Research Paper
Peer Reviewed Journal

ISSN-2455-0736 (Print)
ISSN-2456-4052 (Online)

MICROFINANCE AND FINANCIAL INCLUSION

Merin Jose

Assistant Professor, Department Of Commerce, Pavanatma College, Murickassery.

Merijosekj@Gmail.Com

ABSTRACT

Microfinance is the provision of thrift among people living in rural areas. They were kept out of the official banking network of the nation. They are not able to provide adequate collateral to banks and financial institutions. Rural people have rich knowledge and skill, but that remains unutilized. They need financial and other support for a better life. Microfinance helps these people by providing adequate assistance in various forms. Microfinance has a crucial role to play in a country like India. In India majority of the people are living in rural areas. They are deprived of many facilities and advantages that are being enjoyed by urban people. Financial inclusion is a new innovation in the financial sector. It aims at providing banking facilities to each and every person in the country. Its objective is to remove unbanked areas in the country. Bringing every people in the formal banking system will foster the economic growth of a nation. Financial inclusion is an initiative of RBI on the recommendation of central government.

Key Words: Microfinance, financial inclusion, economic growth, banking network, financial institutions

MICROFINANCE

Over the past centuries, practical visionaries, from the Franciscan monks who founded the community-oriented pawnshops of the 15th century to the founders of the European credit union movement in the 19th century and the founders of the microcredit movement in the 1970s, have tested practices and built institutions designed to bring the kinds of opportunities and risk-management tools that financial services can provide to the doorsteps of poor people. While the success of the Grameen Bank has inspired the world, it has proved difficult to replicate this success. In nations with lower population densities, meeting the operating costs of a retail branch by serving nearby customers has proven considerably more challenging. Hans Dieter Seibel, board member of the European Microfinance Platform, is in favour of the group model. This particular model (used by many Microfinance institutions) makes financial sense, he says, because it reduces transaction costs. Microfinance programmes also need to be based on local funds. The history of microfinancing can be traced back as far as the middle of the 1800s, when the theorist Lysander Spooner was writing about the benefits of small credits to entrepreneurs and farmers as a way of getting the people out of poverty. Friedrich Wilhelm Raiffeisen founded the first cooperative lending banks to support farmers in rural Germany.The modern use of the expression "micro financing" has roots in the 1970s when organizations, such as Grameen Bank of Bangladesh with the microfinance pioneer Muhammad Yunus, were starting and shaping the modern industry of micro financing.

ISSN-2455-0736 (Print)
ISSN-2456-4052 (Online)

PRINCIPLES

1. Poor people need not just loans but also savings, insurance and money transfer services.
2. Microfinance must be useful to poor households: helping them raise income, build up assets and/or cushion themselves against external shocks.
3. "Microfinance can pay for itself."[1] Subsidies from donors and government are scarce and uncertain and so, to reach large numbers of poor people, microfinance must pay for itself.
4. Microfinance means building permanent local institutions.
5. Microfinance also means integrating the financial needs of poor people into a country's mainstream financial system.
6. "The job of government is to enable financial services, not to provide them."
7. "Donor funds should complement private capital, not compete with it."
8. "The key bottleneck is the shortage of strong institutions and managers." Donors should focus on capacity building.
9. Interest rate ceilings hurt poor people by preventing microfinance institutions from covering their costs, which chokes off the supply of credit.
10. Microfinance institutions should measure and disclose their performance—both financially and socially.

Microfinance is considered a tool for socio-economic development, and can be clearly distinguished from charity. Families who are destitute, or so poor they are unlikely to be able to generate the cash flow required to repay a loan, should be recipients of charity. Others are best served by financial institutions.

MICROFINANCE IN INDIA

Muhammad Yunus, a Nobel Prize winner, introduced the concept of Microfinance in Bangladesh in the form of the "Grameen Bank". The National Bank for Agriculture and Rural Development (NABARD) took this idea and started the concept of microfinance in India. Under this mechanism, there exists a link between SHGs (Self-help groups), NGOs and banks. SHGs are formed and nurtured by NGOs and only after accomplishing a certain level of maturity in terms of their internal thrift and credit operations are they entitled to seek credit from the banks. There is an involvement from the concerned NGO before and even after the SHG-Bank linkage. The SHG-Bank linkage programme, which has been in place since 1992 in India, has provided about 22.4 lakh for SHG finance by 2006. It involves commercial banks, regional rural banks (RRBs) and cooperative banks in its operations.

Microfinance is defined as, financial services such as savings accounts, insurance funds and credit provided to poor and low income clients so as to help them increase their income, thereby improving their standard of living. The main features of microfinance are:

- Loan given without security
- Loans to those people who live below the poverty line

ISSN-2455-0736 (Print)
ISSN-2456-4052 (Online)

- Members of SHGs may benefit from micro finance
- Maximum limit of loan under micro finance Rs25,000/-
- Terms and conditions offered to poor people are decided by NGOs
- Microfinance is different from Microcredit- under the latter, small loans are given to the borrower but under microfinance alongside many other financial services including savings accounts and insurance. Therefore, microfinance has a wider concept than microcredit.

FINANCIAL INCLUSION

Financial inclusion or inclusive financing is the delivery of financial services at affordable costs to sections of disadvantaged and low-income segments of society. An estimated 2 billion working-age adults globally have no access to the types of formal financial services delivered by regulated financial institutions. It is argued that as banking services are in the nature of a public good, the availability of banking and payment services to the entire population without discrimination is a key objective of financial inclusion.

The term "financial inclusion" has gained importance since the early 2000s, a result of findings about financial exclusion and its direct correlation to poverty. The United Nations defines the goals of financial inclusion as follows:

- access at a reasonable cost for all households to a full range of financial services, including savings or deposit services, payment and transfer services, credit and insurance;
- sound and safe institutions governed by clear regulation and industry performance standards;
- financial and institutional sustainability, to ensure continuity and certainty of investment; and
- competition to ensure choice and affordability for clients.

In the Indian context, the term 'financial inclusion' was used for the first time in April 2005 in the Annual Policy Statement presented by Y.Venugopal Reddy,the then Governor,Reserve Bank of India. Later on, this concept gained ground and came to be widely used in India and abroad. While recognizing the concerns in regard to the banking practices that tend to exclude rather than attract vast sections of population, banks were urged to review their existing practices to align them with the objective of financial inclusion. Norms were relaxed for people intending to open accounts with annual deposits of less than Rs. 50,000. General credit cards (GCCs) were issued to the poor and the disadvantaged with a view to help them access easy credit. In January 2006, the Reserve Bank permitted commercial banks to make use of the services of non-governmental organizations (NGOs/SHGs), micro-finance institutions, and other civil society organizations as intermediaries for providing financial and banking services. These intermediaries could be used as business facilitators or business correspondents by commercial banks. The bank asked the commercial banks in different regions to start a 100% financial inclusion campaign on a pilot basis. As a result of the

ISSN-2455-0736 (Print)
ISSN-2456-4052 (Online)

campaign, states or union territories like Puducherry, Himachal Pradesh and Kerala announced 100% financial inclusion in all their districts. Reserve Bank of India's vision for 2020 is to open nearly 600 million new customers' accounts and service them through a variety of channels by leveraging on IT. Illiteracy and the low income savings and lack of bank branches in rural areas continue to be a roadblock to financial inclusion in many states and there is inadequate legal and financial structure.

The government of India recently announced "Pradhan Mantri Jan Dhan Yojna,[a national financial inclusion mission which aims to provide bank accounts to at least 75 million people by January 26, 2015. To achieve this milestone, it's important for both service providers and policy makers to have readily available information outlining gaps in access and interactive tools that help better understand the context at the district level.In India, RBI has initiated several measures to achieve greater financial inclusion, such as facilitating no-frills accounts and GCCs for small deposits and credit. Some of these steps are:

Opening of no-frills accounts: Basic banking no-frills account is with nil or very low minimum balance as well as charges that make such accounts accessible to vast sections of the population. Banks have been advised to provide small overdrafts in such accounts.

Relaxation on know-your-customer (KYC) norms: KYC requirements for opening bank accounts were relaxed for small accounts in August 2005. The banks were also permitted to take any evidence as to the identity and address of the customer to their satisfaction. It has now been further relaxed to include the letters issued by the Unique Identification Authority of India containing details of name, address and Aadhaar number.

Engaging business correspondents (BCs): In January 2006, RBI permitted banks to engage business facilitators (BFs) and BCs as intermediaries for providing financial and banking services. The BC model allows banks to provide doorstep delivery of services, especially cash in-cash out transactions, thus addressing the last-mile problem. The list of eligible individuals and entities that can be engaged as BCs is being widened from time to time. With effect from September 2010, for-profit companies have also been allowed to be engaged as BCs.In the grass-root level, the Business correspondents (BCs), with the help of Village Panchayat (local governing body), has set up an ecosystem of Common Service Centres (CSC). CSC is a rural electronic hub with a computer connected to the internet that provides e-governance or business services to rural citizens.

Use of technology: Recognizing that technology has the potential to address the issues of outreach and credit delivery in rural and remote areas in a viable manner,banks have been advised to make effective use of information and communications technology (ICT), to provide doorstep banking services through the BC model where the accounts can be operated by even illiterate customers by using biometrics, thus ensuring the security of transactions and enhancing confidence in the banking system.

Adoption of EBT: Banks have been advised to implement EBT by leveraging ICT-based banking through BCs to transfer social benefits electronically to the bank account of the beneficiary and deliver government benefits to the doorstep of the beneficiary, thus reducing dependence on cash and lowering transaction costs.

GCC: With a view to helping the poor and the disadvantaged with access to easy credit, banks have been asked to consider introduction of a general purpose credit card facility up to

ISSN-2455-0736 (Print)
ISSN-2456-4052 (Online)

`25,000 at their rural and semi-urban branches. The objective of the scheme is to provide hassle-free credit to banks' customers based on the assessment of cash flow without insistence on security, purpose or end use of the credit. This is in the nature of revolving credit entitling the holder to withdraw up to the limit sanctioned.

Simplified branch authorization: To address the issue of uneven spread of bank branches, in December 2009, domestic scheduled commercial banks were permitted to freely open branches in tier III to tier VI centres with a population of less than 50,000 under general permission, subject to reporting. In the north-eastern states and Sikkim, domestic scheduled commercial banks can now open branches in rural, semi-urban and urban centres without the need to take permission from RBI in each case, subject to reporting.

Opening of branches in unbanked rural centres: To further step up the opening of branches in rural areas so as to improve banking penetration and financial inclusion rapidly, the need for the opening of more bricks and mortar branches, besides the use of BCs, was felt. Accordingly, banks have been mandated in the April monetary policy statement to allocate at least 25% of the total number of branches to be opened during a year to unbanked rural centres.

Microcredit and financial inclusion has played a role in changing the standard of living of people of rural areas. It has opened more avenues of growth for them. It has a big role in countries like India where majority of the population are living in rural areas. Financial assistance which is a key component in both microfinance and financial inclusion will help to remove poverty from the rural areas to a certain extent. It is like a big bang theory in the financial sector. It will also help in removing social imbalances in the society.

References and Citation

1. George Ajimon, Modern Banking, Prakash Publications, 2015
2. http://financialservices.gov.in/banking/financialinclusion.asp
3. http://www.in.undp.org/content/dam/india/docs/promoting_financial_inclusion_can_the_constraints_of_political_economy_be_overcome.pdf
4. http://www.thebanker.com/content/search?SearchText=microfinance
5. http://www.cfapubs.org/loi/faj