What Is Microfinance?

Microfinance, also called micro credit, is a type of banking service provided to low-income individuals or groups who otherwise wouldn't have access to financial services.
While institutions participating in microfinance most often provide lending—microloans can range from as small as $50 to under $50,000. But many banks offer additional services such as checking and savings accounts as well as micro-insurance products, and some even offer financial and business education.12 The goal of microfinance is to ultimately give impoverished people an opportunity to become self-sufficient.

KEY TAKEAWAYS

- Microfinance is a banking service provided to low-income individuals or groups who otherwise would have no other access to financial services.
- Microfinance allows people to take on reasonable small business loans safely, in a manner that is consistent with ethical lending practices.
- The majority of micro financing operations occur in developing nations, such as Bangladesh, Cambodia, India, Afghanistan, Democratic Republic of Congo, Indonesia, and Ecuador, among others.

Understanding Microfinance

Microfinance services are provided to unemployed or low-income individuals because most people trapped in poverty, or who have limited financial resources, don't have enough income to do business with traditional financial institutions.
Micro-financing organizations support a large number of activities, ranging from providing the basics—like bank checking and savings accounts—to startup capital for small business entrepreneurs and educational programs that teach the principles of investing. These programs can focus on such skills as bookkeeping, cash-flow management, and technical or professional skills, like accounting.
Unlike typical financing situations, in which the lender is primarily concerned with the borrower having enough collateral to cover the loan, many microfinance organizations focus on helping entrepreneurs succeed. In many instances, people seeking help from microfinance organizations are first required to take a basic money-management class. Lessons cover understanding interest rates, the concept of cash flow, how financing agreements and savings accounts work, how to budget, and how to manage debt.

Benefits of Microfinance

Millions of people have directly or indirectly benefited from microfinance-related operations The Consultative Group to Assist the Poor, a Washington-based global nonprofit organization, estimates that, as of 2021, more than 120 million people had directly benefited from microfinance-related operations.However, these operations are only available to some of the world's poor, while an estimated 1.7 billion people lack access to establishing basic financial accounts.

Concerns About For-Profit Micro financing

In addition to Compartamos Banco, many major financial institutions and other large corporations have launched for-profit microfinance departments, including Citigroup and Barclays, for example.202122 Other companies have created mutual funds that invest primarily in microfinance firms.

By their very nature—and their obligation to stockholders—these publicly traded firms work against the original mission of microfinance: helping the poor above all else.

In response, Compartamos and other for-profit microfinanciers counter that commercialization allows them to operate more efficiently, and to attract more capital by appealing to profit-seeking investors. By becoming a profitable business, their argument goes, a microfinance bank is able to extend its reach, providing more money and more loans to low-income applicants. For now, though, charitable and commercialized microfinanciers do co-exist.

Other Criticisms of Microfinance

In addition to the divide between the nonprofit and for-profit microfinance enterprises, other criticisms exist. Some say that individual microloans of $100 aren't enough money to provide independencerather, they keep recipients working in subsistence-level trades, or just cover basic needs, like food and shelter.

A better approach, these critics maintain, is to create jobs by constructing new factories and producing new goods. They cite the examples of China and India, where the development of large industries has led to stable employment and higher wages, which in turn has helped millions to emerge from the lowest levels of poverty. Other critics have said that the presence of interest payments is a burden. Despite the healthy repayment rates, there still are borrowers who can't, or don't, repay loans, because of the failure of their ventures, personal catastrophe, or other reasons. So, this added debt can make recipients of microcredit even poorer than when they started.

What Are the General Terms of a Microfinance Loan?

Like conventional lenders, microfinanciers must charge interest on loans, and they institute specific repayment plans with payments due at regular intervals. Some lenders require loan recipients to set aside a part of their income in a savings account, which can be used as insurance if the customer defaults. If the borrower repays the loan successfully, then they have gained accrued extra savings.

What Are the Benefits of Microfinance?

The benefits of microfinance extend beyond the direct effects of giving people a source for capital. Entrepreneurs who create successful businesses can then offer jobs and trade to help improve their community. Additionally, the International Finance Corp. (IFC) has helped establish or improve credit reporting bureaus in 30 developing nations. It also has advocated for adding relevant laws that govern financial activities in developing countries.

What Are Some Criticisms of Microfinance?

While some microfinance interest rates are lower than conventional banks' rates, critics have charged that these operations are making money off the poor.[15] Also, many major financial institutions and other large corporations have launched for-profit microfinance departments, raising concerns that, out of a desire to make money, these larger bankers will charge higher interest rates that may create a debt trap for low-income borrowers.[20] And some have argued that individual microloans aren't enough money to provide a realistic path to independence.

The Bottom Line

Microfinance is a form of banking service provided to low-income individuals or groups who otherwise wouldn't have access to financial services. Institutions most often lend amounts of $50 to under $50,000, but they may also offer checking and savings accounts, and some deliver financial and business education. The goal of microfinance is to ultimately give impoverished people an opportunity to become self-sufficient. Some criticisms of the microlending industry as it's grown include excessively high interest rates charged on the small loans extended, profit motives at odds with the original intent of helping the poor, and loans so limited they can't really make their impoverished borrowers self-sufficient.

1. **Microfinance and Poverty Alleviation**

Microfinance intervention has been received with enthusiasm by governments, foundations, community development groups, non-governmental organizations and even for-profit private firms (Carr & Zhong, 2002). Thus, it has been replicated (from the Grameen Bank model) in countries such as the United States hence disproving the notion that developed countries cannot learn from the developing ones, where the movement was started. Developed countries such as the US realized the poten- tial embedded in the provision of microfinance to the poor (Carr & Zhong, 2002). According to Carr and Zhong (2002), the de- veloped country (i.e., USA) also learnt from a developing coun- try (i.e., Bangladesh) about microfinance. Magner (2007) ob- serves that from previous studies and research, it is clear that microfinance is importantly a catalyst for the alleviation of poverty.

This section discusses the impact of microfinance on variables such as income, consumption, savings, assets, employment, diversification of economic activities and local trade.

Financial service	Results	Impact on poverty
Savings facilities of microfinance institutions (MFIs)	• More financial savings • Income from savings • Greater capacity for self-investments • Capacity to invest in better technology • Enable consumption smoothening • Enhance ability to face external shocks • Reduce need to borrow from money lenders at high interest rates • Enable purchase of productive assets • Reduce distress selling of assets • Improve allocation of resources • Increase economic growth	• Reduce household vulnerability to risks/external shocks • Less volatility in household consumption • Greater income • Severity of poverty is reduced • Empowerment • Reduce social exclusion

Credit facilities	• Enable taking advantage of profitable investment opportunities • Lead to adoption of better technology • Enable expansion of microenterprises • Diversification of economic activities • Enable consumption smoothening • Promote risk taking • Reduce reliance on expensive informal sources • Enhance ability to face external shocks • Improve profitability of investments • Reduce distress selling of assets • Increase economic growth	• Higher income • More diversified income sources • Less volatile income • Less volatility in household consumption • Increase household consumption • Better education for children • Severity of poverty is reduced • Empowerment • Reduce social exclusion
Insurance services	• More savings in financial assets • Reduce risks and potential losses • Reduce distress selling of assets • Reduce impact of external shocks	• Greater income • Less volatility in consumption • Greater security
	• Increase investments	
Payments/money transfer services	• Facilitate trade and investments	• Greater income • Higher consumption

1.1. Impact of Microfinance on Income and Consumption

Income and consumption (expenditure) are economic and quantitative impact evaluation indicators. A positive impact is expected to bring an increase in income and expenditure among the poor. Microfinance programs help the poor to establish reliable and regular sources of income (Daley-Harris, 2002; Ahmed, 2010; Zhan & Wong, 2014). Thus impact is realized in terms of ability to access food, healthcare, education, consumption smoothing, assets accumulation and so on. Figure 1 below summarizes how access to finance has a positive influence on food security.

Access to finance by rural farmers enables them to acquire credit and accumulate savings. Savings accumulation increases the production income of farmers in their on-farm and off-farm activities1). Such operations are central to the sustainability of income generating activities. This has an impact on improving the disposable income for consumption and investment hence encouraging local economic development.

1.2. Impact of Microfinance on Savings and Investments

Access to financial services by the poor people capacitates them to mobilise savings. Their savings consequently improve their capacity to invest. An increase in their investment capacity is followed by enabled consumption smoothening and ability (by the poor) to face external shocks hence improving their coping strategies. Microfinance also sets the poor free from the 'chains'

of usurious private moneylenders hence reducing the severity of social exclusion and poverty. Poor people also benefit from in- surance, housing and health facilities that are brought about by microfinance programs that promote savings and investments. A case in point is Grameen Bank of Bangladesh that provides a range of services to the poor.

Microfinance plays a twin role of enhancing agricultural pro- duction and promoting the establishment of non-farm or off-farm activities. Non-farm activities help consumption smoothening in agriculturally dominated rural areas. Zimbabwe's mainstay of the economy used to be agriculture when she enjoyed the 'bread basket of Africa' status. The status was lost as a result of so- cio-political and economic challenges. Small holder farmers and peasants face very wide agricultural gaps due to lack of inputs, droughts, cyclones and other negative conditions. These farmers need to take-up non-farm activities so that the gaps are closed. Assets position can also be influenced through participation in microfinance programmes.

1.3. Impact of Microfinance on Assets

The purchasing power of the poor and low income groups improves when they can access finance. This permits them to accelerate assets accumulation (Gulli, 1998). Microfinance clients accumulate assets through direct loan use or use of profits gen- erated from investing loans. Daley-Harris (2002) notes that the poor's household assets can be categorized into three. These are those contributing to the quality of life, savings-in-kind as- sets and productive assets. The first two categories are used to provide security in the event of future emergencies or shocks. Productive assets are used to promote the poor's small busi- ness activities. Assets that are normally bought are in the small economic activities category that include animals, household utensils, farm equipment and in some cases building houses. Daley-Harris cites a study of SHARE Microfin Limited of India where it was established that the strongest impact on poverty status was the increase in asset ownership. The study found that 59% of the clients were classified as non-poor because of increased assets ownership.

Mosley and Hulme (1998) studied 13 MFIs in seven develop- ing countries2). In all cases the impact of lending tended to in- crease the debtor's income and improve asset position. An in- crease in income and asset position is a widely acceptable measure of poverty alleviation. People that are in a position to increase income and assets get empowered to move out of the poverty trap. Other studies have also established increases in education due to microfinance involvement.

1.4. Impact on Education

Attainment of education represents human capital investment that improves the productive capacity of individuals. An increase in productive capacity will in turn improve production hence re- ducing poverty through increased output, income and employment. They found a positive net impact of credit pro- grams on both human and physical assets. But they found mixed results on education where education for girls increased only when women borrow. According to Brau and Woller (2004), the findings established a significant impact on well-being of poor households and that this impact is greater when targeted at women. They also discovered that women tend to use money towards meeting household needs than men. This suggests that when the program's target is education improvement then women should get credit allocation. Pitt and Khandker (1996)'s study discovered that girl children are sent to school when their mothers are in a position to get earnings.

1.5. Impact on Employment

Unemployment is a macro-economic problem that cascades down to grassroots levels. For example, the rate of unemployment increased tremendously in Zimbabwe due to the economic crises (2000 to 2009) that led to the collapse of industries. In 2008, the rate of unemployment reached 80% (CSO, 2008). During the Zimbabwean crisis, microfinance managed to be resilient hence people survived on small business ventures for a living. ZAMFI (2005) confirms the resilience of microfinance. Other authors have argued that microfinance tends to be resilient during crises periods. For example during the global financial crisis it managed to withstand the financial turmoil

Microfinance helps poor people to create their own employment. Consequently, spill-over effects are that they can also employ other family and/or com- munity members. This has an overall effect of reducing un- employment hence reducing poverty levels and improving the standards of living of the people in the rural communities. Social impacts are also realized.

1.6. Social Impacts of Microfinance

Microfinance activities involve, in the majority of cases, work- ing in groups. This arrangement enables poor people to work in cohesive teams hence improving social integration. Grameen Bank's group methodology helped people to take advantage of 'social capital', which involves networking and cementation of social relations in local communities. Social capital is the glue that brings the society together hence the poor people cooperate for a focused group goal. Most rural areas in developing countries have a higher percentage of women population com- position than men. This is because men migrate to urban areas for employment seeking. Women are left for a long time with children, hence the need for them to be empowered to make economic decisions within the household. Henry et al. (2003) argue that a woman with a husband who stays for a long time at work is regarded the household head, hence the need to improve their participation in community decision making through microfinance program.

1.7. Impact on Basic Needs and Capabilities

Microfinance clients' increase income and economic security which enable them to access basic needs. They also have the ability to improve their capabilities for achieving life-giving 'functionings'. The capabilities approach, expounded by Amartya Sen can be enhanced by the availability of financial resources to the poor and low-income groups. Their coping strategies are improved by their access to finance. There is widely convincing literature for impacts in this area (Daley-Harris, 2002). The case of 'telephone ladies' of Bangladesh is one such an example.

1.8. Other Impacts

microfinance is regarded as an innovative policy instrument that promotes social justice. Often, it is posited that microfinance improves the well-being of participants through job creation, increasing income and building assets (wealth). It makes poor people to be homeowners through schemes such as "housing microfinance", which is a hybrid of microfinance and mortgage finance.

Microfinance program provide access to the financial sector by the poor who suffer from exclusion. They also manage to enjoy the numerous benefits that are associated with the sector such as access to loans, ability to accumulate savings and in other cases managing to get insurance and health facilities. In developing countries, access to traditional banking services is highly limited. The International Poverty Centre reported that even in relatively successful countries such as Ghana and Tanzania, only about 6 percent of the population had access to banking services (Hailu, 2008). This scenario is a result of a number of factors that include, among others, the demand for physical collateral security by traditional banks or lack of mini- mum cash amounts needed to open a bank account. Banks fail to realize 'social collateral' (social capital) that exists among the rural poor (see Vermaak, 2009 for a detailed discussion of so- cial capital). The rural poor may be far away from the banks

Challenges of Microfinance

No poverty alleviation intervention has been found to be insulated from challenges. Thus the microfinance strategy is neither a panacea nor a 'magic bullet' in poverty alleviation. It is one of the strategies that can be employed to assist the poor to manage their precarious lives. The most conspicuous challenge facing microfinance is its 'micro' nature. People do not want to be associated with small things. Usually, they look down upon them. Traditional banks want to deal with large amounts of money and not the 'small' amounts associated with microfinance. The other challenge is the 'customers' that are served by this sector. Rich people do not want to work with poor people.

The provision of microfinance still faces a number of problems. These include; inadequate financial infrastructure, unfavorable policy environment, limited institutional capacity, in- adequate investments in microfinance and rural development, in- adequate investments in social inter mediation and microfinance misconceptions.

The Asian Development Bank (2000) states that the microfinance policy environment remains unfavorable in many countries. It does not support sustainable growth and development of the microfinance industry. This scenario applies to almost all developing countries including Zimbabwe. Government interventions in microfinance, to address perceived market failure through giving subsidized credit to the poor, undermine sustain- able development.

Poorly performing government supported microfinance programs have had an effect of distorting the market thus discouraging new entrants into the industry .

Financial infrastructures incorporate legal, information, regulatory and supervisory systems for micro-finance institutions. The financial infrastructures are, in most cases, weak and non-supportive. Most MFIs have limited institutional capacity. They lack financial leverage and cannot provide a wide range of products to clients. This is because they are not well resourced making them perpetual 'infants' (due to over-dependency) lacking sustainability.

To propel rural development, it is necessary to be cognizant of the sector that underpins growth in the rural areas. Agriculture plays a crucial role hence its growth has a positive impact on the growth and development of rural finance markets. Rural agricultural activities are cut from the markets because of insufficient investments in physical infrastructural development such as roads, irrigation, electricity and other support services such as marketing . All these have negative impacts on rural microfinance. Social inter-mediation supports a sustainable expansion of microfinance and unfamiliar with the complex procedures involved in banking.

Microfinance Institutions (MFIs) serve the rural and urban poor by reaching them so as to cut on transport and other trans- action related costs.

1) Social intermediation is defined broadly as a process in which investments are made in the development of human resources and institutional capital to enable the poor to access effectively and productively the financial services of the formal sector. Such investments, among other things, involve awareness building among services. This calls for an 'integrated' approach to microfinance where the whole package is given to the poor.

Another problem with microfinance loans emanates from the 'fungibility' of financial resources. Sharma and Buchenrieder (2002) note that even if lending institutions impose strict con- ditions, credit may be used for other purposes such as leisure, repaying loans from other expensive sources, financing wedding expenses, purchasing durable goods, paying for funeral ex- penses and other related expenses. This could be reduced by putting in place effective monitoring and evaluation mechanisms.

Microfinance also suffers from misconceptions. Many people associate microfinance with usurious loans offered by private moneylenders. The oldest misconception is that the poor people cannot repay loans, but the Grameen Bank (Bangladesh), the BancoSol (Bolivia), the BRAC (Bangladesh); the Rakyat (Indonesia) experiences have managed to address this perception. Microfinance's penetration into the rural areas re- quires a correction of the aforesaid misconceptions.

At its centre, microfinance is not very different from finance provided by banks. Its challenge is the client segment it serves-the world's poor. Magner (2007) notes that different sets of challenges faced in the provision of microfinance should be recognized. Customers of formal banks tend to be from the mid- dle and higher income groups and live in stable environments. However, microfinance clients live under difficult circumstances. They face a number of negative conditions such as lack of ac- cess to education and other basic needs, poor health, and threats from natural disasters and other environmental woes. These become inhibitors to the success of microfinance in pov- erty alleviation, especially in the rural areas.

The poor lack access to financial resources hence reducing their capability to meet their health requirements. Microfinance could be an alternative for them to be in a position to meet their demand for health services. Could microfinance benefit the poor's access to health? Sickness leads to income losses, and incapacitation of borrowers. A 2005 study carried out by the Harvard Medical School and Harvard Law School established that 50 percent of all people interviewed cited illness and un- affordable medical bills as the primary causes of bankruptcy (Magner, 2007).

One of the challenges of microfinance is that the poor people are not protected by insurance hence their activities tend to be risky. Todd (1996) as cited in Magner (2007) carried out a study of Grameen Bank clients and discovered that serious ill- ness in the family always forces households to liquidate assets in order to pay for medical treatment and/or keep the family afloat. The disaster of illness struck ten of the 17 Grameen Bank families who are still in the poverty group (Magner, 2007, p.11). Poor people are very vulnerable because they lack safety nets. Unfortunately, developing countries do not have established legal and social infrastructures such as bankruptcy laws meant to assist the poor. With the prevalence of the HIV/AIDS pandemic in developing countries such as

Zimbabwe, the poor people are highly exposed and this is a serious inhibitor to the success of microfinance. An introduction of micro-insurance would go a long way.

Lack of education prevents borrowers from sustaining suc- cessful businesses (Magner, 2007). Illiteracy contributes to poor business management hence borrowers backslide into poverty and/or default on loans. To mitigate these challenges micro- finance needs to take an integrated approach so as to provide a full microfinance package. The three inhibiting factors are intertwined. Magner (2007) suggests that microfinance should incorporate some prevention and mitigation measures so as to reduce vulnerability among the poor clients. Microfinance, as a strategy needs to pay attention to policy objectives that address the commonplace challenges. Adoption of the triangle of micro- finance is one such example.

Unit ii

Introduction Fundamentals of banking

The term 'bank' is derived from the French word 'Banco' which means a Bench or Money exchange table. In olden days, European money lenders or money changers used to display (show) coins of different countries in big heaps (quantity) on benches or tables for the purpose of lending or exchanging.

Banking System – Definitions Banking systems refer to a structural network of institutions that provide financial in a country. It deals with the ownership of banks, the structure of banking system, functions performed and the nature of business. The elements of the banking system include: a) Commercial banks b) Investment banks c) Central bank.

The commercial banks accept deposits and lend loans and advances; the investment banks deal with capital market issues and trading; and the central bank regulates the banking system by setting monetary policies besides many other functions like currency issue. A banking system also refers a system provided by the bank which offers cash management services for customers, reporting the transactions of their accounts and portfolios, throughout the day.

defines a bank as "an establishment for custody of money, which it pays out on customer's order." According to Prof. Sayers, "A bank is an institution whose debts are widely accepted in settlement of other people's debts to each other." In this definition Sayers has emphasized the transactions from debts which are raised by a financial institution.

According to the Indian Banking Company Act 1949, "A banking company means any company which transacts the business of banking. Banking means accepting for the purpose of lending or investment, of deposits of money from the public, repayable on demand or other wise and withdrawable by cheque, draft or otherwise."This definition throws light on the three major functions of a bank.

They are: (i) Accepting of deposits and lending loans

(ii) Issue and pay cheques,

(iii) Collect cheques on behalf of the customers. A bank is a financial institution that provides banking and other financial services to their customers.

A bank is an institution which provides fundamental banking services such as accepting deposits and lending loans. As financial intermediaries, banks stand between depositors who supply capital and borrowers who demand capital. When banks accept deposits its liabilities increase and it becomes a debtor, but when it makes advances its assets increases and it becomes a creditor. Banks are a subset of the financial services industry.

The banks are the main participants of the financial system in India. All the banks safeguard the money and valuables and provide loans, credit, and payment services, such as money orders, and cheques. The banks also offer investment and insurance products.

Functions of Banks

The following figure clearly shows the functions of banks: Figure showing the Functions of Bank The functions of commercial banks can be broadly categorized into a) Primary functions b) Secondary functions. Primary Functions Following are the primary functions rendered by banks. Accepting of Deposits The primary function of commercial banks is to accept money from the people in the form of deposits which are usually repayable on demand or after the expiry of a fixed period.

For these deposits, the banks pay a rate of interest, which is called as interest expenditure. Thus, banks act as a custodian of depositors' funds. The deposits may be of various types such as savings deposits, current deposits, fixed deposits and recurring deposits. Savings deposits encourage customers to save money and promote banking habit among the public.

Savings Bank accounts provide a low rate of interest and they have restrictions on the number of withdrawals by the Accepting Deposits Lending Loans Primary Functions Agency Functions Utility Function/ Financial Services Secondary Functions

The SB accounts can be opened in single or joint names. People who prefer these savings bank accounts include salary and wage earners. Now, all the banks allow customers to open a savings bank account with nil balance.

Current Deposit accounts are opened by business people. These accounts have no restrictions on the number of withdrawals and are subject to service changes. There is no interest payment but current account holders can also avail the benefits such as overdraft and cash credit facilities. Fixed deposits accounts can be opened by any person who wants to deposit a lump sum funds at one time for a specific time period.

These accounts provide higher rate of interest depending on the time period for which it is deposited. These accounts do not allow withdrawal before the expiry of the period. Recurring deposit accounts are normally opened and operated by persons who get regular income such as salary class and petty shop owners. A specific amount of money is deposited periodically, say, monthly for a specific period, say, one year.

These accounts provide higher rate of interest and do not allow withdrawal before the expiry of the period. Lending Loans and Advances The second primary function of commerce bank is to lend loans and advances to the corporate sector and households. Normally, the rate of interest levied on these loans and advances is higher than what it pays on deposits. The interest income is the major source of income for commercial banks.

The difference in the interest rates (Interest Received and Interest Paid) is called Interest Spread, which contributes to its profitability. Apart from leading, the banks usually keep some portion of funds to meet the demands of depositors and running expenses. The various types of loans and advances include overdraft, cash credit, loans, discounting of bills of exchange.

MICRO FINANCE DELIVERY MODELS:

MFIs around the world follow a variety of different methodologies for the provision of financial services to low – income families. These methodologies are overwhelmingly based on the Principle of financial services being related to the cash flows of the low-income client groups and thus aim to facilitate relatively frequent and very small or Micro – loan and savings transactions. The focus of such services is on women, based on the observations that in financial matters, they are more responsible than men particularly since their mobility is restricted by family responsibilities. MFIs use two basis methods in delivering financial services to their clients. by Abhay, India Microfinance – MFI‟s use two basic methods in delivering financial services to their clients.

These are:

(1) **Group Method** and

(2) Individual method Group Method This is one of the most common methodologies for providing micro-finance. Group method primarily involves a group of individuals, which becomes the basic unit of operation for the MFIs. As we have discussed earlier, MFIs have to provide collateral free loans, group methodologies help in creating social collateral (peer pressure) that can effectively substitute physical collateral.

Group becomes a basic unit with which MFIs deal. The advantage of group methodology is that

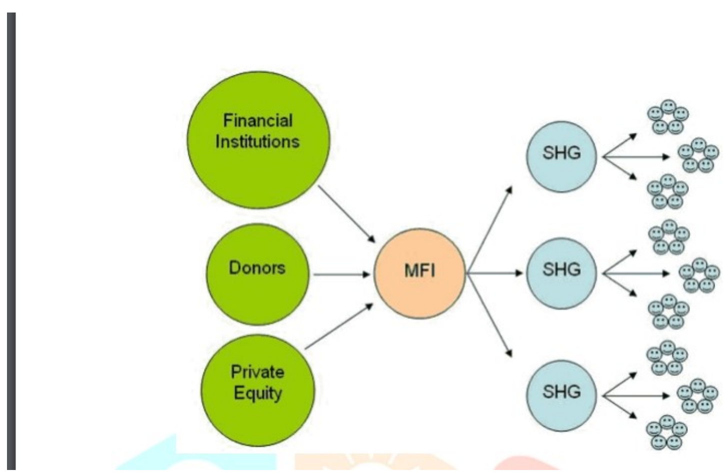
• Groups are trained to own joint responsibility for loans that are taken by individuals in the group.

• Groups ensure repayments from all individuals in that group and incase of a default.

• Groups functions as the forum where the credit discipline and other related issues are discussed.

• Group may have to jointly own the responsibility of defaults and pay on behalf of defaulting client. • Group also help credit appraisal and provide opinion on creditworthiness of each individual in the group.

• Groups methodology also helps in controlling cost. This ensures that even without taking any physical collateral, the MFI is able to manage its credit risk (loan related risk).



MFIs actually deliver the financial service at the client"s location which could be a village in rural areas or a colony/slum in urban area. Having a group helps the MFIs in getting all clients at one spot rather than visiting each individual"s house.

This helps the MFI in increasing the efficiency of staff and controlling the cost. Group methodology creates a forum where individuals come and discuss, can provide opinion, and exert social pressure. The advantage of Group methodology can easily be appreciated by the fact if a MFI employee has to visit each individual house in isolation, it would be very difficult. Also in the absence of a group, if a client refuses to pay there is no forum where such a case can be discussed or there is no method through which the MFI can expert pressure on the client.

Group methodology is also important because in case of larger loan defaults a financial institutions can take recourse o legal action but in small loans legal recourse is not an economically sound option. An MFI who may have an outstanding or Rs 3,000 at default cannot apply legal pressure as the cost of recovery through that method can be higher than the amount to be recovered itself.

Moreover, the clients that the MFIs are dealing with are generally poor and may face genuine problems at times. Rather than taking an aggressive/legal approach, which such vulnerable clients it is always better to have more constructive and collective approach, which is provided by the Groups.

Due to the various advantages, as indicated above provided by groups, this methodology is widely accepted and used in micro-finance across the world. Self-help Group and Joint Liability Groups (Grameen model and its variants) are two common credit delivery models in India

Self –Help Groups (SHGs) Self-help Group concept has its origin in India. SHGs are now considered to be very important bodies in rural development and are therefore found in almost all parts of the country and their number is still rapidly growing. SHGs are formed by Non-Government Organisations as well as Government agencies and are used as channels for various development programmes.

A Self-Help Group is an association of generally up to 20 members (not exceeding 20 members), preferably from the same socio-economic background. SHGs are facilitated by Government agencies or NGOs for members to come together for discussing and solving their common problems either financial or social through mutual help.

An SHG can be all-women group, all-men group, or even a mixed Group. However, it has been the experience that women"s groups perform better in all the important activities of SHGs. Mixed group is not preferred in many of the places, due to the presence of conflicting interests. Some of the distinct features of SHGs are;

(i) Recognized by government: SHGs are well recognized and accepted by government, SHGs can open bank accounts in the name of SHG. They can also receive government grants and funds for development activities.

(ii) SHGs are social intermediaries: SHGs do not restrict their functions only to financial transactions. SHGs are often involved in many social activities. There are example where SHGs have taken up social issues and fought against social evils like alcoholism, violence, against women, dowry, getting into village politics and being elected as Sarpanch.

(iii)Books of accounts: SHGs maintain their own books of accounts. These are simple books to keep records of their savings, loans income and expenditures. Strong SHGs also make their Balance sheets and Income statements.

(iv) Have office bearers: SHGs gave a structure where there is a Group President, Secretary and Treasure. They are elected by the group.

(iv) SHGs are more autonomous as they decide their own rules and regulations.

(v) SHGs mobilize thrift and rotate it internally.

(vi) SHGs can hold bank account and can also borrow from banks and other financial institutions. We see that SHGs are groups, which are more autonomous. While they are involved in financial transactions, their role is not just restricted to it. SHGs are also involved in various social issues.

Joint Liability Group – Grameen Model Grameen model is based on the concept of joint liability. It is the brainchild of Prof.. Muhammad Yunus, founder of Grameen Bank in Bangladesh. Grameen model is the most accepted and prevalent micro-finance delivery model in the world today. Many MFIs have accepted the model as it has high focus on standardization and discipline Grameen model, as mentioned, is a joint liability group model. Here five-member groups are formed and eight such groups form a Center. Hence, in a full-capacity Center there are 40 members (8 x 5). However, over the years people have experimented with Centers of different sizes and now there are variations of 5-8 groups within a Center. Center is the operational unit for the MFI, which means that MFI deals with a Center as a whole. Meetings also take place only at the Central level and individual groups do not meet. Group meetings take place only in front of the Field staff of the MFI. A Grameen model is focused on financial transactions and other social issues are generally not discussed. The Group and Center are Joint liability Groups, which means that all members are jointly responsible („liable‟) for the repayment. MFI recovers full money from Center, if any member has defaulted: the group members have to pool in money to repay to the MFI. If Group members are unable to do it, Center as whole has to contribute and share the responsibility.

Some other features of Grammen Model are:

(i) The group meeting take place every week

(ii) Interest rate are charged on flat basis

(iii) MFI staff conducts the meeting

iv) All transactions take place only in Center meetings.

Grameen model is focused on providing financial services to the clients and hence there is an emphasis on standardization and discipline. The model suggests weekly meeting for frequent interaction with the clients to reduce credit risk. The meetings are conducted for carrying out the financial transactions only. The meetings are conducted systematically in a short-time and other social issues are not discussed. Flat interest is charged again for making the system standardized. In flat rate system installment size of repayment remains small for all weeks and hence is convenient and easier to explain. Also, it is easy to break the loan installment into the principal and interest component.

Joint Liability Groups (JLG)

Grameen model is a particular form of joint liability Group but in India there are other forms of Joint liability Groups as well. MFIs, particularly in urban areas, form JLGs of five-members. These are group of individuals coming together to borrow from the financial institution. They share responsibility ("liability") and stand as guarantee for each other. There is a Group Leader in such JLGs, many MFIs prefer such group in urban business areas. Such JLGs do not hold periodic meetings.

Individual Method

So far we have discussed the Group based lending method. However MFIs are also increasingly providing loans to individuals. In Individual lending method, MFIs provide loans to an individual based on his/her own personal credit worthiness. Individual lending is more prevalent with clients who generally need bigger size loans and have the capacity to produce guarantee and generate enough comfort to the MFI. MFIs generally base their decision on personal knowledge of the client, his/her reputation among peers and society, client"s income sources and business position. MFIs also ask for individual guarantors or take post-dated cheques from clients.

Characteristics of Microfinance Delivery Models in India

Financial Service	Characteristic	Description
Credit	Loan amount	Determined by the longevity of the client's association with the MFI. Not often directly related to the credit needs of the borrower.
	Loan term	Usually 12 months, occasionally less, sometimes greater
	Repayment installments	Monthly or weekly – usually fixed, equal amounts.
	Interest charges	Range: 24-36%, usually levied as a flat charge, partly to simplify calculations for both the MFI and the client. Some MFIs charge lower rates but suffer from poor

	Collateral	No physical collateral but often linked to some compulsory savings component whic acts as financial collateral. Reinforced by joint liability (Grameen) with other clients or peer pressure arising from membership of a community group revolving its own as well as borrowed funds (SHGs, cooperatives). Some MFIs also create reserve funds to cover the risk of default.
Savings	Amount deposited	Grameen: Compulsory – usually a fixed proportion of the repayment Installment. SHG: Compulsory – fixed amounts per (weekly or monthly) meeting to be deposited as part of the group fund; occasionally also voluntary Some MFIs now offer long term fixe deposits.
	Withdrawals	Compulsory savings cannot be withdrawn except when the client leaves the group. Voluntary savings often require some notice of withdrawal.
	Interest paid	Most programmes pay 4-6% interest (not consistent)
Insurance	Life	Some MFIs are starting to offer life insurance covering client loan repayments plus a small payment to the family in case of the death of the client. A reserve fund is created for the purpose or insurance is bought from the organised sector on behalf of the client.
	Animal	Usually linked with a formal insurance company which obtains bulk business from the MFI while the latter provides the service of premium collection; assists in the verification of claims

Common Characteristics of Microfinance Models

In practice, the average microfinance client‟s relationship with an MFI can be defined by a fairly standard *set of obligations*.

- Attendance of regular weekly (fortnightly or monthly) meetings of her group.

 Training in „loan utilisation" or participation in discussions of developmentally relevant issues such as social discrimination, gender awareness, health, sanitation and education.

 Contribution of fixed amounts, termed „savings", to a fund managed.

 Either by her group or by the MFI with direct access of the member.

 Limited or even barred.

 Repayment of fixed amounts as instalments on any loan she obtains from the MFI or from her group.

 What she actually *receives* in return for fulfilling these obligations are:

 Fixed amounts of loan apparently „for productive activities" – with the size of the loan usually determined by the longevity of her relationship with the MFI rather than by her financial needs.

Delivering financial services to poor

The Poor and Financial Services

The Economic Environment of the Poor: the Savings, Credit and Insurance Nexus

The economic environment of the poor has two features that have particular significance in shaping their use of financial services.

The first is that they operate in a mini-economy in which production, consumption, trade and exchange, saving, borrowing and income-earning occur in very small amounts. The effect of this is that transaction costs tend to be high as the 'unit' of transaction is generally minuscule. This has important implications for the use of formal sector institutions where the charging of any standardised administrative cost will commonly make transactions unattractive to the poor.

The second characteristic is that there are high levels of insecurity and risk. These arise because flows of income and expenditure commonly do not coincide, because of household-specific factors (loss of earnings because of sickness, urgent medical expenses, premature death, theft, insecure conditions of employment, difficulties of contract enforcement), and because of broader environmental factors (natural hazards, harvest failure due to drought or flooding, national economic crisis). The covariant nature of the risks associated with this latter group are particularly problematic as they weaken the capacity of community-based social security networks to provide support.

These characteristics have a number of consequences.

(i) They limit the interactions of poor people with formal sector institutions.

(ii) They foster strategies of risk-spreading by the poor: these encourage diversification of economic activities and the development of financial 6 relationships with networks of individuals, groups and agencies.

(iii) They lead to the use of savings and credit mechanisms by the poor as substitutes for insurance (Platteau and Abraham, 1984; Alderman and Paxson, 1992; Fafchamps, 1992) so that savings, credit and insurance have to be treated in a unified way

The Money Management of the Poor:

Towards A Typology Historically (and contemporarily, as well) the provision of financial services to the poor has often been seen as means to achieve some other 'greater' end. Such ambitions have included rescuing people from the exploitation of moneylenders, rehabilitation in the wake of natural disasters, promotion of co-operation among villagers, teaching people the virtues of thrift, poverty alleviation, the adoption of HYV technologies or empowerment. McGregor (1991) rightly points out that when colonial governments introduced rural credit projects, their intentions were often more moral and didactic than financial.

We can categorise these needs into three main groups. Life-cycle needs: In South Asia, the dowry system makes marrying daughters an expensive matter. In parts of Africa, burying deceased parents is very costly.

These are just two examples of 'life-cycle' events for which the poor need to amass relatively large lump sums. Other such events include childbirth, education, homebuilding, widowhood and old-age generally, and the desire to bequeath a lump sum to heirs.

There are also recurrent festivals like Eid, Christmas, or Diwali. In each case the poor need to be able to access sums of money which are much bigger than the amounts of cash which are normally found in the household. Many of these needs can be anticipated, even if their exact date is unknown. The awareness that such outlays are looming on the horizon is of great anxiety for many poor people.

Emergencies: Emergencies that create a sudden and unanticipated need for a large sum of money come in two forms - personal and impersonal. Personal emergencies include sickness or injury, the death of a bread-winner, the loss of employment, and theft. Impersonal ones include events such as war, floods, fires and cyclones, and - for slum dwellers - the bulldozing of their homes by the authorities. Each creates a sudden need for more cash than can normally be found at home. Finding a way to insure themselves against such events could help millions of poor people.

Opportunities: As well as needs for accessing large sums of cash, there can be opportunities when such access is important. There may be opportunities to invest in an existing or new business, or to buy land or other productive assets. The lives of some poor people can be transformed if they can afford to pay a bribe to get a permanent job (often in government service). One opportunity– the setting up of a new business or expanding an existing one - has recently attracted a lot of attention from the aid industry and from the new generation of banks that work with the poor. But business investment is in fact just one of many needs and opportunities that require the poor to access lump sums of cash at short notice.

The first method - the sale of assets - is usually a straightforward matter that does not ordinarily require any 'financial services'. However, poor people sometimes sell, in advance, assets that they do not currently have but expect to hold in the future. The most common example is the advance sale of crops. These 'advances' are a form of financing, since the buyer provides, in effect, a loan secured against the yet-to-be harvested crop. The advance may be spent on financing the farming costs required to provide that crop. But they may equally be used on any of the other needs and opportunities identified earlier. The second method - mortgage and pawn - enables poor people to convert assets into cash and back again. It is the chance (not always realised) to regain the asset that distinguishes this second method from the first. As with the straightforward sale of assets, such services require the user to have a stock of wealth in the form of an asset of some sort. They allow the user to exploit their ownership of this stock of wealth by transforming it temporarily into cash. The most common examples are the pawn shop in urban areas and mortgaging land in the countryside.

This requires the users to have a flow of savings, however small or irregular. It allows them to exploit their capacity to make savings through a variety of mechanisms by which these savings can be transformed into lump sums.

The three main mechanisms are:

• Savings deposit, which allow a lump sum to be enjoyed in future in exchange for a series of savings made now

• Loans which allow a lump sum to be enjoyed now in exchange for a series of savings to be made in the future (in the form of repayment instalments), and

• Insurance, which allows a lump sum to be enjoyed at some unspecified future time in exchange for a series of savings made both now and in the future

The legal framework for MFIs in India with reference to its registration and other parameters can be broadly narrated as under:

1. **For Societies** – Registration for this is a very easy process with no minimum capital requirement. Further, they are not allowed for deposit mobilization/ collection from the public. It has to operate amongst its members only.
2. **For Trust**—Registration for this is very easy with no minimum capital requirement. It is not allowed for deposit mobilization/ collection from the public. It is sometimes problematic as the funds for further expansion may not be available. It has limited scope for expansion.
3. **For Sec. 25 Companies**—Registration is easy but not that easy as those of trusts and societies, especially for an existing company to convert into a Section 25 company. It is not allowed for deposit mobilization/ collection from the public. However, it contributes a lot to the process of financial inclusion.
4. **For NBFC-MFI**— Registration for this is to be taken up with RBI and it is difficult to obtain due to stringent provisions of the RBI. It requires minimum capital of Rs. 5 crores (Rs. 2 crores for North-East India region) to start MFI operations. It is not allowed for deposit mobilization/ collection from the public. It has a large scope and provides a good background for scaling up of the operations as it has investors' confidence with it. It is observed that many MFIs in India, especially in South India and West Bengal, have grown and developed its activities/ operation remarkably.RBI is a strict regulator for MFIs and it monitors very closely from time to time.
5. **For Cooperative Societies**— Registration for this is very easy (except in the state of Maharashtra) with the minimum capital requirement. It has very minimal regulatory requirements to fulfill in this matter. It is allowed to collect the deposits from its members only. It is relatively easy to scale up/ expand its activities. It is observed that many cooperative societies in Maharashtra and South India have progressed very much in terms of size and activities undertaken.

Governance, ownership and Microfinance Performance:

An important topic in the microfinance governance literature deals with the question whether the type of ownership of MFIs explains the performance. The microfinance sector is characterized by various organization types, such as banks, Non-Bank Financial Institutions (NBFI), credit unions and non-Governmental Organizations (NGO). The category banks includes rural banks and banks which can be both publicly owned or privately owned (Mersland, 2009). Also among banks in developed countries we observe various organizational types. For example, the Dutch cooperative bank Rabobank ranks among the world's 25 largest banks and in Germany the ownerless Sparkassen holds more than 40% of the banking market. Nevertheless, the many organizational types in microfinance can be a particular challenge since they operate in markets with normally limited competition and under different regulatory regimes (Merland, 2009). Table 1 presents a characterization of different MFI ownership types.

MFI governance and risk taking

This section deals with the impact of MFI governance on risk. Governance risk is an underestimated topic in the banking literature. The current financial crises shows that bank governance did not protect banks from taking excessive risks, so good governance is especially important for investors. The success of microfinance has induced more commercial debt and equity holders to invest in microfinance. Commercial investors are typically more concerned about investment risks than traditional, non-profit–driven microfinance investors. In addition, there are strong indications that the current financial crisis has severely affected MFI performance, which in turn has induced managers in MFIs to take excessive risks.

Design Model Formation of Microfinance Institutions in the Framework 202

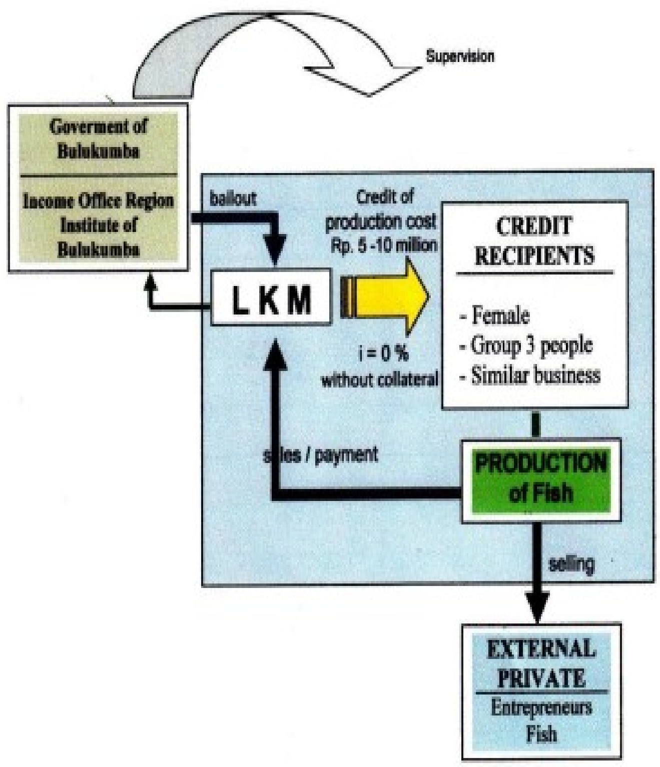


Figure 1. Model of Establishment of Microfinance Instituations Within the Framework of Coastal Community Empowerment in Bulukumba, 2016.

The impacts of microfinance and microcredit

Before the creation of Microfinance Institutions (MFI), bank loans were unavailable for poor people, and money lenders exploited many of the underbanked (da Silva, 2007) especially in developing countries. Today, microfinance facilitates financial inclusion and linkage (Ashta, 2009; Karmakar, 2008) and expands financing channels for vulnerable groups such as the members of the base of the pyramid. Hence microfinance can be called economic innovation that has the goal to fight poverty (Jonker, 2009).

4In addition to pure financial support, microfinance spreads the idea of democracy and human rights, and aims to improve women's social status (Chaudhry, Nosheen, 2009; da Silva, 2007; Montgomery, Weiss, 2011). In terms of quality of life, MFIs care about the health and education of the borrowers' families as well. For instance, Montgomery and Weiss (2011) found a relation between being a microfinance borrower and better medical treatment, nutrition and education for the borrowers' families. DeLoach and Lamanna (2011) demonstrated positive effects on the health of children of microloan borrowers as well and explained this effect with social and financial capital, economic growth and the ability of smooth consumption. All these examples and analyses demonstrate that microfinance is able to create an impact that exceeds pure financial support.

5Some studies state that the availability of financial capital for SMMEs is often a major success factor that should be measured through impact analysis. Therefore Hartarska and Nadolnyak (2008) analyzed whether the microfinance industry in a certain region improved the local credit markets and found positive results. In contrast, some studies suggest that capital is not the predominant problem for the poor and that knowledge, leadership, product prices, and risks are major hurdles for conducting a successful business. Additionally financing of SMMEs can cause a need of additional labor, which often is child labor. In this case microfinance does not support schooling but prevents children from attending school (Maldonado, González-Vega, 2008). Therefore, microfinance institutions should collaborate with economic development projects to educate their clients and to facilitate economic development (Song, Xue, Zhong, 2010).

Types of microfinance institutions

6To date we find two main types of microfinance institutions: those that follow the poverty alleviation approach and those following the financial systems approach. Traditional financial institutions focus on profit maximization. In contrast, microfinance enables financial institutions to think about human capabilities, their creativity, and the potential to serve society (Yunus, Weber, 2007). Therefore a large group of microfinance institutions, for instance 39% of the institutions listed on mixmarket.org, are NGOs (see also Gutiérrez-Nieto, Serrano-Cinca, Mar Molinero, 2007). Others are listed as banks or credit-unions. Enabling the poor to be professional, productive and profitable, and providing microloans to help people establish self-sustaining businesses seem to be in the focus of many MFIs.

7Traditionally microfinance is seen as a poverty reduction tool, which grants loans to different segments of the poor (da Silva, 2007). But it should be used to alleviate social problems and provide the poor with financial assistance to help them improve their quality of life as well (Yunus, Weber, 2007). A number of institutions that focus on poverty alleviation are dependent on donor subsidies to manage the high costs of lending. The costs are caused because of the approach to provide small loans to as many borrowers as possible. Hence, often traditional microfinance institutions following the poverty alleviation approach are often dependent on donor monies. Therefore, until to date, investments in microfinance were mainly done because of philanthropically motives (J.P. Morgan, 2010). However, recently microfinance has been spotlighted as an investment that creates financial returns as well. Thus in-line with other base-of-the-pyramid business strategies (Karnani, 2007) conventional investors see microfinance as an investment opportunity as well. Following this approach some microfinance institutions like the Indian SKS Microfinance or the Mexican Compartamos are already listed on stock exchanges in order to attract investors. Those and similar institutions follow the financial systems approach (Hermes, Lensink, 2007a; Robinson, 2001). This approach is striving to serve as many poor people as possible as well. Additionally it emphasises the financial sustainability of microfinance that goes along with commercial viability and institutional growth in order to avoid donor reliance and to be attractive for investors that want to support the growth of microfinance.

Outreach measurement

8 Because of the strong link to the conventional financial sector, some worry that the financial systems approach will depart from its social mission and only focus on financial returns. In contrast proponents of the financial systems approach argue that a large-scale and long-term outreach to the poor can only be guaranteed by financially sustainable institutions that have access to capital. Therefore, many outreach studies focus on the question whether the financial systems approach changes the outreach of microfinance. Usually they compare the number and the size of loans and the group of borrowers receiving the loans. If smaller loans are provided to borrowers at the base of the pyramid, a greater outreach is assumed.

9 Often the assumption is tested whether microfinance institutions that follow the financial systems approach tend to provide larger and fewer loans to decrease administrative costs. However, using this methodological approach, a number of scholars such as (Hishigsuren, 2007; Mersland, Strøm, 2010; Morduch, 1999; Yaron, 1992b) could not find differences in the outreach or social performance between microfinance institutions that follow the different approaches. Other studies found that those that follow the financial systems approach tend to grant less but higher loans to less poor borrowers in order to decrease costs (Cull, Demirgueç-Kunt, Morduch, 2007). However, Hermes and Lensink (2007b) generally criticize the validity of common outreach measures because they are often not comparable. A solution for this problem could be the use of multi-criteria measurements that include both financial and social criteria (Bartual Sanfeliu, Cervelló Royo, & Moya Clemente, in press). Criteria could be used such as the housing index, monthly household income per capita, caste, geographical and sectorial distribution of loans, or quality and scope of outreach (Aubert, de Janvry, Sadoulet, 2009).

Social cost-benefit analysis

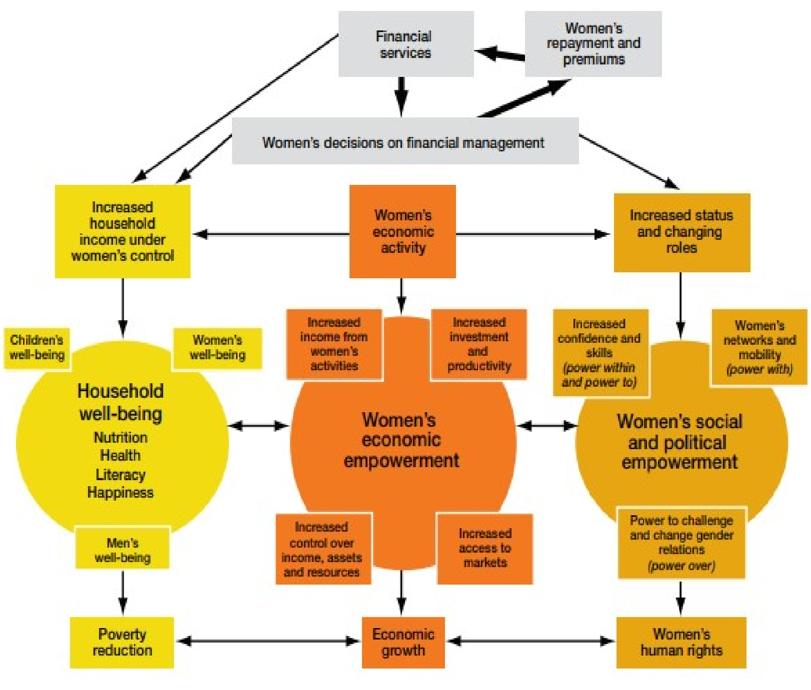
10 Originally social cost-benefit analysis is used to evaluate projects with regard to their social or profitability (Stewart, 1975). Often shadow prices are used to measure the value of social costs and benefit. While in general project management social cost-benefit analysis focuses on both social cost and benefit, in microfinance it is usually used to analyze the social benefit compared to the financial costs for creating the benefit. Microfinance, as well as other means to alleviate poverty, has to demonstrate its efficiency and a positive cost-benefit relation (Bhatt, Tang, 2001). The social cost-

benefit approach defines efficiency as the cost-benefit ratio of microfinance compared with other available poverty interventions such as publicly financed development aid (van de Walle, 1997). This analysis has to take the donor subsidies that many microfinance institutions receive into consideration. In addition to his administrative costs, the costs of capital or cost of defaults have to be taken into consideration on the cost side of the analysis. Benefits of microfinance could be increased income for borrowers, better educations, better health, empowerment and other social benefits. Using social cost-benefit analysis Gutierrez-Nieto *et al.* (2007) found significant differences in the efficiency of microfinance institutions. They found that those declaring themselves as NGOs were more efficient than for-profit institutions because they saved costs through voluntary work.

11A method to measure the cost-benefit of microfinance taking subsidies into account was developed by Yaron (1992a). He claims that a microfinance institution achieves self- sustainability when the return on equity equals or exceeds the opportunity costs of funds. Given that many microfinance institutions depend on donor subsidies an indicator for the cost benefit calculation according to Yaron could be the increase in the average interest rate that is required to eliminate the subsidies while keeping the return on equity equally.

12In contrast to Yaron, Mordoch (2000) argues that as long as funding is available and as long as benefits of microfinance outweigh its costs, measuring benefits without taking subsidies into consideration is not an option. In his opinion subsidized programs eventually have a higher outreach than financially sustainable programs and thus cannot just be compared by cost benefits analyses. However, a cost-benefit analysis conducted by Khandker (1998) compared different microfinance institutions and other poverty alleviation programmes in Bangladesh and found cost-benefit differences between both, microfinance and other development initiatives and different microfinance institutions. His results show the complexity of the measurement as, for example, some microfinance institutions offer training and education programs in addition to their loans while others do not. Therefore, similar benefits are created with different costs. Further more it seems that the ability to avoid loan defaults is one of the most important issues in order to deliver a good cost-benefit ratio (Burgess, Pande, 2005). Therefore Sadik (1978) stated that especially the “benefit” part of the cost-benefit analysis is relatively uncertain and is often regarded as much more certain than it is.

FIGURE 1
Microfinance and women's empowerment: virtuous spirals



Importance of gender mainstreaming:

Potential vicious circles Despite the potential contribution of microfinance to women's empowerment and well-being, there is a long way to go before women have equal access to financial services in rural areas or are able to fully benefit from them. This is partly because of contextual differences in the gender division of labour. Although there are significant differences among and within regions in the types of crops and other economic activities in which they are involved, women tend to be restricted to subsistence food crops and the marketing of lower-profit goods. Although there are significant differences in household, family and kinship structures, women are also almost universally disadvantaged in access to and control of incomes (from their own or household economic activities) and assets (particularly land).

These differences and inequalities affect the types of financial services they need and also the ways in which they are able to use and benefit from them. This does not mean that microfinance should cease attempting to target women – they have a right to access all types of financial services and to the removal of all forms of gender discrimination among financial service providers. The right of women to equality is enshrined in agreements and conventions on women's human rights signed by most governments.

Microfinance business model

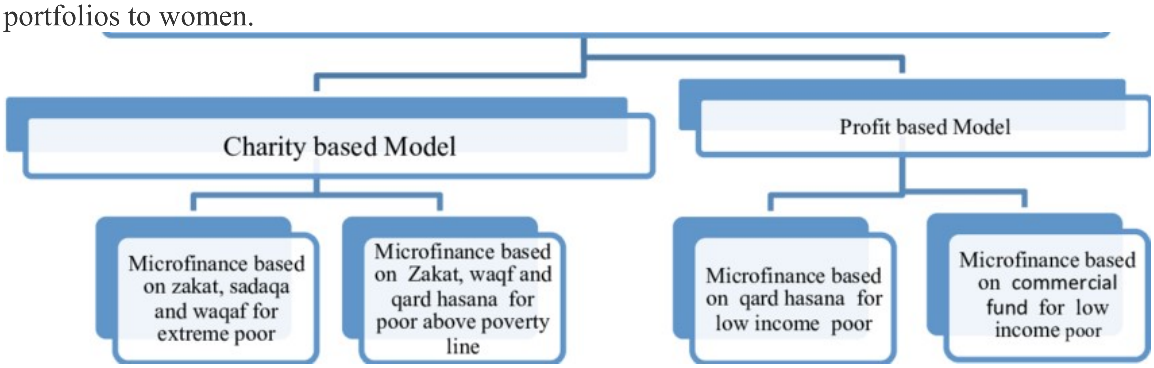
Microfinance institutions aim to serve customers ill-served by traditional commercial banks and thus the associated business model is challenging by definition. And yet the industry has achieved impressive scale reaching 211 million customers globally in

2013. Paradoxically, recent evidence suggests that the benefits of microcredit to borrowers may be modest. For example, six prominent randomized controlled trials found small impacts of access to microcredit on the incomes and consumption levels of marginal borrowers, though the studies found some “potentially important” (though modest) impacts on “occupational choice, business scale, consumption choice, female decision power, and improved risk management.”

Even if one takes those modest benefits at face value, it would be wrong to consider the microfinance business model a failure without paying greater attention to the costs incurred to achieve those benefits. Modest benefits to borrowers could nonetheless feed into sizable benefit-cost ratios if the costs are also proportionally small. Indeed, this was a fundamental premise of microfinance.

To better understand how microfinance institutions target their customers and cover the costs associated with reaching them, we use proprietary data from 930 microfinance institutions that jointly served 80 million customers in 2009. We show that there is no single microfinance business model, but rather a number of models pursued by different types of institutions.

Those chartered as non-governmental organizations (NGOs) tend to make smaller loans (panel A), which are substantially more costly per dollar lent (panel B), and thus require higher interest rates (panel C), than microfinance providers chartered as banks or non-bank financial institutions (NBFIs). Not only do they make smaller loans (the proxy for lending to poorer borrowers in much of the literature and in our analysis), NGO microfinance institutions also lend substantially higher shares of their portfolios to women.



Different Models of Microfinance in India

Associations Model

The target community forms an 'association' through which various microfinance (and other) activities are initiated. Such activities may include savings. These associations or groups can form of a youth, women. It is also formed around political/religious/cultural issues. It can create support for microenterprises and other work-based issues.

According to NABARD, **SHG-BLP** is the world’s largest microfinance program in the world.

Bank Guarantees Model

A Bank guarantee is used to obtain a loan from a commercial bank. This guarantee may be arranged externally (through donor/donation, government agency, etc.) or internally (using member savings). The loans obtained may be given to an individual or they may be given to the self-formed group. It is a form of capital guarantee scheme. Guaranteed funds may be used for various purposes, including loan recovery and insurance claims. The guaranteed funds can be used for various purposes such as loan recovery or insurance claims.

Bellwether Microfinance Funds (India) is one such example.

Community Banking Model

In India, community banking looks very different. Self Help Groups (SHG) are often instituted in which members of the local community join together and pool capital resources for lending to members. They value transparency in their practices and utilizing their savings for their purposes of lending.

Cooperatives Model

A co-operative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-owned enterprise. The members are the shareholders and have their share in equity capital. They also share the profit.

Co-operative Development Forum Hyderabad is a successful example of this model. It has built a network of women's thrift groups and men's thrift groups.

Credit Unions Model

This model is based on a member-driven credit union, a self-help financial institution. A union of members is formed. These members form the common community. They agree to save together and give loans to each other at a nominal rate of interest. A credit union's membership is open to all who belong to the group, regardless of race, religion, color, or creed.

The members are people of some common bond:

- Working for the same employer
- Belonging to the same church
- Labor union
- Social fraternity
- Living/working in the same community

Grameen Banking Model

It promotes credit as a human right and is based on the premise that the skills of the poor are underutilized. The **Grameen Bank (GB)** is based on the voluntary formation of slight groups of five people to provide mutual, morally necessary group guarantees instead of the collateral required by conventional banks.

The whole center is jointly responsible for the repayment. Grameen model is being followed by Sarv Seva Abhiyan (ASSEFA), Activities for Social Alternatives.

Intermediary Model

This model positions a third party between the lending institutions and the borrowers. The intermediary plays a critical role in generating credit awareness and education among the borrowers. Intermediaries could be individual lenders, NGOs, microenterprise/microcredit programs, and commercial banks (for government-financed programs). The intermediaries are incentivized in monetary and non-monetary forms.

Individual Banking Model

This is a straight forward credit lending model where microloans are given directly to the borrower. The individual banking model is a shift from the group-based model. The MFI gives loans to an individual based on his or her creditworthiness. It also assists in skill development and outreach programs. Co-operative banks, Commercial banks, and Regional Rural Banks mostly adopt this model to give loans to the farming and non-farming unorganized sector.

Self-employment women's association in India s one such example to have adopted this model. The members own and govern the group.

NGO Model

NGOs are one of the key players in the field of micro-financing. They help the cause of micro-financing by playing the intermediary in multiple dimensions. Non-governmental Organizations (NGOs) played a vital role in rural reconstruction, agricultural development, and rural development even during a pre-independent era in our country. NGOs became a supplementary agency for the developmental activities of the government and in some cases, they become alternatives to the government.
Non-governmental Organizations are committed to the upliftment of poor, marginalized, underprivileged, impoverished, and downtrodden and they are close and accessible to their target groups.
Various NGOs are helping the cause of micro-financing. For example, **MYRADA** in Karnataka, **SHARE** in Andhra Pradesh, **RDO (Rural Development Organization)** in Manipur, **RUDSOVAT (Rural Development Society for Vocational Training)** in Rajasthan, and ADITHI in Bihar.

ROSCA Model Or Chit Funds

Rotating Savings and Credit Associations or ROSCAs, are essentially a group of individuals who come together and make regular cyclical contributions to a common fund, which is then given as a lump sum to one member in each cycle. At the end of a cycle, the total fund collected goes to any one member. Rotating Savings and Credit Associations are a means to save and borrow simultaneously. There are lakhs of ROSCA functioning in India today.

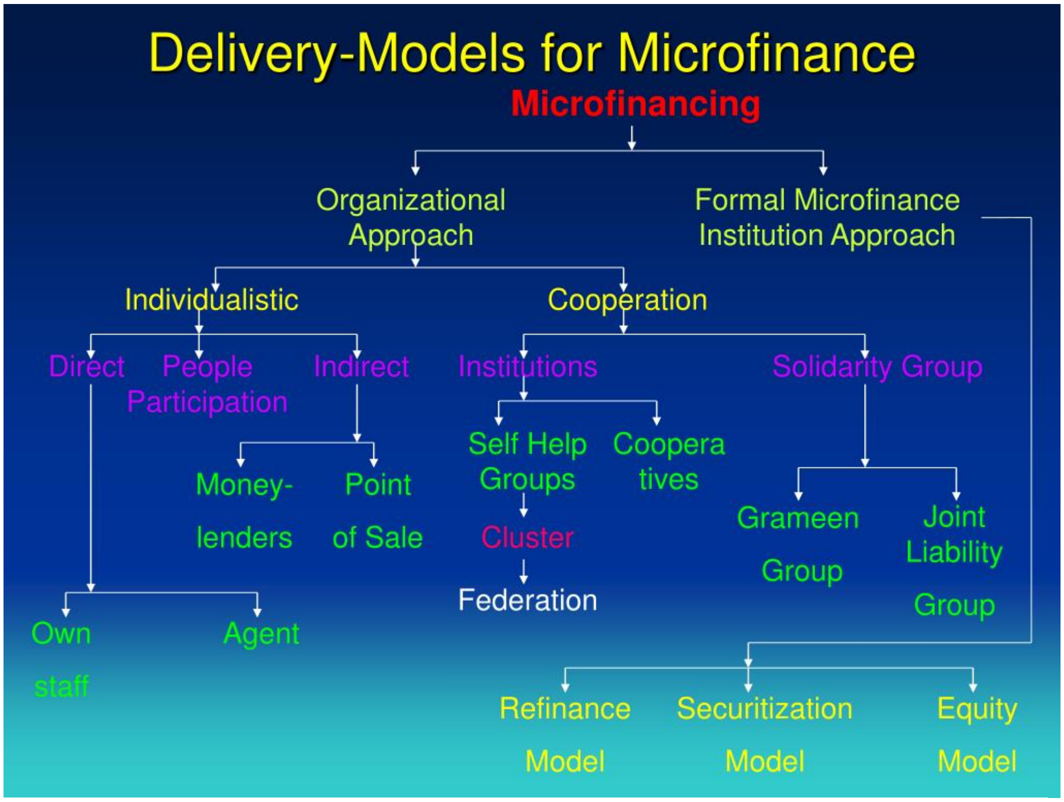
Village Based Model

It is closely related to the community banking and the Group model, this is the community-based saving and credit model. A group of 25-50 people gets together to enhance their income through self-employment activities. They get their first loan from the implementing agency, which helps them form the community credit enterprise.

Small Business Model

This model places a big responsibility on small and medium enterprises. This has been changing, as more and more importance is placed on small and medium enterprises (SMEs) - for generating employment, for increasing income, and providing services that are lacking.

Delivery models



Future of Microfinance in India

- Affordable borrowing for one and all: Easy access to microcredit
- Reaching the doorstep of every unbanked customer
- The road ahead for a digital microfinance
- Leveraging women empowerment and mobilizing the entrepreneurial landscape

India aims to become a USD 5 trillion economy by 2025 and the microfinance industry will play a leading role in uplifting the lives of millions of low-income households and enabling them to contribute to the country's economic growth.

Emerging issues in microfinance

Problems of Microfinance in India: The Way Ahead

Microfinance has shown to be a significant tool in enhancing the welfare levels of the poor by increasing disposable household income during the last few decades. However, broader benefits on social welfare, such as health, nutrition, education, and female empowerment, have yet to be widely recognised. Nonetheless, microfinance is widely regarded as a valuable instrument for reducing poverty in low-income countries.

The following are the solutions to overcoming the **problems of microfinance in India** and reaching more people:

1. Interest rate transparency

MFIs should adhere to an actual interest rate on products and amounts disclosed to clients.

2. Proper regulation

When microfinance was in its infancy and individual businesses were free to experiment with new business models, a restrictive environment requirement wasn't a major problem.

However, the organisation now requires constraints to preserve stakeholders' interests while promoting growth.

3. Rural poor focus

Instead of lowering the initial cost in places where MFIs exist, these institutions should begin focusing on the rural poor and open additional branches throughout the areas.

4. Range of products

MFIs should provide a comprehensive range of products, including credit, savings, remittance, financial advice, and so on, to help consumers transition away from commercial banks.

5. Use of technology

MFIs should use new technologies, IT tools, and applications to reduce operational costs.

Microfinance institutions should be encouraged to reduce their operating expenses by using cost-cutting methods.

6. Different fund sources

In the absence of sufficient finances, MFIs' expansion and reach are limited, and to mitigate this disadvantage, MFIs may look for additional funding sources for their loan portfolio.

7. Field supervision

In addition to proper regulation of the microfinance sector, field visits can be used to monitor conditions on the ground and, if necessary, take corrective action.

This can be used to monitor MFI ground staff's performance and loan recovery operations.

Microfinance institutions have undoubtedly proliferated and played an essential role in the cause of financial inclusion, but there is still much to be done.

The Indian microfinance sector is complicated, as evidenced by the foregoing research. And it requires prompt attention from the RBI in the form of a comprehensive regulatory framework designed to protect the help provided to the poor and financially marginalized

Social assessment in microfinance

Defining the Social Impact of Microfinance

The social impact of microfinance goes beyond conventional financial metrics like loan repayment rates and profit margins. It goes deeper into the transformative changes that microfinance brings to the lives of borrowers, their families, and their communities. These changes encompass various dimensions, including improved standards of living, enhanced education opportunities, increased access to healthcare, women's empowerment, and overall poverty reduction.

Key Metrics for Microfinance Impact Assessment

1. Income and Economic Well-being: One of the primary objectives of microfinance is to improve the economic conditions of the clients. Metrics such as changes in income levels, asset accumulation, and household expenditure patterns offer insights into the financial well-being of clients.

2. Women's Empowerment: Over the years, Microfinance has been shown to play a significant role in empowering women. Metrics such as women's participation in decision-making, control over financial resources, and access to training are essential indicators of gender equality and women's empowerment.

3. Education and Health Outcomes: Access to education and healthcare services is a critical aspect of social impact. Monitoring metrics such as school enrollment rates, improvements in literacy, and better health outcomes can help gauge the effectiveness of microfinance in these areas.

4. Poverty Alleviation: Measuring the number of microfinance clients who successfully transition out of poverty provides a clear indication of microfinance's success in contributing to poverty alleviation in communities.

Methods for Assessing Social Impact in Microfinance

1. Client Surveys and Interviews: Conducting surveys and interviews with microfinance clients can provide valuable qualitative data on their experiences and the changes in their lives as a result of accessing financial services. These testimonials offer rich insights into the social impact and transformational effects.

2. Social Performance Management (SPM) Tools: SPM tools, such as the Progress out of Poverty Index (PPI) and the Poverty Probability Index (PPI-Short), provide quantitative measures to estimate the poverty levels of clients and assess the effectiveness of microfinance initiatives.

3. Randomized Control Trials (RCTs): RCTs involve randomly assigning participants into control and treatment groups, enabling researchers to isolate the impact of microfinance by comparing outcomes between these groups.

4. Social Return on Investment (SROI) Analysis: SROI analysis quantifies the social value created by microfinance investments, taking into account both monetary and non-monetary impacts. It helps in understanding the cost-benefit ratio of social interventions.

5. Client Testimonials: Client testimonials involve gathering feedback and personal narratives directly from microfinance clients. It is a qualitative method where borrowers share their experiences, successes, challenges, and how microfinance has impacted their lives. Testimonials provide valuable insights into the human side of microfinance and highlight the changes it has brought about in individuals' livelihoods.

6. Case Studies: Case studies involve in-depth examinations of specific microfinance projects or individual clients. Researchers gather comprehensive data through interviews, surveys, and document analysis. Case studies provide a detailed understanding of the impact of microfinance, offering rich insights into the complexities and nuances of the intervention's effects on clients and communities.

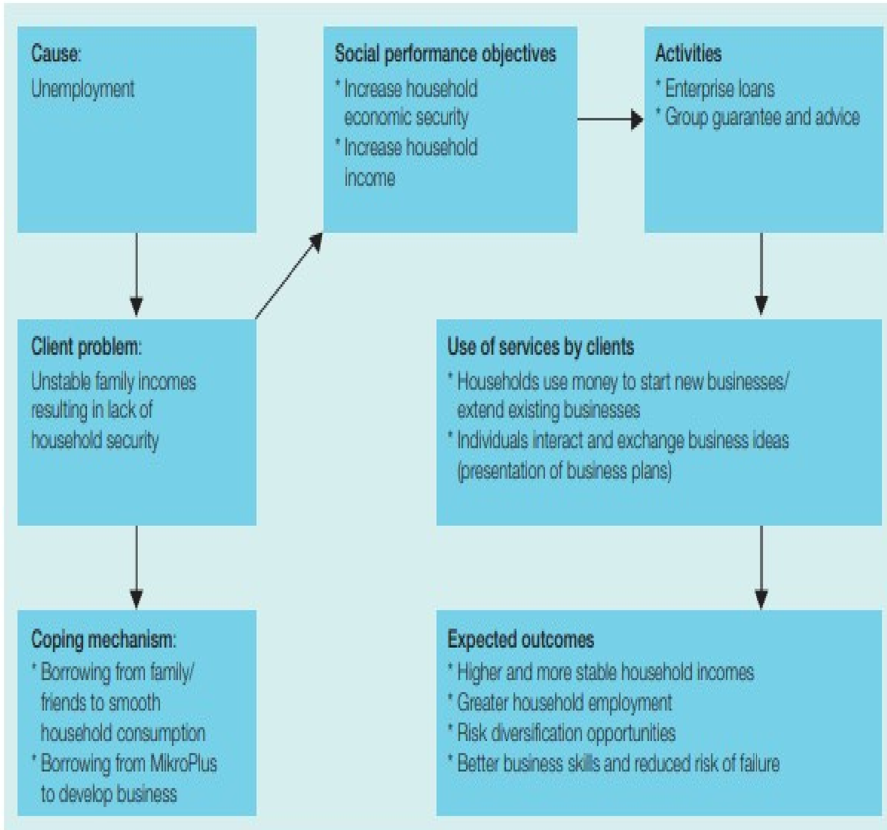
7. Focus Groups: Focus groups are interactive group discussions with microfinance clients or stakeholders. These discussions allow participants to express their views, experiences, and opinions on the social impact of microfinance initiatives. Focus groups offer a platform for participants to share their perspectives and engage in collective brainstorming.

8. **Cost-Benefit Analysis:** Cost-benefit analysis is a quantitative method that compares the costs incurred in implementing a microfinance program with the benefits generated from its social impact. By assigning monetary values to both costs and benefits, decision-makers can assess whether the intervention is economically viable and if the benefits outweigh the expenses.

9**. Beneficiary Feedback Mechanisms:** Beneficiary feedback mechanisms are systems put in place by microfinance institutions to receive feedback directly from the clients they serve. This could include suggestion boxes, helplines, or online platforms. Beneficiary feedback mechanisms enable continuous engagement with clients, helping MFIs to respond to their needs and concerns and improve their services accordingly.

10**. Qualitative and Quantitative Analysis:** Assessing the social impact of microfinance requires a comprehensive approach using both qualitative and quantitative data analysis. The qualitative analysis uncovers themes and emotions, providing in-depth insights. The quantitative analysis measures impact and identifies statistical relationships. Integrating both methods through a mixed-methods approach ensures a robust understanding and informs effective decision-making.

Impact pathways, MikroPlus, Croatia



Source: Microfinance Centre for Central and Eastern Europe and the New Independent States (MFC)

FINANCIAL PRODUCTS AND SEVICES in microfinance

microfinance has focused on providing a very standardized credit product. The poor, just like anyone else, need a diverse range of financial instruments to be able to build assets, stabilize consumption and protect themselves against risks. Thus, we see a broadening of the concept of microfinance--our current challenge is to find efficient and reliable ways of providing a richer menu of microfinance products.

Microfinance products

Product	Purpose
Income Generation Loan (IGL)	Income generation, asset development
Mid-Term Loan (MTL)	Same as IGL, available at middle (week 25) of IGL
Emergency Loan (EL)	All emergencies such as health, funerals, hospitalization
Individual Loan (IL)	Income generation, asset development

Who are the clients of microfinance?

The typical microfinance clients are low-income persons that do not have access to formal financial institutions. Microfinance clients are typically self-employed, often household-based entrepreneurs. In rural areas, they are usually small farmers and others who are engaged in small income-generating activities such as food processing and petty trade. In urban areas, microfinance activities are more diverse and include shopkeepers, service providers, artisans, street vendors, etc. Microfinance clients are poor and vulnerable non-poor who have a relatively stable source of income.
Access to conventional formal financial institutions, for many reasons, is directly related to income: the poorer you are the less likely that you have access. On the other hand, the chances are that, the poorer you are the more expensive or onerous informal financial arrangements. Moreover, informal arrangements may not suitably meet certain financial service needs or may exclude you anyway. Individuals in this excluded and under-served market segment are the clients of microfinance.
As we broaden the notion of the types of services microfinance encompasses, the potential market of microfinance clients also expands. For instance, microcredit might have a far more limited market scope than, say, a more diversified range of financial services which includes various types of savings products, payment and remittance services, and various insurance products. For example, many very poor farmers may not really wish to borrow, but rather, would like a safer place to save the proceeds from their harvest as these are consumed over several months by the requirements of daily living.

How does microfinance help the poor?

Experience shows that microfinance can help the poor to increase income, build viable businesses, and reduce their vulnerability to external shocks. It can also be a powerful instrument for self-empowerment by enabling the poor, especially women, to become economic agents of change.
Poverty is multi-dimensional. By providing access to financial services, microfinance plays an important role in the fight against the many aspects of poverty. For instance, income generation from a business helps in not only expanding the business activity but also in contributing to household income and its attendant benefiting on food security, children's education, etc. Moreover, for women, who, in many contexts, are secluded from public space, transacting with formal institutions can also build confidence and empowerment.

he financial modelling of MFIs is not complicated. Financial Revenue is the key item amongst the other P&L items to understand the structure and assess the scalability of microfinance businesses. It is calculated as interest rate multiplied by Loan Portfolio. In this blog, I would like to focus on the **Loan Portfolio** because the other factor, the interest rate, is capped by regulators in some countries, and is not always a parameter which MFIs can freely change.

The loan portfolio can be broken down as follows. The 3 items colored in red are the key indicators on which I would like to elaborate further.

EOP Loan portfolio = BOP Loan portfolio - Collections + Disbursements
= BOP Loan portfolio - Collections + Loan size * # of disbursed loans / LO * # of LO
= BOP Loan portfolio - Collections + Loan size * # of disbursed loans / LO * LO / Branch * # of branches

EOP: End of period
BOP: Beginning of period
LO: Loan officer

1. **Productivity (# of disbursed loans / LO):** One of the most important factors is Productivity, which here means the number of loans disbursed per loan officer. This indicator shows how many loans a loan officer can handle at a time, or how many new loans a loan officer can disburse in a certain period.

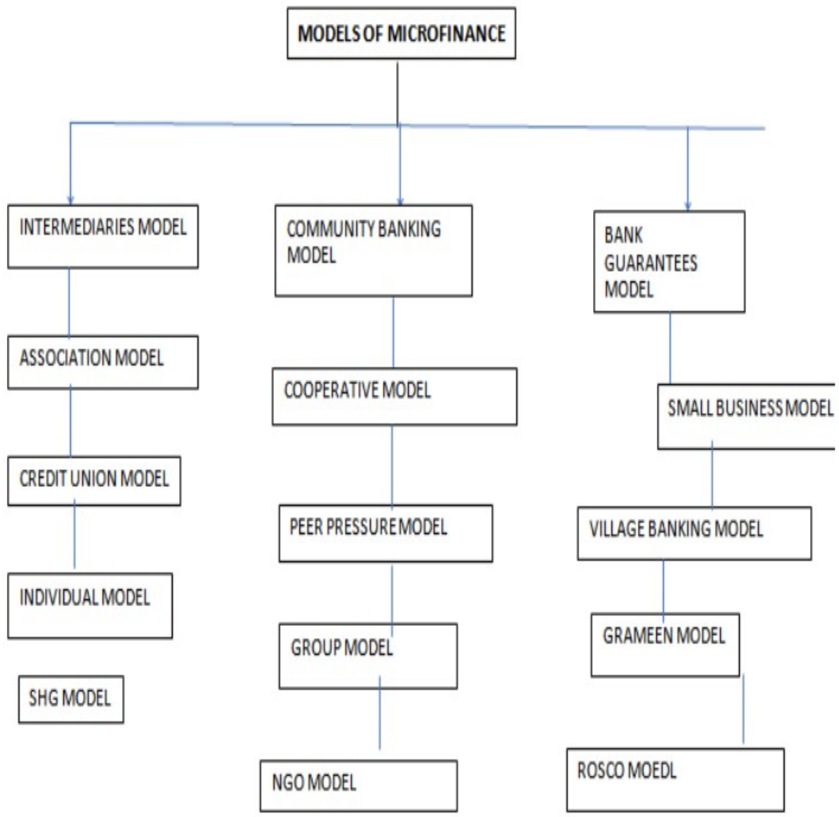
   This indicator can be further broken down by branch or product. The productivity is highly correlated with branch vintage, i.e. the productivity tends to be lower at a newly opened branch but it improves as time goes by as officers get trained and become more experienced. Also, this indicator can be further improved through streamlining operations / processes through technology, such as the use of a Digital Field Application, automated underwriting, cashless payments etc.

   One example of this at Gojo is a Digital Field Application called Bridge, developed by our tech team, whose MVP succeeded in significantly reducing the registration and loan approval time from 3 days to just 40 minutes! With the device, the loan officers are able to spend more time on client sourcing instead of becoming engaged in unproductive paperwork.

1. **Loan size:** MFIs are willing to offer larger loans to customers who have repaid previous loans, as they can see more of the customer's credit history than before. But for the MFI to be selected as the customer's lender of choice, they need to keep a good relationship with customers through close and constant communication, otherwise the customers would end up changing their lenders. The MFI offers larger loans when the MFI is confident enough that the customers will repay the loans.

   Therefore, to offer larger loans, it is critical for the MFI to have a deep and up-to-date understanding of customers, including but not limited to, their business, financial situation and personal events. Considering this, although I mentioned the role of technology above, the microfinance industry will not immediately transition to fully tech-equipped services, unlike many other industries, but "tech & touch" will be the key concept for MFIs at least for several years going forward. Given that many MFI customers still do not own smartphones/smart wallets, data about their business situation, financial needs and other life events cannot be collected through these kinds of devices but needs to continue being collected through human touch to some extent. Modelling loan size therefore means we have to take into account the MFI's current and future capacity to collect data on customers and assess their creditworthiness.
1. **Branch expansion (# of branches):** Room for branch expansion largely varies by country. For instance, in some countries such as Bangladesh, financial services have already spread widely to the bottom of the pyramid, but other countries still contain large numbers of underbanked or unbanked people. In more competitive markets, the MFI needs to have some unique selling point or advantages compared to existing players, whereas in less competitive markets they would be able to enter more easily.

   The decision on whether to open a branch depends on potential demand for credit, risks, economics, the competitive environment, and many other factors. An additional factor to take into account is the strategy of a MFI, as some MFIs focus more on urban areas while others target rural areas. There are financial institutions which do not have physical branches, rather operating through agent networks. For such institutions, we would possibly use the number of agents instead of the number of branches.



1. **ASSOCIATIONS MODE**L The target community forms an 'association' through which microfinance and other operations are launched. Savings is one of these activities. Youth and women can form associations or groups around political, religious, and cultural themes, as well as support structures for microenterprises and other work-related issues. In some countries, an 'association' can be a legal entity with benefits such as fee collecting, insurance, tax exemptions, and other safeguards. On the one hand, there is a distinction established between associations, community groups, people's organisations, and other mass, community-based organisations, and NGOs, etc., which are mainly external organisations.
2. **BANK GUARENTEES MODEL** A bank guarantee is used to acquire a loan from a commercial bank, as the name implies. This assurance can be obtained from an external source, such as a donor or a government agency, or it can be obtained internally using member savings. The loans collected can be given to an individual or a self-formed group. A capital guarantee programme is a type of bank guarantee. Guaranteed funds can be utilised for a variety of things, such as loan repayment and insurance claims. Several international and UN agencies have been working on developing international guarantee funds that banks and NGOs can join to lend or start microcredit programmes.
3**. COMMUNITY BANKING MODEL** The Community Banking concept takes the entire community as a single unit and builds semi-formal or formal institutions to disburse microfinance. Such institutions are frequently founded with the assistance of NGOs and other organisations, which also teach community members in the community bank's numerous financial activities. Savings components and other

revenue-generating projects may be included in the structure of these institutions. Community banks are frequently part of larger community development programmes that employ financial incentives to motivate people to take action. It has a lot in common with the village banking paradigm.

4. **COOPERATIVES MODEL** A co-operative is an autonomous group of people who have come together voluntarily to achieve their common economic, social, and cultural needs and objectives through a democratically governed and collectively owned business. The mandate of certain cooperatives includes member-financing and savings operations. “Taking into consideration the growth and potential of microfinance sector in India , other organisation ad international agencies have also made their entries in the sector by providing loans and grants to NGO‟s for different income generating projects as well as for incorporating microfinance in the service delivery projects of social development”(Nair and Tara, 2000). “Co-operative banks have been late entrants to micro-finance through SHGs. The performance of co-operative banks has to a large extent been influenced by the state government policies” (Joy, Deshmukh, and Murthy, Ranjani 2007). The model‟s unique features are as follows: “It consists of around 250 to 300 people. It started with smaller groups but slowly and gradually became bigger group. The group is divided into smaller groups and each group has a leader who is an elected member. The leader of the group has to keep the track records of savings, credit and loan creation and scrutiny of repayment of loans. The primary cooperatives constitute the General body and adopt a uniform set of laws. The Director and Chairperson are elected.”(Saptarshi M and Prashant P, YEAR?)

5. CREDIT UNIONS MODEL

A credit union is a member-owned and operated financial cooperative. It is operated by and made up of members of a specific group or organisation who have agreed to pool their funds and offer loans to one another at reasonable rates of interest. Members have a shared link, such as working for the same company, belonging to the same church, labour union, social fraternity, or living/working in the same neighbourhood. A credit union's membership is open to everyone who wants to be a part of the organisation, regardless of race, religion, colour, or creed. A credit union is a non-profit financial cooperative that is democratically run. Each is owned and administered by its members, who have a say in who the directors and committee representatives are elected.

6. GRAMEEN MODEL

The Grameen model emerged from the poor-focussed grassroots institution, Grameen Bank, started by Prof. Mohammed Yunus in Bangladesh. It essentially adopts the following methodology: A bank unit is set up with a Field Manager and a number of bank workers, covering an area of about 15 to 22 villages. The manager and workers start by visiting villages to familiarize themselves with the local milieu in which they will be operating and identify prospective clientele, as well as explain the purpose, functions, and mode of operation of the bank to the local population. Groups of five prospective borrowers are formed; in the first stage, only two of them are eligible for, and receive, a loan. The group is observed for a month to see if the members are conforming to rules of the bank. Only if the first two borrowers repay the principal plus interest over a period of fifty weeks do other members of the group become eligible themselves for a loan. Because of these restrictions, there is substantial group pressure to keep individual records clear. In this sense, collective responsibility of the group serves as collateral on the loan.

Features of Grameen Bank:

- High Recovery rate
- Women empowerment
- Low Transaction Cost
- No collaterals
- Repayment of Loans quicker and in smaller amounts
- Bank goes to customers.
- Less formalities
- 5 members as Team
- Training given for 7 days which is compulsory.
- 8 groups to form a centre.
- Bank official meets centre once a week.
- Discipline and dedication is encouraged.

Loan generally varies from Rs. 4000 to Rs. 10,000. Loan amount increases every year by Rs. 1000. Benefit of timely payment is to repeat loans and continuing access for the credit.

7. **GROUP MODEL** The Group Model's basic philosophy lies in the fact that shortcomings and weaknesses at the individual level are overcome by the collective responsibility and security afforded by the formation of a group of such individuals. The collective coming together of individual members is used for a number of purposes: educating and awareness building, collective bargaining power, peer pressure etc. The Group model is closely related to, and has inspired, many other lending models. These include Grameen, community banking, village banking, self-help, solidarity, peer pressure etc. "Apart from the SHG-bank linkage programme, many NGOs are using a variety of delivery mechanisms (including adaptations of Bangladesh Grameen Bank) for providing micro credits services with financial support from external donors and other apex institutions, including the Rashtriya Mahila Kosh (RMK) set up by the Government and the SIDBI Foundation for micro credit set up by a sister apex development institution"(Misra and Indira 2003). One example of the Group Model is "Joint Liability". When a group takes out a loan, they are jointly liable to repay the loan when one of the group's members defaults on the repayments.

8. INDIVIDUAL MODEL

This is a straightforward credit lending model where micro loans are given directly to the borrower. It does not include the formation of groups or generating peer pressures to ensure repayment. The individual model is, in many cases, a part of a larger 'credit plus' programme, where other socio-economic services such as skill development, education, and other outreach services are provided. "While the individual banking model is suited to lending to enterprises, the group model is best suited to lending to premicro enterprises and micro enterprises" (Vikas Batra and Sumanjeet, 2011).

9. **INTERMEDIARIES MODEL** Intermediary model of credit lending positions a 'go-between' organization between the lenders and borrowers. The intermediary plays a critical role of generating credit awareness and education among the borrowers including, in some cases, starting savings programmes. These activities are geared towards raising the 'credit worthiness' of the borrowers to a level sufficient enough to make them attractive to the lenders. The links developed by the intermediaries could cover funding, programme links, training and education, and research. Such activities can take place at various levels from international and national to regional, local, and individual levels. Intermediaries could be individual lenders.

10. **NGOs, model** microenterprise/microcredit programmes, and commercial banks (for government financed programmes). Lenders could be government agencies, commercial banks, international donors, etc. Most models mentioned here invariably have some form of organizational or operational intermediary - dealing directly with microcredit, or non-financial services. It is also called the 'partnership' model. MFIs like the Grameen Bank charge belowmarket rates to promote social equity". (Armendáriz de Aghion, Beatriz and Morduch, Jonathon.)

The NGOs work on:

• Providing Basic Education

• Promoting a feeling of Health and Hygiene in addition to developing saving and credit facilities.

• Encourage couples to start a family

. • Raising awareness about the importance of environmental protection

• Most importantly, fostering a gender-equal environment.

11. **PEER PRESSURE MODEL** Peer pressure relies on moral and other connections between borrowers and project participants to guarantee that microcredit programmes are completed and reimbursed. Peers could be other members of a borrowers group (in which the other members do not receive loans unless the original borrowers in the group repay).Hence pressure is put on the initial members to repay); community leaders usually identified, nurtured, and trained by external NGOs; NGOs themselves and their field officers; banks etc. Frequent visits to the defaulter, community meetings where they are recognised and asked to comply, and other forms of 'pressure' can be used. To ensure repayment among its loan groups, the Grameen model heavily relies on peer pressure.

12. **ROSCA MODEL ROSCAs**, or Rotating Savings and Credit Associations, are simply a group of people who assemble together and make regular cyclical contributions to a common fund, which is subsequently handed as a lump amount to one member each cycle.

13. **SMALL BUSINESS MODEL** "The prevailing vision of the 'informal sector' is one of survival, low productivity and very little value added. But this has been changing, as more and more importance is placed on small and medium enterprises (SMEs) - for generating employment, for increasing income and providing services which are lacking"(Srinivas, 2021).Direct interventions in the form of supporting systems such as training, technical advice, management principles, and so on, as well as indirect interventions in the form of an enabling policy and market environment, have traditionally been the focus of policies. Finance, notably microcredit, has always been a significant component that has been introduced as a sort of common denominator. Microcredit has been provided to SMEs directly, or as a part of a larger enterprise development programme, along with other inputs. Features Self-dependence between poorer sections of the society Leadership qualities generated within the community. Creation of Savings, credit and loan is being created. Training to the members by the members NGO trying to spread SHG model for educating and networking. Group members are generally of the same social strata. This is driven by women and women empowerment.

14. **THE SHG MODEL** Growth of SHG"s in India Structure of SHG A savings and credit organisation (SHG) is a group of roughly 10 to 20 people, often women, from a similar social class and region who come together to join a savings and credit organisation. They pooled their financial resources to provide their members with small interestbearing loans. This technique instils a value system that prioritises

saving over spending. "Many believe that savings mobilized from local depositors will ultimately be the largest source of capital for microfinance. Foreign capital provides 22 percent of funding for the „Top 100" MFIs, but savings is the first source of capital, representing 41 percent of all assets in 2005", (Reddy 2007). The setting of terms and conditions and accounting of the loan are done in the group by designated members.
The World Bank reports that societies that discriminate on the basis of gender are in greater poverty, have slower economic growth, weaker governance, and lower living standards. (World Bank. Engendering Development: Through Gender Equality in Rights, Resources,) • Ability to save and access loans. • Opportunity to undertake an economic activity. • Mobility-Opportunity to visit nearby towns. • Awareness- local issues, MFI procedures, banking transactions • Skills for income generation • Decision making within the household. • Group mobilization in support of individual clients- action on social issues • Role in community development activities

productivity can be defined as a way to measure efficiency. To take it a step further, it is how we measure the output that results from units of input. To provide an example, let's take a look at farming. Utilizing one acre of land, the input, to produce 50 stalks of corn, the output, is not very efficient. On the other hand, utilizing one acre of land to produce 3,000 stalks of corn is much more efficient and therefore productive. Translating this example to an office environment, business owners will want to see that the time and effort their employees spend on specific tasks, such as making phone calls to potential clients, performing research, or in meetings with colleagues, is helping to achieve the overall goals of the company.

The Productivity and Profitability Relationship

Understanding the importance of both productivity and profitability is key to running a successful business, as it is difficult to have one without the other. Research has shown that the most successful work environments are those that maintain a high level of employee engagement through continuous support, security, and making each team member feel valued. In work environments like this, employees are more likely to feel a vested interest in the success of the business, and are inspired to perform at a high rate of productivity. They'll want to go above and beyond, feel comfortable sharing innovative ideas, and form important, trusting relationships with coworkers. All of this positivity, in turn, ensures a company is profitable.

Productivity can be described as the measure of how efficiently any organization can utilize its available resources to generate goods or services. In short, productivity measures the final output any organization can produce for each input unit.

The prior objective of productivity is to make sure that there is utilization of the available resources, including time, labor, and time, in such a manner that it can maximize profitability and efficiency.

By enhancing the level of productivity and reducing the cost, a company or business can become more efficient and competitive.

Depending upon the industry in which you operate your business, there are various ways to evaluate productivity. However, some of the common measures include revenue per square foot or sales per employee.

Understanding Efficiency

When we talk about business efficiency, it defines the capability of any organization to minimize its time, effort, as well material while at the same time enhancing its profitability.

If we closely observe from a financial landscape, then efficiency can be defined by the correlation between the input and output of any organization.

In this case, the input is the resources that are essential to keep the operation ongoing, for instance, time, money, and the employees who are working for that particular organization.

Whereas the outcome can be described as the final outcome made by the company that covers customer acquisition, quality, and revenue.

Now you must be thinking what is the role or significance of the level of efficiency in any organization well, the answer is quite simple.

It becomes a tough task when you have to keep track of and improve the financial proficiency of any organization. If you are aware of the company's efficiency, then you can easily optimize the effort, time, and money to enhance the profit of the company in the long term.

Factors that affect productivity

Low productivity in business or the workplace is not something uncommon. But you can always rectify this, and you recognize where you are lagging. Here are some of the major reasons behind the low productivity:

1. Multitasking

Imagine you have been given two projects at a time, and the deadline is the next day, Now you had this in your mind that you have to finish it up before the headline, and for this reason, you started working on both projects at a time.

This will cause nothing but lots of stress to accomplish the tasks beforehand. This is a clear indication of low productivity. You will neither be able to deliver work on time nor keep your focus on a single task.

2. Stress at your workplace

Another major reason behind the low productivity is stress at your workplace. It can happen because of multiple reasons, such as lack of concentration, getting distracted, or your team being overburdened with the work pressure. All these things are clear signs of stress in the workplace.

3. Lack of acknowledgment of your work

Acknowledging the work done by the employees is the easiest way to manage and motivate the team. One of the key factors that affects productivity is lack of acknowledgment.

For instance, you have worked really hard to accomplish a task, and the final output becomes an asset for the company or business, The bare minimum gesture an employee would ever expect is an acknowledgment of their contribution to this entire task.

Most of the time, people neglect their team in terms of recognizing their contribution to the task. That becomes a reason behind low productivity in many cases.

4. Poor management

Last but not least reason behind the low productivity is poor management. In many cases, it was observed that managers do micromanagement, which directly affects the workflow of an employee.

No foolproof strategy, time management, and lack of clarity in achieving the final output are the factors that come under poor management. All these things can collectively cause low productivity for any company.

Factors that affect the efficiency

With the help of automation technology, you can easily monitor and report the level of efficiency in your company. There are different types of factors that can affect efficiency, which include:

1. Cutting off redundancy

One of the most common factors that can affect the efficiency of the company is redundancy or ineffective procedures in place. Most of the time, organizations keep the process because they have always done this; irrespective of this fact, the it is outdated and needs process improvement. Later on, these outdated methods can affect the growth of the company.

Periodic audits are one of the most essential factors for the growth of any company. By cutting off these redundant procedures, companies can improve their efficiency and easily streamline the entire workflow. The primary motto of the company is to include value-added systems and practices that will be satisfied by cutting off redundancy from the system.

2. Consistent Procedures

There is always a bridge between planning out the strategies and making them successful. That bridge is called implementing all the practices and procedures consistently. By the use of an operational process, a company will be capable of establishing cohesive structures that, later on can be replicated across all the departments.

This method will help you to keep everything on the same page and eliminate redundancy. By this, you can compensate for the loss and error caused by lack of confusion and communication.

3. Remove bottlenecks from the workflow.

Completely eliminating bottlenecks from any organization's workflow is one of the primary ways that can affect the organization's efficiency. Bottleneck effects are used in various areas of the workflow in any organization or business, which later becomes an obstacle to the company's profitability.

In case you are using this method in any step, it will create a certain limit for the ability of the system, and you will not be able to achieve the desired output. If you are consistently using this method, then that can affect the system of your organization, profitability, **business productivity** as well as the overall output of the company.

4. Performance Benchmarks KPIs

Another factor in this list is performance KPIs. Performance benchmarks are also called key performance indicators. A low KPI is a clear indication that there is a requirement for adjustments in one or many areas. Whereas in the case of high KPIs kit will clearly show how effectively the resources are used, including other primary factors such as time, labor, materials, and budget. All these factors are basically the backbone of operation efficiency.

5. Management of strategic relationships

During the execution of any plans, every business has relations that assist with daily task management, manufacturing products, and services. For instance, in the case of manufacturing, there is a correlation between the supplier of the materials and the organization that has taken it.

Just like that, there is a relationship between the head of the department and the employees working in that specific department. All these relationships are quite difficult to execute smoothly.

6. Current and long-term priorities

When there is a question on the level of operational efficiency, then setting long-term goals is quite essential. In order to grow any business, it is quite essential to have a clarity and defiable goal. It will help the company to achieve the targeted goals and profitability.

7. Executing plans

If you carefully plan out everything for the organization, then you can easily take your business from lackluster to setting a new benchmark and can make a good amount of profit out of it. By executing plans that have crystal clear goals and effective steps, you can easily enhance the level of efficiency of the business. Make sure to execute all your plans, including short-term goals and long-term benefits.

Difference between Productivity and Efficiency

In simple terms, productivity means the art of getting things done, while efficiency means doing things right. Here are some of the points that describe the key differences between productivity and efficiency:

Aspect	Productivity	Efficiency
Meaning	Achieving goals	Minimizing waste
Definition	Output per input	Goals with minimal effort
Calculates	Output / Input	Useful output / Total input
Motivation	Thrives on motivation	Relies on consistency
Quality	May prioritize quantity	Values both quality and quantity
Behavior Impact	Affected by distractions	Minimizes negative impact
Balancing	Can lead to burnout	Prioritizes well-being
Adaptability	May not encourage it	Promotes adaptability
Collaboration	Achievable individually	Thrives in teamwork

Risk Management in Microfinance

Introduction The new modern microfinance trend calls for the redesign of microfinance risk management. The literature has paid little attention to risk analysis in microfinance. Moreover, it has focused mainly on credit risk and fraud risks. But the particular nature of microfinance, the complexity of modern financial structures, the variety of beneficiaries and institutions involved require a more structured approach of risk management. This chapter aims to lay the basis for a risk management model that could fit modern microfinance. In order to achieve this, the first step is to set a taxonomy of risk for microfinance.

A rational investor, then, would be interested in measuring ex ante the level of risk associated with each investment in order to estimate the risk–return trade-off and to decide whether to invest and at what price. Since rational investors incorporate expected changes in their decisions, the effective risks arise only from unexpected changes. Risk management, then, deals with the definition, the measurement and the control of risks (expected and unexpected changes) in order to price the investment correctly and to reduce losses determined by changes in future events or outcomes. The scarce attention dedicated to risk management in microfinance can be explained mainly by the fact that the main goal of microfinance lies in social and humanitarian objectives. This approach, together with the dependency from public subsidies, has created a tendency to underestimate the financial performance of microfinance programmes or institutions. In recent years, the need for private resources has stimulated a growing awareness among practitioners of the concept of sustainability.

CATEGORIES OF MICROFINANCE RISK

At the initial stages of growth in the microfinance industry, most MFIs were concerned only about financial risks.

Even in the financial risk category, their focus was almost exclusively on credit risk. When the demand for loans began to rise exponentially, MFIs also began to be concerned about a particular type of liquidity risk wherein the MFIs would run out of enough cash to meet the demand for loans.

The industry evolution has brought additional risks. In a publication released in 2000, Deutsche Gesellschaft für Technische Zusammenarbeit (GTZ) cited three major risk categories: financial, operational, and strategic. GTZ also listed subcategories of risk under each main category. More recently, Churchill and Frankiewicz (2006) listed four risk categories, namely: institutional risks, operational risks, financial management risks, and external risks. As shown in Table 1, they also identify subcategories of risks in each primary category.

Table 1: Typology of risk in microfinance

Source				
GTZ (2000)	**Financial Risks** 1. Credit Risk is the risk to earnings or capital due to borrowers' late and nonpayment of loan obligations. Credit risk includes both transaction risk and portfolio risk. - Transaction Risk refers to the risk in individual loans. - Portfolio Risk refers to the risk inherent in the composition of the overall loan portfolio. 2. Liquidity Risk is the risk that an MFI cannot meet its obligations on a timely basis. 3. Market Risk includes interest rate risk, foreign currency risk, and investment portfolio risk. - Interest Rate Risk is the risk of financial loss from changes in market interest rates. - Foreign Exchange Risk is the potential for loss of earnings or capital resulting from fluctuations in currency values. MFIs most often experience this risk when they borrow or mobilize savings in foreign currency and lend in local currency. - Investment Portfolio Risk refers to longer-term investments decisions rather than short-term liquidity or cash management decisions.	**Operational Risks*** 1. Operational Transaction Risk: the document does not give a definition) - Human Resources Risk: (the document does not give a definition) - Information and Technology Risk is the potential that inadequate technology and information systems will result in unexpected losses. 2. Fraud Risk is the risk of loss or earnings or capital as a result of intentional deception by an employee or client. 3. Regulatory and Legal Compliance Risk is the risk of loss resulting from noncompliance with the country's regulations and laws.	**Strategic Risks** 1. Governance Risk is the risk of having an inadequate structure or body to make effective decisions. This risk arises from an ineffective oversight, poor governance structure, or both of these. 2. Reputation Risk refers to the risk to earnings or capital arising from negative public opinion, which may affect an MFI's ability to sell products and services or its access to capital or cash funds. 3. External Business Environment Risk refers to the inherent risks to the MFI's business activity arising from the external business environment.	
Churchill and Frankiewicz (2006)	**Institutional Risks** 1. Social Mission 2. Commercial Mission 3. Dependency 4. Strategic 5. Reputation	**Financial Management Risks** 1. Asset and Liability 2. Inefficiency 3. System Integrity	**External Risks** 1. Regulatory 2. Competition 3. Demographic 4. Macro-economic 5. Environmental 6. Political	**Operational Risks** 1. Credit 2. Fraud 3. Security 4. Personnel

Asian Journal of Agriculture and Development, Vol. 4, No. 2 4

Priority Sector Lending

- What is Priority Sector Lending?
- Understand the Priority Sector Lending in-details
- Categories of the Priority Sector Lending

What is Priority Sector Lending?

Priority sector lending refers to the mandatory lending requirement imposed on banks by the Reserve Bank of India (RBI) to ensure that a certain portion of their lending is directed toward the priority sectors of the economy. The priority sectors are identified as those sectors which are crucial for the growth and development of the economy but may not have access to credit from traditional sources.

Understand the Priority Sector Lending in-detail

Here is a glossary of key terms related to priority sector lending:

1. Priority sector:

The sectors identified by the RBI for priority sector lending includes agriculture, micro, small and medium enterprises (MSMEs), education, housing, and other specified weaker sections and segments of society which are crucial for the growth and development of the economy.

2. Priority sector lending targets:

The percentage of total bank loans that must be directed towards priority sectors, as set by the RBI. Currently, the target for total priority sector lending is set at 40% of Adjusted Net Bank Credit (ANBC) or Credit Equivalent Amount whichever is higher.

Categories of Priority Sector Lending

In broadly, priority sector lending can be categorized into the following sectors:

- Priority Sector Lending for Agriculture
- Priority Sector Lending for Weaker sections
- Priority Sector Lending for MSMEs
- Priority Sector Lending for Education
- Priority Sector Lending for Non-performing assets

Priority Sector Lending for Agriculture

The primary sector of the economy, which includes farming, cultivation of crops, livestock rearing, fisheries, and forestry, requires direct or indirect finance to the individual farmers by the scheduled commercial banks. Priority sector lending includes short-term, medium/long-term direct or indirect loans and credits to the farmers, such as Farm Credit, Ancillary Activities, and even Agriculture Infrastructure.

Priority Sector Lending for Weaker sections

Here, Priority sector lending is given to those sections of society that are socio-economically disadvantaged, such as low-income groups, minorities, and women.

Priority Sector Lending for MSMEs

Micro enterprises are the ones where the investment in plant and machinery or equipment does not exceed one crore rupees and turnover does not exceed five crore rupees.

Small enterprises are the ones where the investment in plant and machinery or equipment does not exceed ten crore rupees and turnover does not exceed fifty crore rupees.

Medium enterprise, where the investment in plant and machinery or equipment does not exceed fifty crore rupees and turnover does not exceed two hundred and fifty crore rupees

In this category, the Priority sector lending involves small or medium Enterprises that manufacture, process, or preserve goods or services with investment in plant and machinery up to INR 50 million and INR 250 million, respectively.

Priority Sector Lending for Education

In this category, Priority sector lending involves loans to individuals for educational purposes, including vocational courses, not exceeding Rs 20 lakh..

Priority Sector Lending for Non-performing assets

Generally, in this sort of Priority sector lending, loans that have stopped generating income for the lender or have been in default for a specified period.

Other activities covered under priority sector lending

Other than the above, some other main categories also involve priority sector lending, such as education loans, microcredit, housing loans, Renewable Energy, Social infrastructure, etc.

What are Development Banks?

- Development banks are nothing but financial institutions providing long-term funds for capital-intensive investments for a long period of time. Their lending yields low rates of returns, such as irrigation systems, urban infrastructure, mining, and heavy industries, etc.

- They are also known as development finance institutions (DFI) or long-term lending institutions.
- These banks lend at low and stable interest rates so as to promote long-term investments along with social benefits.
- Development banks are not the same as commercial ones. Instead, development banks mobilize short to medium-term deposits and lend for similar periods of tenure to avoid a maturity mismatch, which causes a bank's solvency and liquidity.

Features

- Unlike commercial banks, the development banks do not accept deposits from the public. Hence, they do not entirely depend upon saving mobilization.
- Development banks are specialized institutions that provide medium and long-term credit lending facilities.
- Their main objective is to serve the public interest instead of earning profits.
- They provide financial assistance to both public as well as private sector institutions.

Importance of Development Banks

- Lays the foundation for industrial growth and development in the country
- Meets long-term capital needs
- Undertakes promotional activities
- Helps small and medium sectors

Objectives

- Promotion of industrial growth
- Creation of employment opportunities
- Promotion of self-employment projects
- Reviving sick units
- Improving the capital market in the country
- To generate more exports and promote import substitution
- To promote science and technology in new areas by extending risk capital
- Improving the management of large industries by providing them adequate training
- Encouraging modernization and improvement in the technology sector

Various Types of Development Banks in India

In this section, we shall learn more about the different types of development banks in India. These include:

- SIDBI (Small Industries Development Bank of India)
- EXIM (Export-Import Bank of India)
- NABARD (National Bank for Agriculture & Rural Development)
- NHB (National Housing Bank)
- IFCI (Industrial Finance Corporation of India)
- IDBI (Industrial Development Bank of India)

Below, let us see in detail about all the above-listed banks in terms of their functions and objectives.

SIDBI

The Small Industries Development Bank of India (SIDBI) was set up in 1990 under an Act of Parliament. It was a wholly-owned subsidiary of the Industrial Development Bank of India. Presently, SIDBI's ownership is held by 33 government of India-owned/ controlled institutions. SIDBI is headquartered in Lucknow.

SIDBI Functions:

- To take initiatives for technical upgradation and modernization of the existing units.
- To expand the channels for marketing the small-scale industry products in both domestic as well as international markets.
- To promote employment-generating industries, particularly in the semi-urban areas for creating more employment opportunities.
- To keep a check on the migration of the people to urban areas.

NABARD

The National Bank for Agriculture & Rural Development (NABARD) is the prime development bank in India. Under the special act by the parliament, the NABARD was set up on 12th July 1982.

Its main focus is to uplift rural India by increasing the credit flow for the promotion of the agriculture and non-farm sector. NABARD is headquartered in Bombay (Maharashtra). It is considered as the apex bank of the country, which takes care of the cottage industry, small and village industries, and other rural establishments.

Role:

- To undertake to monitor and evaluating projects it has been refinancing
- Refinancing the financial institutions that finance the rural sector
- Regulating the institutions that provide financial assistance to the rural economy
- Providing training facilities to the institutions assisting the rural development
- Regulating the cooperative banks and the Regional Rural Banks (RRBs) in India

EXIM Bank

The Export-Import Bank of India (EXIM Bank) is a financial institution created by the Export-Import Bank of India Act of 1981. It is a public sector financial institution. The main aim of the EXIM Bank is to finance the Indian exports that generate foreign exchange for the country. It also extends term loans for foreign trade.

The Financial Statements and Operational Reports The purpose of financial management is to maintain financial integrity and high performance levels within the microfinance institution. Financial management helps the organisation evaluate performance, plan, and make decisions. Financial reports allow the manager to sort through all the information generated, and to organise it into a meaningful framework. Financial information is like a map that tells what is actually going on in an MFI and where it is headed. Who uses Financial Information? The key stakeholders of the organisation all need access to financial information. Key stakeholders include: MFI credit staff (supervisors and credit officers), Branch managers, the Executive Director, and the Board of Directors. There are also external stakeholders like banks, donors, investors, raters and perhaps also the Central Bank, if the MFI is regulated. What Financial Information and Reports? Generally, an MFI's financial status can be determined by three types of financial reports that have their basis in two separate, yet interdependent systems: Financial statements (from the accounting system) – the Balance Sheet, the Income and Expense statement Cash flow statements (from the accounting system) – Cash Flow Statements; Cash Flow Projections can be prepared from the statements as well in order to plan for smooth operations Portfolio reports (from the client portfolio system, essentially the sub-ledger of the accounting system) and operational reports The Financial Statements The starting point for sound financial management is the timely and accurate production of financial reports. This is absolutely critical to the health of a microfinance program. If financial records are not produced accurately and punctually, the ratio analysis becomes misleading and unreliable. An MFI should produce financial statements from its accounting system on a monthly basis. Though the particular format varies somewhat from country to country, financial statements include: the Income Statement, also called Profit and Loss Statement, or Income and Expense Statement, and the Balance Sheet

The EXIM Bank is a statutory corporation wholly owned by the government of India. It was established on 01st January 1982 with an aim to finance, facilitate, and promote foreign trade in India.

Functions:

- **To finance imports and exports of goods and or services in India as well as in the developing countries in the world.**

- To provide a lease for exports and imports of machinery and equipment
- To finance joint ventures in the foreign countries
- To undertake limited merchant banking operations like the issue of shares, bonds, stocks, debentures, etc. of the Indian companies involved in the international trade.
- To provide technical, financial, and administrative assistance to businesses that carry out export and import.

National Housing Bank

The National Housing Bank (NHB) is a state-owned bank and regulatory authority in India established under section 6 of the National Housing Bank Act of 1987. It was created on 08th July 1988. The NHB is headquartered in New Delhi.

The NHB is responsible for regulating and re-financing social housing activities including research, etc. It is owned by the Reserve Bank of India and was established to promote private real estate acquisition. The institution further aims to promote inclusive expansion with stability in the housing finance sector.

Functions

One of the major activities of the NHB includes extending financial assistance to various eligible bodies in the housing sector through:

Refinance: The NHB extends refinancing to various primary lending firms like scheduled banks, housing finance companies, cooperative sector bodies, etc.

Direct Finance: NHB also offers direct finance for integrated land development and shelter projects of public agencies in respect of land development and shelter projects, housing infrastructure projects, etc.

IFCI

The IFCI (Industrial Finance Corporation of India) was the first specialized financial institution to provide term finance to large businesses in India. It was set up under the Industrial Finance Corporation Act (1948) on 01st July 1948.

Objectives of IFCI

The primary objective of the IFCI is to provide long and medium-term financial offerings to large-scale businesses. It especially offers its services when ordinary bank accommodation does not suit the undertaking or the finance cannot be raised in a profitable manner from the issue of shares.

Functions of IFCI

- Setting up a new industrial undertaking
- Expansion and/ or diversification of existing industrial business
- Renovation and modernization of existing businesses
- Meeting the working capital needs of the industries, with some exceptions

IDBI

The Industrial Development Bank of India, popularly known as IDBI, came into existence as a Development Institution under the IDBI Act of 1964. It is headquartered in Bombay, Maharashtra.

The IDBI is regarded as a public financial institution as per the Companies Act 1956. It continued as DPI till 2004 when it was converted into a banking organization. The Industrial Development Bank of India Act of 2003 was passed to convert the DPI into a bank.

Under the name of the Industrial Development Bank of India Ltd., a new company was incorporated as a government company under the Companies Act on 27th

September 2004. Thus, w.e.f. 01st October 2004, it came to be known as IDBI Ltd. it works as a bank in terms of the Repeal Act.

The IDBI Bank Ltd. was finally merged with IDBI Ltd. and was known as IDBI Ltd. with effect from 02nd April 2005. It is a public sector bank as the government of India owns more than 70% shareholding of the bank.

Income Statement presentation generally includes two or even more columns of data. It will show the current period's activity, and also a column that shows the past period's activity. Some MFIs show budget columns, percentage of budget, current quarter activity, year to date activity and so on. Information on the Income Statement is normally divided between revenue accounts and expense accounts. It also generally segregates operating from non-operating accounts. Operating accounts relate to the core business of an MFI – its financial service activity. Non-operating accounts include any revenue and expenses from other activities. Income Income is what a microfinance organisation receives for what it does, provide financial services, including lending money. MFIs also generate income from non-operating activities – such as training, the sale of merchandise or books, and from external sources. Most MFIs generate internal income from their financial service activity.
These include:
interest income
fees for services
penalties for late loan payments
registration and application fees
External income is the amount received as grants from donors in support of the MFI. It is generally considered as non-operating activity and reported on separately in the Income and Expense Statement.
This enables analysis and performance to be measured on the basis of microfinance activities only. Expenses Expenses are costs the MFI must incur to carry out its activities. Expenses are broken down into different categories such as salaries, rent and transportation. Expenses are usually considered direct or indirect. Direct expenses are those which relate to a particular activity, product or service.
For example, salaries for credit officers are the direct expense of the credit department. Indirect expenses, also called overhead, are those expenses which cannot be tied exclusively to a single activity. For example, the salary of the Executive Director is considered overhead when he/she is part of an MFI that has many products and services, and may also provide non-financial services to its clients. Typical expenses for the MFI include: financial costs (interest on loans or debt investments, interest paid on deposits or any other client savings) provision for loan losses (the estimate of future losses incurred) operating expenses (all other expenses incurred in operating the activities of the MFI) Handout 2.1 Sample Income and Expense Statement illustrates a typical MFI Income and Expense Statement. It is taken from the SEEP document "Measuring Performance of Microfinance Institutions: A Framework for Reporting, Analysis, and Monitoring", 2005. The Balance Sheet The balance sheet is a statement of financial position of the MFI at a particular point in time. It is like a stock statement, giving account for the MFI's financial structure. It reflects the state of affairs on a given date, usually at the end of a particular period, a month or a year. Most MFIs produce a balance sheet on a monthly basis at a minimum, giving the ending balance of all assets, liabilities and equity accounts – the three balance sheet components. Equity is also referred to as net worth or capital at

times. A balance sheet always balances, meaning that the debits must equal the credits. The basic accounting equation applies to the balance sheet:

Microfinance in India

The Self-Employed Women's Association (SEWA) in Gujarat was the first to pioneer microfinance in India, establishing SEWA Bank in 1974. Since then, this bank has been providing financial services to those in rural areas who want to start their own enterprises. Kudumbashree, Kerala's Poverty Eradication Mission, which began in 1998, is an example of a successful initiative. Neighborhood Groups (NHGs) is a female-led community organization that brings women from rural and urban communities together to fight for their rights and empower them.

Women work on a number of subjects through these NHGs, including health, nutrition, and agriculture. They can earn money and apply for microcredit while working under this programme. Small-scale efforts like these help people in impoverished places gain financial independence.

To meet the needs of India's huge rural population, microfinance facilities are required. Microfinance's key goals in India should be to promote socioeconomic development at the grassroots level through a community-based strategy, empower women, and increase household income.

The formation of the Self Help Group (SHG) – Bank Linkage Programme (SBLP), which began as a pilot project in 1992 by NABARD, lay the groundwork for the microfinance movement. The programme was a success, and it has now become India's most popular microfinance model. Microfinance has so become a popular catchphrase in India

Current Trends in Microfinance: The Growth of Commercial Microfinance

As commercial banks have realized that poor people's finance can be profitable, an increasing number have gone down market to tap lower income clientele. The World Bank's microfinance unit, the Consultative Group to Assist the Poor, estimates that there are currently around 225 commercial banks "engaged in microfinance"— a figure that is increasing.

The main reasons for the emergence of commercial banks at the low-income level are:

1) Competition in existing markets driving banks into new ones, 2) Excellent repayment rates by micro-entrepreneurs, and

3) Technology allowing the poor greater access while transactions remain cost-effective. Though governments in some developing countries have required commercial banks to work in certain sectors, banks are increasingly lured in by the low risk, stability, and potential growth opportunities in the microfinance market. They are entering either directly by utilizing their own resources such as an internal microfinance unit, or with existing providers through partnerships.

Partnerships between MFIs and commercial banks have enabled each to leverage their competitive advantages. While MFIs are more knowledgeable at the community level for instance, banks have the advantage in greater access to capital and existing infrastructure. The meeting of the commercial and microfinance sectors has come about through their collaboration. MFIs have scaled up to "access higher levels of credit, augment their portfolios, and strengthen management and efficiency levels," while commercial banks have purposely scaled down to profit from this emerging industry. Both types of institutions "scale-up and scale-down" by redesigning their financial products to suite the clientele they are targeting.

Integration between these sectors leads to another current trend in microfinance—the increase in deposits as a source of funding. It is important for MFIs to turn from foreign debt investment, which is vulnerable to foreign exchange risk, to their own domestic and regional markets so that *domestic* savings can be transformed into "productive loans for the poor." Due to limited knowledge and a lack of trust beyond the community, the local poor may therefore be more inclined to make deposits into local savings accounts. Within the last year for instance, the number of accessible savings and loan accounts among the poor has gone from 750 million to 1.4 billion. Furthermore, and importantly, foreign currency risk can be avoided when MFIs borrow and lend in the local denomination.

One of the main links between these trends is technological advancement. Efficient technology has allowed smaller and simpler banking transactions to become more cost effective, motivating commercial banks to scale down and reach a greater number of people. Low cost ATMS with picture and voice prompts for example, are bringing in rural and illiterate clientele. An in-country example is the State Bank of India, which is reaching out to whole villages through 10,000 personal computer kiosks with ATMs.

Regional MFIs that are scaling up on the other hand, are able to link into international ATM networks, forcing greater integration of the two sectors. Local currency deposits have the potential to increase further from an expansion of service machines and phone banking systems. Such progress in physical banking and financial services infrastructure poises microfinance to emerge as an asset class.

FINANCIAL SECTOR IN INDIA :

REGULATIONS AND REFORMS INTRODUCTION India‟s financial sector is diversified and expanding rapidly. It comprises commercial banks, insurance companies, non-banking financial companies, cooperatives, pensions funds, mutual funds and other smaller financial entities1 . Ours is a bank dominated financial sector and commercial banks account for over 60 per cent of the total assets of the financial system followed by the Insurance. Other bank intermediaries include regional rural banks and cooperative banks that target under serviced rural and urban populations. Many non banking finance companies (NBFC) operate in specialized segments (leasing, factoring, micro finance, infrastructure finance), though some can accept deposits. Pension provision covers 12 percent of the working population and consists of civil service arrangements, a compulsory scheme for formal private sector employees, and private scheme offered through insurance companies.

CURRENT REGULATORS OF THE FINANCIAL SYSTEM

The regulation and supervision of the financial system in India is carried out by different regulatory authorities. The Reserve Bank of India (RBI) regulates and supervises the major part of the financial system. The supervisory role of the RBI covers commercial banks, urban cooperative banks (UCBs), some financial institutions and non-banking finance companies (NBFCs). Some of the financial institutions, in turn, regulate or supervise other institutions in the financial sector, for instance, Regional Rural Banks and the Co-operative banks are supervised by National Bank for Agriculture and Rural Development (NABARD); and housing finance companies by National Housing Bank(NHB). Department of Company Affairs (DCA), Government of India regulates deposit taking activities of corporate, other than NBFCS. registered under companies Act, but not those which are under separate statutes. The Registrar of Cooperatives of different states in the case of single state cooperatives and the Central Government in the case of multi-state cooperatives are joint regulators, with the RBI for UCBs, and with NABARD for rural cooperatives. Whereas RBI and NABARD are concerned with the banking functions of the cooperatives, management control rests with the State/ Central Government. This „dual control‟ impacts the supervision and regulation of the cooperative banks. The capital market, mutual funds, and other capital market intermediaries are regulated by Securities and Exchange Board of India (SEBI), Insurance Regulatory and Development Authority (IRDA) regulates the insurance sector; and the Pension Funds Regulatory and Development Authority (PFRDA) regulates the pension funds

SALIENT FEATURES OF THE PRESENT REGULATIONS

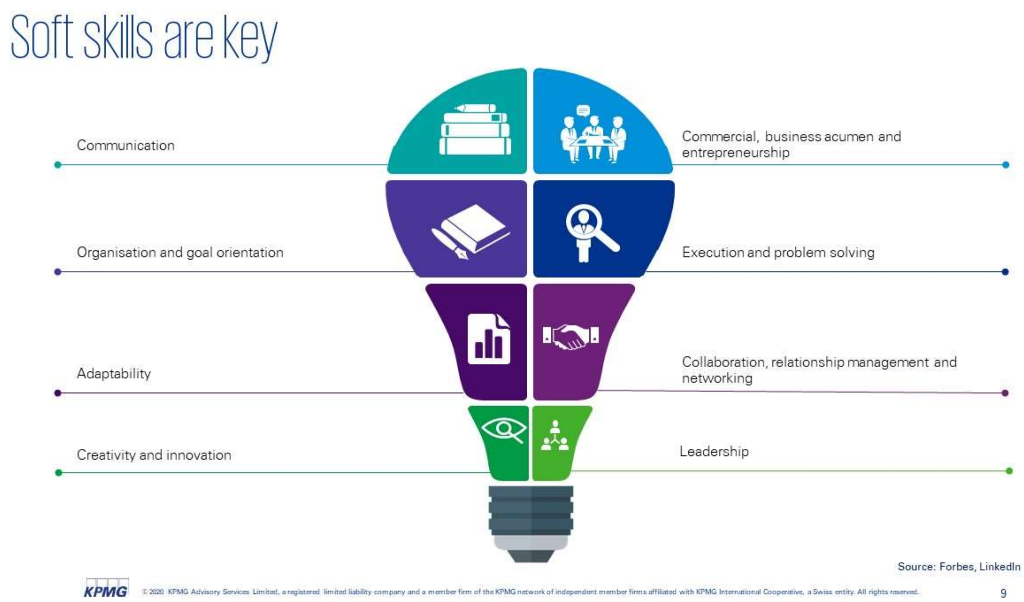
At present, financial regulation in India is oriented towards product regulation, i.e. each product is separately regulated. For example, fixed deposits and other banking products are regulated by the Reserve Bank of India (RBI), small savings products by the Government of India (GoI), mutual funds and equity markets by the Securities and Exchange Board of India (SEBI), insurance by the Insurance Regulatory Development Authority of India (IRDA) and the New Pension Scheme (NPS) by the Pension Fund Regulatory and Development Authority (PFRDA). All these regulators have a key mandate to protect the interests of customers - these may be investors, policy holders or pension fund subscribers, depending on the product4 . India has a legacy financial regulatory architecture. The present work allocation between RBI, SEBI, IRDA, PFRDA, and Forward Market Commission (FMC). designed; it has evolved over the years, with a sequence of piecemeal decisions responding to immediate pressures from time to time5 . Each regulator have their own rules on registration, code of conduct, commissions and fees to monitor the product providers and distributors. RBI, SEBI and IRDA have grievance redress procedures through sector financial Ombudsmen service

FINANCIAL SECTOR REFORMS IN INDIA

The role of the financial system in India, until the early 1990s, was primarily restricted to the function of channeling resources from the surplus to deficit sectors. Whereas the financial system performed this role reasonably well, its operations came to be marked by some serious deficiencies over the years. The banking sector suffered from lack of competition, low capital base, low productivity and high intermediation cost.

The main thrust of reforms in the financial sector was on the creation of efficient and stable financial institutions and markets. Reforms in respect of the banking as well as non-banking financial institutions focused on creating a deregulated environment and enabling free play of market forces while at the same time strengthening the prudential norms and the supervisory system. In the banking sector, the focus was on imparting operational flexibility and functional autonomy with a view to enhancing efficiency, productivity and profitability, imparting strength to the system and ensuring accountability and financial soundness. The restrictions on activities undertaken by the existing institutions were gradually relaxed and barriers to entry in the banking sector were removed.

According to **Dr. C. Rangarajan** there are six approaches to financial inclusion , and they are as follows: Going beyond credit and providing a helping hand to the rural areas Simplifcation of procedure Commercial Banks to open for granting loans to small branches in rural areas borrowers Effective implementation of Strengthening the SHG-Bank business facilitator and Linkage program correspondent models As evident from the infographic above, almost all of them pertain to the microfinance industry. Microfinance is contributing towards all these approaches and slowly but successfully accelerating financial inclusion. The regulators play an important role in driving responsible, inclusive formal credit while striking a balance between providing growth, managing risks and not over burdening borrowers with excess debt. Given the importance of MFIs in providing credit to the masses and the rapid growth of NBFC-MFIs, the regulator - the Reserve Bank of India (RBI) recognised Microfinance Institutional Network (MFIN), followed by Sa-Dhan as two Selfregulatory Organizations (SRO) formed to assist the Microfinance sector. All NBFC-MFIs are encouraged to be part of at least one SRO and are expected to follow the code of conduct of that particular SRO.



Microfinance in this regard has proven an important tool for achieving something that several public and private agencies alike have been attempting for a number of years now – bringing women into the financial arena. Reports have suggested that India's economy could benefit significantly from better inclusion, and many have been involved in promoting this scenario.

Global management consultancy Accenture, for instance, set up a learning centre for rural girls in 2016, equipped with state-of-the-art educational facilities. In February last year, Big Four accounting and advisory firm Deloitte launched the WorldClass programme, aimed at training as many as 10 million women in India over the next decade.

Microfinance appears to be serving a crucial purpose in the Indian economy, which has been driven by a variety of actors. The Reserve Bank of India has kept a watchful eye on the sector, with the intention of protecting borrowers and lenders alike, given the high levels of financial risk involved.

The importance of microfinance

Microfinance holds profound importance as a potent tool for socio-economic transformation, particularly in low-income and underserved communities. By providing financial services such as credit, savings, insurance, and payment systems to individuals who are traditionally excluded from formal financial institutions, microfinance empowers individuals to break free from the cycle of poverty. This empowerment takes various forms, from fostering entrepreneurship and livelihood generation to promoting women's economic autonomy and enabling access to critical services like education and healthcare. Moreover, microfinance often operates through community-based models like Self-Help Groups (SHGs), fostering social cohesion and community development. As a result, microfinance acts as a catalyst for financial inclusion, poverty alleviation, gender equality, and overall local economic growth, driving sustainable development in diverse contexts worldwide.

The importance of microfinance extends beyond financial empowerment, as it addresses broader issues of social inequality and economic disparity. It recognizes the potential of marginalized communities and leverages financial tools to unlock that potential, facilitating grassroots development and creating pathways for individuals to actively contribute to their own betterment. By offering opportunities for self-sufficiency, resilience-building, and fostering a sense of ownership and agency, microfinance serves as a critical bridge towards a more equitable and inclusive society.

The current status of microfinance in India

Microfinance recorded a growth of 21% in FY2023 at INR 3,51,521 crore, compared to the previous year's INR 2,89,845 crore, as per a report by Sa-Dhan. The same report states that NBFCs and MFIs have recorded double-digit growth in the same period (49% and 37%, respectively). Total disbursements of all lenders was at INR 3,19,948 crore compared to INR 2,53,966 crore in FY 2021-22. Additionally, the number of loan accounts for microfinance recorded a YoY growth of 10% in FY 2022-23.

Impact: Empowerment and Alleviation

Despite the challenges, the impact of microfinance in India has been remarkable:

1. **Poverty Alleviation:** Microfinance has provided the poor with access to credit for income-generating activities, breaking the cycle of poverty and enabling economic mobility.
2. **Women Empowerment:** A significant proportion of microfinance borrowers are women. Access to credit has empowered them to become active participants in their households and communities.
3. **Financial Inclusion:** Microfinance has played a pivotal role in bringing the unbanked and underbanked population into the formal financial system, fostering financial inclusion.
4. **Employment Generation:** The funds from microfinance have contributed to the growth of small businesses, leading to job creation and local economic development.
5. **Education and Healthcare:** Improved access to credit has enabled families to invest in education and healthcare, resulting in improved overall well-being.
6. **Community Development:** Through SHGs and community-based approaches, microfinance has facilitated social cohesion and community development.

The Future of Microfinance

A major source of financing for the poor and no longer a niche industry Over the past four decades, microfinance—the provision of loans, savings, and insurance to small businesses and entrepreneurs shut out of traditional capital markets—has grown from a niche service in Bangladesh and a few other countries to a significant global source of financing.

Some 200 million people globally now receive support from microfinance institutions, with most of the recipients in the developing world. In the beginning, much of the microfinance industry was managed by non-governmental organizations, but today the majority of these institutions are commercial and regulated by governments, and they provide safe places for the poor to save, as well as offering much-needed capital and other financial services.

Now out of infancy, the microfinance industry faces major challenges, including its ability to deal with mobile banking and other technology and concerns that some markets are now over-saturated with microfinance. How the industry deals with these and other challenges will determine whether it will continue to grow or will be subsumed within the larger global financial sector. This book is based on the results of a workshop at Lehigh University among thirty-four leaders in the industry.

The editors, working with contributions from more than a dozen leading authorities in the field, tell the important story of how microfinance developed, how it has met the needs of hundreds of millions of people, and they address key questions about how it can continue to meet those needs in the future.