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   HYPOTHESES

   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

   CONCLUSIONS

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MICROFINANCE IN FINANCIAL INCLUSION

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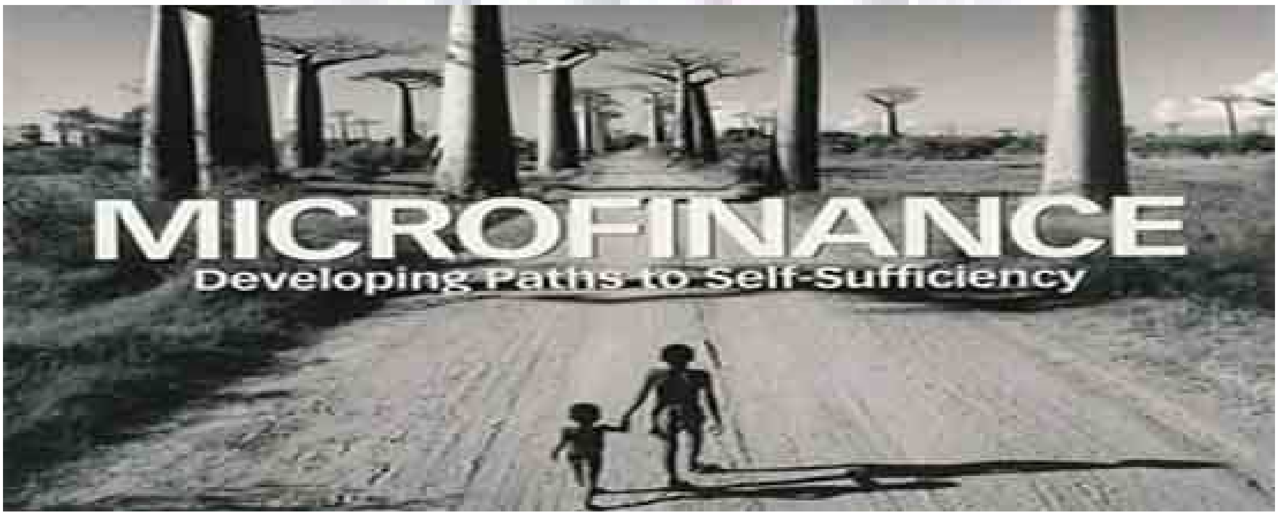
ABSTRACT
Micro-finance refers to small savings, credit and insurance services extended to socially and economically disadvantaged segments of society. Indian context terms like "Small and Marginal Farmers", "Economically weaker sections "have been used to broadly define micro-finance customer. Large part of micro finance activities is confined to credit. It is effective intervention for the poverty alleviation. It therefore, holds promise to further the agenda of financial inclusion as it seeks to reach out to the excluded category of population fro banking system. Financial Inclusion (FI) is enabling access to/delivery of banking services at an affordable cost to the vast sections of disadvantaged and low-income groups. Unrestrained access to public goods and services is the sine qua non of public policy of a nation. As banking services are in the nature of public service, provision of banking and payment services to the entire population without discrimination should be the prime objective of the public policy. Large size and population of around 1000 million, India's GDP ranks among top 15 economies of world.Around300 million people or about 60 million households are living below the poverty line. Group of micro finance practitioners estimated the annualize credit usages of all poor families about Rs45000crores of which some 80 percent is met by informal sources. Credit on reasonable terms to poor can bring a significant reduction in poverty. About 60 million households below or just above the austerely defined poverty line and with more than 80 percent unable to access credit at reasonable rate. There are certain roles of microfinance in the development of economy. Microfinance institution are engaged in deposit taking in order to mobilize household saving, they became financial intermediaries. Consequently financial regulations become necessary to ensure the solvency and financial soundness of institution and to protect the depositors. Excessive regulations that do not consider the nature of microfinance institution and their operation can hamper their viability. Micro finance institution have expanded frontiers of institutional finance and have brought the poor, especially poor women into formal finance system and enabled them to access credit and fight poverty. Some significant strides have made in upscalling the large quantities of microfinance, observed that microfinance had an asymmetric growth across country with diverse rate of interest being charge to member which are area of concern. There are some agencies which provide bulk funds to system through NGO. Organization engaged in micro finance activities in India may be categorized as wholesaler, NGOs supporting SHG and NGOs directly retailing credit borrowers or group of borrower. Wholesalers will includes agencies like NABARD, Rashtriya Mahila Kosh, New Delhi and Women's world Banking,ASA in Trichy, RDO Layalam Bank in Manipur. There are some agencies which provide bulk funds to system through NGO. Organization engaged in micro finance activities in India may be categorized as wholesaler, NGOs supporting SHG and NGOs directly retailing credit borrowers or group of borrower. Wholesalers will includes agencies like NABARD, Rashtriya Mahila Kosh, New Delhi and Women's world Banking,ASA in Trichy, RDO Layalam Bank in Manipur. Microfinance can contribute to solving the problem of inadequate housing and urban service as an integral part of poverty alleviation programs. Microfinance institutions have a lot of contribution to this by building financial discipline and educating borrowers about repayment requirements.

KEYWORDS
Microfinance, Credit, Banking.

INTRODUCTION
Micro-Finance is emerging as a powerful tool, reaching to poor household yet to reach by Formal Financial sector. It is effective intervention for the poverty alleviation. It therefore, holds promise to further the agenda of financial inclusion as it seeks to reach out to the excluded category of population fro banking system.Financial inclusion (FI) is access the service at an affordable cost ton the vast section of low-income groups.

FIG. 1



Micro-finance refers to small savings, credit and insurance services extended to socially and economically disadvantaged segments of society. Indian context terms like "Small and Marginal Farmers", economically weaker sections have been used to broadly define micro-finance customer. Large part of micro finance activities is confined to credit.

Microfinance also refers to small scale financial services such as micro-saving, micro credit and micro-insurance to the people who operate micro enterprises which generate income and allowing them to meet financial needs and emergency. These short term loans are enough to start or expand business, weaving baskets, raising chicken or buying wholesale product to sell in the market. The aspect of microfinance has contributed to its success of its credit plus approach where focus has not only been on providing adequate timely credit to low income groups but to integrate it with other development activities such as community organizing and development, leadership, training, skill and entrepreneurship. The ultimate aim is to attain social and economic empowerment. The microfinance program has major impact on improving living standard of poor people.

The institutions, united under the banner of "microfinance", share a commitment to serving clients that have been excluded from the formal banking sector (ibid). According to National Sample Survey Organization's (NSSO), 59th Round (2003), only 48.6 per cent of the total number of cultivator households received credit from both formal and informal sources (financial inclusion in a broader sense) and remaining 51.4 per cent did not receive any credit (total financial exclusion). In the same survey it is further revealed that 22 per cent of the cultivator households received credit from informal sources (financial inclusion in narrow sense). Only 27.6 per cent of the farmer households has availed credit from the formal institutions like banks, cooperatives and government (Jeromi, 2006). Further, a Rural Finance Access Survey 2003, conducted by the World Bank and NCAER, revealed that 79 per cent of the rural households have no access to credit from formal sources (Basu, 2005). Hence, the tasks of microfinance are the promotion of greater financial inclusion2 and in the process improve the social and economic welfare of the poor.

Large size and population of around 1000 million, India's GDP ranks among top 15 economies of world.Around300 million people or about 60 million households are living below the poverty line. Group of micro finance practitioners estimated the annualize credit usages of all poor families about Rs45000crores of which some 80 percent is met by informal sources. Credit on reasonable terms to poor can bring a significant reduction in poverty. About 60 million households below or just above the austerely defined poverty line and with more than 80 percent unable to access credit at reasonable rate. The micro credit summit campaign reports that 14.2 millions of the world's poorest women now have to access to financial services accounting for nearly 74 per cent of the 19.3 million poorest served women. There are certain roles of micro-finance in economic development.

MFI's DIFFERENT MODES

Microfinance sector has covered a long journey from micro savings to micro credit and then to micro enterprises and now entered the field of micro insurance, micro remittance, micro pension and micro livelihood.

Micro-savings: These are deposit services that allow one to save small amounts of money for future use. Often without minimum balance requirements, these savings accounts allow households to save in order to meet unexpected expenses and plan for future expenses.

Micro credit: Micro credit is the extension of micro loans to the unemployed, to poor entrepreneurs and to others living in poverty that is not considered bankable. Micro credit can be offered, often without collateral, to an individual or through group lending. Region Rural Banks was created to take the banking services to poor people. They focus on credit rare than savings & insurance. RBI in its Annual Policy Statement for the year 2005-06.RBI has introduced the basic banking *'no frills'* account either with nil or very minimum balances as well as that would make such accounts accessible to vast section of population. General Purpose Credit Card (GCC) facility is issued by bank without insistence on collateral, with a revolving credit limit up to Rs25, 000 based on cash flow of household. RBI has set up Special Committee to advanced financial inclusion.

Micro-insurance: It is a system by which people, businesses and other organizations make a payment to share risk. Micro insurance products are mainly targeted at low income groups in the unorganized sector-farmers and craftsmen. The amount of premium in these schemes ranges Rs.200 to Rs.500. the finance ministry recently considered two schemes- _Aam Admi Bima yojna' to extend death and disability insurance and _Rashtriya Swasthya Bima Yojna', a health insurance scheme for below poverty line families .

MICRO FINANCE AND DEVELOPMENT GOALS

The implementation of Micro finance can make an important contribution to achieve the development goals such as **Poverty alleviation** – by borrowing, saving in insurance, the poor can build & diversify income sources, reduce the vulnerability by investing in assets. By using microfinance to invest in business opportunity the poor can have more stable income flows, reduce the poverty. **Primary Education** – house access to microfinance are sending their children to school. Improvement in income and better access to credit & saving can reduce the need to rely the child labors. **Women empowerment** - It helps to build the self-confidence, resulting in great decision making power, control over assets & mobility with broader community. **Environmental stability** – Microfinance helps to promote environmentally sustainable business and household practices. The considerable amount of microfinance provided for agriculture purpose, there is scope for financial service providers to take a lead in advocating environmentally sustainable practices.

GROWTH OF MICROFINANCE IN INDIA

During the financial year 2007-2008, microfinance in India through its two major channels-SHG-linkage-bank and MFI served over 33 millions India up by 9 million over the previous financial year and 4 out of 5 microfinance clients in India are women.

TABLE 1

Particulars	2002	2003	2004	2005	2006	2007	2008
No of new SHG provided with Bank Loan	461478	717360	1079091	1618456	2238565	2924973	3477965
No of new SHG Financed during the year	197653	255882	361731	539365	620109	686408	552992
Rate of growth of loan to new SHG(%)	32	29	41	49	15	11	(-16)
No of SHG Receiving repeat loans	41413	102391	171669	258092	344502	457410	186883
Rate of growth of repeat loan	91	147	68	50	33	33	Incomplete
Proposition of repeat loans to total loan	17	29	40	32	36	40	11
Bank loan disburse during year(cr)	545	1023	1855	2994	4499	6643	4228
Bank loan disburse to new groups(cr)	453	691	4458	1727	2330	3044	2542
Bank loan disbursed as repeat loan(cr)	92	332	693	1268	2169	3599	1686
Average loan size new	22919	27005	32013	32019	37574	44343	45960
Repeat loan size	22215	32425	40660	49130	62960	78682	90195

The table shows the growth of MFI in India. The MFI draws mostly capital from the private banks, SIDBI and foreign investors. The number groups that have borrowed from bank increase to 3.48millio and extent of finance availed is increased to 42.28billion.

FORMAL AND INFORMAL SECTORS IN INDIA

FORMAL SECTORS

The formal sector banking institution in India have been serving only the needs of commercial sector and providing loans for middle and upper income groups. For housing the HFIs primarily perceived risk of lending to this sector. Risks generally perceived by formal sector, Financial Institutions are credit risk, High transaction and services cost, Irregular flow of income due to seasonality, Lack of tangible proof of assessment of income, Absence of land tenure of financing housing. Formal Financial Institutions are concerned are Commercial Banks, Housing Finance Institution(HFI),NABARD, Rural Development Banks(RDB),Land Development Banks and Cooperative Banks(CBs).

The government has taken several initiatives to strengthen the institution rural credit system. The rural branch network of commercial banks have been expanded and certain policy prescriptions imposed, in order to ensure great flow of credit to agriculture and other preferred sectors. The commercial banks are required to ensure that 40% of total credit is provided to priority sectors out of which 18% in the form of direct finance to agriculture and 25% to priority sector in favor of weaker sections besides maintaining a credit deposit ratio of 60% in rural and semi urban branches. Further IRDP introduction in 1979 ensure supply of credit and subsidies to weaker section beneficiaries.

INFORMAL SECTORS

Informal sectors generally include funds available from family sources or local money lender. Local money lenders charge exorbitant rates, generally ranging from 36% to 60% interest due to their monopoly in the absences of any other source of credit for non-conventional needs.

NGOs engaged in activities related to community mobilization for their socio-economic development have initiated saving and credit program for their target groups. Community based financial system (CBFS) can be categorized into two models. Group base financial intermediary and NGO linked financial intermediary.NGOs like SHARAN in Delhi, FEDERATION of THRIFT AND CREDIT ASSOCIATION (FICA) or SPARC have adopted first model where they initiate groups and provide necessary management support.SEWA pertain to second model.

Experience of these informal intermediaries shows that although saving of group members, small in nature do not attract high returns, it is skill practiced due to security reasons. Most of loans are unsecured. Personal or group guarantees or other collaterals like jewellery is offered as security. There are some agencies which provide bulk funds to system through NGO. Organization engaged in micro finance activities in India may be categorized as wholesaler, NGOs supporting SHG and NGOs directly retailing credit borrowers or group of borrower. Wholesalers will includes agencies like NABARD, Rashtriya Mahila Kosh, New Delhi and Women's world Banking,ASA in Trichy, RDO Layalam Bank in Manipur.

PROGRAMMES TARGETED AT LOW INCOME GROUPS

GRAMEEN BANK IN BANGLADESH

Grameen Bank lending system is simple but effective. To obtain loans, potential borrowers must form a group of five; gather once a week for loan repayment meetings and to start with learn the bond rules and "16 Decision", which they chant at start of their weekly session.There decision incorporate code of conduct that members are encourage to follow in their daily life, e.g.: production of fruits and vegetables in kitchen gardens, investment of improvement of housing and education for children, safe drinking water for health,etc.For this physical training are held at meeting.Key-unit in credit program is first necessary step to receive credit. Initially loans are providing to individuals in group, there were under pressure from other members to repay the loan. Credibility of group members and benefits in term of new loan will be stopped if any one default to repay and the group members are fined or expelled a member if they fail to attend the meeting.

FINANCIAL MODEL FOR SELF-HELP GROUPS

SHG-MGI SYSTEM

Typical SHG consist of 12 or 30 member. It is not only saving and loan association but serves as "affinity" group that provides platform for issues. SHG is system raises funds from individual and also from MCI. MCI arise fund from three sources: Capital, SHG saving and borrowing from outside and MCI have regulatory restriction on assets, liabilities and interest rates.

Some of the principles underlying that were issued to implementing:

- SHG use almost 60% for lending to their members and rest for depositing.
- Joint liability of members is to serves as substitute for physical collateral and saving are to come first.
- Interest rates on saving and credit for members are market rates to determine locally by participating institutions.
- All NGOs and SHGs will charge an interest margin to cover their costs.
- SHGs may levy an extra charge to interest rate of internal fund generation which will force saving.

CHALLENGES OF MICROFINANCE

The importance of microfinance in the process of poverty eradication is realized, it faces multiple problems. Offering financial services to poor individual and in it leads to various challenges. Challenges are divided as

CHALLENGES TO MICRO ENTREPRENEURS

1. Inability to offer marketable collateral for loans - They are either small businesses or poor individual who have few assets and low income. These clients have cannot offer any collateral for loans. Due to this microfinance providers may raise their interest rate or turn down hundreds of application.
2. Poor institutional viability of micro enterprises - Business ideas with a lack of consideration of demand and cost render the micro venture unsustainable and microfinance may incorrectly get blame for it. For instance, In the case of micro crop farming farmer often fail to account for their personal consumption between the sowing and harvesting periods and realize they face shortage of more. Due to this they often end up using the micro loan for personal matter and problem arises when its time to pay back the loan, farmer are forced to take another loan.
3. Knowledge regarding sources of microfinance is lack - Many micro entrepreneurs live in remote villages, so they have no access to microfinance service offered by MFIs.
4. Misallocation or shortage of finance - Lack of fund, which can solve if MFIs build up their capital base by accessing various sources of funds without fund micro ventures, cannot grow.
5. Inability to exploit growth opportunities - Shortage of finance is a contributor to this problem, because lack of access to funds means micro entrepreneurs cannot inject money into their business to grow. They may have little information pertaining to their market such as customer needs and competitor strengths and weakness, this may result May critics.
6. Lack of organizational resources and governance - They may have limited skill, qualification and exposure to handling business. They need to be trained through capacity building initiative by MFIs; many micro entrepreneurs may not grow because of this problem.
7. Low bargaining power - Micro entrepreneurs operates in competitive markets, their individual bargaining power is diminished. There still isn't any respite because micro entrepreneurs deal with MFIs on individual basis, which also erode their bargaining power.

Most problems faced by micro entrepreneurs are caused by small size, improper skill, and location. When venture secures loan and begins to grow these problems will eventually.

CHALLENGES TO MICROFINANCE PROVIDERS

The importance of microfinance in the process of process of poverty eradication is realized, it faces multiple problems. The challenges to microfinance providers are

1. High risk of micro entrepreneurship and small business - Micro entrepreneur usually no collateral to offer microfinance providers, no alternate source of income. Micro entrepreneurs are considered high risk ventures and micro finance providers are forced to compensate for this by changing interest rate.
2. High costs for Micro Lending - Small micro enterprises increase the transaction cost for MFIs, because they cannot process micro loan in bulk. In study conducted by Asian Development Bank, Microfinance providers change interest rate ranging from 30 to 70% per year.
3. Fund shortage - There are plenty of financial options available for MFIs there is an emerging shortage of money. This is due to lack of awareness of funding source by MFI managers.

4. Difficulty in measuring the social performance of MFIs - Micro finance is delivering the economic returns its proponents promised but there are only a handful of tools available that measure the social return of microfinance.
5. Mixing of charity with business - If microfinance providers fail to protect themselves against loan delinquency, they will in effect, prioritize social at expenses of financial sustainability. Improper delinquency management is result of inadequate implementation of corporate governance principle. As result loses control over microfinance deals will lead to higher default rates.
6. Lack of solution for poor - Targeting of poor households by microfinance programs is common problem because MFIs fail to understand the various needs of micro entrepreneurs. MFI must spend time to develop microfinance tools for each micro entrepreneur.
7. Lack of microfinance training for MFIs - Micro finance sector is different when compare to traditional financial sector, microfinance providers need special training to ensure they avoid problem such as under-serving clients.
8. Poor distribution system of MFIs and lack of information about microfinance investment opportunities.

CHALLENGES TO WOMEN

Micro-finance has been successful in supplying production loans to women; these initiatives may produce negative results

1. The workload may lead to poor health, exhaustion and overwork.
2. The problem of male influence is one of the most difficult challenges related with women as micro-finance clients.
3. They turn the money to their husband, rather than using for business and Even after the disbursement of loan they don't know how to use it.
4. The domestic responsibilities of women consume major portion of time and spend on this enterprise.

CONCLUSION

All these problems can broadly fall into either financial or operational in nature, they should not be impossible to solve as microfinance sector move towards its optimal performance level in next several years. Microfinance can contribute to solving the problem of inadequate housing and urban service as an integral part of poverty alleviation programs. Microfinance institutions have a lot of contribution to this by building financial discipline and educating borrowers about repayment requirements. Micro Finance have more opportunity if the state Reduced direct involvement, increased outlays, Structuring of outlays and finding right outlets, Creating incentives and regulatory environment for implementation. The micro-finance also proved it to the success of women empowerment. In the recent years micro-finance programs have confined themselves to distribution of loan to women, but the receipt of loan and utilization of loan helps in improving the economic status of women. The bank would have to evolve specific strategy to expand the outreach of their services in order to promote the financial inclusion. One of the way in which this can be achieve in cost-effective manner is through forging linkage with microfinance institution and local communities. Financial inclusion can emerge as commercial profitable business in future.

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