CHAPTER - I

INTRODUCTION

India with the 1.20 billion people represents a huge market with tremendous opportunities for expanding financial access, especially among its poor. The microfinance sector in India has a rapid growth during the last few years. The availability of a large market, willingness of banks to lend to microfinance institutions (MFIs) for meeting their priority sector targets as also because they sense a good market has all helped the rapid growth of the microfinance sector. Growth in the microfinance sector in terms of outreach has also meant institutional growth in India. In South of India, the MFIs in AP, Tamil Nadu and Karnataka account for 52 percent of the clients. Whereas, growing number of start-ups have initiated operations in the Northern and North-Eastern States.

MEANING AND CONCEPT OF MICROFINANCE

The term microfinance denotes small scale financial services - both credit and savings - that are extended to poor people of the society. Microfinance (Development and Regulation) Bill, 2010 defines micro-credit not to exceed Rs. 50,000 per borrower.

In fact, microfinance is the provision of thrift, credit and other financial services and product of very small amount to the poor for enabling them to raise their income levels and improve their living standards. It has been recognised that microfinance helps the poor people to meet their needs for small credit and other financial services. The informal and flexible services offered to low income borrowers for meeting their modest consumption and livelihood needs have not only made
microfinance movement grow at a rapid pace across the world, but in turn has also impacted the lives of millions of poor positively.

The modern concept of microfinance reveals that the microfinance is the extension of small loans and other financial services such as savings, insurance, money transfer, counseling etc to the low income groups. It is an economic development tool which has been designed to spread financial inclusion and assist the poor to work their way-out of poverty and uplift their social status.

Bangladesh is a prime mover in microfinance. The Bangladesh Grameen Bank Model is Pioneer for financing the poor and downtrodden. The microfinance programme in Bangladesh is widely accepted. Today, the idea of small, collateral free loans for poor women known as ‘micro-credit’ or ‘microfinance' has become a common place around the world. According to Nobel Laureate Mohammed Yunus, Microfinance is a form of social business that can eradicate poverty, “You can provide microcredit to poor people so they can create their jobs through self-employment”. Professor Yunus also focuses on new category of business named social business.

The Microfinance Institutions (MFIs) have emerged with an ambitious vision of alleviation of people living below poverty line and to bring the poorest of the poor to the mainstream of the economy. This paved the way for poor, especially the rural poor, to become economically independent. Microfinance has evolved as one of the important economic development tool to support low income group by providing financial assistance for self-employment.

Microfinance programmes / schemes have the potential to transform power relations and empower the poor-both men and women. There is a relationship of
respect between the provider and the client that is inherently empowering. As a consequence, the microfinance has become a central component of many donor agencies and national government, gender, poverty alleviation and community development strategies. But simply putting financial resources in the hands of the poorest of the poor is not enough to bring about empowerment and welfare. It needs to support them with their own enterprise in their own villages specially women in rural backlogs. The finance is provided at a very reasonable rate of interest and flexible repayment facilities to poor families to help them engage in productive activities to grow their tiny business. Today, microfinance is very much in the agenda of public policy and it has been increasingly used as a vehicle for reaching the otherwise unreached poor in the country.

In essence, the microfinance is about providing financial services to the active poor who are traditionally not served by the conventional financial institutions. It is the provision of very small loans (Micro-Credit) to the poor, to help them engage in new productive business activities. It includes a broader range of services mainly credit, savings, insurance, money transfers loans and other financial products targeted at the poor. It is an effort to improve the productive capacity of the rural and urban poor, enhance their economic standing which alleviates the level of poverty and aggregated to improve development of the national economy.

**OBJECTIVES OF MICRO FINANCE**

- Reduction of poverty to the bear minimum by financing for the development of skills of the rural folks.
- Providing employment opportunity to the poorest of the poor.
- Cultivating the habit of saving from the little earning.
• Providing the credit at the affordable rate of interest.
• Disbursing the credit amount in short notice.
• Eliminating the collateral security for providing credit.
• Eliminating the informal money lenders from the credit link.
• Encouraging the rural folks especially women entrepreneur.
• Providing better living to rural folks.
• Ultimately to provide better social status to the rural households.

CONCEPT OF MICROFINANCE

Today, the concept of microfinance has become a major credit disbursement mechanism in many parts of the world. It now refers to loans, savings, insurance, transfer services and other financial products targets at low income clients. It covers the following activities.

1. **Micro-credit:** It is a small amount of money lent to a client by a bank or other institution. Microcredit can be offered, often without collateral, to an individual or through group lending Micro Finance (Development and Regulation) Bill 2010 defines micro-credit not to exceed Rs. 50,000 per borrower.

2. **Micro-savings:** These are deposit services that allow one to save small amounts of money for future use. Often without minimum balance requirements, these savings accounts allow house holds to save in order to meet unexpected expenses and plan for future investments.

3. **Micro-insurance:** It is a system by which business and other organizations

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1The Journal of Indian Institute of Banking & Finance, October - December 2011, P. 54
make a payment to share risks. Access to insurance enables entrepreneurs to concentrate more on developing their businesses, while mitigating other risks that could affect the business.

4. **Remittances:** These are transfers of funds from people in one place to people in another usually across borders to family and friends. Compared with other sources of capital that can fluctuate depending on the political or economic climate, remittances are a relatively steady source of funds.

In addition to financial intermediation many MFIs provide social intermediation services such as group formation, development of self confidence, and training in financial literacy and management capabilities among members of a group. Hence the definition of microfinance often includes both financial intermediation and social intermediation. Microfinance is not simply banking, it is a development tool.

**MICROFINANCE ACTIVITIES AND CLIENTS**

Microfinance activities usually involve:

- Small loans to poor people typically for working capital.
- Informal appraisal of business and investment.
- Collateral substitutes such as group guarantees on compulsory savings.
- Access to repeat and larger loans, based on repayment performance.
- Streamline loan disbursement and monitoring.
- Secure savings.
- Enterprises development services such as skill training and marketing and social services.
**Microfinance Clients**

Microfinance clients are typically self employed, low income entrepreneurs in both urban and rural areas. Clients are often traders, street vendors, small farmers, service providers such as hair dressers, drivers, rose plantains sellers and artisans and small producers such as blacksmith and welders. Usually their activities provide a stable source of income.

The poor are bankable, as they can save, invest, repay loans and have need for insurance services.

**HISTORY OF DEVELOPMENT OF MICROFINANCE CONCEPT**

The history of the micro financing can be traced back as along to the middle of the 1800s when the theorist Lysander Spooner was writing over the benefits from small credits to entrepreneurs and farmers as a way of getting the people out of poverty. One of the earliest and longer lived micro credit organisations providing small loans to rural poor with no collateral was Irish Loan Fund System, initiated in the early 1700s by the author and nationalist Jonathan Swift.

The concept of microfinance is not new. Savings and credit groups that have operated for centuries include the ‘Susus’ of Ghana, ‘Chit funds’ in India, ‘Tandas’ in Mexico, ‘Orison’ in Indonesia, ‘Cheetu’ in Srilanka, ‘Tandas’ in West Africa and ‘Pasanaku’ in Bolivia as well as numerous savings clubs and burial societies found allover the world. Their principal purpose was making small loans with interest for short period.

**GLOBAL HISTORICAL VIEW**

Formal credit and savings institutions for the poor have also been around for decades, providing customers who were traditionally neglected by commercial banks
a way to obtain financial service through cooperatives and development finance institutions.

In the 1800s, various types of larger and more formal savings and credit institutions began to emerge in Europe, organized primarily among the rural and urban poor. These institutions were known as people’s banks, credit unions, and savings and credit co-operatives. The credit union's intrinsic motive was to assist the rural population to break out of their dependence on money lenders and to improve their welfare. From 1870, the unions expanded rapidly over a large sector of the Rhine province and other regions of the German States. The Cooperative movement quickly spread to other countries in Europe and North America, and eventually, supported by the Cooperative Movement in developed countries and donors, also to developing countries.

In 1895, in Indonesia, the Indonesia People's Credit Bank (BPR) or the Bank Perkreditan Rakyat was opened. The BPR became the largest microfinance system in Indonesia with close to 9000 units.

In the early 1990, various adaptations of these models began to appear in the parts of Rural Latin America while the goal of such rural finance interventions was usually defined in terms of modernisation of the agricultural sector, they usually had two specific objectives: (i) Increased commercialisation of the rural sector, by mobilising ‘idle’ savings and increasing investment through credit, and reducing oppressive feudal relations that were enforced through indebtedness. In most cases, these new banks for the poor were not owned by the poor themselves as they had been in Europe, but by government agencies or private banks. Over the years, these institutions became inefficient and at times, abusive.

Between 1950s and 1970s, governments and donors focused on providing
agricultural credit to small and marginal formers, in hopes of raising productivity and incomes at below market interest rates. These subsidised schemes were rarely successful. Rural development banks suffered massive erosion of their capital base due to subsidised lending rates and poor repayment discipline and the funds did not always reach the poor, often ending up concentrated in the hands of better off farmers.

Meanwhile, starting in the 1970s, experimental programmes in Bangladesh, Brazil and few other countries extended tiny loans to groups of poor women to invest in micro-businesses. This type of microenterprise credit was based on solidarity group lending in which every member of a group guaranteed the repayment of all members. These ‘microenterprise lending’ programs had an almost exclusive focus on credit for income generating activities targeting very poor borrowers.

In 1980s the policy of targeted subsidised rural credit has shown a disappointing performance due to especially poor loan recovery, high administrative costs, agricultural development banks insolvency and accrual of a disproportionate share of benefits of subsidised credit to larger farmers. Meanwhile, micro credit programmes throughout the world improved upon the original methodologies and defined conventional wisdom about financing the poor. First, they showed that poor people, especially women, had excellent repayment rates among the better programmes, second, the poor were willing and able to pay interest rates that allowed micro-finance institutions (MFIs) to cover their costs.

In 1990s these two features - high repayment and cost-recovery interest rates - permitted some MFIs to achieve long-term sustainability and reach large numbers of clients.

Another flagship of the Microfinance movement is the village banking unit system of the Bank Rakyat Indonesia (BRI), the largest microfinance institution in
developing countries. This state owned bank served about 23 million micro savers with autonomously managed micro banks in mid-1980s.

The 1990s saw growing enthusiasm for promoting microfinance as a strategy for poverty alleviation. The microfinance sector blossomed in many countries, leading to multiple financial services firms serving the needs of micro entrepreneurs and poor households. These gains however tended to concentrate in urban and densely populated rural area.

In mid-1990s the term ‘microcredit’ began to be replaced by a new term ‘Microfinance’ referring to a range of financial services to the poor, that included not only credit, but also savings and other services such as insurance and money transfers.

Today, the view is increasingly focusing on expanded financial services to the poor and on integration of microfinance in financial systems development, which emphasizes favorable policy environment and institution building, has improved the overall effectiveness of microfinance interventions. This means, reaching Specific Millennium Development Goals (MDGs) in education, women's empowerment and health, the microfinance is an essential element in any country's financial system.

INDIAN HISTORICAL VIEW

The microfinance sector in India has been rapid growth during the last few years. The availability of large market, willingness of banks to lend to microfinance institutions (MFIs) for meeting their priority sector targets as also because they sense a good market has also helped the rapid growth of the microfinance sector. In fact last few years have been very monumental in the growth of the microfinance sector.

According to Prof. Sriram, microfinance in India started in the early 1980's in
forming formal self-help group (SHG) and had grown rapidly in the last two decades\(^1\). The movement started in participation of informal sector, particularly by NGOs. The movement entered the second phase in 1992 with participation of formal sector like commercial banks, cooperative banks and regional rural banks. Thus 1992 can be termed as turning point in the history of microfinance movement in India.

Growth in the microfinance sector in terms of outreach has also meant institutional growth. At least four institutions have crossed milestones of one million client outreach and private equity players are making investments in the burgeoning microfinance sector, which is slowly but surely moving towards achieving the status of a niche industry with in the overall financial sector.

In the beginning of the microfinance movement in India could be traced to the self help groups. Bank Linkage Program (SBLP) started as a pilot project in 1992, by the National Bank for Agricultural and Rural Development (NABARD). This program not only proved to be very successful, but also emerged as the most popular model of microfinance in India. Other approaches like microfinance institutions (MFIs) also emerged subsequently in the country.

Recognising the potential of microfinance to positively influence the development of the poor, the Reserve Bank, NABARD and small industries development bank of India (SIDBI) have taken several initiatives over the years to give a further fillip to the microfinance movement in India.

**IMPORTANCE OF MICROFINANCE IN RURAL DEVELOPMENT**

Microfinance is coming of age but, is it yet to be mainstreamed? To consider this the scholar has made an attempt to look at what is necessary for the sector to

\(^1\)The Journal of Indian Institute of Banking & Finance October - December 2011-P. 54
\(^2\)ibid, July - September 2009. P. 5
achieve this status - to be fully integrated with the Indian financial sector in the economy of India.

In India, nearly two third of the population live in rural areas and most of them are depending on agriculture for survival. As per national sample survey organisation (NSSO) data collected on its 59th round of survey, rural household in India are nearly 148 million of which around 40 million (26% of total rural households) are living in extreme poverty, earning less than Rs. 30 per day. Another 20 million rural households are living at the borderline of poverty. So an aggregate of around 60 million rural households are struggling with the poverty, spreading across the country-situating in different areas of different states. Similarly, in urban areas around 15 million households are in the poverty due to large scale unemployment. Thus, like any other developing country, poverty in rural and urban India is a major threat to economic prosperity.

The structure of rural population in rural India consists of artisans, agricultural labourers and small entrepreneurs besides farmers and cultivators. There is also a migration of people from rural to urban areas and also within and outside India necessitating remittance services. What is required is the provision of all types of financial services to safeguard them from all types of risks besides pension products so there is a need of designed inclusion of rural people within the purview of the formal financial system who remain outside the realm of banking services. The data disclose that in spite of vast banking network comprising of 150000 retail rural outlets 36% rural disadvantaged section has to still depend on informal credit channel viz. money lenders, shopkeepers merchant relative etc. for meeting their credit needs.¹ They find it difficult to access the financial services from the formal financial system.

¹ All India Debt and Investment Survey 1991.
Since the 1950's, various governments in India have experimented with a large number of grant and subsidy based poverty alleviation programmes. The studies show that these mandatory and dedicated subsidised financial programmes, implemented through banking institutions, have not been fully successful in meeting their social and economic objectives. The formal financial institutions have not been able to reach the poor households and particularly women in the unorganized sector. Structural requisites and overheads lead to a high cost of making small loans. The organisational philosophy has not been oriented towards recognising the poor as creditworthy.

In the upliftment of the rural people in India, the microfinance has achieved a remarkable success in reaching finance to the poor and helped them to keep their heads above the water, to catapult them to high brackets of income. Small amounts of finance are enough to help the poor survive but to grow in economic status, larger amounts of finance become critical because of poor governance of MFI, lack of transparency in the nature of transactions and risks underlying them, inadequate human capital leading to poor management, inefficient processes and systems etc.

The non-availability of credit and banking facilities to the poor and under privileged segment of the society has always been a major concern in India. Accordingly, both the Government and Reserve Bank of India have taken several initiatives from time to time such as nationalisation of banks, proscription of priority sector lending norms and concessional interest rate for the weaker sections. It was, however, realised that further direct efforts were required to address the credit needs of poor. In response to this requirement, the microfinance movement started in India with the introduction of SHGs, bank linkage programme (SBLP) in the early 1990s. The Reserve Bank, NABARD and SIDBI have also taken a range of initiatives to provide a momentum to the microfinance movement in India.
The emerging rate of MFIs as institutions other than banks engaged in providing financial services to the poor is being recognised and the banking sector has been extending loans to MFIs for on-lending to SHGs. During the year 2006-07, banks loans amounting to Rs. 1,152 crores were disbursed to 334 MFIs, taking the total loans outstanding to Rs. 1584 crores to 550 MFIs as on March 2007.\(^1\) There are several instances in other years also of SHG that have made a positive impact on income and employment situation of the poor.

**GUIDING PRINCIPLES OF MICROFINANCE**

The field of microfinance is diverse and still evolving. There is no single approach that fits in all the circumstances. The concept of microfinance implies informal and flexible approach to the credit needs of the poor. As such the guiding principles have been tailored according to the circumstances and the local needs. In this heading an attempt has been made to trace out the guiding principles evolved in India.

Several initiatives have been taken by the Reserve Bank, NABARD and also SIDBI with a view to giving further fillip to the microfinance movement in India. These are as follows.

1. In January 1993, SHGs, registered or unregistered were allowed to open savings bank account with banks.

2. In 1994 the Reserve Bank constituted a 'working group on NGOs and SHGs. Banks that were financing to SHGs should be included by them as part of their lending to weaker sections and that SHG lending, should be reviewed at the state level bankers committee (SLBC) level and by the banks at regular

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\(^1\)The Journal of Indian Institute of Banking and Finance July-September 2009, P. 61.
intervals.

3. In 1998, the banks were advised by RBI that SHGs which were engaged in promoting the savings habit among their members would be eligible to open saving bank accounts and such SHGs need not necessarily have availed of credit facilities from banks before opening saving bank accounts.

4. Subsequent to monitory and credit policy announcement for the year 1999-2000, the banks were also advised that interest rates applicable to loans given by banks to micro-credit organisations or by the microcredit organisations to SHGs/member beneficiaries would be left to their discretion.

5. The Reserve Bank as a member of Task Force looked into the entire gamut of issues related to microfinance, particularly regulatory framework issues.

6. Recognising the growing importance of microfinance, the Reserve Bank constituted a micro-credit special cell in the bank in 1999 to suggest measures for mainstreaming micro credit and accelerating flow of credit of MFIs.

7. Several non-banking finance companies (NBFCs) and Residuary non banking companies (RNBCs) also started entering the micro finance sector in January 2000, were advised by RBI that those who were engaged in micro financial activities, licensed under section 25 of companies Act, 1956 and which were not accepting public deposits were exempted from the purview of section 45-1A (registration), 45-1B (Maintenance of liquid assets) and 45-1C (Transfer of a position of profit to reserve fund) of the Reserve Bank of India Act, 1934.

8. In February, 2000, the Reserve Bank issued comprehensive guidelines to banks for mainstreaming micro-credit and enhancing the outreach of micro credit providers. These guidelines inter alia, stipulated that micro credit
extended by banks to individual borrowers directly, or through any intermediary, would from them onwards be reckoned as part of their priority sector lending. Banks were given freedom to formulate their own models or choose any intermediary for extending micro credit. Banks were also permitted to prescribe their own lending norms so as to provide maximum flexibility with regard to micro lending. Such credit was to cover not only consumption and production loans for various farm and non-farm activities of the poor, but also include their other credit needs. Banks were asked to delegate adequate sanctioning powers to branch managers and to keep the loan procedures and documents simple for providing prompt and hassle free micro credit.

9. It was announced in the Annual Policy Statement for the year 2004-05 that in view of the need to protect the interest of depositors, MFIs would not be permitted to accept public deposits unless they complied with the extant regulatory framework of Reserve Bank.

10. Banks were permitted in January, 2006, to use the services of NGOs / SHGs, MFIs (other than NBFCs) and other civil society organisations as intermediaries in providing financial and banking services through business facilitators.

11. In 2008-09 the Union Budget of the RBI instructed the Banks to meet the entire credit requirements of self-help group members.

12. NABARD, recently undertaken a thorough assessment of SHGs bank linkage program and issued revised guiding principles in March 2012 on the SHG Bank Linkage Program(SHG 2) to all schedule commercial banks and
Regional Rural Banks in SHG 2, NABARD has made the following changes in the product design:

(i) Allowing voluntary savings

(ii) Purpose of bank loans i.e. income generation, housing, education, marriage etc.

(iii) Cash credit / overdraft facility for SHGs.

(iv) Enabling joint liability group (JLGs) within SHGs.

(v) Improving risk mitigation system

(vi) Building second tier institution

(vii) Strengthening the monitoring mechanism

(viii) Addressing training requirements

MICRO FINANCE IN INDIAN PERSPECTIVE

EMERGENCE

According to the planning commission of India around 40,000 crores have been spent on Poverty Alleviation Programmes (PAPs). However, a large section of Indian population is still living below poverty line. Poverty has multi dimensional effects i.e. low income, illiteracy, ill health, gender inequality and degradation of environment. Poverty means denial of access to the basic necessities i.e. food, shelter, health, education of human existence. Poverty is characterized by lower standard of living. Basically, poverty is the effect of lack of income and access to credit. As most of the poor people are deprived of access to basic financial services and increasing their access to these services, particularly credit, has been the prime responsibility of all the states since the early years of the country's independence.
One of the major steps in this direction was the review of the cooperative structure undertaken in the mid 1950s, following the report of the All India Rural credit survey, which suggested that the state should partner the cooperatives. The decade of the 1960s also continued to focus on institutional credit source including cooperatives. The decade of the 1970s was marked by directed lending following the nationalization of banks in 1969 and the introduction of the lead bank scheme. Since the early 1990s, there have been many significant state initiatives in the institutional and policy spheres to facilitate access to financial services by more poverty stricken groups. Growth in the micro finance sector in terms of outreach has also meant institutional growth. Private equity players are making investment in the burgeoning microfinance sector. Microfinance sector continues to have a disproportionate presence in the South of the country with MFIs in AP, Tamil Nadu and Karnataka accounting for 52 per cent of the clients and 59 per cent of the outstanding loans.

PROSPECTS

Although there have been a spectacular growth in providing banking services to the masses. However, there are certain under banked states, such as Bihar, Orissa, Rajasthan, Uttar Pradesh, Chattisgarh, Jharkhand, West Bengal and a large number of North-Eastern states, where the average population per branch office continues to be quite high compared to the national average, particularly in rural areas.

The fact that bank expansion has been skewed becomes apparent when we consider deposits of scheduled commercial banks and bank credit as a proportion of Net State Domestic Product (NSDP) at current prices. For instance, the percentage of bank deposits is pretty high in Bihar and Jharkhand so these states are not as under banked as they are thought to be. While it is well known that the Northeastern states are under banked, states such as Andhra Pradesh, Haryana and Rajasthan, too, have a
low bank credit-deposit ratio. In contrast to this scenario, banks have already tapped most of the potential states such as Punjab and Maharashtra as far as bank deposits are concerned.

Hilly states, such as Sikkim, Himachal Pradesh and even Arunachal Pradesh have a surprisingly high proportion of bank deposits compared to Net state domestic product.

Due to the nature of the expansion of banking services in the country and constraints on banking entities, microfinance activities of banks and SHGs need to be grown to new heights. Furthermore, correcting the problem of access is best done by expanding the number of financial institutions available to people as well as the capacity of those institutions. Despite vast network of bank branches only 27 percent of the total farm households have access to bank finance and there continues to be wide gap in the availability of banking services in rural areas as the schedule commercial banks covered only 18.4 per cent of the rural population in deposit accounts and 17.2 per cent by way of loan account. The basic reasons for rural poor servicing excluded from banking system were (1) High transaction cost at client level. (2) Cumbersome documentation and procedures at the formal sector (3) Lack of awareness (4) Small size loan (5) Availability of door step services from informal sector and (6) Indifference of formal banking system.

The 1980s saw the emergence of self help group (SHGs) in India. SHGs are small, economically homogenous affinity groups of rural poor (10-20 members each), voluntarily formed to save and mutually contribute to a common fund to be lent to its members as per the group member’s decision. The SHGs can, therefore be called member-run mini banks. The SHG Bank Linkage Programme (SBLP) was an outcome of pilot projects during the 1980s for improving access of India's rural poor
to formal institutional financial services. For banks it was a way of reducing their transaction costs by dealing with groups of people rather than individuals and reducing their risks through 'peer pressure' and making people save. Recognizing the potential of micro-finance to positively influence the development of the poor, the Reserve Bank, NABARD and SIDBI have taken several initiatives over the years to give a further fillip to the microfinance movement in India. Reserve Bank of India through NABARD (The National Bank for Agriculture and Rural Development), introduced a Pilot Project in 1992, for extending microcredit to the rural poor by linking about 500 Self Help Groups (SHGs) with commercial banks, cooperative banks and Regional Rural Banks across the country. This project played a key role in initiating the unique SBLP model as a cost effective mechanism for providing financial services to our country's unreached and underserved poor. In Union Budget of 1999, the Govt. of India accorded national priority to SHG movement and in 2011, announced a proposal to create a women's SHGs Development Fund with a corpus of INR 500 million to empower women and promote their SHGs\(^1\).

Viewing the success of NABARD's Pilot project initiated in 1992, RBI advised the banks to consider lending to SHGs as part of their regular credit operations both at policy and implementation levels. They were also advised to include SHG linkage in their corporate strategy/plan, training curriculum of their officers and staff, implement it as a regular business activity and review it periodically.

In India, at present, a little over 80 percent of the SHGs linked to banks are exclusive women groups, a distinguishing feature of the microfinance sector in India. Over the past two decades, the SHGs have empowered rural women especially, in

\(^1\)The Indian Banker Vol. VII No. 7, July 2012, P. 23
South India. SHG banking which started in 1992, has already resulted in setting up of about 7.5 million Self Help Groups so far and more than ninety million households have been linked to banks.

**LAUNCH OF SHG 2**

In the process of expanding the coverage of microfinance in the past two decades, NABARD, recently undertook a thorough assessment of SHG Bank linkage programme and issued revised instructions in March 2012 on the SHG Bank Linkage Programme (SHG 2) to all schedule commercial banks and regional rural banks. These new instructions are aimed at giving the bank linkage programme the much needed thrust and re-investigating the SHG movement in the country.

**STRUCTURE OF MICROFINANCE IN INDIA**

Currently in India, players in the microfinance sector can be classified as following in two major groups.

a) SHG Bank Linkage model accounting for about 58 per cent of the outstanding portfolio.

b) MFIs accounting for the rest of the 42 per cent of the outstanding portfolio.

**MICROFINANCE INSTITUTIONS - AN INTRODUCTION**

Microfinance Institutions (MFIs) in India exist in a variety of forms like trust registered under the Indian Trust Act 1882, Public Trust Act 1920; Societies registered under the Societies Registration Act 1860; Cooperatives registered under the Mutually Aided Cooperative Societies Act of the States and non-banking Financial Companies (NBFC)-MFIs, which are registered under Section 25 of the Companies Act 1956 or NBFC registered with the Reserve Bank of India. These
MFIs are scattered across the country and due to the multiplicity of registering authorities, there is no reliable estimate of the number of MFIs. The most frequently used estimate is that there number is likely to be around 800.

Banks can use MFIs as their agent for handling credit, monitoring, supervision and recovery. The bank is a lender and MFI acts as an agent for handling work relating to credit monitoring, supervision and recovery, while the borrower is the individual. The MFI acts as an agent, it takes care of all relationships with client, from first contact to final payment. Sometimes, NBFC holds the individual loans in its books before securitising them and selling them to bank. Such refinancing through securitisation provides a greater funding access to MFIs.

In January 2006, the Reserve Bank permitted banks to utilise the services of NGOs, MFIs (other than NBFCs) and other Civil Society Oranisations as intermediaries in providing financial and banking services through the use of business facilitator and business correspondent. This allows banks to do ‘Cash in-cash out’ transactions at a location much closer to the rural population. In 2008-09, the Union Minister permitted to engage retired bank employees, ex-serviceman and retired government employees as business correspondents (BCs) with effect from April 24, 2008.

NABARD has been playing a crucial developmental role for the microfinance sector in India. NABARD has been organising/sponsoring training programmes and exposure visits for benefit of bank officials, NGOs, SHGs and government agencies to enhance their effectiveness in the field of microfinance. NABARD also provides support for capacity building, exposure and awareness building of SHGs and NGOs. In addition, NABARD also provides promotional grant support to NGOs, RRBs, DCCBs, farmers Clubs and individual volunteers and assists in developing capacity
building of various partner agencies. NABARD has been making efforts to increase the number of partner institution as self-help promoting institutions.

SIDBI was one of the first institutions that identified and recognised NGO/MFI route as an effective delivery channel for reaching financial services to those segments of the population not reached by the formal banking network. As a result of bulk lending funds provided, coupled with the intensive capacity building support to the entire microfinance sector, it has come to occupy a significant position in the Indian microfinance sector. Today, SIDBI is one of the largest providers of microfinance through the MFIs.