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A REVIEW ON GROWTH OF MFI'S OVER THE YEARS

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Abstract:

Microfinance sector has grown rapidly over the past few decades. Nobel Laureate Muhammad Yunus is credited with laying the foundation of the modern MFIs with establishment of Grameen Bank, Bangladesh in 1976. Today it has evolved into a vibrant industry exhibiting a variety of business models. Microfinance Institutions (MFIs) in India exist as NGOs (registered as societies or trusts), Section 25 companies and Non-Banking Financial Companies (NBFCs). Commercial Banks, Regional Rural Banks (RRBs), cooperative societies and other large lenders have played an important role in providing refinance facility to MFIs. Banks have also leveraged the Self-Help Group (SHGs) channel to provide direct credit to group borrowers. The research has takes a look at the growth of MFI's over the years in India.

Introduction

Microfinance is the provision of financial services to low-income clients or solidarity lending groups including consumers and the self-employed, who traditionally lack access to banking and related services.

Microfinance is not just about giving micro credit to the poor rather it is an economic development tool whose objective is to assist poor to work their way out of poverty. It covers a wide range of services like credit, savings, insurance, remittance and also non-financial services like training, counselling etc.

Salient features of Microfinance:

- Borrowers are from the low income group
- Loans are of small amount – micro loans
- Short duration loans
- Loans are offered without collaterals
- High frequency of repayment
- Loans are generally taken for income generation purpose

Micro Finance Institutions

Those institutions which have microfinance as their main operation are known as micro finance institutions. A number of organizations with varied size and legal forms offer microfinance service. These institutions lend through the concept of Joint Liability Group (JLG). A JLG is an informal group comprising of 5 to 10 individual members who come together for the purpose of availing bank loans either individually or through the group mechanism against a mutual guarantee. The reason for existence of separate institutions i.e. MFIs for offering microfinance are as follows:

- High transaction cost – generally micro credits fall below the break-even point of providing loans by banks
- Absence of collaterals – the poor usually are not in a state to offer collaterals to secure the credit
- Loans are generally taken for very short duration periods
- Higher frequency of repayment of installments and higher rate of Default

Non-Banking Financial Companies (NBFCs), Co-operative societies, Section-25 companies, Societies and Trusts, all such institutions operating in microfinance sector constitute MFIs and together they account for about 42 percent of the microfinance sector in terms of loan portfolio. The MFI channel is dominated by NBFCs which cover more than 80 percent of the total loan portfolio through the MFI channel.

Sl. No.	Type of MFI	Number	Legal Registration
Not-for Profit MFIs			
1	NGOs	400-500	Society Registration Act, 1860 Indian Trust Act, 1882
2	Non-Profit companies	20	Section-25 of Indian Companies Act, 1956
Mutual Benefit MFIs			
3	Mutual benefit MFIs – Mutually Aided Cooperative Societies (MACS)	200-250	Mutually Aided Co-operative societies, Act enacted by State Governments
For Profit MFIs			
4	Non-Banking Financial Companies (NBFCs)	45	Indian companies Act, 1956 Reserve Bank of India Act, 1934

Indian Microfinance industry will continue to demonstrate sustainable growth

The microfinance industry has seen tremendous growth over the past five years, growing at a 45% CAGR. It has witnessed rapid evolution with regulatory reforms post the Andhra Pradesh crisis in 2010 to regulate product, pricing and protection of customer interest. This included the growth of regulated NBFC MFIs - a special class of RBI regulated entities carrying out microfinance, the formation of the first ever Self-Regulatory Organizations (SROs) of the RBI, Aadhar based lending by NBFC MFIs an and transformation of some of the entities into universal and small finance banks.

Today, with over 45 million end clients with a loan outstanding of over Rs 1 lakh crore across the private JLG (Joint Liability Group) and the public SHG (Self Help Group) programmes, employing over 120,000 people across 10000 branches in 28 states of India, it is a key force for financial inclusion in the country. However, this level of progress is still lower than 25% of the demand across India and indicates the future potential for growth.

The key reason for the growth of the sectorr has been adaptability to change, resilience in the face of challenges and an ability to maintain high repayment rates of almost 99.5%. The Nobel Prize winning Grameen model of social collateral combined with a high touch model and rigorous credit bureau discipline has helped to maintain high levels of repayment for small ticket sized unsecured loans.

The USPs of the sector have been microloans, door step delivery and frequent repayments. The business thrives on a very high level of customer connect before, during and after the credit approval with all clients being met face to face in a weekly, fortnightly or a monthly meeting for about 30-45 minutes in a group setting. Unfortunately, the business is still highly cash oriented - both on disbursements and repayments.

With demonetisation, this proved to be an Achilles heel for the sector. Lack of availability of new notes hit the informal cash intensive economy of the low income groups served by microfinance in the weeks following the old Rs 500 and Rs 1000 notes being declared illegal tender. Microfinance institutions were forced to ask customers to get new notes or repay their loan amounts in other denominations.

Recommendations

1. Proper Regulation: The regulation was not a major concern when the microfinance was in its nascent stage and individual institutions were free to bring in innovative operational models. However, as the sector completes almost two decades of age with a high growth trajectory, an enabling regulatory environment that protects interest of stakeholders as well as promotes growth, is needed.

2. Field Supervision: In addition to proper regulation of the microfinance sector, field visits can be adopted as a medium for monitoring the conditions on ground and initiating corrective

action if needed. This will keep a check on the performance of ground staff of various MFIs and their recovery practices. This will also encourage MFIs to abide by proper code of conduct and work more efficiently. However, the problem of feasibility and cost involved in physical monitoring of this vast sector remains an issue in this regard.

3. Encourage rural penetration: It has been seen that in lieu of reducing the initial cost, MFIs are opening their branches in places which already have a few MFIs operating. Encouraging MFIs for opening new branches in areas of low microfinance penetration by providing financial assistance will increase the outreach of the microfinance in the state and check multiple lending. This will also increase rural penetration of microfinance in the state.

4. Complete range of Products: MFIs should provide complete range of products including credit, savings, remittance, financial advice and also non-financial services like training and support. As MFIs are acting as a substitute to banks in areas where people don't have access to banks, providing a complete range of products will enable the poor to avail all services.

5. Transparency of Interest rates: As it has been observed that, MFIs are employing different patterns of charging interest rates and a few are also charging additional charges and interest free deposits (a part of the loan amount is kept as deposit on which no interest is paid). All this make the pricing very confusing and hence the borrower feels incompetent in terms of bargaining power. So a common practice for charging interest should be followed by all MFIs so that it makes the sector more competitive and the beneficiary gets the freedom to compare different financial products before buying.

6. Technology to reduce Operating Cost: MFIs should use new technologies and IT tools & applications to reduce their operating costs. Though most NBFCs are adopting such cost cutting measures, which is clearly evident from the low cost per unit money lent (9%-10%) of such institutions. NGOs and Section 25 companies are having a very high value of cost per unit money lent i.e. 15-35 percent and hence such institutions should be encouraged to adopt cost-cutting measures to reduce their operating costs. Also initiatives like development of common MIS and other software for all MFIs can be taken to make the operation more transparent and efficient.

7. Alternative sources of Fund: In absence of adequate funds the growth and the reach of MFIs become restricted and to overcome this problem MFIs should look for other sources for funding their loan portfolio

Conclusion:

The key focus areas and building blocks for stable and prudent growth of this business to play its role in furthering the financial inclusion objective of the country would be: strengthening/ restoring the credit discipline and culture of repayment, operating cost optimisation through IT enablement, a stronger self-regulatory commitment from all players in the sector including banks and NBFCs, safeguarding of the business model from natural calamities and external

activism and mainstreaming of the business within the larger financial services sector in the country. If these factors are taken care of, it can become possible to reach the last Indian in need of financial services, thereby taking a significant step towards greater development and economic parity in the country.

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