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ROLE OF MICRO FINANCE IN FINANCIAL INCLUSION

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ABSTRACT

Financial inclusion may be defined as the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost. Yet, the extent of financial exclusion has been staggering. Out of the 600,000 habitations in the country, only about 30,000 had a commercial bank branch. Just about 40 per cent of the population across the country had bank accounts. The proportion of people having any kind of life insurance cover was as low as 10 per cent and proportion having non-life insurance was an abysmally low 0.6 per cent. People having debit cards comprise only 13 per cent and those having credit cards only marginal 2 per cent.

KEYWORDS: *Financial Inclusion, Reserve Bank, Social Contracts, Grameena Bank, Micro Finance*

INTRODUCTION

Financial inclusion may be defined as the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost.(Financial Inclusion Committee Chairman, Dr. C. Ranga rajan.) Financial Inclusion efforts are not new, both government and the Reserve Bank have been pursuing this goal over the last several decades through building the rural co-operative structure in the 1950's, the social contracts with the banks in the 1960's and the expansion of bank branch networks in the 1970's and 1980's. These initiatives have paid off in terms of a network of branches across the country. Yet, the extent of financial exclusion has been staggering. Out of the 600,000 habitations in the country, only about 30,000 had a commercial bank branch. Just about 40 per cent of the population across the country had bank accounts. The proportion of people having any kind of life insurance cover was as low as 10 per cent and proportion having non life insurance was an abysmally low 0.6 per cent. People having debit cards comprise only 13 per cent and those having credit cards only marginal 2 per cent.

OBJECTIVES OF THE STUDY

1. To examine the extent of financial inclusion;
2. To enquire in to the role of micro finance in helping the rural population in the case of financial inclusion;
3. To study the extent of progress made by micro finance in rural India and
4. To look in to the challenges ahead for micro finance in India.

IMPORTANCE OF MFI's

The National Sample Survey Data revealed that nearly 51 per cent of farmer households in the country did not seek credit from either institutional or non institutional sources of any kind. Millions of people across the country are thereby denied the opportunity to harness their earning capacity and entrepreneur talent, and are condemned to marginalization and poverty. A sound system of institutions and instruments of intermediation is essential for promoting an efficient system. Increasing access to credit for the poor has always remained at the core of Indian Planning in it's fight against poverty. Recognizing this dilemma, the evolution of Financial Inclusion, that aims to broaden and deepen access to development finance for all, of which Micro Finance is a subset, is timely. Micro Finance Sector has grown rapidly over the past few decades. Nobel Laureate Muhammad Yunus is credit with laying the foundation of the modern MFI's with establishments of Grameena Bank, in Bangladesh in 1976. Today it has evolved in to a vibrant industry exhibiting a variety of business models. The unique aspect of micro finance in India is that it is delivered through a variety of Commercial Banks and Regional Rural Banks directly dispensing micro credit and through their Business Correspondents (BC's), Self Help Groups (SHGs) linked to bank branches, co-operative banks and primary co-operative societies, micro finance institution (MFIs) as NBFC's and in other forms, obtaining funds from a variety of sources, domestic and external. Ultimately, it is an issue of reaching out to low-income families in a cost-effective, hassle-free and sustainable manner particularly to those who, otherwise, would not have had such access to financial services.

Micro Finance as a model facilitates financial inclusion. The logic and rationale of SHG based micro finance has been established firmly enough to prove that micro credit has effectively graduated from an "experiment" to a widely-accepted paradigm of rural and developmental financing in India. This is no mean achievement. In fact, to the extent people's mindset is the biggest road block in the success of innovation, it may well be one of the most important steps in the saga of Micro Finance. Micro Finance is recognized as a cost effective and sustainable way of taking the banking system to the rural poor. The broad principle behind micro finance initiatives are:

1. To act as a cost effective avenue for the formal financial sector to expand it's coverage of poor
2. To develop effective collateral substitutes
3. To emphasize on the poor masses, both rural and urban especially women and
4. To focus on the objectives of macro-economic growth.

Indirectly, micro finance improves schooling, health and women's empowerment. Globally, in the last two decades, the micro finance sector has opened up considerably in the early 1990's when it was realized that micro credit providers could recover loans to poor and low income people as well as cover their costs, focus was on a single product (credit) which was delivered by specialized micro finance institutions. Micro credit subsequently, developed in to the concept of buildings entire financial systems for the poor, focusing on inclusive growth.

The basic idea of Micro Finance is that poor people are ready and are willing to pull themselves out of poverty if given access to economic inputs. The need for informality in credit delivery and easy access is demonstrated by the fact that SHG's and MFI's contribute the fastest growing segment in recent years in reaching out to small borrowers. Micro Finance is a new development in which Indian institutions have acquired considerable expertise and where up-scaling holds great promise both to expand the nature of financial services offered to micro enterprises and to make these the spring board to entrepreneurial development. (Planning Commission, 2006) Micro Finance is often considered as a tool in the fight against poverty while it has to be understood first and foremost as a tool against financial exclusion. MFI's plays a significant role in facilitating inclusion, as they are uniquely positioned in reaching out to the rural poor. Many of them operate in a limited geographical area, have a greater understanding of the issues specific to the rural poor, enjoy greater acceptability amongst the rural poor and have flexibility in operations providing a level of comfort to their clients. It is roughly estimated that there are about 1000 NGO-MFI's and more than 20 company facilitating the activities in all over India. RBI has adopted Bank Led Model for achieving financial inclusion; certain NBFC's which were supplementing financial inclusion efforts at the ground level. Bank Led Model for financial inclusion, which seeks to leverage on technology. The FI initiatives would have to be ICT based and would ride on new delivery models that would need to be developed by the market participants to best suit their requirements. FI is better served through mainstream banking institutions as only they have the ability to offer the suite of products required to bring in effective/meaningful financial inclusion. Other players such as mobile companies should be allowed to partner with banks in offering services collaboratively.

As Banks and SHG's involved in MFI's, to meet the criterion of availability of banking services, a minimum of 4 basic products must be offered to customers. a) a check in account with emerging credit facility b) payment services and remittances facility c) a pure savings product such as a recurring deposit d) facility of entrepreneurial credit to deserving people.

The task of FI is gigantic and cannot be done without actively leveraging technology and without the involvement of society as a whole. The Financial Inclusion strategies and delivery models being developed by banks are primarily technology driven. However, models adopted by banks are technology neutral, which facilitates easy up scaling and customization, as per individual requirements. And another approach is BC model. Click and mouse technology will be helpful in extending financial inclusion especially in geographically dispersed areas. Banks need to make effective use of technology to provide banking services in remote areas through the BC model. The BC model allows banks to provide doorstep delivery of services, especially cash transactions. Banks have been mandated to allocate at least 25 per cent of all new branches to unbanked rural areas. Banks have also been mandated to open intermediary brick and mortar structures between the base branch and customer locations which will lead to efficiency in cash management documentation, redressal of customer grievances and close supervision of BC operations.

Structured , planned approach to financial inclusion where in all banks have prepared Board approved (FIP's) Financial Inclusion Plans, with a 3 year horizon extending up to 2013 containing self set targets which are congruent with their business strategy and comparative advantage. The initial goal should be providing access to banking services. The focus should be shifted from just opening accounts to the volume of business transacted in these accounts, which is the key for making FI model a success. Recently the RBI Governer Raghuram Rajan outlined, in conceptual terms, what inclusion should be "simplicity and reliability in financial inclusion in India, though not a cure all, can be away of liberating the poor from venal politicians", he said. Further " inorder to draw in the poor, the products should address their needs a safe place to save, a reliable way to send and receive money, a quick way to borrow in times of need or to escape the clutches of the money lender, easy to understand life and health insurance and an avenue to engage in savings for the old age."

While over the years the government has taken several steps to spread the banking habit, formidable tasks lie ahead. Of the 24.67cr. do not have access to banking services. In rural areas, 44% households and in urban areas 33% still do not have a bank account. The government's latest plan of action, as envisaged in the CFIP or Sampoorna Vittiga Samavesham, hopes to extend coverage of basic financial services all excluded households. In the first phase, the CFIP will endeavour to provide universal access to all the beneficiaries through subservice areas (SSA's). each SSA will consists of 100 to 500 families in a cluster of villages and each SSA will be serviced by a BC agent (BCA), whose task will be facilitate to account opening and smooth banking operations.

The latest inclusion plan will have its focus households ratherthan geographical areas. After satisfactory conduct of accounts it is proposed to offer reasonable need based credit facilities for which overdraft facilities will be sanctioned. A smart card (Rupay Card) will be issued to enable customers to operate their accounts even without BC's. And in the second phase, there is a proposal to make available a pension scheme for identified individuals in the unorganized sector and offer microfinance products through government owned insurance companies.

CHALLENGES AHEAD FOR MICROFINANCE IN INDIA

An evaluation of SHG's carried out by the Regional offices of the Reserve Bank revealed that there was scope for improvement in the area of maintenance of books of accounts, rotation of group leaders was generally not followed by SHG. There would be need for greater transparency in their functioning and for facilitating their reach to unbanked population of the country. Interest rates in microfinance sector have to significantly higher than in the banking sector reflecting the much higher cost of doing business. This attracts criticism.

There have been incidents of State government's imposing restrictions on microfinance institutions in a manner (for instance, in AP (Krishna districts story) which does not reflect an appreciation on realities on the ground. Excessive regulation and control is dangerous as it can prevent the development of a healthy and competitive microfinance sector which could compete with money lenders (planning commission, 2006).

CONCLUSION

Finance is the lubricant, which oils the wheels of development. Therefore microfinance model extends credit and savings to the poor, the challenges faced by the industry has to be rectified in due course for the effective working model. Therefore inorder to draw in the poor, we have to take active steps from account opening, savings for old age, insurance schemes etc; and they should be educated about governments plans and policies for instance like, Jan Dhan Yojana. So, by utilizing banking or financial services properly financially excluded people can overcome poverty and escape from clutches of the money lenders to some extent.

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