Chapter 3
MICROFINANCE IN INDIA;
SCOPES AND LIMITATIONS
Chapter 3

Microfinance in India; Scopes and Limitations

The literature surveyed in the previous chapter clearly bring an idea about the problems and prospects of microfinance, its impact on society, the growth and development of interest free financial institutions and its scope. Interest free financial institutions including banks and microfinance institutions are developed to fill up the gap created by conventional financial institutions. The present chapter is deal with structure, working and regulatory measures of microfinance sector in the country. Last part of this chapter discusses the crisis of Indian microfinance sector and giving a brief picture about interest free microfinance institutions in the country.

3.1 Definition of Microfinance Institutions

The proposed Microfinance Services Regulation Bill of India\(^1\) defines microfinance services as “providing financial assistance to an individual or an eligible client, either directly or through a group mechanism for:

i. an amount, not exceeding rupees fifty thousand in aggregate per individual, for small and tiny enterprise, agriculture, allied activities (including for consumption purposes of such individual) or

ii. an amount not exceeding rupees one lakh fifty thousand in aggregate per individual for housing purposes, or

iii. Such other amounts, for any of the purposes mentioned at items (i) and (ii) above or other purposes, as may be prescribed.”

The bill further defines Micro Finance Institution as “an organization or association of individuals including the following if it is established for the purpose of carrying on the business of extending microfinance services:

i. a society registered under the Societies Registration Act, 1860,
ii. a trust created under the Indian Trust Act, 1880 or public trust registered under any State enactment governing trust or public, religious or charitable purposes,

iii. a cooperative society / mutual benefit society / mutually aided society registered under any State enactment relating to such societies or any multistate cooperative society registered under the Multi State Cooperative Societies Act, 2002 but not including:

A cooperative bank as defined in clause (cci) of section 5 of the Banking Regulation Act, 1949 or a cooperative society engaged in agricultural operations or industrial activity or purchase or sale of any goods and services.”

Microfinance institutions have witnessed enormous growth during the last couple of decades. The Consultive Group to Assist Poor (CGAP)² under UN has given eleven key principles of microfinance. These are as follows:

### 3.2 Key principles of Micro finance

1. Poor people need a variety of financial services, not just loans.
2. Microfinance is a powerful tool to fight poverty.
3. Microfinance means building financial systems that serve the poor.
4. Microfinance can pays for itself, and must do so if it is to reach very large numbers of poor people.
5. Microfinance is about building permanent local financial institutions that can attract domestic deposits, recycle them into loans, and provide other financial services.
6. Microcredit is not always the answer. Other kind of support may work.
7. Interest rate ceilings hurt people by making it harder for them to get
8. The job of government is to enable financial services, not to provide them directly.

9. Donor funds should complement private capital, not compete with it.

10. The key bottleneck is the shortage of strong institutions and managers.

11. Microfinance works best when it measures and discloses its performance.

3.3 Objectives of microfinance

The organizations working to promote microfinance institutions in different parts of the world determine various objectives to microfinance. The important among them are listed as follows.

1. Promote socio-economic development at the grass root level through community-based approach

2. Develop and strengthen people’s groups called Self-Help Groups and facilitate sustainable development through them

3. Provide livelihood training to disadvantaged population.

4. Promote activities which have community participation and sharing of responsibilities

5. Promote programs for the disabled

6. Empower and mainstream women

7. Promote sustainable agriculture and ecologically sound management of natural resources

8. Organize and coordinate networking of grass root level organization

9. Get benefits by reducing expenditure and making use of local resources as inputs for livelihood activities

10. Increase the number of wage days and income at household level
3.4 Major Models of Microfinance initiatives

The literature on microfinance listed 12 various models of microfinance institutions working in different countries. This classification is on the basis of regulatory structure and operational methods. Few models are not common in international level and few others are complimentary. NGOs and self help groups are example. Most of the self help groups have a promoter NGO. At the same time many NGOs have direct microfinance chains. Like that commercial banks are implementing microfinance operations through its SHGs. In these cases two models are working together to serve poor. Some models are working in the informal sector only. Major models are grameen, village bank; credit union, co operatives, self help groups, commercial banks, NBFCs, Association of persons, nidhi model, community banking, NGOs and ROSCAs.

3.5 Recent History of Micro Finance in India

As we discussed in earlier chapters microfinance operation is not a new concept in the financial transactions. There were different forms of credit and lending activities existed in different parts of the world since the development of human history\(^3\). It includes individual money lending, various types of chitties, and also kurikkalyanam in Malabar area of Kerala. All these indigenous financial institutions were conducted microfinance activities in one way or the other. But modern types of microfinance were started its development since later half of 20\(^{th}\) century especially after 1970. Our country also witnessed the development of such like institutions in the same period.

Government’s initiative to reduce poverty by improving access to financial services to poor started since independence. India’s overwhelming majority of poor is located in rural areas and this motivated the government to give special attention to
rural credit. Following the report of All India Rural Credit Survey in mid 1950’s, the government took crucial steps in reviewing Cooperative structure including the partnership of State in cooperatives. Also the policy initiative of ‘social banking’ concept led to the nationalization of commercial banks, adoption of direct lending programmes to rural areas and development of credit institutions such as Regional Rural Banks (RRBs) and National Bank for Agriculture and Rural Development (NABARD).

The microfinance sector has emerged mostly from the efforts of Non-Governmental Organizations (NGOs), and as a response to the failure of existing structures to deliver financial services to the poor. The efforts by NGOs have emerged from grassroots and represent diversity. They do not fit into a straitjacket. Therefore, unlike the other structures like cooperatives, Regional Rural Banks (RRBs) and commercial banks, it is difficult to get statistics on microfinance. It is also difficult to make policy recommendations that impact the sector as a whole.

There are different channels for microfinance services in the country. SHG (Self Help Group)-Bank Linkage Channel (SBLC) is the first one, which was developed early 1990s by NABARD. More recently, many Non Governmental Organizations (NGOs), Community Based Organizations (CBOs) and Self Help Groups have started micro finance delivery systems successfully in rural areas. These organizations motivate the poor to join the credit groups, helps to manage their savings, loan-deposit and recovery process and may also provide an interest free loan to the group that acts as a start-up fund⁴.

The second channel is Micro Finance Institution (MFI). The MFI in India was first introduced in 1974, but the momentum was achieved only during the 1990s. In the country Self Employed Women’s Association (SEWA) Bank is the oldest micro
Finance organization. It was founded in 1974 in Ahmadabad, Gujarat as a trade union first, started organizing self-employed women. Initially the formal financial institutions were reluctant to be involved with the MFIs, and social entrepreneurship was also in short supply. But after 1990s banks and other financial institutions, helped by supportive public policies, have become more aware of the commercial viability of the micro finance services. Innovative partnership models have been developed between the banks and the MFIs. These have pumped huge funds to the sector and have subsequently enabled MFIs to increase their scale of operations and outreach.

It has witnessed tremendous growth of microfinance over the last two decades. A Microfinance Information Exchange\textsuperscript{5} (MIX) survey involving 78 countries revealed that India’s microfinance sector saw the largest per-MFI percentage increase in active borrowers in 2005 than any other country. According to microfinance Sector report of the ACCESS alliance, the MFI operations expanded by 13 times in four years to end the year 2009. Whereas there was only one for-profit MFI in the country in the middle of the 1990s, this number had spiraled to 149 registered micro finance institutions by 2009. Of these, about 11 per cent of the large micro finance companies had a disproportionally larger share in the credit market, having 82 percent of the clients and controlling about 88 per cent of the loan portfolio\textsuperscript{6}.

There are several legal forms of MFIs. However, firm data regarding the number of MFIs operating under different forms is not available. Therefore it is no uniformity in the number of MFIs we got from different sources. Rangarajan (2008)\textsuperscript{7} estimated that there are about 1,000 NGO-MFIs and more than 20 Company MFIs. Further, in Andhra Pradesh, nearly 30,000 cooperative organizations are engaged in
microfinance activities. However, the companies MFIs are major players accounting for over 80% of the microfinance loan portfolio. There are more than 2000 NGOs involved in the NABARD SHG-Bank linkage program. Out of these, approximately 800 NGOs are involved in some form of financial intermediation. Further, there are 350 new generation co-operatives providing thrift and credit services.

During the last decade, the union and state governments has considered microfinance as a tool to meet the financial service requirements of the poor. It has framed policies that enable the increased access to financial services for the poor. Series of measures are introduced for the same. The following have been the significant initiatives:

- Encouraging National Bank for Agriculture and Rural Development (NABARD) to set targets for the self-help group (SHG) – Bank linkage programme
- Emergence of SIDBI Foundation for Micro-Credit as a financier of microfinance institutions (MFIs)
- The pronouncements of the Reserve Bank of India (RBI) from time to time – such as
  - including lending to SHGs as a part of priority sector targets
  - exempting non-profit companies doing microfinance from registering as an NBFC
  - permitting the establishment of local area banks (now withdrawn)
  - Appointed a committee to study about regulatory measures to implement for smooth functioning of MFIs. (Melegam committee)
- Setting up of the Rashtriya Mahila Kosh to re-finance microfinance activities of NGOs
Routing some poverty oriented schemes such as the *Swarnajayanti Gram Swarozgar Yojana* (SGSY) through SHGs

The close linkage built by DWCRA schemes

The initiatives of various state governments in promoting schemes such as *Swa-Shakti* (Gujarat), *Velugu* (Andhra Pradesh), *Kudumbasree* (Kerala) etc.

### 3.6 Micro Finance Models in India

A wide range of microfinance models are working in India. Experts opinion is that India host the maximum number of microfinance models. Each model has succeeded in their respective fields. The main reason behind the existence of these models in India may be due to geographical size of the country, a wide range of social and cultural groups, the existence of different economic classes and a strong NGO movement. Micro Finance Institutions in India have adopted various traditional as well as innovative approaches for increasing the credit flow to the organized sector. They can be categorized into six broad types.

1. Grameen model
2. SHG model
3. Federated SHG model
4. Cooperative Model
5. ROSCAs
6. Micro-finance companies (MFCs)

#### 3.6 a. The Grameen Model

The Grameen model has been a case of exceptional success in Bangladesh. It turns out that many organizations in India have adopted the Grameen Bank model with little variations. Some of the notable examples are SHARE Microfinance
Limited, Activists for Social Alternatives (ASA) and CASHPOR Financial and Technical Services Limited.

Some of the significant features of Grameen bank model are low transaction costs, no collateral (peer pressure is sufficient), repayment of loans in small and short interval and quick loan sanctions with little or no paper works and no formalities. Repayment of loans in small chunk is one of the major reasons of high loan recovery rate of a Grameen Bank. Furthermore, loans are provided for all purposes like housing loans, sanitation loans, supplementary loans etc. Also the interest rates are nominal making it easy for the poor people to repay their loans timely. Some of the salient features of Grameen model are mentioned below:

a) Homogenous groups of five members are formed at local level.

b) All the group members got a 7-day compulsory training

c) Some groups undergo the Group Recognition Test for screening serious and non-serious groups.

d) Those who passed the GRT she should become members of bank by paying a one-time membership fees.

e) Eight Groups affiliate together to form a centre.

f) Centre meets every week, at a defined time. A staff of the bank attends the meeting.

g) Group discipline is enforced through peer pressure

h) The savings are compulsory for the members. Every member saves Rs. 10 every week.

i) The size of the loan generally ranges from Rs 4000 to Rs 10000 for general yearly loans. The first year size is Rs 4000 and there is an annual increase of Rs. 1000 in loan size, for every year thereafter.
a) All loans including agriculture loans are repayable within a year, equal installments spread over 52 weeks.

b) The provision of 5% tax of all productive loans disbursed to a member is one of the most important strategies to increase group fund. This fund remains with the group.

c) The group leader collects the loan repayments and savings prior to the meeting and hands it over to the centre leader who in turn during the meeting gives it to the field worker.

d) The interest rates varies from 15-24%.

e) Collateral is replaced by peer pressure. The incentive to timely repayment is repeat loans and continues access to increasing credit from Bank.

The most remarkable aspect of the Grameen model is very low default, repayment rate is in the range of 98% and above. It has led to low cost of credit and attracted low cost funds from the government and international donors. While the Grameen model is limited to less than a dozen major NGO-MFIs or NBFCs, it is an important alternative credit delivery system to mainstream finance.

3.6 b. Self Help Groups (SHGs).

An SHG is a group of five to 20 people from same income category formed on principle of lending their own savings. They also seek external funding to augment these resources. This group is a voluntary one, formed on the areas of common interest so that they can think, organize and operate for their own development. The SHGs function on the basis of co-operative principles and provide a forum for members to extent support to each other. SHGs play a crucial role in improving the savings and credit and also in reducing poverty and social inequalities. Almost 90% of the SHGs in India are female only due to the known fact that world’s poorest households tend to rely more heavily on income generated
by women of the house. In India, SHGs have been the most popular way to help the poor and make them bankable. They can play important role in:

(1) Preventing exploitation of the poorer sections by creating self-reliance
(2) Building leadership qualities among group members
(3) Helping group members in documentation for obtaining credit
(4) Motivating members for prompt repayment of credit
(5) Providing training to its members.

In the country this model was popularized by NABARD’s SHG-Bank linkage programme. A number of nongovernment organizations (NGOs) are specializing in promoting and motivating SHGs. Once the basic group is identified the NGO facilitator builds in processes and systems that make the SHG a viable, sustainable institution. The group meets regularly, mostly weekly, at a determined time and place and carries out its financial transactions of savings and credit. The group mobilizes savings from its members and makes need based loans to them out of the pool of funds created. The rules and the norms of the group are determined by the group members themselves and the NGO facilitator does not impose any thing.

Features of SHG Model

1) The SHG model has mainly evolved in the NGO Sector. NGOs primarily have the missionary for enabling, educating and networking

2) Strengths of members are 10 to 20. Group members are socially and economically homogenous.

3) Groups are composed either by male only or by female only. In India 90 percent of the SHGs are composed of female only.
4) Members are selecting groups as their choice. NGO acts as a facilitating agency to build in processes and systems that make the SHGs viable and sustainable institutions.

5) The SHG members meet regularly at a fixed time and place for carrying out their savings and credit activities and other issues of development.

6) The group mobilizes thrifts among the members and issues loans to the members.

7) The rules and norms for the group are decided by members themselves.

8) The main motive of the SHG is to empower poor socio-economically and improve their living standard.

Any way SHG is the popular model of microfinance in the country because advantages out weights disadvantages. Even the government considers SHG as the core of their strategy to promote different socio economic objectives. Undoubtedly SHG as emerged as the ‘Indian’ model of micro finance. There are SHGs in India promoted and sponsored by different institutions and organizations including governmental agencies. These are listed under.

1) SHGs promoted and financed by banks.

2) SHGs promoted by NGOs/Govt. Organizations and finance by banks.

3) SHGs promoted by financed through by NGOs by raising bank loans.

4) Federated SHG approach.

5) SHGs promoted by NGOs/Societies/other organizations and financed by Microfinance Institutions.

6) SHGs promoted by Micro-finance promotion institutions (MFIs)

7) SHGs promoted by interest free institutions
3.6 c. Federated Self Help Groups (SHG FEDERATIONS)

Self Help Groups have been very successful in empowering women by providing direct and indirect benefits to them. However, SHGs are small in size and are limited in the types of financial services they can provide. Since Self Help Groups are a widely successful delivery model a need arises to scale them up without compromising with the success. The Federated Self Help Group model is one such way to scale up the previous model. Federation of SHGs bring together several SHGs. Compared to a single SHG, federation of SHGs have more than 1000 members.

In federated SHG model, there is a three tier structure – the basic unit is the SHG, the middle tier is a cluster and the topmost unit is an apex body, which represents the entire SHG. At the cluster level, each SHG is represented by two of its members. The representatives of each SHG meet regularly. Information about the groups to the apex body and vice versa is given by the cluster unit. The apex body usually made up of 10 – 15 members and they form the link between the SHGs and the NGO supporting them. With the help of federations, an NGO with limited resources can have an impact on a large number of people. Few notable examples of Federated Self Help Group model in India are PRADAN, Chaitanya, SEWA and Dhan Foundation. The important features of federations are listed below.

Features and functions of federations

1) Being small in size, Self-help Groups (SHGs) are somewhat limited in the financial services that they can provide. Federations of self-help groups, which bring together several SHGs. Have the ability to overcome the limitations of individual SHGs.

2) Federations are registered, usually under the Societies Registration Act. They have between 1000 to 3000 members.
3) There are three tier structures for federations. The SHG is the basic unit, the cluster is the intermediate unit and an apex body, a federation, represents the entire membership.

4) At the cluster level, each SHG participates directly in the representative body, with two members from each SHG attending the monthly cluster meetings. Information from the groups to the federations and vice versa is channeled through the cluster level representative body.

5) The leaders of the cluster, who are in closer contact with the groups, are thus a highly effective tier for group monitoring and strengthening. By creating clusters, the operations of the apex body are decentralized.

6) The executive body at the apex level is the executive committee, which is typically made up of 9 to 15 members.

7) Federations also have paid staff members working for them. The staff manages the day-to-day operations, with guidance from the supporting NGO.

8) As apex institutions representing several SHGs, the federations are fairly competent in helping groups with loan recovery and in strengthening weak groups.

9) Paucity of funds and idle money both been problems in SHGs models, have been solved by federations, which helped to

   a) Productively channelize the idle money of SHGs, where the demand for loans is much lower than their available money supply

   b) Enable SHGs, where natural demand for loans greater than the available credit, to access more funds

   c) In a way, this is a crucial role played by federations, whereby the utilization of scarce local capital is optimized and the returns on this capital are maximized.
d) Compared to SHGs, federations provide members with more opportunities to save and also make larger loans available. They are also able to provide specialized financial services (like insurance) to the members because of the (larger) scale of their operations.

1) Federations also facilitate to

   a) Enable SHGs to access and manage external funds,

   b) Help in the promotion of newer SHGs and also the strengthening of existing groups through capacity building inputs,

   c) Facilitate financial and non financial inter-group exchange,

   d) Help in maintaining linkages between SHGs and other agencies and

   e) Assisting SHGs with loan recovery.

While savings occur through the self-help groups (SHGs), the role of the federation with regard to the savings is different. Sometimes, the federation provides other options to members for saving, in addition to what is saved with the group. The members thus have savings with the group and in addition, with the federation. In other cases, the federation has developed special savings schemes, which allow members to save for specific purposes. The federation, by virtue of its size and scale of operations, is thus able to expand the savings opportunities for members. The credit giving patterns also vary. While, generally, federations have credit activities occurring at the group level, the federation also provides credit to their members. These loans are given from members’ savings that may be deposited with the federation, and from external funds that it is able to access independently. Federations are thus able to increase the amount of credit available to members.
3.6 d. Co Operative credit Unions

Cooperative credit unions are another important microfinance model developed in the country. The leading organization that has been successful in using the cooperative form in rural microfinance in India has been the Cooperative Development Forum (CDF), Hyderabad. CDF’s approach has relied on a credit union model involving a savings first strategy. It has built up a network of financial cooperatives based upon women’s and men’s thrift groups. After the implementation of Andhra Pradesh Mutually –Aided Societies Act for flexible functioning of cooperatives, it has registered the associations of thrift groups promoted by it under this Act. The MACS Act has become landmark legislation, which has been used by other organization as well to register associations based on other approaches such as SHGs and Grameen joint liability groups as MACS.

Features of CDF system

1. The primary bodies in CDF’s micro-finance (cooperative) system are the women’s/ men’s thrift cooperative (WTCs and MTCs) which consist of 300 members, usually from the same village.

2. CDF has started off by promoting much smaller units, but over time it encouraged these small units to merge into larger units as it felt that smaller units would not be viable.

3. The WTCs and MTCs are divided into smaller groups (10 to 15 members) to facilitate better monitoring of thrift and loan payments. Each group headed by a leader, who convenes the group meetings, collects savings, and monitors the repayment of loans.

4. The size of a group is often dictated by the capability of its leader, who is nominated by the members of the group.
5. Though groups serve some administrative purposes, CDF has encouraged members to identify more strongly with their thrift cooperatives rather than the groups, as they are the primary legal entities and viable units of operation.

6. All the members of the primary cooperatives constitute the General Body and adopt a uniform set of bylaws. The General Body meets once every year to elect the directors, review operations and discuss other issues. The Board of Directors consists of 12 directors who are elected from amongst the members.

7. The directors elect a chairperson and appoint managing directors from among themselves. Both the chairperson and Managing Director have a one–year term. They are however, eligible for re-election.

8. A set of geographically contiguous cooperatives federate to form an association of women’s/ Men’s thrift cooperatives.

3.6 e. Rotating Savings and Credit Associations (ROSCAS)

ROSCAs are an alternative means of providing credit to groups of individuals. Individuals join groups centered around shared features such as community, ethnicity, or professions and make periodic donations in order to receive loans in the future. Each member systematically received a loan and repaid it in time for the next member to begin the loan process. Each member is dependent on the others to repay the loans or else the cycle will stop. Group members provide both support and sanctioning devices for each other.

Chit funds are the Indian equivalent of the Rotating Savings and Credit Associations (ROSCA) that are famous throughout the world. ROSCAs are a means to „save and borrow” simultaneously. It is considered one of the best instruments to cater to the needs of the poor. It enables poor people to convert their small savings into lump sums. A chit scheme generally has a predetermined value and duration. Each scheme admits a particular number of members (generally equal to the duration of the scheme),
who contribute a certain sum of money every month (or everyday) to the “pot”. The “pot” is then auctioned out every month. The highest bidder (also known as the prized subscriber) wins the “pot” for that month. The bid amount is also called the “discount” and the prized subscriber wins the sum of money equal to the chit value less the discount and the fixed fee to the foreman. The discount money is then distributed among the rest of the members (or the non-prized subscribers) as “dividend” and in the subsequent month, the required contribution is brought down by the amount of dividend.

In many parts of India, Chit Funds address gaps left by the traditional banking sector. They mobilize huge amounts of small savings, and in return allow members to have access in the form of loans to lump sum amount of money that they would often not be able to get from traditional banks. Easy accessibility and flexibility are important aspects of this form of financing. Compared to banks, Chit Funds require less documentation, are more flexible about collateral\(^9\). There are lakhs of ROSCAs are functioning in our community in different forms.

3.6 f. Microfinance companies

Microfinance companies are registered in two regulatory set up; Non Banking financial Companies (NBFC) under reserve bank of India or companies act. Many microfinance companies are registered in our country as NBFC. NBFCs are collecting savings and utilising their funds for loans and other activities. The micro finance institutions including BASIX, Asmitha, SKS and Janasree microfinance Kerala is registered as NBFC. NBFC is working by forming SHGs and direct lending model exists. Melegam committee appointed by RBI to study about regulatory measures of microfinance recommended separate structure for microfinance NBFCs. Other form of microfinance is registered as companies act. Most of this type of institutions is introduced as individual microfinance institutions working to make profits. In the last
decade the number microfinance companies registered in India had increased several times due to this sector developed as a business model instead of social service.

3.7 Regulatory structure of Microfinance in India

As we mentioned earlier India has no uniform structured law to regulate microfinance institutions. Different forms of organisations are depends on various existing regulatory frameworks for the functioning. All microfinance institutions aim social and economic upliftment of beneficiaries. But there are different forms of institutions are functioning to attain the same. They are broadly classified in to non profit institutions, mutual benefit institutions and for profit institutions. The goal of non profit institutions are only the financial and social empowerment of the beneficiary class. Such ventures are registering in different formats including as society under societies registration act of 1860, Charitable trusts under trust act and as section 25 company. Mutual benefit institutions are working only for the benefit of its members. Those are registered under co operative which can be just a savings and credit co operative or be further licensed as co operative bank, mutual benefit trust, under chitties act and mutual benefit section 620 nidhi companies. For profit entity may be registered as association of persons, investment trusts and company which is further either an NBFC or a bank.

Therefore there are mainly three channels for the regulation of microfinance institutions. NBFCs are registered under Reserve Bank of India. Further co operative institutions are registered under concerned state co operative society’s act and multi state co operative society under central government. Non profit entities are registered under societies or trust acts under the concerned state. Company under Indian companies act 1956 also possible for mutual benefit and profit based undertakings.
NGO-MFIs are non-profit MFIs left almost entirely unregulated and registered mainly under societies act or trust act. The major NGO-MFI sample includes All Backward Class Relief & Development Mission, Bharat Integrated Social Welfare Agency (BISWA), Cashpor Micro Credit, Evangelical Social Action Forum (ESAF) and Indian Association for Savings and Credit (IASC).

Table 3.1

Type of microfinance institutions in India

<table>
<thead>
<tr>
<th>Type of entity</th>
<th>Non-profit</th>
<th>Mutual benefit</th>
<th>For-profit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Association</td>
<td>Society under Societies Registration Act 1860</td>
<td>Cooperative which can be just a savings and credit cooperative or be further licensed as cooperative bank.</td>
<td>Association of persons</td>
</tr>
<tr>
<td>Trust under Indian Trusts Act 1920</td>
<td>Charitable trust</td>
<td>Mutual benefit trust</td>
<td>Investment trusts</td>
</tr>
<tr>
<td>Company under Indian Companies Act, 1956</td>
<td>Section 25 Company</td>
<td>Mutual Benefit (Sec 620A Nidhi Company)</td>
<td>Company which is further either an NBFC or a bank</td>
</tr>
</tbody>
</table>

Source: Rangarajan (2008) Report of committee on financial inclusion, government of India, chapter 8

3.8 NABARD; government initiative in microfinance in India

The National Bank for Agriculture and Rural Development (NABARD) was established by the Government of India in 1982 as a development bank for providing and regulating credit and other facilities for the promotion and development of agriculture, small scale industries, cottage and village industries etc. Later in 1986-87, the NABARD has also included to facilitate and support the orderly growth of the microfinance sector through diverse modalities for enlarging the flow of financial services to the poor particularly for women and vulnerable sections of society consistent with sustainability. Then NABARD launched a pilot project to provide micro-credit by linking SHGs with nationalized and different state cooperative banks.
in the year 1991-92. These banks acted also as promoter of MFI's. The SHG-Bank Linkage Programme’s aim was to improve rural poor’s access to formal credit system in a cost effective and sustainable manner by making use of the SHGs.

However, the NABARD promoted the Self Help Group (SHG) - bank linkage approach as the core strategy that has been used by the banking system in India for increasing their outreach to the poor. The strategy involved forming SHGs of the poor, encouraging them to pool their thrift regularly and using the pooled thrift to make small interest bearing loans to members, and in the process learning the nuances of financial discipline. The Bank credit to such SHGs promoted by the NABARD saw the promotion and bank linking of SHGs not merely as a credit programme but as part of an overall arrangement for providing financial services to the poor in a sustainable manner leading to empowerment of the members of these SHGs.

3.9 The crisis of Microfinance sector in India

In fact the microfinance is a new model for development and poverty alleviation. At the same time this sector attracted many investors both foreign and Indian vied with each other to build and fund these institutions as these became safe haven for investments. The reason was that the poor people are good borrowers, not only the return on capital was very high but also it provided highest level of safety as repayment of loan was almost 100%. It obviously helped rapid growth of MFIs in India particularly in southern states but gradually in other states also. This double edged benefit obviously made these institutions not only attractive to private equity firms but also enabled to raise money by floating shares even at a high premium. Few Microfinance ventures in India raise capital through share market at a very high premium rate last decade. This is when microfinance institutions began to be molded to the requirements of the wealthier class. The shareholders were naturally expecting
a high profit for their investment. The pressure started mounting on the companies and typical target sales and profit maximization tactics slowly crawled into the nerves of these once benevolent institutions. Although profit making MFIs cater to a large number of clients their outstanding bad debt.

Due to such over blown microfinance activities, in Andhra Pradesh the sector reached a saturation point. MFIs particularly in Andhra Pradesh registered a faster pace of growth when compared to others in the various parts of the world. Multiple loans availed by the clients resulted in a complicated situation of delinquency which in turn resulted in many customers taking the extreme step of suicide. Those poor people were lured into this debt trap by growth savvy MFIs and then overloaded them with loans without giving much importance to their repayment capabilities. Thus that innocent and ignorant clientele ended up with a huge amount of liability which was way beyond their ability to repay. Most of the borrowers became clueless about repayment schedule and was startled to see the rude reality only when MFIs started realizing loans with ruthless tactics. The borrowers were then forced to borrow more and more even from money lenders which in turn only worsened their debt woes. The situation became critical and came out bursting for the entire world to see its dirty face. Andhra Pradesh reported enormous number of suicides owing to this microfinance mismanagement

Indeed this proved to be an eye opener to people and then lot of hue and cry was raised to question the opaque procedures and products of these institutions. Then the state government of Andhra Pradesh in 2010 introduced separate regulation for microfinance institutions. The RBI was taken a step to appoint a sub committee to study about regulatory problems of MFIs in the country. The committee under Mr.
Melegam was submitted its report on January 2011, which suggests separate microfinance NBFC regulatory structure under RBI and fixed an interest cap at 24%\textsuperscript{11}.

There are now valid questions being raised by scholars about the model itself. One interesting book from Bangladesh published last year on this subject is *Microfinance and its Discontents: Women in Debt in Bangladesh*, by Lamia Karim. She has raised questions on the economic models behind these ideas also.

The real questions are what do the poor do with the money and can they really afford the high rate of interest of 24-60% per annum (if RBI regulation implemented 24% plus processing charge) usually charged by MFIs\textsuperscript{12}. Generally it would have to generate a rate of return of minimum 20-25% just to repay the debt and get some decent living out of the investment. Not only this is really impossible with the kind of assets that they can buy with the small amount of money made available to them, but even getting sufficient returns to pay the interest is difficult, considering that most of them have low skills with hardly any financial training. This factor should be seen along with the fact that most of such investment is in agriculture and livestock where returns are low. Investment in these sectors is also risky because of natural factors such as rainfall and disease, and due to price fluctuations in markets for such output. The situation is all the more serious because, in many cases, to increase the loan portfolio, MFIs also financed pure consumption loans.

But then how did the model work if the likelihood of paying this rate of return is so low? Recent studies suggest that this was done merely by rolling over the debt, with more and more MFIs competing with each other to offer money. But, in many cases, it was also the selling off of assets that helped the poor repay loans. Thus MFIs, which were seen as a helping hand of the poor from the moneylenders, were the same old, but much bigger Shylocks. Actually microfinance is a good model for poverty
alleviation and employment creation. But when we added the role of interest in it this model has becomes an instrument for making profit by exploiting the poor

But this also means that the problem cannot be seen only as a regulatory failure. The solution does not lie in knee-jerk reactions such as new regulations. Many scholars argue that MFIs cannot be a solution to the large-scale poverty that ails our rural areas. Nor is this the solution to financial inclusion. Financial inclusion requires much more than regulating MFIs. Financial inclusion cannot be measured by the number of bank accounts. The objective of financial inclusion has to be integrated to a strategy of making poor enterprises viable through building skills, training, insurance and market access.

3.10 Problems affecting Microfinance Institutions

It is understood from previous discussions that although there have been various successful stories about microfinance institutions helping the poor, they face with many problems. Many researchers pointed out the problems faced by this sector. Important among them are the following.

1. Ethical Reasons:

Microfinance Institutions can be often viewed as a profit making organization. The desire to make MFIs an industry, commercialize micro-lending or enable them to be a profit making institutions should not distract them from one important aspect for which they are formed in the first place: social service by enabling poor to work on profit making projects or small businesses. Many a times, the lack of this aspect can lead the microfinance institutions to behave similar to the local moneylenders.

Corruption is another ethical problem. Many MFIs in India or elsewhere in world suffer from corruption at various levels: corruption in the MFI itself, corruption
in the Micro Enterprises, these MFIs support or corrupt channels, officials or individual service providers.

2. Managerial Reasons:

One of the major problems which the MFIs can resolve is managerial problems. Managerial problems are a major factor and they have more effects than any other problems discussed. Poor record keeping and lack of managerial capacity are the major problems. For office bearers and group members, record keeping seems like a waste of time. Lack of record keeping can have its share of problems including increase in defaulters.

3. Legal Reasons:

Microfinance Institutions can be viewed as a social organization helping the poor and a profit organization too. In many countries, profit organizations are registered under different set of acts and non-profit organizations come under different legislations. These legalities sometimes create complications. But a charitable institution is not allowed to indulge in to money lending. The above case was a lack of a legislation especially serving microfinance institutions. There are some random acts which prohibit the growth of microfinance institutions and delimit their impact.

4. “Unfortunate” Reasons:

Sometimes microfinance institutions have to face problems which cannot be resolved. These problems arise in cases when something “unfortunate” happens to a person or a community. A flood or famine can kill the hopes of farmers to pay their loans. Personal plights are another reason which might affect the MFI.
5. Other Reasons:

There are various other factors for the failure of MFI. They can be listed as follows: Lack of vision is a factor which pushes new MFIs into extinctions. MFIs need trained staff to operate. In several cases, drop out of trained staff is very high which reduces the reach of an MFI. Furthermore, the “dropping out” rate is more than the “coming in” rate. MFIs serve society but they are also a profit-making institution. In many cases, MFIs achieve a lot of success in their programs in initial period, but they fail to maintain the same record in the long run because of lack of proper commercial orientation, thus making them unsustainable.

3.11 Microfinance and Neo liberalism

Microfinance in principle is not a recent origin. It has many forms in history of every civilization. It was the only way of finance to them before the development of banks and other financial institutions. But the reason behind the emergence of new generation MFIs is inadequacies of the formal financial system to cater to the needs of the poor at the grassroots level. Numerous government schemes have tried to provide various subsidized services to the poor households. Studies have exposed the limitation of these programs, showing the lack of access of mainstream financial services for these poor households and their over-dependence on the local moneylenders in meeting their consumption and micro-enterprise demands. Despite having a wide network or rural bank branches in the country and implementation of many credit linked poverty alleviation programs, a large number of the very poor continue to remain outside the fold of the formal banking system. Various studies also suggested that the policies, systems and procedures and the saving and loan products often did not meet the needs of the very poor.
Scholars are questioning these arguments about the introduction of microfinance initiatives. If a microfinance venture is introduced with only an objective for making available financial services to the poor and resultant improvement the policy makers of this sector does not given much importance for profitability and sustainability of microfinance. Now most of the large microfinance institutions are donor funded from international institutions under World Bank group or similar others. And even corporate are introduced their own microfinance networks. Microfinance is now known as “microfinance business”. Radha G Friedman (2005) examines the impact of donor sponsored microfinance in the country to alleviate poverty. She argues that actually microfinance is the agenda of World Bank and IMF to implement their liberalized financial policies that advises to the government to withdraw from public utility services and subsidized poverty eradication programmes. She also observe that uniform model of poverty alleviation like “cloneable” SHGs are not fit for poverty eradication in a large country like India because our poor are heterogeneous groups. She explains that when microfinance institutions replace their goal to commercialization and sustainability, its priority shifts to satisfying of investors instead of empowerment of poor.

Chao-Beroff (1997) criticizing microfinance in the following words, “There is thus great risk of diverting the newly created professor of ‘people’s banker’ or of the ‘micro-financing for the poor’ from its proper objective. The fact is that if priority is given to making (MFIs) profitable as quickly as possible, then the poorest will automatically be marginalized in favor of populations that are supposed to be more creditworthy. Similarly, the rural areas, in favor of urban areas, which are more densely populated and provide better commercial opportunities.” Thus, the fact that
many MFIs now favor institutional sustainability over poverty alleviation or empowerment as their primary objective must be taken with a large grain of salt.

There raise a question by proponents of microfinance sector that why most of the studies supports the developmental role of microfinance? Radha G Friedman answers that this is what refers to as a “media monopoly.” That is, the institutionist position has a positional advantage in its articulation in virtually all of the literature coming out of the World Bank, CGAP, and USAID. In other words, virtually all of the published literature in the field of microfinance favors the institutionist approach, lending it a somewhat hegemonic dominance in the industry and representing clear implications for new donors who want to exist microfinance sector as a feeding industry to their wealth. Further, Mayoux (2002)\textsuperscript{16} argues that poorly designed MFIs may not only have no positive impact, but may actually increase household poverty and promote further marginalization among already marginalized populations.

MFIs under pressure from donors to become financially self-sufficient in a short period of time target less poor or moderately poor borrowers who can take out larger loans. Many complain that they cannot cover their costs when traveling to remote villages and areas to find potential clients. Others attempt to pass on their costs to their clients by charging exorbitant interest rates which are not much higher than those of predatory moneylenders, while forgoing sometimes costly services to improve the productive capacity of their clients. Microcredit will never be the only solution to poverty, especially when it comes with exorbitant interest rates which create a debt burden on the poor.

Modern interest based financial system itself is a product of capitalist economic system. How the present interest based system works to favor the rich and kill the poor is succinctly explained by James Robertson\textsuperscript{17} in the following words.
“The pervasive role of interest in the economic system results in the systematic transfer of money from those who have less to those who have more. Again this transfer of resources from poor to rich has been made shockingly clear by the third world debt crisis. But it applies universally. It is partly because those who have more money to lend get more in interest than those who have less; it is partly because those who have less often have to borrow more; and it is partly because the cost of interest repayments now forms a substantial element in the cost of all goods and services, and the necessary goods and services looms much larger in the finances of the rich. When we look at the money system that way and when we begin to think about how it should be redesigned to carry out its functions fairly and efficiently as part of an enabling and conserving economy, the arguments for an interest free inflation free money system for the twenty first century seems to be very strong.”

The same author in another book comments as follows “The transfer of revenue from poor people to rich people, from poor places to rich places, and from poor countries to rich countries by the money and finance system is systematic one cause of the transfer of wealth from poor to rich is the way interest payments and receipts work through the economy”\(^\text{18}\).

Khurshid Ahmad (1998)\(^\text{19}\) asks why third world nations become poor after a richer past. He answers that that is because of flow of wealth from poor to the rich countries are the real reason behind the poverty of the nations. If this system exists the exploitation will continue in future and result would be increasing poverty and vulnerability in the world.

As we know every country is conducted a wide campaign for financial inclusion by the expansion of modern banks. But still around half of the population is financially excluded; most of them are less affluent people including poor and
moderate poor. It means they have not paid interest to the capitalist class. Microfinance is an agenda of capitalist class to financial inclusion means, poor are compelled to pay interest and they are subject to exploitation. Poor people generally not receive interest because they have no money to save or invest. Therefore Microfinance is a net to catch small fishes; it mobilizes huge amount of interest from poor class and flow it to the rich. When rich people got loans from commercial banks and other financial institutions at low rate of interest (from 4% to 12% in India) the poor receives the same from microfinance institution at very high rate from 24% and above. Then it is celebrating as a tool for poverty alleviation.

When we examine the statistics of poverty and growth of microfinance sector in our country for the last two decades, it shows that while microfinance institutions and number of clients increased since 1990, but did not affect poverty. The table 3.2 shows the poverty estimation by planning commission of India. It is seen that from 1973-74 to 2004-05, the percentage of people come under poverty line has a decline; from 54.9 to 37.2. But the number of poor has increased from 321.3 to 407.1. Within the period of 30 years around 80 million poor people increased in the country. The highest growth is within 15 years of reform period, we see an increase in number of poor around 10 crores. (In 1987-88, 307.1 to 2004-05, 407.1) It shows that after the implementation of many poverty alleviation measures poverty is still continues as a problem in the country; and an increasing trend in post reform period. The table and chart following give the true picture of poverty of the country during the last decades²⁰.
Table 3.2

Number of poor in India 1973-74 to 2004-05

<table>
<thead>
<tr>
<th>year of study</th>
<th>Percentage</th>
<th>Number in Millions</th>
</tr>
</thead>
<tbody>
<tr>
<td>1973-74</td>
<td>54.9</td>
<td>321.3</td>
</tr>
<tr>
<td>1977-78</td>
<td>51.3</td>
<td>328.9</td>
</tr>
<tr>
<td>1983</td>
<td>44.5</td>
<td>322.9</td>
</tr>
<tr>
<td>1987-88</td>
<td>38.9</td>
<td>307.1</td>
</tr>
<tr>
<td>1993-94</td>
<td>36</td>
<td>320.3</td>
</tr>
<tr>
<td>1999-2000</td>
<td>26.1</td>
<td>260.2</td>
</tr>
<tr>
<td>2004-05</td>
<td>27.5 (pre revised)</td>
<td>301.7</td>
</tr>
<tr>
<td>2004-05</td>
<td>37.2 (Tendulkar)</td>
<td>407.1</td>
</tr>
</tbody>
</table>

Source: Planning Commission

Chart 3.1

Various studies also prove the failure of these institutions in eliminating poverty. Fernando (2004)\(^1\) and Robinson (2000)\(^2\) claim that instead of eliminating poverty, microfinance is in fact perpetuating it. Cited from The Consultative Group to Assist the Poor (CGAP) in 2003, Fernando argues that the users of microfinance are
generally those who are living within poverty lines, and those who are among the poorest in the society remain neglected and invisible by the microfinance. According to them the requirement set by microfinance cannot be fulfilled by the poorest or extremely poor groups in the society.

Before the reform period we have lot of programs to come directly to the poor people for upliftment of their living standard. At that period the main problem we have faced was huge percentage of unbankable population. But by the introduction of microfinance institutions, up to a limit moderate poor are become the members of these institutions; by charging high rate of interest the exploitation has increased. On the one hand taking loan from MFI to do business, farming or self employment is become a loss making activity and they fell in a debt trap. To repay a loan in an institution the poor takes another loan from same institution or the other. The debt trap is increasing year by year up to the loss of their assets like land or house. Consequently these people become poorest of the poor. On the other side the poorest of the poor people never become a member of any microfinance institution and they can’t receive any benefit of poverty alleviation program because they are not a member of any MFI. Both of these sides lead to the increase in size of poverty in the country. This tendency may lead to rise in poverty in rural areas while microfinance operations increasing.

On the basis of the statistics, literatures and true facts in our country it is to be argued that microfinance is an instrument of neo liberal policies introduced to withdraw government from social welfare programs. When more microfinance institutions are coming to operate the state is withdrawing direct poverty eradication programs and implement all these through SHGs. By mobilizing saving from the members of microfinance huge amount of fund is mobilized to utilize for
microfinance ventures. At the same time they provide loans at the interest rate up to 60%, and the poor people are exploited by the corporate. Thus the poor are subjected to massive exploitation and are deprived of the welfare measures of the government. The root cause of the pathetic situation of poverty estimates in recent years can be seen here.

### 3.12 Interest free microfinance

As we understood from previous discussions microfinance broadly means provision of micro financial services to the common public. It has no single or uniform model to microfinance. As CGAP emphasizes, "diverse approaches and channels are needed to get diverse financial services into the hands of a diverse range of people who are currently excluded". Making this vision a reality microfinance institutions are developing in different forms offering various types of services. Interest free and Islamic microfinance is an alternative approach and model to microfinance.

The main feature which distinguishes Islamic microfinance from its conventional counterpart is the concept of social responsibility and working for the common good. Eradication of poverty, socio-economic justice and equitable distribution of income are among the primary goals of Islam and should be great features of an Islamic economic system. The philosophical basis of the whole Islamic financial system is that of *al-adl* (social justice) and *al-ihsan* (benevolence) which should be reflected in its operations. In other words, the spirit of the entire Islamic economics and financial system is based on the concept of ‘social justice’ by ensuring that wealth is fairly distributed among members of society to promote social and financial inclusion.
The rationale for the introduction of Islamic micro-financing is that conventional micro-finance does not cater for the needs of less affluent peoples and therefore, the suggested alternative is the introduction of micro-finance institutions working on the principles of Shari’ah\textsuperscript{25}. Islamic micro-finance can be defined as the investment of capital (in cash or in kind) based on Islamic modes of finance to poor entrepreneurs in order to help them start or maintain their businesses\textsuperscript{26}. In other words, Islamic micro-financing/micro-credit refers to a faith-based way of providing financing to those rejected by the mainstream financial services.

Several studies indicate that interest free Islamic microfinance developed as an alternative to conventional MFIs to reduce its negative effects. Theoretically, the main point of departure for Islamic microfinance from conventional credit/finance systems comes from the concept of joint liability. Conventional micro financing violates Islamic principles by charging interest rate. This is a matter of concern for Muslims due to the consequences of dealings with interest. One of the primary and the most frequently articulated rationales by Muslim scholars is that charging interest is a form of social and economic exploitation, which violates the core Islamic teaching of social justice. Thus elimination of this is intended to promote economically just, socially fair, and ethically and morally correct economic behavior\textsuperscript{27}.

### 3.13 Interest free microfinance in practice

There are different forms of interest free microfinance is functioning in different parts of the world. There are two categories in it; for profit institutions and nonprofit institutions. Various instruments and operational methods of these institutions are discussed in chapter 4 of the study. There are lots of informal and formal microfinance institutions are working in interest free basis. ROSCA on interest free basis is important one. Other member based organizations like co operatives,
qard hasan funds, nidhis, credit unions, village banks etc are developed in many countries. Non Banking Financial Companies include mortgage lenders, leasing companies, insurance companies, small community rural banks specialized microfinance banks also are the important types of institutions in the formal sector providing microfinance services. The main feature of these institutions is participatory approach. CGAP listed 105 such institutions in its report on 2007.

India has the history of more than a century in developing interest free microfinance setup. Studies show various numbers of such institutions. (Rahmathullah 1999, Bagsiraj 2002, Shariq Nisar 2009) These institutions basically follow three distinct models, and are registered with three different authorities. And also large number of institutions is not registered which classified as Financial Association of Persons. Muslim Funds, Welfare Societies and Bait-ul-Maals (public fund of Muslims) are registered under Society or Trust Act is classified as Islamic Financial Societies. The institutions registered as interest-free Co-operative Credit Societies registered with the Registrar of Co-operative Societies are classified as interest free Co-operative Credit Societies. Interest-free investment and financial companies registered under Companies Act or RBI are classified as Islamic Investment and Financial Companies.

Large number of interest free financial arrangements in our country is unregistered in organised in the form of Financial Associations of Persons (FAPs). They do not have any specific format or model. These are the result of private efforts of ordinary Muslims, living or working together in market, educational institutions, working places etc. They are generally organised in the form of co operatives, Chit Funds or loan funds. Every member of the Group gets an assured lump sum at no cost, which he or she left to himself or herself is not able to save or accumulate. Some
FAPs formed by Muslim businessmen collect their daily savings and provide loans of Rs.0.5 lakh to Rs.1.00 lakh, which are also refunded on daily basis within 3 to 6 months at nominal cost.

Bagsiraj (2003) classified interest free institutions in India as financial societies, interest free co-operative credit societies, interest free investment and financial companies and financial association of persons. State-wise largest number of IMFIs, 25% of the total are found in UP. Kerala accounts for 61 or 20.89% of them. Maharashtra and Karnataka are the only other states with over 10% IMFIs. Assam and Punjab have reportedly only one IMFI each.

Table 3.3
Geographical distribution of interest free financial institutions in India

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>State</th>
<th>IIFCs %</th>
<th>ICCSs %</th>
<th>IFSs %</th>
<th>FAPs%</th>
<th>TOTAL %</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Andhra Pradesh</td>
<td>4 22.2</td>
<td>2 11.1</td>
<td>7 38.9</td>
<td>5 27.8</td>
<td>18 6.2</td>
</tr>
<tr>
<td>2</td>
<td>Assam</td>
<td>-</td>
<td>-</td>
<td>1 100.0</td>
<td>-</td>
<td>- 0.3</td>
</tr>
<tr>
<td>3</td>
<td>Bihar</td>
<td>-</td>
<td>-</td>
<td>22 91.7</td>
<td>2 8.3</td>
<td>24 8.2</td>
</tr>
<tr>
<td>4</td>
<td>Gujarat</td>
<td>-</td>
<td>2 28.6</td>
<td>3 42.9</td>
<td>2 28.6</td>
<td>7 2.4</td>
</tr>
<tr>
<td>5</td>
<td>Karnataka</td>
<td>6 20.0</td>
<td>4 13.3</td>
<td>8 26.7</td>
<td>12 40.0</td>
<td>30 10.3</td>
</tr>
<tr>
<td>6</td>
<td>Madhya Pradesh</td>
<td>-</td>
<td>-</td>
<td>2 50.0</td>
<td>2 50.0</td>
<td>4 1.4</td>
</tr>
<tr>
<td>7</td>
<td>Maharashtra</td>
<td>12 37.5</td>
<td>6 18.8</td>
<td>8 25.0</td>
<td>6 18.8</td>
<td>32 11.0</td>
</tr>
<tr>
<td>8</td>
<td>Punjab</td>
<td>-</td>
<td>-</td>
<td>1 100.0</td>
<td>-</td>
<td>- 0.3</td>
</tr>
<tr>
<td>9</td>
<td>Rajasthan</td>
<td>-</td>
<td>-</td>
<td>3 100.0</td>
<td>-</td>
<td>3 1.0</td>
</tr>
<tr>
<td>10</td>
<td>Tamilnadu</td>
<td>1 7.1</td>
<td>-</td>
<td>10 71.4</td>
<td>3 21.4</td>
<td>14 4.8</td>
</tr>
<tr>
<td>11</td>
<td>Uttar Pradesh</td>
<td>3 4.1</td>
<td>-</td>
<td>39 53.4</td>
<td>31 42.5</td>
<td>73 25.0</td>
</tr>
<tr>
<td>12</td>
<td>Delhi</td>
<td>20 100.0</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>- 6.9</td>
</tr>
<tr>
<td>13</td>
<td>West Bengal</td>
<td>-</td>
<td>-</td>
<td>2 50.0</td>
<td>2 50.0</td>
<td>4 1.4</td>
</tr>
<tr>
<td>14</td>
<td>Kerala</td>
<td>3 4.9</td>
<td>-</td>
<td>41 67.2</td>
<td>17 27.9</td>
<td>61 20.9</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>49 16.8</td>
<td>14 4.8</td>
<td>144 49.3</td>
<td>85 29.1</td>
<td>292 100.0</td>
</tr>
</tbody>
</table>


3.14 Interest free finance institutions in Kerala

The ‘Interest Free Financial Institutions’ in Kerala are considered as microfinance ventures because its size of operation are micro level. These institutions
mainly provide loans to poor and needy people without interest on a systematic repayment basis. The capital is mobilized by accepting donations and saving deposits. These institutions invest a part of these deposit amounts in productive ventures and distribute the profit share to the depositors. Its functions mainly based on charity as it provides temporary advances for emergencies and necessities.

These region based indigenous arrangements which are familiar in different names like ‘paraspara sahaya nidhi’ (mutual help fund) or ‘palisha rahitha nidhi’ (interest free fund). There is an umbrella NGO to coordinate, guide and supervise these institutions, known as INFACC. According to the official records presently there are 390 establishments registered with INFACC. The total capital of all these institutions accounts for Rs 10 Crore. They are allowing loans for needy people for small trades, house repairing, cultivation, self employment projects, medical treatment, and durable consumption purposes. The self employment projects include production of Note books, Umbrellas, school bags, School uniforms and other textiles. Other short run loans are also provided to individuals for various purposes on personal or asset guarantee. As per the experience of INFACC, the repayment rate is more than 99%. (Hussein 2008)\textsuperscript{31}. Though the number of institutions registered in INFACC is 390, there are many such unregistered institutions functioning in Kerala. These indigenous institutions play a crucial role in the socio-economic life of Kerala. The role, performance and impact of such institutions in the society and economy are not looked into. (Ramzan 2008)\textsuperscript{32}

From the discussions in this chapter got an idea about functioning of microfinance institution in India, its limitations, problems and we discussed interest free microfinance as an alternative and solution for these problems. And also familiarized the growth of interest free micro ventures in the country especially Kerala. Next
chapter is specialized for theoretical framework and operational methods of interest free institutions.

**End Note:**

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