Chapter 2

Microfinance – General Description
MICROFINANCE - GENERAL DESCRIPTION

The concept of microfinance goes beyond the provision of small credit to the poor. Microfinance as 'the means of providing a variety of financial services to the poor based on market-driven and commercial approaches' (Christen R.P., 1997)\(^1\). This definition encompasses provision of other financial services like savings, money transfers, payments, remittances, and insurance, among others. However many microfinance practices today still focus on micro-credit: providing the poor with small credit with the hope of improving their labour productivity and thereby lead to increment in household incomes.

Recent development in the field of financial system and a growing research from around the world shows that well developed and inclusive financial systems are associated with faster growth and better income distribution. Finance helps the poor catch up with the rest of the economy as it grows. Finance also helps extend the range of individual, households, and firms that can get footholds in the modern economy, and it reduces damaging concentration of economic power. Microfinance emerged as a tool for empowerment, and provides financial access to poor people. It is perhaps symbolic of this evolutionary thinking that ‘building inclusive financial systems that work for the poor’ has become the slogan of the United Nations International Year of Microcredit 2005.

In the global arena there is already the impression that microfinance is successful in reducing poverty. Many policy makers are therefore engaged on how to make microfinance sustainable and available to poor households in the future. Many stake holders in the microfinance industry especially donors and investors argue that, “Microfinance can pay for itself, and must do so if it is to reach very large numbers of poor households” (CGAP, 2003)\(^2\). The overall message in this argument is that unless microfinance providers charge enough to cover their costs, they will always be limited by the scarce and uncertain supply of subsidies from governments and donors. The main underlying assumption in this argument is that microfinance is already good for the clients, and therefore what is really urgent is to make the financial service available to as many poor people as possible. Morduch (2000)\(^3\) correctly points out that this kind of enthusiasm for microfinance rests on an enticing win-win proposition that: Microfinance institutions that follow the principles of good banking will also be
the ones that alleviate the most poverty. The assumption being that with good banking practices it is possible to cover costs and operate in a sustainable manner to continue serving clients and alleviating poverty.

The growth of microfinance has been described as a revolution (Robinson, 2001)⁴. Yunus (1998)⁵ has described it, perhaps somewhat exaggeratedly, as a “revolutionary way to reduce poverty”⁶. The first Microcredit Summit held in Washington D.C., in 1997, brought together over three thousand people from 137 countries. It was organized by RESULTS⁷ Educational Fund. The Summit launched a nine year campaign to reach over 100 million of the world’s poorest families. The year 2005 was designated by the United Nations (UN) as the “International Year of Microcredit”. In 2006, the Nobel Peace Prize was awarded to Muhammad Yunus, the founder of Grameen Bank, one of the earliest and perhaps the best known microfinance institution (MFI). These milestone events have drawn international attention to the microfinance sector.

In the global arena there is already the impression that microfinance is successful in reducing poverty. Many policy makers are therefore engaged on how to make microfinance sustainable and available to many poor households in the future. Many stakeholders in the microfinance industry especially donors and investors argue that, “Microfinance can pay for itself, and must do so if it is to reach very large numbers of poor households” (CGAP). The overall message in this argument is that unless microfinance providers charge enough to cover their costs, they will always be limited by the scarce and uncertain supply of subsidies from governments and donors. The main underlying assumption in this argument is that microfinance is already good for the clients, and therefore what is really urgent is to make the financial service available to as many poor people as possible.

From the late 1980s, the emergence of the Grameen Bank in Bangladesh drew attention to the role of 'micro-credit' as a source of finance for micro-entrepreneurs. Lack of access to credit was seen as a binding constraint on the economic activities of the poor. Micro-loans delivered to the groups of poor women seemed to offer a simple and direct remedy and the connection between providing credit and removing poverty

---

⁴ Rigorous evaluation studies have however yet to establish conclusively the link between microfinance and poverty reduction.
⁵ RESULTS (not an acronym) is a grassroots based advocacy group headquartered in the USA.
was intuitively appealing. It was also politically attractive. Resources could be made available through the political process, while government sponsorship of mass credit bought vote banks. Less well understood was the need for micro-credit to be financially sustainable. Also, emphasis on credit to the exclusion of other financial services obscured the need to develop organic systems of financial intermediation, commencing with grassroots savings mobilization.

2.1 Definition of Microfinance:

Microfinance is the provision of a broad range of financial services such as deposits, payment services, money transfers, and insurance to poor and low-income households and, their microenterprises. In the development paradigm, Microfinance has evolved as a need based policy and programme to cater to the neglected groups of the society especially women, poor people, rural deprived, etc. The basic idea of Microfinance is that; if poor people are provided access to financial assistance, including credit, they may be able to start or expand micro-enterprises that will allow them to break out of poverty. Microfinance enables poor self-employed people to create productive capital, to protect the capital they have, to deal with risk, and to avoid the destruction of capital. It attempts to build assets and create wealth among people who lack them. For the very poor, microfinance becomes a liquidity tool that helps smooth their consumption patterns and reduce their level of vulnerability.

Microfinance is a logical approach to development because it functions at the grassroots level, can be sustainable is capable of involving large segments of the population, and builds both human and productive capacity. Robinson (2001) defines microfinance as “small-scale financial services- primarily credit and savings- provided to people who farm, fish or herd” and adds that it refers to all types of financial services provided to low-income households and enterprises.

Asian Development Bank (ADB) defines microfinance as “the provision of broad range of financial services such as deposits, loans, money transfers, and insurance to all enterprises and households”.

Consultative Groups to Assist Poor (CGAP) defines microfinance as a credit methodology that employees effective collateral substitutes to deliver and recover short-term, working capital loans to microenterpreneurs.
Microfinance is the provision of broad range of financial services to low income micro-enterprises and households. The range of financial services usually includes savings, loans, insurance, leasing, and money transfer. On the other hand Microcredit emphasises on providing credit to low income clients. Microcredit often associated with an insufficient appreciation of the value of saving services to the poor. Microfinance models usually refer to the products and services provided as well as the method in which they are provided. Internationally, the most well-known microfinance models include the Grameen Bank model, the Latin American Solidarity group, community-owned village banks, savings and loans associations, credit unions, and Self Help Groups (SHGs).

Microfinance is often defined as financial services for poor and low-income clients offered by different types of service providers. In practice, the term is often used more narrowly to refer to loans and other services from providers that identify themselves as “microfinance institutions” (MFIs). These institutions commonly tend to use new methods developed over the last 30 years to deliver very small loans to unsalaried borrowers, taking little or no collateral. These methods include group lending and liability, pre-loan savings requirements, gradually increasing loan sizes, and an implicit guarantee of ready access to future loans if present loans are repaid fully and promptly.

More broadly, microfinance refers to a movement that envisions a world in which low-income households have permanent access to a range of high quality and affordable financial services offered by a range of retail providers to finance income-producing activities, build assets, stabilize consumption, and protect against risks. These services include savings, credit, insurance, remittances, and payments, and others.

2.2 Approaches of Microfinance:

Most of the developed nations of the world started their growth path from the development of the agriculture sector. For a long time, it was felt that the growth of developing countries is dependent on the growth path developed countries, i.e. through the trickle down strategy. This is the economy theory which advocates letting ultimately trickle down to lower income individuals and the rest of the economy. In other words, this is a theory of economic development that claims higher standards of
living for the poor will develop gradually with economic growth. The same applied on
the macro level in the individual countries, which started believing on the concept of
laissez-faire policy. However, there were countries like India and Israel; which did not
believe in the free market economy and continued with their public expenditure
programmes. Along with it, attention was made to make a self-sustained economy at
least from the view point of the agriculture sector. However, it took a long time to
realize that if the gains of development have to go to the poor, then some different
strategy has to be adopted.

When the Grameen Bank of Bangladesh started its foray into microfinance in
the middle of 1970s, it was realized that it can definitely be a good way for the benefit
of the poor then it was the realized that it is not the trickle down approach but it is the
trickle up approach which should be adopted to upgrade the living of the poor. Trickle
up would therefore mean that the benefit should be directly provided to the poor so
that they can invest it accordingly for their own development and would try to
improve their living standard. The countries were providing direct finance earlier also,
but since the late 1970s it was realized that if one wants benefits to be passed to the
poor ensuring its true use and accountability, then microfinance is the best alternative.

In the development paradigm, microfinance has evolved as a credit based
policy and programmes to cater to the so far neglected target groups (women, poor,
rural, deprived etc.). Its evolution is based on the concern of all developing countries
for empowerment of the poor and alleviation of poverty. Development organization
and policy makers have included access to credit for poor people as a major aspect of
many poverty alleviation programmes. Microfinance programmes have in the recent
past become one of the more promising ways to use scare development funds to
achieve the objectives of the poverty alleviation. The basic idea of microfinance is
simple; if poor people are provided access to financial services including credit, they
may very well be able to start or expand a microenterprise that will allow them to
break out of poverty.

The concept of Microfinance influenced by two major schools; the
Institutionalist school and the Welfarist school. Institunalist school focuses on
developing financially sustainable institution in order to serve the poor. The issue of
providing financial services to poor is the basic foundation of this approach. In this
approach numerous large scales, profit seeking MFOs that provides high quality of
financial services to the large number of poor. The Institutionalist position is expressed in nearly all literature published by World Bank, CGAP, USAID, ACCION International and Ohio State Universities Rural Finance Programme.

Believers of Institutionalist approach are opposed to the idea of dependency on subsidiaries because earlier attempts on poverty alleviation through subsidies credit by development agencies, Non-Governmental Organisation (NGO) and the governments of developing countries failed. The reason behind this failure includes; high cost of transactions, lack of assets for poor households, institution lacking in saving mobilisation and high level of corruption. The impact was so insignificant and that leads the dried up donor fund. The failure of past subsidized programme leads the core arguments of institutionalist thought; includes,

- Lower - income household desire access to credit, not cheap credit.
- Only financial sustainable programs can made a significant impact on poverty alleviation.
- Subsidized programs are insufficient and often end up in the hand of non-poor.

According to Institutionalist, a significant impact of poverty can be achieved only if MFIs are financially self-sufficient and independent from any subsidize funding from donor or government. Example of MFI's operate under Institutional approach includes; Bank Rakyat Indonesia, Banco Solidario de Ecuador and Uganda Microfinance Union. Institutionalist, approach have significant impact on poverty can be achieved only if MFIs are financially self-sufficient and independent from any subsidised funding from donor or government.

Examples of MFIs operating under this approach are Bank Rakyat Indonesia, SKS Microfinance, and Uganda Microfinance Union etc.

On the other hand Welfarist approach focuses on immediate improvement of economic safety of the poor. They focused on providing financial services to the poorest of the poor at subsidized interest rate. MFO’s who fall under this approach are heavily reliant on government subsidiary and grants as well as donor subsidiaries. Saving mobilization is not a part of lending process in this approach. Though they are understand and aware that the long term sustainability of MFO is very important, they do not agree that avoiding donor subsidiaries completely will be required to achieve that state. Example of MFO operate under institutionalist approach includes Grameen
Bank of Bangladesh, FINCA in Latin America, and most of the MFO’s in Africa and Asia.

Woller and Woodworth (2001)\textsuperscript{7}, explain the difference of two approaches in three different ways. First, the difference in service delivery method of MFI’s includes individual verses group based. Second is the difference in institutional structures; with or without donor fund. Third is the difference in population segment. When MFI’s focus on financial sustainability, the poorest of the poor might become neglected.

2.2.1 Two Approaches to Microfinance:

Microfinance in the 1990s was marked by a major debate between two leading views on how to fill the absurd gap in microfinance, the financial systems approach and the poverty lending approach. Both approaches share the goal of making financial services available to poor people throughout the world. But the poverty lending approach focuses on reducing poverty through credit and other services provided by institutions that are usually heavily funded by donor and government grants and subsidies and other concessional funding. A primary goal is to reach the poor, especially the poorest of the poor, with credit. Except for mandatory savings required as a condition of receiving a loan, savings is not normally a significant part of the poverty lending approach to microfinance. And frequently the poor are not permitted to save in such an institution unless they also borrow from it. As indicated by the term poverty lending, the emphasis has been on microcredit, not microfinance. Many institutions using the poverty lending approach provide microcredit to poor borrowers at low cost to the borrower. But these institutions are typically not sustainable, primarily because their interest rates on loans are too low for full cost recovery and also because they are often inefficient. In addition, they do not meet the large demand among the poor for voluntary savings services. And with a few exceptions, such institutions have very limited outreach. The poverty lending approach, although it has contributed much to microfinance, is not a globally affordable model.

Thus to meet microfinance demand from hundreds of millions of households over the long term, it is necessary to look elsewhere. The financial systems approach focuses on microfinance-commercial financial intermediation among
poor borrowers and savers; the emphasis is on institutional financial self-
sufficiency. But sustainability is not the goal. It is the means to large-scale provision
of financial services to low-income people. The financially self-sufficient institutions
in the Micro-Banking Standards Project show that sustainable commercial
microfinance is found in many countries. These institutions provide loans and
voluntary savings services to the economically active poor, and they offer borrowers
easy access to credit at reasonable cost. Some (but not all) also mobilize substantial
voluntary savings. Their loan portfolios are financed by savings, commercial debt,
investment, and retained earnings in varying combinations. These institutions are the
leaders of the emerging microfinance industry for two reasons; they have been able to
attain wide outreach to low-income clients profitably, and they represent a globally
affordable model.

The world’s foremost example of the financial systems approach in
microfinance—Bank Rakyat Indonesia’s micro banking system—is located in an APEC
member country. Numerous institutions in other APEC member countries also
provide commercial microfinance; some are industry leaders. Some of these
institutions are financially self-sufficient, others are working toward sustainability.
APEC’s members in Asia, Latin America, and Eastern Europe have among them a
variety of types of commercial microfinance institutions, including banks, regulated
nonbank financial institutions, and finance companies. Some examples are Fundación
Contigo in Chile; Asociación Programa Compartamos, I.A.P. in Mexico; Banco de
la Microempresa (Mibanco), Caja Municipales de Arequipa, EDYPME Pro Empresa,
and Solucion – Financiera de Crédito del Perú in Peru; Center for Agriculture and
Rural Development (CARD) in the Philippines; Opportunity International and the
Russian Women’s Microfinance Network in Russia; and the Bank for Agriculture and
Agricultural Cooperatives in Thailand.

2.3 Evolution of Microfinance:

Microfinance - the provision of loans and other financial services to those who
have traditionally been denied access to the formal financial sector has grown from an
idea into an industry, brought to the world’s attention in 2006, when Muhammad
Yunus and the Grameen Bank won the Nobel Peace Prize for “their efforts to create
economic and social development from below”, the rapid growth of the microfinance
movement across the developing world has spurred both accolades and accusations.
Those who promote microfinance, consider it a powerful tool in poverty alleviation and women’s empowerment.

Informal financial institutions catering to the poorer sections of society are documented as far back as the 15th century in Nigerian history. In Europe they were first developed in the 18th century in response to the immense poverty engendered by the 30 years’ war (1618-48). The term microfinance was formally employed in academic literature in the 1980s. The well-known author Jonathan Swift began the first loan fund for the poor in Ireland, in 1720. In 1823 a special law legalized the operation of such charitable institutions as formal financial intermediaries. The loan funds created under the auspices of charitable work began to return rich profits and served over 20 per cent of Irish households as per conservative estimates, until the government reigned in these booming businesses by regulating the permissible interest rates.

The Raiffeisen Credit Cooperatives started in Germany by Friedrich Wilhelm Raiffeisen, in 1847, were famously meant to “control the use made of money for economic improvements, and to improve the moral and physical values of people and also, their will to act by themselves”. By the year 1910, the cooperatives were servicing 1.4 million people. The British introduced this German model in the Indian city of Madras in the 1880s and consequently more than 9 million Indians were part of a vast credit-cooperative movement by the mid-20th century. Simultaneously, the Dutch colonial administration designed a rural cooperative banking system (the Badan Kredit Desas) in Indonesia, based on the Raiffeisen model, which later spawned the Bank Rakyat Indonesia, which is today one of the world’s largest microfinance institutions (MFIs).

One of the most important departures has involved the shift from “microcredit”—which refers specifically to small loans—to “microfinance.” The broader term embraces efforts to collect savings from low-income households, to provide insurance (micro-insurance), and, in some places (BRAC in Bangladesh has pioneered here), to also help in distributing and marketing clients’ output. Robinson (2001)8 provides a rich description of a “microfinance revolution” that is just beginning.

While the words microcredit and microfinance are often used interchangeably, they have different resonances and are loosely attached to contrasting beliefs about
the state of rural finance and the nature of poverty. The small difference in language signals, for some, a big difference in opinion. Microcredit was coined initially to refer to institutions like the Grameen Bank that were focusing on getting loans to the very poor. The focus was explicitly on poverty reduction and social change, and the key players were NGOs. The push to "microfinance" came with recognition that households can benefit from access to financial services more broadly defined (at first the focus was mainly on savings) and not just credit for microenterprises. With the change in language has come a change in orientation, toward "less poor" households and toward the establishment of commercially oriented, fully regulated financial entities.

The push to embrace savings is a welcome one, because it recognizes the pent-up demand for secure places to save, and in that context, the shift from microcredit to microfinance should not be contentious.

2.3.1 The Rise of Microfinance since 1970s:

Well into the 21st century, development has been driven either by governments or donor-financed credit programs. It is widely recognised that in spite of the high costs of administering aid driven initiatives, they have failed to make a significant impact on poverty reduction. Some critics also believe that charity has ruined the credit culture of the poor. From the 1950s, international aid donors and governments alike subsidized credit delivery to small farmers. The 1960s and 70s saw major efforts to expand rural finance in developing countries and Agricultural Development Banks were responsible for the delivery of this cheap credit.

In much of the developing world after the colonial era, governments were misguided into implementing development strategies premised on 'supply-leading finance theory'. This entailed the provision of loans in advance of the demand for credit, for the purpose of fostering economic growth. These loans were heavily subsidized and suffered alarmingly high default rates, between 50 to 90 per cent. Often these loans were used as hand-outs by corrupt politicians to strengthen their vote-banks, while the credit-institutions continued to suffer financial losses due to the unsustainably low interest rates charged by them.

The provision of this subsidized credit was subject to the whims of governments and donors and the credibility and financial viability of these programs
was often jeopardized when public funds were used to waive off outstanding loans at election time. At any rate, access by the poor to these programs tended to be low due to the misappropriation of loan funds despite the subsidies, and the costs of borrowing high, because of widespread inefficiency and corruption.

The mid-1970s saw trenchant criticism of this model with the consequence that donors and governments alike shifted focus from interventionist to market-based solutions. The failure of the earlier attempts resulted in concerted interest in alternate development tools such as microfinance. The microfinance revolution of today is essentially a financial and technological revolution, which began in the 1970s, developed in the 1980s and took off in the 1990s.

The Bank Dagan Bali (BDB) in Indonesia was started in September 1970 and is one of the earliest commercial microfinance institutions to serve a low-income clientele, without any subsidies. In 1973 ACCION International, a United States based non-governmental organization (NGO) disbursed its first loan in Brazil and famously in 1974 Professor Muhammad Yunus started what later became known as the Grameen Bank by lending the modest sum of $27 from his own pocket to 42 people in Bangladesh. A year later the Self-Employed Women’s Association (SEWA) started to provide loans of about $1.5 to poor women in India. These institutions proved beyond doubt that poor people made good creditors, with repayment rates exceeding 95per cent, even when the interest rates charged were higher than those of traditional banks.

At the Microcredit Summit (1996), held in Washington, US$20 billion was raised to provide micro-credit to 100 million of the poorest households of the world, in the next ten years. Writing at the time, Buckley and Rogaly questioned whether micro-credit was the best form of aid for the poorest. Critics argued that it constituted a large part of the aid budget and had diverted funds from other initiatives aimed at better healthcare, food aid or monetary aid, as the case may be, without having proven its success.

2.4 Objectives of Microfinance:

Microfinance is a very good instrument to reduce poverty and it is also very good tool for the rural development. Providing access to credit to the vulnerable and poor section, especially women and ethnic minorities and tribal and backward area
people by doing so, poor people can improved their living standard and it also helps
the empowerment of rural as well as urban women. Eradication of poverty, women
empowerment and financial inclusion is the main objectives of the microfinance
across the world. And by achieving above mentioned objectives pave the way to
achieve the other objectives of microfinance because the above mentioned objectives
are the major problem in developing country in Asia, in Africa and in Latin American
countries.

(a) **Main Objectives of Microfinance are:**

- Reduction of poverty and rural development.
- To empower rural women.
- To create employment opportunities.
- To improve the living standard of the rural people.
- To make easy access to institutional credit facilities.
- To mobilize rural savings.

(b) **The Important Features of Microfinance are:**

- Microfinance is a tool for the empowerment of poor women;
- Loans under microfinance programmes are very small;
- Microfinance targets the poor rural and urban households;
- Credit under microfinance follows thrift i.e. mobilize savings and lend the
  same;
- Low transaction cost due to group lending’s;
- Transparencies in operation;
- Short repayment period;
- Simple procedure for reviewing, processing and approving loan applications
  and delivery credit;
- Chances of misutilization are rare and there are assured repayment;
- Peer pressure act as the collateral security required for loans;
- Need based loan disbursement;
- Prompt repayment; and
- There is no ceiling from the RBI in respect of minimum and maximum
  amounts.
The following are the main features of microfinance services provided by Rashtriya Mahila Kosh (RMK) in India:

(i) It is a tool for the empowerment of the poorest;
(ii) The higher the income and better the asset position of the borrower, the lower the incremental benefit from further equal doses of micro-credit is likely to be;
(iii) Delivery is normally through Self Help Groups (SHGs).
(iv) It is essentially for providing self-employment. The opportunities of wage employment are limited in developing countries - microfinance increases the productivity of self-employment in the informal sector of the economy - generally used for;

(a) Direct income generation;
(b) Rearrangement of assets and liabilities for the households to participate in future opportunities; and
(c) Consumption smoothing.

Microfinance is not a financing system but a tool for social change, especially for women. It does not spring from market forces along - it is potentially welfare enchainment there is public interest in promoting the growth of microfinance - this is what makes it acceptable as valid goal for public policy.

2.5 Rationale and Growth of Microfinance:

The Microfinance sector have grown overtime with more and different types of actors becoming involved, with increasing numbers of geographic regions around the world being serviced with new types of products and services being developed and with new ideas and technology to support it.

The global picture regarding microfinance outreach is quite impressive. From a mere 7.6 million poorest families in 1997, The Microcredit Summit campaign reported an outreach of more than 92 million clients by December 31st, 2004. This number includes 66.6 million families who were among the poorest when they started with a program of these 66.6 million largest poorest clients, 55.7 million or 83.6 per cent were served by 52 largest individual institutions, all with 100,000 or more clients. Among these largest MFIs, 79 per cent are in Asia, 17 per cent are in Africa and only 4 per cent are in Latin America.
Of the 3164 institutions that had reported to the Microcredit Summit Campaign by December 31, 2004, 1628 were in Asia, 994 in Africa, 388 in Latin America and Caribbean, 48 in North America, 34 in Middle East, 72 in Europe and the newly independent states. The increase is definitely an indication of an impressive growth in the field of microfinance.

Of the over 92 million people reached by the end of 2004, 81.5 million were in Asia, 7 million in Africa and 3.8 million in Latin America and 4 million in Caribbean only 5.2 million of the 61.5 million poorest families in Africa and the Middle East were covered by Microfinance programmes by the end of 2004. Asia, which is home to some 67 per cent of the world’s people living on less than US$ 1 a day can therefore rightfully boast of vibrant microfinance sector.

2.5.1 Growth Potential for Microfinance:

Although there has been remarkable progress worldwide, in terms of growth in the number of MFIs and their outreach, there is still a lot to do. As MFI outreach to the poorest families is only 38 per cent in Asia, 8.5 per cent in Africa and the Middle East, 11.6 per cent in Latin America and the Caribbean and 1.7 per cent in Europe and the NIS (Newly Independent States), there are millions of poor people in different regions that can be and should be reached with microfinance to help them overcome poverty.

Table 2.1 Growth of Microfinance Coverage as Reported to Microcredit Summit Campaign, 1997-2007

<table>
<thead>
<tr>
<th>End of Year</th>
<th>Total number of institutions</th>
<th>Total number of clients (millions)</th>
<th>Number of “poorest” clients reported (millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td>655</td>
<td>16.5</td>
<td>9.0</td>
</tr>
<tr>
<td>1998</td>
<td>705</td>
<td>18.7</td>
<td>10.7</td>
</tr>
<tr>
<td>1999</td>
<td>964</td>
<td>21.8</td>
<td>13.0</td>
</tr>
<tr>
<td>2000</td>
<td>1477</td>
<td>38.2</td>
<td>21.6</td>
</tr>
<tr>
<td>2001</td>
<td>2033</td>
<td>57.3</td>
<td>29.5</td>
</tr>
<tr>
<td>2002</td>
<td>2334</td>
<td>67.8</td>
<td>41.6</td>
</tr>
<tr>
<td>2003</td>
<td>2577</td>
<td>81.3</td>
<td>55.0</td>
</tr>
<tr>
<td>2004</td>
<td>2814</td>
<td>99.7</td>
<td>72.7</td>
</tr>
<tr>
<td>2005</td>
<td>3056</td>
<td>135.2</td>
<td>96.2</td>
</tr>
<tr>
<td>2006</td>
<td>3244</td>
<td>138.7</td>
<td>96.2</td>
</tr>
<tr>
<td>2007</td>
<td>3352</td>
<td>154.8</td>
<td>106.6</td>
</tr>
</tbody>
</table>

The above table shows the results of a survey conducted by Microcredit Summit Campaign. By the end of 2007, the campaign had reports of 154.8 million microfinance clients served world-wide by over 3350 microfinance institutions. Of these clients, 106.6 million were reported as being in bottom half of those living below their nation’s poverty line or were living in households earning under $1 per day per person (defined as the “Poorest”; Daley-Harris, 2009)\textsuperscript{iii}. Between 1997 and 2007, the numbers grew on average by about 30 per cent per year, and the movement’s leaders expect continued expansion as credit unions, commercial banks, and others enter the market.

**Table 2.2 Poorest Clients that are Women in 2007 as Reported to Microcredit Summit Campaign, 2009**

<table>
<thead>
<tr>
<th>Region</th>
<th>Total number of institutions</th>
<th>Per cent of poorest clients that are women</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sub-Saharan Africa</td>
<td>935</td>
<td>63</td>
</tr>
<tr>
<td>Asia and the Pacific</td>
<td>1727</td>
<td>85</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>613</td>
<td>66</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>85</td>
<td>78</td>
</tr>
<tr>
<td><strong>Developing World Totals</strong></td>
<td>3360</td>
<td>83</td>
</tr>
<tr>
<td><strong>Industrialised World Totals</strong></td>
<td>192</td>
<td>60</td>
</tr>
<tr>
<td><strong>Global Totals</strong></td>
<td>3552</td>
<td>83</td>
</tr>
</tbody>
</table>

*Source: Daley-Harris, State of the Microcredit Summit Campaign Reports, 2009.*

In a Women’s World Banking Focus Note, Frank (2008) investigates the relationship between commercial transformation and outreach to women. She examines 27 transformed institutions and finds that women make up a smaller fraction of their clients five years after transformation from NGO status, compared to their own client mix before transformation and to that of control group of non-transformed institutions. For the transformed set, the percentage of women clients served decreased from an average of 88 per cent two years before transformation to 78 per cent at transformation and 60 per cent five years after transformation. In contrast, the non-transformed institutions increased their fraction of women clients from 72 per cent to 77 per cent over a parallel five year period.

---

\textsuperscript{iii} Daley-Harris, *State of the Microcredit Summit Campaign Reports 2009.*
2.5.2 Grameen Bank and the Beginning of Microfinance:

The roots of microfinance can be found in many places, but the best-known story is that of Muhammad Yunus and the founding of Bangladesh’s Grameen Bank. In the middle of the 1970s, Bangladesh was starting down the long road to build a new nation. The challenges were great, independence from Pakistan had been won in December 1971 after a fierce war, and two years later widespread flooding brought on a famine that killed tens of thousands (Sen 1981)\(^9\). Government surveys found over 80 per cent of the population living in poverty in 1973–1974 (Bangladesh Bureau of Statistics 1992)\(^10\).

Muhammad Yunus, an economist trained at Vanderbilt University, was teaching at Chittagong University in southeast Bangladesh. The famine, though, brought him disillusionment with his career as an economics professor. In 1976, Yunus started a series of experiments lending to poor households in the nearby village of Jobra. Even the little money he could lend from his own pocket was enough for villagers to run simple business activities like rice husking and bamboo weaving. Yunus found that borrowers were not only profiting greatly by access to the loans but that they were also repaying reliably, even though the villagers could offer no collateral. Realizing that he could only go so far with his own resources, in 1976 Yunus convinced the Bangladesh Bank (the central bank of Bangladesh) to help him set up a special branch that catered to the poor of Jobra. That soon spawned another trial project, this time in Tangail in North-Central Bangladesh. Assured that the successes were not region-specific flukes, Grameen went nation-wide. One innovation that allowed Grameen to grow explosively was group lending; a mechanism that essentially allows the poor borrowers to act as guarantors for each other. With group lending in place, the bank could quickly grow village by village as funding permitted. And funding-supplied in the early years by the International Fund for Agriculture and Development, the Ford Foundation, and the governments of Bangladesh, Sweden, Norway, and the Netherlands-permitted rapid growth indeed.

Grameen’s “classic” group lending contract works very differently from a standard banking contract for small business. In a standard relationship, the borrower gives the bank collateral as security, gets a loan from the bank, invests the capital to generate a return, and finally pays the loan back with interest. If borrowers cannot repay, their collateral is seized. But Grameen clients are most often too poor to be
able to offer collateral; instead, the classic Grameen contract takes advantage of
clients’ close ties within their communities. To take advantage of those relationships,
the loan contract involves groups of customers, not individuals acting on their own.
The groups form voluntarily, and, while loans are made to individuals within groups,
all members are expected to support the others when difficulties arise.

The groups consist of five borrowers each; loans go first to two members, then
to another two, and then to the fifth group member. In this “classic” contract, the
cycle of lending continues as long as loans are being repaid. But, according to the
rules, if one member defaults and fellow group members do not pay off her debt, all in
the group are denied subsequent loans. This feature gives customers important
incentives to repay promptly, to monitor their neighbours, and to select responsible
partners when forming groups (Fugelsang and Chandler 1993). Moreover, the five-
member group is part of a “center” composed of eight groups. Repayments are made
in public, that is, before the forty members of the center, in weekly instalments. Group
lending thus takes advantage of local information, peer support, and, if needed, peer
pressure. The mechanisms rely on informal relationships between neighbours that
facilitate borrowing for households lacking collateral (Besley and Coate 1995);
Armendáriz (1999a). The program thus combines the scale advantages of a standard
bank with mechanisms long used in traditional modes of informal finance.

Since 1985-86 poverty has risen consistently in the country due to rapid
increase in the working age population, increasing landlessness and low growth of
employment in non-farm sector. According to the Bangladesh Bureau of Statistics
Sources, 47.5 per cent of the population in 1991-92 lived below poverty line.

Rural credit in Bangladesh is provided by three different types of institutions
as formal, semi-formal and informal credit agencies. Formal agencies include
agriculture banks, rural branches of nationalised commercial banks, Gramin banks,
co-operative networks and private banks. The semi-formal agencies include Non-
Governmental Organisations (NGO). The informal sector includes private money
lenders, relatives. Gramin Bank is the largest provider of micro-credit in Bangladesh.
Prof. Mohammad Yunus, the man behind the Gramin Bank, realised that getting
credit from the banking system without collateral was an impossible task for the poor,
who were in dire need of it, and the money lenders were exploiting the poor beyond
imagination. Therefore he obtained the certain amount from the bank for on lending
without any security/collateral to the poor who were organised into small groups. Prof. Yunus started the experiment in Chittagong district in 1976 by giving small amounts to the borrowers to buy raw materials.

The Bank was constituted under Gramin Bank Ordinance of the Government of Bangladesh in 1983. The Bank lends without any collateral security to groups and a group consists of five members coming from different families. There is no membership fee and saving is not compulsory for access to loan in first instance. The loans carry interest rate ranging between 5 to 20 per cent per annum. Repayment instalments consist of principal, interest and compulsory deposit of the borrowers. The Bangladesh Rural Advancement Committee (BRAC) was established in 1972, initially, with an aim to provide relief and rehabilitation to the refugees. It shifted its emphasis in 1973 to community development involving the rural poor. In 1976, it adopted a target group approach consisting of the landlessness and the poorest, particularly the women. It has also decided to discontinue taking donor funds and to make itself sustainable by 2001. The aim of BRAC is to help the poor, who are willing to embark on activities to better their lives, through its saving and credit programme.

Bangladesh distinguishes itself by reaching more than 75 per cent of poor families with microfinance. It is home to 31 per cent of the largest programmes in the world, who have individually reached more than 100,000 clients. Microfinance programmes in Bangladesh reached over 18 million poorest clients by the end of 2004. The intensity and density of microfinance is greater in Bangladesh than in any other country.

2.5.3 Asia and the Pacific:

Asia is the home of the largest number of MFI’s and its outreach. But even in Asian countries there is still high scope for expanding and deepening MFI outreach. Consider the case of the four most populous countries in Asia (China, India, Indonesia and Pakistan) that have many microfinance programs but at the same time have millions of poor people without any access to formal or semiformal financial services. There is an enormous demand for microfinance in China, which according to a report of the China Association for Microfinance (CAM) has a poor population of about 110 million people. As reported by CAM, the total number of poor clients so far reached
by NGO-MFIs, RCCs, the government—mainly through Agricultural Development Bank—and the City Commercial Bank for urban entrepreneurs is only slightly over 7 million. About 26 per cent of 1.1 billion people in India are still under the poverty line. Only an estimated 10 to 12 per cent of the poor in India are reached by microfinance including the outreach of SHGs, NGO MFIs, NBFCs, Commercial Banks and Cooperatives. Indonesia, the fourth most populous nation (over 245 million people) in the world has over 40 million people who are living below the poverty line.

Although there are several formal, semi-formal and informal microfinance providers working in the country and serving a few million, the need and potential for increasing microfinance outreach to millions of both rural and urban poor who are still excluded is very large. In Pakistan 32 per cent of its 164 million people are under the poverty line. Although a number of microfinance providers including NGOs and banks are working in the country, their outreach is still less than one million. As a believer in the poverty fighting capacity of microfinance and as a pioneer in the development of legal and regulatory framework, the country needs a great breakthrough to increase the microfinance outreach at a faster rate. Microfinance development in most of the Asian countries except Bangladesh has remained skewed and slow. In India for instance, almost three-fourths of the total microfinance clients are concentrated in four southern states, namely Andhra Pradesh, Tamil Nadu, Karnataka and Kerala. Large parts of Northern and North-Eastern states have remained underserved by the sector. Although the countries in the Pacific region have relatively small populations, a large percentage of them live under the poverty line. For instance, 37 per cent of the 6 million people in Papua New Guinea, the most populous country in the region, are living under the poverty line. Other countries in the region with much smaller populations have significant numbers of poor. They have microfinance programs with little capacity, outreach and exposure to best practices. How the outreach can be increased in the region is an issue that should be addressed taking into consideration the constraints the MFIs are facing on the ground.

2.5.4 Africa:

The global concern for the level of poverty in Africa is well known to all. Africa is hardest hit by the crippling problems of chronic hunger and malnutrition. The great concentration of poverty in Sub-Saharan Africa is also a matter of concern.
for all. Despite such disappointing facts, microfinance in Africa is growing. A broad range of diverse institutions offers financial services to low-income clients in Africa. These include non-government organizations, non-bank financial institutions, cooperatives, credit unions, rural banks, Rotating Savings and Credit Associations (ROSCA), postal financial institutions, and an increasing number of commercial banks. Countries with a high number of MFIs in Africa include Kenya, Uganda, Ethiopia and Senegal. Kenya with K-Rep contributed to the growth of microfinance especially in East Africa. There is a growing number of MFIs in Rwanda, Zambia and Tanzania. As a country, Uganda has the largest outreach in the microfinance sector. But in countries such as Nigeria, Ghana, Liberia, Sierra Leone, Libya, Tunisia, Cameroon, Zambia, Angola and Mozambique, there is low density of MFIs. Although East Africa is the leading region in the microfinance sector in Africa, even there a large number of potential members are yet to be reached. In countries like Mozambique where rural areas are characterized by low population density, poor infrastructure, limited participation of the rural poor in the cash economy and restricted diversification of income sources, it is very challenging to develop a sustainable microfinance program. Political instability, the AIDS epidemic, lack of familiarity with best credit and savings practices also hinder in the development of microfinance in Africa.

2.5.5 Arab World:

Microfinance in the Arab world, which is spread over both Africa and Asia, is also growing. The experience of micro-financing in this region in terms of scale and outreach is encouraging. From less than 10,000 in 1997, the outreach has gone to over one million by 2006. Yet it still has more than 20 million potential clients to reach. Although Morocco has the largest outreach in the Arab World, even in this country there are lots of poor without any access to microfinance. In the Arab world, the microfinance programs are predominantly urban. The majority of MFIs in the region are NGOs. They are mostly dependent on donor funding. There is the presence of some large government sponsored programs in Tunisia, Jordan, Egypt and Syria. They reportedly do not follow good practices. There is, therefore, a lot of room for developing viable programs to serve the millions of unserved people who could benefit from microfinance in the Arab World.
2.5.6 Latin America and the Caribbean:

Unlike Asia and Africa, the majority of the poor live in urban areas in Latin America. While 38 per cent of the population in urban areas is below the poverty line, 62 per cent of the population in rural areas is also poor. As there is a high concentration of microfinance programs in urban areas in many of the Latin American countries, the need for making more microfinance services available to the rural poor is great. The current microfinance providers in Latin America include NGOs, microfinance institutions and commercial banks. They are mostly working in urban areas. When they can expand their operations to new areas, the new programs can also be started and supported to serve the areas which are without any microfinance program. In many of the countries in Latin America and the Caribbean including Bolivia, Brazil, Columbia, Dominican Republic, Guatemala, Haiti, Honduras, Mexico, Nicaragua, Peru, where millions of poor are under the poverty line and not reached by microfinance there is a lot of scope for its expansion to both urban and rural areas. As Argentina has the lowest microfinance coverage in Latin America it provides a challenge to those who want the rapid expansion of poverty focused microfinance programs in countries which are lagging behind.

2.5.7 Europe and North America:

There is a need and opportunity to step up efforts to promote self-employment and growth through microfinance in the member states of the European Union where 12 per cent of all households live below the threshold of poverty. There are MFPs in many European countries including Albania, Bosnia, France, Germany, Italy, Netherlands, Norway, Spain and Kosovo. Their outreach may be increased to give every poor person the right to economic initiative and the opportunity to generate self-employment. Over 35 million people, or nearly 12 per cent of the population in the United States, the third most populous country in the world, live below the poverty line. Although microfinance is used as a tool to fight poverty in the USA, its outreach is limited. According to estimates, there are over 750 organizations in the USA providing microfinance and/or related business training. Many of them are reportedly run as social welfare programs. None of them recover all their costs. The best reported cost recovery is 70 per cent. There is, therefore, the challenge to increase outreach and develop sustainable microfinance programs in the USA. Such is also the case in Canada, which has 16 per cent of its population living below the poverty line.
To begin with, microfinance was the exclusive domain of state driven and charitable aid. Microfinance today is based on the principle of free markets, where resources are meant to be capitalized on. However, while on the one hand the Indian microfinance giant, SKS Microfinance is aspiring to an initial public stock offering (IPO), entirely self-sustaining MFIs are still far from the norm. It is generally agreed that while microfinance aims to become self-sustaining, governments still have an important role to play in terms of providing the opportune policy environment in which these institutions can flourish and be regulated. It is my contention that it would be presumptuous to assume that microfinance and free markets are a panacea for poverty.

2.6 Microfinance and Rural Development:

The words of Kofi Annan at the beginning of the Microcredit Summit in 2006, convey the importance of financial inclusion on poverty reduction. The levels of poverty throughout the world are not only due to the lack of wealth distribution or merely to a lack of credit, which was established as a "universal right" according to the 2005 UN Millennium Development Goals. Yet due to the underlying financial and economic systems that run the global economy, today there are millions of "potential bank clients" made up of the so-called poor; low-income individuals with micro enterprises who could potentially benefit from a micro-loan, but who also require a variety of services in a comprehensive development framework to be able to escape poverty. Until recently this group of poor pertained to a stable and growing middle class, which in the developing world over past few decades has consistently seen its jobs lost through inadequate policy, combined with an ever-increasing tendency towards wealth and opportunity being distributed among fewer hands.

Achieving balanced and inclusive economic growth is a key challenge faced by policymakers in countries around the world. The gains of economic growth are accessible to a greater extent by the relatively advantaged, who find it easier to participate in the growth process. Poorer people, who are separated by distance from the urban areas where economic activity is concentrated, have to wait much longer to reap the benefits of economic growth. Engaging these sections of society in the economic mainstream is essential to achieve balanced growth, which is critical for the long-term sustainability of social development and economic prosperity. Access to financial services is a key element of the process of socio-economic empowerment.
Only by delivering financial services to people in rural areas and lower income strata can they be brought within the ambit of economic activity. Only then can the full potential of the country’s physical and human resources be realised. The rural economy represents a large latent demand for credit, savings and risk mitigation products like insurance. Governments and regulators the world over have articulated the expansion of financial service delivery to this segment of the population as a priority objective.

Provisioning and delivering financial services and adequate timely credit to poor has been an important issue in the economic agenda of India where about 70 per cent of the population depends upon agriculture for their livelihoods. Moreover, 40 per cent of our GDP is contributed by the rural sector. Economic development of our country can be achieved on with the uplifment of village folk consisting of farmers, agricultural workers, rural artisans and small industrial workers. Rural Credit Delivery System of India has many diversities and peculiarities. Informal sources of lending once were the only and dominant source of credit. It consists of village money lenders, indigenous bankers, land lords and relatives. Later developed the institutional lending or the formal sources of credit. So far as the organised and formal sources are concerned, there exists a multiagency approach consisting of co-operatives, commercial banks and Regional Rural Banks. With rise in the institutional finance to rural sector, the share of informal lending has dropped substantially. Still informal source dominate the rural credit delivery system to cater the credit need of rural masses.

People in general and rural people in particular are largely illiterate, unaware and lack enough courage to approach the formal credit institutions for their credit needs. Again financial sector reform has brought a big change in the attitude and objectivity of the banks. In this context there has been for an imperative need for supporting rural sector development through provision of credit to rural poor through microfinance.

Role of microcredit in eradication of poverty was stressed by the UN in its Economic and Social Council Meet on July 25, 1997, in which the council called for strengthening the microcredit institutions. Also it recognised the importance of access to microcredit of the people living below poverty line to develop farm sector and to
undertake microenterprises to generate self-employment and to contribute to achieve empowerment of rural poor, especially women.

Development of local resource based economy will provide additional employment and employment to people living in rural area. In this context Schumacher (1974)\textsuperscript{14} observed that in order to bring work to the people, not people to the work it was absolutely necessary to establish million and millions of small scale industries in rural areas.

Developing countries aim at maximum utilisation of their own man power resources. Even such countries availing raw materials in abundant and labour resources in cheap and surplus they cannot achieve their targeted growth rate without having sufficient financial resources. In a labour extensive economy it is necessary to liberalise and fluctuate the financial and monetary policy which is the tools to achieve the multi-dimensional life goals of rural poor. To achieve these goals and keep rural people from the burden of prescribed by the money lenders; Government, NGOs and voluntary organisation plays a crucial multi linked role in rotating microfinance. Now a day’s micro finance is a worldwide scheme and it is broadly established to uplift the rural poor.

Muhammad Yunus (2004)\textsuperscript{15} stated that lessons from the experiences of other developing countries like Bangladesh, Indonesia, Bolivia and Philippines motivated India too to start SHGs is a brainchild of Grameen Bank of Bangladesh which was founded by Prof. Muhammad Yunus in the year 1975. In India NABARD initiated it in 1986-87, but the real effort was made after 1991-92 from the linkage of SHGs with the banks.

Credit is the life-blood and key input for over all development. Microcredit lays a very important role in rejuvenating rural economy. Credit is an important source for all sectors of the economy to carry on day to day activities and also for growth and progress, credit is consciously used as a lever of development. The importance of agriculture is the best summarised in a famous Chinese proverb saying that economic life is just a tree whose roots are presented by agriculture, stem by industry and branches and leaves by trade and commerce. Though agriculture sector has made rapid strides since the late sixties yet, it could not have achieved desired results production and productivity both lag far behind the international achievement
records. Our country has not achieved the rate of modern input consumption at par with advanced countries.

2.7 Microfinance and Poverty Reduction:

United Nations Development Program (UNDP) estimates that of the 3 billion poor worldwide, about half or 1.5 million could be considered working poor or potentially eligible for a micro-credit loan or other types of small-scale financial products. According to the World Bank, there are more than one billion persons worldwide that live on less than two dollars per day, 150 million of which live in Latin America. In the region it is estimated that some 360 million live on the margin of the economy with subsistence-level income and lack basic services such as running water, electricity, medical care and housing. Such poverty is manifested in a wide variety of channels: conditions of minimal survival, lack of education, lack of social integration, lack of access to basic goods and services. In essence, the poor have few alternatives to protect themselves from risk or to manage risks they face daily. According to Amartya Sen, winner of the Nobel Prize in Economics in 1998, the poor continue to be poor because they lack autonomy and power. Sen states, “once empowered, through greater inclusion and access to traditional systems, they become able to change their lives and overcome obstacles that previously were considered insurmountable.” However, individuals cannot transform their lives by their efforts alone, or without a society and financial system which allows them the opportunity for development and progress. Sen claims that the first step is to change the way poor are viewed; he explains, “instead of being seen as needy and incapable, society must change its paradigm to consider this group as potential architects of their own personal and socioeconomic development.” In addressing the challenge of poverty reduction and the impact of access to financial services in this goal, a recent report by FELABAN (Latin American Bank Federation) reveals the important relationship between access to the financial system – defined as the percentage of the population that can freely use financial services – and the reduction of poverty and inequality. Understanding the problem of the lack of access to financial services is particularly important in Latin America, as the levels of poverty continue to be alarmingly high and it is the region with the most income disparity in the world, despite the many reforms that have been implemented in the region over the past half century.

66
The collateral based formal banking institutions make the poor difficult to procure loans. In addition, the bureaucratic cumbersome procedures discourage the poor to get loan for self-employment. That is why there is always urban and rich bias in providing loan by the formal financial institutions. However, microfinance programme helps poor people for getting loans from conventional formal financial institutions. As discussed earlier, it provides opportunities to the resource-less people to establish their own enterprises and strengthen their financial position. Generally, most of the beneficiaries of this programme are women, they contribute to enhance family income and become productive members of the economy. This also helps in increasing consumption standard and the education standard of the family. In this sense microfinance may be considered as one effective tool amongst many others for poverty alleviation. However, according to Sadegh (2006)\textsuperscript{16}, "The equation between microfinance and poverty alleviation is not straightforward, because poverty is a complex phenomenon and many constraints that the poor in general have to cope with."

An Asian Development Bank study conducted by Khandker (2001)\textsuperscript{17} in Bangladesh shows that 'microfinance participants do better than non-participants in both 1991/92 and 1998/99 in per capita income, per capita expenditure and household net worth. The incidence of poverty among participating households is lower in 1998/99 than in 1991/92 and lower than among non-participating households in both periods.' A case study of Asian countries conducted by Remenyi and Quinones (2000)\textsuperscript{18} concluded that household income of the beneficiaries of microfinance has risen significantly higher than non-beneficiaries. According to this study, in Indonesia, the annual average income of the borrowers increased by 12.9 per cent while only 3 per cent rise was reported by no borrowers. In Bangladesh, a 29.3 per cent annual average rise in income was recorded against 22 per cent annual average rise in the income of non-borrowers. Sri Lanka indicated an increase in income by 15.6 per cent by borrowers and only 9 per cent by non-borrowers. In case of India, 46 per cent annual average rise in the income was reported among borrowers with 24 per cent increase by non-borrowers. The study shows that the effects on income were higher for those just below the poverty line. In a study of Zimbabwe conducted by Barnes and Erica (1999)\textsuperscript{19}, it was observed that the repeat clients of microfinance have shown almost double of the income as compared to non-member clients.
Microfinance emerged in the 1970s as social innovators began to offer financial services to the working poor those who were previously considered “un-bankable” because of their lack of collateral – once, given the opportunity, not only did clients (poor) of MFIs, expand their business and increase their incomes, but their high repayment rates that is higher than 95 per cent has strengthened the capital base of MFIs, therefore enabling MFIs, to re-lend these funds to even more people has strengthened the capital base MFIs, therefore, microfinance institution are now innovating to empowers the world’s poor to improve their own lives. Credit extended to members has created employment opportunities due to increase in sales which has led to additional staff hence reducing poverty. However, the existing technical capacity to handle MFIs governance is very low due to the level of education.

About 1.3 million people of the world live with less than one dollar a day (World Bank). About half of the world’s people (nearly three billion people) live on less than two dollars a day. The total wealth of the world’s three richest individuals is greater than the combined gross domestic product of the 48 poorest countries; (about a quarter of the entire world states (Ignacio 1998)\textsuperscript{20}. Little wonder that poverty and inequalities have become global concerns. Poverty can be generally defined as the inability to attain a certain predetermined minimum level of consumption at which basic needs of a society or country are assumed to be satisfied. The core concept of this general definition of poverty is the fact that to be poor is defined by access to basic goods and services like food, shelter, healthcare and education. The food concept in this definition goes beyond just food passed but also includes clean water and sanitation services.

The rural finance policy pursued is more developing countries beginning from 1950s was based on providing subsidized credit through state controlled or directed institutions to rural segments of population. Expansion of credit coverage through state interventions was based on various theoretical assumptions. Seibel and Parshusip (1990)\textsuperscript{21} mention that this approach was based on the premise that rural micro-entrepreneurs are unable to organize themselves, they need subsidized credit for increasing their and are too poor to save. Yaron, Benjamin and Piprek (1997)\textsuperscript{22} have traced this traditional approach in rural finance leaving to heavily towards direct interventions to Keynesian influence. Under this approach, in addition to the
assumptions listed above, the key problem areas visualized in rural financial markets included a lack of credit in rural areas and prevalence of usurious money lenders.

Microfinance has played an important role and become meaning full tool for the development of the poor section of society those are unable to access market on their own capacity. Formation of Self-Help Groups (SHGs), motivation to accumulation of small savings to show the regular saving habit, unity of the group and their managerial capacity and small amount of credit hence forth will undoubtedly provide self-employment to the members and help in transition of their poverty to achieving minimum standard of living.

Inclusive growth encompasses ideas related to basic needs and equity thereby taking all sections of society with growth. It focuses on broad based growth, results of which reach all strata of society. Reduction in poverty and disparities of income ensuring everyone a basic minimum standard of living are the objectives of inclusive growth. Improvement of the standard of living results from access to productive assets and finance to utilize assets for income generating activities. It has to become integral part of the efforts to promote inclusive growth. In fact, providing access to finance of the vulnerable groups.

In Indian context, to provide rural financial services strong institutional network has been established during the five year plan. The institutions which currently provide financial services in rural areas include branches of commercial banks, regional rural banks, co-operative societies and microfinance institutions. Now, there is a need to find ways and means to effect improvements within the existing formal credit delivery mechanism and evolve new models for extending inclusive growth policy. In a broad sense, we need to address issues on the supply side as well as demand side. The formal banking system, the rural co-operatives and non-governmental organisations need to evolve a model to reach the excluded section of the society. The financially excluded section requires products which are customised to meet their needs.

Part of understanding the costs and benefits of various organizational forms of MFI s, involves understanding the overarching goal that motivates most MFI s: poverty reduction. The way microfinance impacts overall poverty reduction in a given country is then shaped by the nature of poverty in that country. India has over a quarter of its
population below the poverty line. The World Bank reports that India is still home to some 260 to 290 million poor, numbers that rise to 390 million if poverty is measured by the international standard of those living on less than US$1 dollar a day. Almost half of India’s poor, approximately 133 million, are concentrated in three states: Uttar Pradesh, Bihar, and Madhya Pradesh. Rural areas in India are home to three quarters of India’s poor which is strengthened by the increasing urban/rural disparities. There are substantial disparities within the country as the gap between the rich and poor widens. The Indian government’s poverty reduction strategy focuses on infrastructure, social development (especially education and health), and rural livelihoods.

The improvement of rural livelihoods is the aspect of poverty reduction that MFIs focus on. In the past fifteen years poverty reduction has become an integral part of development paradigms. It has emerged as a World Bank objective in the 1990s and was adopted as one of the UN Millennium Development Goals in 2000. Just as poverty is not restricted to developing nations, neither is microfinance. Although it is most entrenched in parts of South Asia and Latin America, it is also being promoted in Canada, France, Germany, Ireland, United Kingdom and the United States.
References:


18. Remenyi, Joe; and Quinones, Benjamin (2000), Microfinance and Poverty Alleviation: Case studies from Asia and the Pacific. Pinter, New York.


