Micro finance sector in India at the cross roads: What does it hold for rural women?

Micro finance movement is at the critical juncture of its evolution as the government steps in to regulate the sector through legislation…..

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The times have not been benevolent for the industry, after the 2010 implosion of the micro finance (MF) sector in India. Its blazing growth was reversed after the Andhra Pradesh 'crises', highlighting various issues and problems that stump heightened public perceptions of MF as a force for good that shall alleviate poverty and empower women. Fitting would be to say that the episode was catastrophic for the sector, though it has not been its death knell.

It was in this somber mood that several representatives and stakeholders at the ISST-HBS (The Institute of Social Studies Trust in association with the Heinrich Böll Foundation) organized Gender and Economic Policy Discussion Forum [1]congregated. The objective was to contribute to the ongoing re-thinking process that builds a climate of responsible, ethical micro finance, viable for the industry and bettering the lives of the people linked to micro-credit. A fierce, frank discussion identifying some of the fault lines in the system unfolded. After providing some background on the crisis of the micro finance sector, this article summarizes the highlights of this meeting held on the 28th of March, 2012.

After media came down heavily with reports of unscrupulous, aggressively profit-seeking micro-finance organizations in Andra Pradesh 2 years ago, there has been a nationwide backlash, and the MF industry has ever since been spiraling downwards. While the question whether the sector will boom anytime soon is uncertain, uncontested is the revolutionary impact of the social enterprise model of MF on the lives of rural women.

The role of women in the micro finance has best been illustrated by the Noble laureate and founder of Bangladesh based Grameen Bank, Professor Muhammad Yunus, who says "give a man a fish and he eats for a day. Teach a man to fish and he eats for the rest of his life. However, if we teach a woman even a little about financial planning and provide her a loan to purchase a fishing rod, not only does she eat for the rest of her life, but help others in getting credits through interest paid by woman like her on the loan".

From the several decades of experience of the Grameen Bank, which Yunus had founded, it became apparent that women were most likely to repay their loans (a repayment rate of 95%) in comparison to their male counterparts. Though Grameen Bank initially extended credit to both men and women at equal rates, women at present constitute more than 90% of the bank's clients, as they have better credit rating. Globally, women constitute close to 70% of all micro credit recipients.

State of micro finance in India

Micro finance activities in India started in the early 1980s with small efforts at forming informal self-help groups (SHG) of 10-20 people, usually women coming together to pool financial resources and making small interest bearing loans to their members. From this small beginning, the microfinance sector has grown significantly in the past decades with pronounced emergence in southern parts of India particularly in the state of Andhra Pradesh. After witnessing steady growth, during 2005-2010, amidst reports of use of coercive re-collection practices and usurious interest rates in Andhra Pradesh, there is had been decline in the growth of business for MFI (Micro Finance Institutions). The MFIs are not able to collect their dues as the Andhra Pradesh MFI (Regulation of Money Lending) Act, 2010 restricts their operations-banning repayment of micro loans.

The stringent Andhra Pradesh Act has virtually put Rs 6000 crore ($ 1.2 billion) credit recovery on hold by MFIs resulting in problem of liquidity. An estimated 9 million households in Andhra Pradesh have been adversely affected as access to finance has dried up in the southern Indian state. The estimated size of MFI in India has shrunk to around Rs 10,000 crore from Rs 30,000 crore two years back. Meanwhile, the Micro Finance Institutions (Development and Regulation) Bill 2011 has been cleared by the Union Cabinet prior to its introduction in the parliament. The Bill (which will now go through parliamentary scrutiny) seeks to bring *all* MFIs under India's Central Bank, the Reserve Bank of India (RBI). The Bill is based on the recommendations of the Report of the Sub-Committee of Central Board of Directors (also known as the Malegam Committee Report) set up in Oct 2010.

Niche role for both self help groups and MFIs

A milestone in the SHG movement was in 1992, when the Self Help Groups-Bank partnership model was initiated by the National Bank for Agriculture and Rural Development (NABARD). Under this model, SHGs were provided with bank loans generally for income generation purpose. Soon afterwards the RBI recommended to other commercial banks to consider lending to SHGs as part of their rural credit operations, thus creating the SHG-Bank Linkage. This model has spread multi-fold and improved livelihoods across rural India. Many of the social security schemes sported by the government are presently being run by SHGs across India. Again, women have been the largest beneficiaries of the MF movement. They form 85% of the SHGs in the country and have deposited 75.5% of all SHG savings with the banks.

The focus of concern leading up to the Andhra Pradesh micro-finance crises has been the commercialized Non-Banking Finance Companies (NBFCs) operating as MFIs, which act as intermediary between the women borrower's at the local level and the commercial banks. There are numerous kinds of entities working in the micro finance sector, such as those that come under the section 25 of the Company Act, but also Trusts, Societies, local banks and Co-operatives. However, the recent debate around MF is dominated by a focus on the for-profit entities. These MFI's grew in significance since the late eighties and first half of nineties. The significance of for-profit, micro-finance sector NBFCs in India has to be underscored by their contribution to the Government's agenda of financial inclusion, by making available credit to the un-banked segments of rural society. However, NBFCs have met flak for being driven by high- profit seeking business model, short term loans, driven by private capital, investment funds and integration into global market based mechanisms of capital accumulation.

MFI-SHG linkage: a complementary role?

India' Rural Development Minister Jairam Ramesh sees SHGs and MFI not as competitive but complementary institutions. MFI's have the core competency in providing quick credit, have the capability to model product based on local needs and by having multiple products for diverse geographical spread, they could expand coverage. Bank-linked SHGs provide institutional support to the livelihood strategies of the poor, minimize risks related to irregular cash flows, and have taken on functions beyond borrowing with a long term perspective. It would be desirable to create an environment of convergence in the functioning of the two institutions of SHGs and MFIs. He however stressed "the need for effective supervision to build a more sound regulatory apparatus for the MFIs."
Ramesh further added that the government has taken on the task of expansion of the bank-linked SHG movement. It is going for enrolment of around seven crore women with a view to enabling one women of every BPL household to be associated to bank-linked SHGs.

Women's need for diverse product development

One of the key challenge faced by MFI in India is to design products specifically for women which cater to their need to expand business opportunities. Vijayalakshmi Das, Managing Director and Promoter Director of Ananya Finance for Inclusive Growth (P) Limited, criticized MFIs who 'started off as facilitators but they are now increasingly getting directly involved, leading to reduced participation of the women borrowers in deciding the kind of financial services and products they need'. She emanded flexibility in the design approach that relates to the women's ground realities and invests in knowledge and skills, in order to create self-controlled social capital around borrowing, which is imperative to the sustenance of livelihoods.

Although Das acknowledged that MF has given women greater bargaining power in the households and elevated their status within the family, it would be wrong to assume that MF alone is responsible for empowering women. Gender mainstreaming is beyond providing financial services or banking alone; such an attempt demands synergy of a lot of players from the development sector. Social policies and developmental programmes must support the borrowers self efforts through micro-financing towards coping and moving out of poverty. There is an increasing discussion on a process that would enable women to move up the value chain with the support of MF and State development programmes, given that MF services integrate into the wider development process.

Vijay Mahajan, CEO and Chairman of BASIX Group, a key stake holder in the micro-finance sector, also stressed the need for customization of loan products to empower women. Mahajan expressed concern over the poor availability of credit service and inappropriate design of loan products. . Mahajan critiqued the MF sector for its non-responsive attitude to the plight of the low-income earning credit borrowers. Agriculture, animal husbandry, handicraft industry, small trading and local services are the five economic activities most widely practiced by rural women in IndiaMahajan criticized the common practice of short term lending in microfinance. To insist on weekly or monthly repayments of loans is out of synergy with the processes and time period taken for 'ready product' in activities for example like agriculture and animal husbandry that have a longer product cycle. The borrower would possibly in a position of repayment when returns from the 'ready product' start to come. Hence, here is a mismatch in cash flow and micro-credit cycle, pointing to the need to tailor MF products to better suit the economic activity of the clients.

There is an urgent need to make available long term credit, to enable petty traders comprising mostly of women, to move out of the vicious poverty cycle of debt and low income. This must be incorporated as an option in the range of micro-credit loan option. "Availability of credit alone does not promote livelihood, and if our interest is in ensuring women to have steadier income streams with low risk and high returns, then the MFI has to go beyond the world of mere finance to a more development sector approach," Mahajan said.

MFIs: Need for stricter compliance with the objective of stimulating rural-upliftment through credit expansion

While stating that micro finance sector is in 'doldrums', Mathew Titus, Executive Director of Sa-Dhan, an Association of Community Development Finance Institutions, also urged for recognizing the contributions of the MF sector in increasing credit access and flow to the marginalized.

On the issue of rising non-performing assets (NPA) in the micro finance sector, Titus highlighted that 48% of the NPAs are from the priority sector [2], even though the sector accounts for 31% of the bank advances. He pointed out that "As the bad loans or defaults kept rising, it would be expected that at some point the RBI will step-in, regardless of the origins of the NPAs."

Reflecting similar view, deputy governor of RBI, Anand Sinha, also stated that the need for Central Bank regulation arose only because of the failure of MF sector's self-regulation. Currently only NBFCs are subject to prudential regulation (including a minimum capital requirement, capital adequacy requirement and foreign investment restrictions). There is very little regulation (no regulator) for NGO-MFIs, co-operatives and Section 25 Companies, other than registration. Even for NBFCs, as there are many kinds, there is no specific regulation relating to Micro finance institutions operating as NBFC.

"RBI's aim in regulating the MFIs is to ensure sustained financial stability to the crisis-hit sector. These regulations by definition will be restrictive in nature. While the geographical spread of the MF sector makes microscopic supervision of the sector a difficult task for RBI, regulation of the sector is most crucial to bring stability in the present MF sector environment," Sinha observed. Besides, the government needs to act on the Malegam committee's recommendation which include creation of a separate category of Non-Banking Finance Companies (NBFCs) operating in the microfinance sector to be designated as NBFC-MFIs with the intent of determining which institutions qualify for priority sector lending.

Sinha also supported the need for a strong credit information bureau. The availability of credit-information will help not only MFIs but will strengthen the financial system as a whole. Without individual identity it has been very difficult for credit-information companies to function. However, with the coming of Aadhaar/Unique Identification Number Card (taken through biometrics data) the problems of irregularities and documentation of individual's identity information will be resolved.

Based on the dialogue, Institute of Social Studies Trust has developed the following recommendations for broader dissemination:

- Need to customize loan products that will suit the need and time required for repayment by the borrower.
- Need to go beyond the world of finance to other aspects of development in order promote overall well-being through sustainable livelihood of borrowers.
- Need to build supportive systems such as IT, UID for smooth functioning and expansion of micro-finance services in the country.
- Need to urgently address the issue of increasing number of NPAs in both MFIs and SHGs.
- Need to implement the Malegam Committee regulatory guidelines in order to restore credibility to the MF sector.
- Need to allow alternate models of delivery to achieve the aim of financial inclusion.
- Need to recognize that MFI-SHG models are complementary to each other.
- Given the high degree of participation by women's in SHGs, there is a need to make SHGs self-sustaining.

[1] The Gender and Economic Policy Discussion Forums are envisaged as regularly held platforms that facilitate quality reflection and debate, with a perspective of shifting public discourse, around selected key economic policy issues in the direction of gender sensitivity.

[2] Priority sector lending is a government initiative to allocate a percentage of their portfolios to investment in specified priority sectors at reduced interest rate. Currently only micro-finance institutions registered as NBFC-MFI are designated as priority sector