organisations such as Grameen Bank of Bangladesh was established under leadership of Mohd. Yunus. He conferred with Noble Peace Prize for his contributions in Microfinance in 2006.

Another pioneer in this sector in South Eastern Asia is Dr. Akhtar Hameed Khan. He led the way in rural development and poverty alleviation. He was founder of Bangladesh Academy of Rural Development (BARD) in the year 1959 and Orangi Pilot Project (OPP) in Karachi, Pakistan in the year 1980.

At that time a new wave of microfinance initiatives introduced many new innovations into the sector. 'Shorebank' was the first formal microfinance bank founded in 1974 in Chicago.

The history of microfinance in India can be traced back to the early 1970s when the first attempts were made to provide small loans to poor people who lacked access to credit from traditional sources. The modern microfinance movement in India, however, began in the mid-1980s with the establishment of NGOs (non-governmental organizations) like MYRADA, PRADAN and BASIX, which pioneered the concept of providing financial services to the poor. One of the most significant milestones in the history of microfinance in India was the establishment of the Self Employed Women's Association (SEWA) Bank in 1974. SEWA Bank was the first microfinance institution in India and was set up with the primary objective of providing financial services to poor women. Over the years, SEWA Bank has become one of the most successful microfinance institutions in India, providing a wide range of financial services to millions of poor women.

Another major milestone in the history of microfinance in India was the launch of the National Bank for Agriculture and Rural Development (NABARD) in 1982. NABARD was set up with the objective of providing credit facilities to rural areas and promoting rural development. NABARD played a crucial role in promoting microfinance in India by providing refinancing facilities to microfinance institutions and introducing policies and guidelines for regulating the microfinance sector.

In the 1990s, microfinance in India saw significant growth with the emergence of new microfinance institutions like SKS Microfinance, Spandana Sphoorty, and Share Microfin. These institutions adopted innovative lending methodologies like group lending and pioneered the use of technology to improve efficiency and reduce costs.

Present Scenario of Microfinance

In recent years, microfinance in India has faced several challenges, including concerns about over indebtedness and high interest rates. However, microfinance continues to be an important tool for poverty alleviation in India, and several initiatives are underway to strengthen the microfinance sector and ensure its sustainability in the long run.

Today the World Bank estimates that more than 16 million are served by some 7000 microfinance institutions all over the world. In a gathering at a Microcredit Summit in Washington DC, the goal was set to provide microcredit to 100 million world's poorest people.

To achieve this goal, the year 2005 was proclaimed as the International year of Microcredit by the economic and social council of the United Nations. The major goals of International Year of Microcredit were:

1. **Raise awareness:** The International Year of Microcredit aimed to raise awareness among individuals, governments, and organizations about the potential of microcredit to help in alleviation of poverty.
2. **Promote best practices:** The International Year of Microcredit aimed to promote best practices in microfinance, such as transparent lending practices, fair interest rates, and client protection.
3. **Increase access:** The International Year of Microcredit aimed to increase access to microfinance services for the poor, especially in developing countries.
4. **Encourage innovation:** The International Year of Microcredit aimed to encourage innovation in microfinance, such as the development of new financial products and services that could better meet the needs of poor households.

Microfinance Institutions

Financial organisations that provide Micro-finance are called Micro-Finance Institutions. Mostly, these organisations are non-profit organisation but it also includes commercial banks and other financial institutions. Microfinance is access of services like Credit, Savings, Insurance and Pensions. These financial services are meant

to help them in undertaking economic activities, mitigating vulnerabilities to income shocks, smoothening consumptions, increasing savings habits and supporting self-empowerment.

India's microfinance sector is divided into Microfinance Companies, Non-Government Organisations (NGOs) and Commercial banks. The top 10 Microfinance companies in India account around 74% of total loan outstanding. Currently, this sector has a total loan portfolios worth USD 1.785 trillion and loan disbursal at a rate of 20% in terms of volume. This growth can be attributed to the rapid evolution of regulatory reforms, mass adaptation of UPI-based payments, developments in small finance banks and several initiatives by the Government and regulatory authorities.

The NABARD (The National bank for Agriculture and Rural Development), in keeping with its role as an apex institution in the field of rural credit with a mandate for ensuring integrated development of the rural economy, has been working to build a more meaningful link between the development plan at the district level and the process of credit planning for supporting agriculture and rural development. The NABARD has introduced a very important tool of microfinancing in rural areas i.e. the Self Help Group model to further enhance financial inclusion of the excluded segments. With the primary objective to connect the informal workforce to the formal banking sector, the SHG employ their members through the agency of Banks. The bank issues credit against the groups' guarantee and size of loans could be multiple times that of resources deposited with the banks. NABARD is responsible for refinancing such credits, and the progress made by this initiative is reflected in 102.43 lakh savings-linked SHGs covering about 12.4 crore households in India by March-end 2020(12).

The main objective of MFIs is to provide small loans to purchase productive assets, boosting the poor's revenue allowing repayment over short period of time in small instalments without taking collaterals. The services/products provided by microfinance institutions can be divided into following categories.

1. Microloans:

The loans provided by Microfinance institutions are significant as these are provided to borrowers without any collateral. The end result of microloans should be to have its recipient outgrow smaller loans and be ready for traditional bank loans. It offers a better overall loan repayment rate than traditional banking product. It enhance the possibility of future investments as it is a sustainable process. It gives people confidence in availing and repaying it which leads to non-stressful life.

2. Microsavings:

Micro savings accounts are those accounts which are remain operative with no minimum balance. These accounts help users to learn financial discipline and develop an interest in saving for future. The poor people and small businessman with low income can operate their account with no minimum balance.

3. Microinsurance/ Pensions Schemes:

Microinsurance is a type of coverage provided to borrowers of microloans. These insurance plans have lower premiums than traditional insurance policies.

The importance of microinsurance is that it is the machinery to protect the poor people from all the mishap that might take place in furture, example : Accidents, chronic disease etc. It addresses to all kind of risks that people of low income group or poor people face globally.

4. Micro-Pension Schemes: Atal Pension Yojana formerly known as Swavalamban Yojana is a government-backed pension scheme primarily targeted at the unorganized sector. In order to incentivize people to enroll in this scheme and widen its reach, the government announced that it would co-contribute 50% of the total contribution or maximum ₹1,000 per annum, whichever is lower, to each eligible subscriber account, for a period of 5 years. Only subscribers who had enrolled in APY between 1 June 2015 and 31 March 2016, and were not beneficiaries of any social security schemes, besides not having any taxable income were eligible for this co-contribution. The minimum eligible age for a person to join APY is 18 years and the maximum is 40 years. An enrolled person would start receiving pension on attaining the age of 60 years. Therefore, a minimum period of contribution by the subscriber under APY would be 20 years or more.

III. Conclusion

The challenge of rural development is enormous due to persistent poverty, complex social stratification, unsatisfactory infrastructure and weak governance; problems that are well known, but not well understood. An effort is needed to change this perception and to search for real solutions and strategies to meet development challenge must be considered in the light of India's overall development agenda. The performance lags seriously behind national trends and is a significant contributing factor to the growing income gap across states. If rural people do not enter the mainstream of national economic growth and prosperity, its performance disparities will continue to widen significantly.

Microfinance is one of the prominent tool to eradicate poverty with relation to rural household. Microfinance changed the habit of small saving which enable them to borrow from financial institution which leads to free them from moneylender. Microfinance has enabled rural women to build up their economic

contribution towards their households thus in this way microfinance played an important role for empowerment of rural women.

The main goals of microfinance can be enlisted as:

1. Target to poor for poverty alleviation.
2. Increasing income through self-employment.
3. Fiscal sustainability through micro-finance institutions.
4. Act as a tool of women empowerment.

Overall, microfinance has provided important contribution to the development of rural mass. As savings is vital and perhaps more important to poor and the poorest and microfinance cater this goal as well. Microfinance prove itself useful tool in fight against poverty. The people of rural areas have very low access to the institutionalized credit, so deep invasion of microfinancing institutions works as a boon for the people living in rural areas which help them to have stability with respect to their financial issues.

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