

Deepening Micro-finance

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ABSTRACT

Micro-finance in India has been in the news for all the wrong reasons, unfortunately. Micro-finance need not be looked upon in the manner the Reserve Bank of India (RBI) defines it or other government agencies look upon it. Such an outlook is uncalled for at least in the Indian context. Such an outlook gives rise to avoidable controversies, mutual recriminations and confusion in the investing community and the end-users of micro-finance as well.

1. Introduction

If micro-finance is looked upon as a modest financial help extended to economically vulnerable sections of society so they can eke out their livelihood with honour and dignity, it will do immense good for the country as a whole. Unfortunately, it is not to be.

Instead of creating dedicated institutions to finance economically weaker sections of society if the government and the central bank of the country can come out with policies that make it easier for bankers to disburse loans to the weaker sections of society in a timely and hassle-free manner, the purpose will be served.

2. Review of Literature

1. Rajan Alexander in "What's wrong with Micro-finance Institutions? Practically everything as the case of SKS illustrates" rightly states that when we started out on the country's development a couple of decades ago, we instinctively targeted to reduce the influence of moneylenders, if not eliminate them completely. The reason was that they were seen as the traditional oppressors and exploiters in society. Their powers often overlapped with those of their caste and traditional village leadership. On the other hand, micro-savings and revolving loans often worked very well. Self-Help Groups (SHGs) being small and homogeneous, were controlled by members where borrowers themselves played a key role in the development of SHGs. They contributed small savings, regularly attended the meetings and participated in making rules related to loans, interest rates, repayment schedules and mechanisms. These groups were thus more likely to be characterised by self-management and self-reliance.

However, it all changed once the much-hyped micro-finance institutions (MFIs) arrived. They started easing out NGOs on the specious argument that the SHGs were not equipped adequately for the purpose, given their limited capability to run micro-finance lending programmes. The MFIs believed that access to

expensive credit was better than no credit and at the observed rate, demand equalled supply. Ironically, they are the same principles that guide the traditional money lenders. Then how can MFIs be superior to the traditional moneylenders?

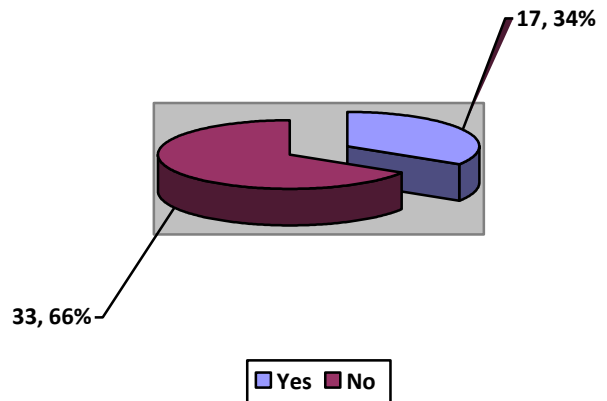
2. Sriram M S¹ in "What is wrong with Indian Microfinance" argues that the microfinance industry is now stuck in its own web, although the industry hailed itself as the savior of the poor. From people carrying a sling bag on their shoulders and dressed in a khadi kurta, the microfinance industry has moved up market either to suits or FabIndia kurtas. A notebook has replaced the sling bag. In about a decade, microfinance has moved from helping the poor in accessing finance at a competitive price to an interesting business at the bottom of the pyramid. This paradigm shift happened with the entry of funding, initially from Silicon Valley, and then from the people who funded and fuelled the growth of Silicon Valley. Somebody from Silicon Valley would typically be an entrepreneur who started small, scaled up fast, used the asymmetries in the market and logically and legally became rich. Many were first generation entrepreneurs and did not forget their roots. It was logical for them to invest their surpluses into the business of rendering service to society. However, their own success and experience dictated that while they do good, they should also do well. Doing well translated into good business plans, targets and also growing at a scorching pace. All was well for us, within the industry, when the base was small. There were several 100 percents in the microfinance sector. The growth rate was in excess of 100 percent, recovery was 100 percent and the sustainability indices quickly crossed 100 percent. Voila, we had found a magic mantra where the poor could be served, we could look good and put "eradication of poverty" as our mission statement and of course, lead a

¹ What's wrong with Microfinance Institutions in India ?, India Microfinance Business News, dated May 5, 2010

comfortable life. The alternative sources that were funding the poor made us look like messiahs. Now things have deteriorated to such a state that many state governments strongly suspect that MFIs are the traditional moneylenders masqueraded as MFIs.

No	33	66
Total	50	100

Figure-1
Window dressing on the part of the beneficiaries



It is clear from the foregoing Table and Figure that 17 of the 50 beneficiaries admit that they resort to window dressing. 33 maintain that they do not resort to window dressing.

34% of the beneficiaries resort to window dressing.

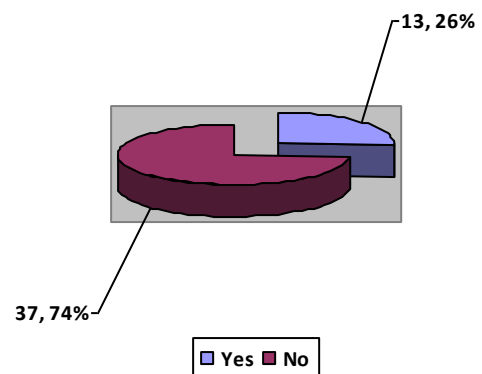
Are MFIs no different from the traditional moneylenders?

It is increasingly argued that MFIs are the traditional moneylenders masqueraded as MFIs in the sense that they charge usurious rates of interest and employ coercive methods to recover the money lent. The researcher sought the views of the respondents on the subject. Their replies to the query appear in the following Table and Figure.

Table-2
Are MFIs no different from the traditional moneylenders?

Are MFIs no different from the traditional money lenders?	No of Respondents	Percentage
Yes	13	26
No	37	74
Total	50	100

Figure-2
Are MFIs no different from the traditional moneylenders?



It is clear from the foregoing Table and Figure that 13 of the 50 beneficiaries believe that MFIs are no different from moneylenders. 37 of the 50 beneficiaries do not believe so.

The researchers have clinically analysed the status of the microfinance industry today. Every word they have uttered about the microfinance industry is true. In fact they must have gone to the extent of stating that MFIs are nothing new to the Indian milieu. They existed and still exist in another form. The extant framework can be fine-tuned to match the MFIs in terms of fulfilment of the professed objectives. The researchers could have suggested how to go about it. It is this gap that the present study seeks to bridge.

3. Data Collection & Research Methodology

The methodology applied is analytical in nature. It analyses the problems that the MFI beneficiaries face in the confusing scenario that the MFIs find themselves in today.

Data required for the research has been collected from both primary and secondary sources. Primary data has been collected from 50 beneficiary respondents who have been availing of financial assistance from MFIs. Secondary data has been collected from reputed journals, magazines, newspapers and microfinance websites.

4. Research Questions

In the context of the oft-repeated allegation that financial literacy is important to ensure that the entire population of the country is served optimally by institutional finance, the study has set for itself the following objectives:

1. To ascertain if MFIs' performance is overestimated through window-dressing
2. To ascertain if MFIs are no different from the traditional moneylenders
3. To ascertain the inadequacies associated with MFI lending

5. Analysis of Data

Window dressing on the part of the beneficiaries

One of the reasons that is cited for the increasingly poorer performance of MFIs is that window dressing on the part of the beneficiaries has been on the rise. By window dressing is meant the practice of taking loan from one MFI to settle an outstanding or overdue loan with another MFI with the result that the loan amount keeps rising all the time without any part of it finding its way into productive activities. Eventually, the loan remains unpaid and the beneficiary ends up as a net debtor. Hence the researcher sought to ascertain from the beneficiaries if they resorted to window dressing. Their replies to the query appear in the following Table

Table-1
Window dressing on the part of the beneficiaries

Whether window dressing is resorted to?	No of Respondents	Percentage
Yes	17	34

26% of the respondents believe that MFIs are no different from the traditional moneylenders.

34% of the beneficiaries resort to window dressing.

Major inadequacies in MFI lending

Several inadequacies are associated with MFI lending. Hence the researcher sought to ascertain from the beneficiaries the weaknesses associated with MFI lending. Their replies to the query appear in the following Table.

Table-3
Major inadequacies in MFI lending

Major inadequacies in MFI lending	No of Respondents
Interest rates are high	50
Does not finance agriculture	50
Repayment conditions are harsh and impractical	50
Too many guarantors	39
Transactions lack transparency	23
Corruption is rampant	19

Well, all the beneficiaries believe that interest rates are high in respect of the loans they take from MFIs. Also all of them believe that MFIs do not finance agriculture and the repayment conditions the MFIs set forth are harsh and impractical. MFIs demand too many guarantors according to 39 beneficiaries. Their transactions lack transparency, according to 23 beneficiaries. Corruption is rampant according to 19 beneficiaries.

6. Conclusions & Recommendations

1. Window-dressing has led to many commercial banks, regional rural banks and co-operative banks being saddled with bad debts. MFIs are bound to meet the same fate if they continue this trend. In this backdrop

it is better that they be regulated by the RBI than the state government machinery.

2. If MFIs are no different from moneylenders, they should be tightly regulated by the banking regulator. State governments are not adequately equipped for the job. All the terms and conditions attaching to the MFI loans should be regulated by the RBI
3. If MFIs do not fund agricultural activities, they are staying away from the most essential activity rural India is associated with.
4. Commercial banks and even more, the regional rural banks of the country have the experience and expertise to disburse such loans. In fact they have been already into such disbursements. In the circumstances, the banking regulator and the government of India as also the relevant state government should come out with more borrower-friendly schemes that could be administered by commercial banks in general and the regional rural banks in particular. This will ensure that complaints of corruption, usurious interest rates, etc are completely taken care of.
5. To ensure local 'feel and touch' and better follow-up, commercial banks and regional rural banks can finance the beneficiaries indirectly as they presently do. They presently lend indirectly by using co-operative societies as the intermediaries. They should mandate MFIs to reconstitute themselves into co-operative societies so they can lend scrupulously and competitively the way commercial and regional rural banks lend. Additionally, their activities and books of accounts will be subject to the oversight of the financing commercial bank or regional rural bank.

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