BUSINESS MODELS OF MICROFINANCE COMPANIES: A STRATEGIC ANALYSIS

Sunildro L.S. Akoijam
Research Scholar in Manipur Institute of Management Studies (MIMS), Manipur University (A Central University), Imphal – 795003, India.

Dr. Ch. Ibohal Meitei
Associate Professor in Manipur Institute of Management Studies (MIMS), Manipur University (A Central University), Imphal – 795003, India.

Abstract

In recent times, microfinance has emerged as a major innovation in the rural financial marketplace. Microfinance largely addresses the issue of access to financial services. In trying to understand the innovation of microfinance and how it has proved to be effective, one has to look at certain design features of microfinance. The thing that is of great importance here is to see how various models are being used to bridge the gap between the need for financial services across time, geographies, and risk profiles.

In providing services that bridge this gap, formal institutions have limited access to authentic information both in terms of transaction history and expected behavior and, therefore, resort to seeking excessive information thereby adding to the transaction costs. This paper has attempted to analyse the various microfinance models being used by MFIs in India and also suggest some measures to improve the drawbacks of various models. It has also attempted to analyse the various challenges and prospects of microfinance in the Indian scenario.

Keywords: Business, microfinance, poverty, financial service, intermediaries and strategy.
1. Introduction: In today’s scenario, Microfinance becomes an important term for the inclusive economic growth. It can be defined as the supply of loans, savings, and other basic financial services to the poor. People living in poverty, like everyone else, need a diverse range of financial instruments to run their businesses, build assets, stabilize consumption, and shield themselves against risks. Financial services needed by the poor include working capital loans; consumer credit, savings, pensions, insurance, and money transfer services.

At the core of microfinance is a fundamental belief that access to financial services empowers the poor by reducing their vulnerability and giving them choices. Whether they save or borrow, evidence around the world shows that when poor people have access to financial services, they choose to invest these savings or loans into building a range of assets that will make them less vulnerable. Such assets can be sending their children to school, buying medicines and more nutritious food, fixing a leaky roof, or building income-earning potential by investing in their own enterprises. In essence, access to financial services enables poor people to build their own way out of poverty.

Today, the microfinance industry and the greater development community share the view that permanent poverty reduction requires addressing the multiple dimensions of poverty. For the international community, this means reaching specific issues as education, women's empowerment, and health, among others. For microfinance, this means viewing microfinance as an essential element in any country's financial system.

This study has been specifically prepared in order to an in-depth insight of Microfinance and its impact on the poor people in real terms. Efforts have also been made to study the regulations and various models as concerned with Microfinance.

2. Review of Literature:

Berenbach and Guzman (1994), states that solidarity groups have proved effective in deterring defaults as evidenced by loan repayment rates attained by organisations such as the Grameen Bank, who use this type of microfinance model. They also highlight the fact that this model has contributed to broader social benefits because of the mutual trust arrangement at the heart of the group guarantee system.

Holt (1994), defined Village banks as community-managed credit and savings associations established by NGOs to provide access to financial services, build community self-help groups, and help members accumulate savings.

Mohammed Yunus (1996) states that the Grameen model emerged from the poor-focused grassroots institution, Grameen Bank. It is one of the most successful model adopted worldwide by various MFIs.

Fernandez (1998), states that the formation of SHGs for savings and credit, and their linkage to commercial banks, was initiated in India by MYRADA in the mid-1980s.

Grameen Bank (1999) highlighted that the financial performance of the institutions which use the Grameen system is well documented. The Grameen Bank itself made a profit of just over one hundred million taka in 1998, before taxes and after providing some 750 million taka against bad debts.
Otero (1999, p.8) defines Microfinance as “the provision of financial services to low-income poor and very poor self-employed people”.

Otero (1999) states that the aim of microfinance according to is not just about providing capital to the poor to combat poverty on an individual level; it also has a role at an institutional level. It seeks to create institutions that deliver financial services to the poor, who are continuously ignored by the formal banking sector.

Robinson (2001) states that 1980s represented a turning point in the history of microfinance in that MFIs such as Grameen Bank began to show that they could provide small loans and savings services profitably on a large scale. Microfinance had now turned into an industry.

Harper (2002) states that ROSCA model is a very common form of savings and credit. He states that the members of the group are usually neighbours and friends, and the group provides an opportunity for social interaction and are very popular with women.

According to Zeller (2003), low income customers are more likely to borrow from microfinance institutions they see as financially viable rather than any other sources.

According to Chankova S, Goldberg N & et al, (2004), the predominant financing model for SHGs is one in which the MFIs act as facilitator between banks and SHGs.

M-Crill Review (2009), highlighted that India has the fastest growing microfinance sector in the world and is rapidly moving towards having the largest microfinance as well.

3. Objectives:
   - To assess the importance and scope of Microfinance in a country like India.
   - To analyse different types of business models adopted by MFIs in India and to find out the relative weaknesses of the existing models, so that a new model can be generated that provides help to the poor people more efficiently and effectively.
   - To study the various challenges and prospects of microfinance in the Indian economy.

4. Scope: In the current scenario, the government has been talking about getting the focus back on rural India and putting a thrust on increasing access to agricultural credit in particular and providing greater access to financial services in the rural markets in general.

During the early plan periods, there was significant Microcredit available through government and government-sponsored institutions. Although cooperatives have been functioning from the early 20th century, they have been unable to meet expectations and have suffered from a number of ailments. There was, therefore, a need to look at commercial banks as an additional source. The achievements of microfinance programme in the country have been impressive. The performance of SHGs and MFIs in the south has been much better than the east, north-east, the central part of India or even some parts of western India.

The World Bank estimates that there are now over 7000 microfinance institutions, serving some 16 million poor people in developing countries. The total cash turnover of MFIs worldwide is estimated at US$2.5 billion and the potential for new growth is outstanding. This study is concerned with knowing about the subject and analyzing its importance.

This study restricted itself to the importance and the existing models of Microfinance and making some suggestions about the existing models. This study doesn’t aim to make any
comment upon the workings of a particular institute or organization. The focus is only to study about Microfinance and to research on this topic.

5. Research Methodology: This study has been made after making a thorough study of the subject. For this very purpose, primary as well as secondary data have been used. For Primary data, personal visits and discussion with various MFIs in Manipur and Delhi NCR have been made. In order to have basic understanding of some current issues and challenges of Micro finance, participation on the annual general meeting of Sa-Dhan, an association of MFIs in India at India Habitat Centre, New Delhi and Regency International, Bangalore proved fruitful. For secondary data, the reports provided by Sa-Dhan, M-Cril and Crisil are used. In addition to it, various articles and magazines by professionals in this field have been used for making this study as a learning experience. Further many relevant websites dedicated only to the micro finance and its activities have been referred for better knowledge of the subject.

6. Microfinance Models: The various micro finance models are one of the success factors for many MFIs. Some of them are as follows:

6.1 Associations/Group Model: This is where the target community forms an 'association' through which various microfinance (and other) activities are initiated. Such activities may include savings. Associations or groups can be composed of youth, women; can form around political/religious/cultural issues; can create support structures for microenterprises and other work-based issues. The Group Model's basic philosophy lies in the fact that shortcomings and weaknesses at the individual level are overcome by the collective responsibility and security afforded by the formation of a group of such individuals. The collective coming together of individual members is used for a number of purposes: educating and awareness building, collective bargaining power, peer pressure etc.

In some countries, an 'association' can be a legal body that has certain advantages such as collection of fees, insurance, tax breaks and other protective measures. Distinction is made between associations, community groups, peoples organizations, etc. on one hand (which are mass, community based) and NGOs, etc. which are essentially external organizations.
6.1.1 The SHG system: According to Ajay Tankha (2002), a variety of group based approaches that rely on social collateral and its many enabling and cost reducing effects. The term SHG can be defined as a wide range of financial and non financial associations in India. The members form a group of up to 20 members. The group formation process may be facilitated by a non-governmental organization (NGO) or by the MFO or bank itself, or it may evolve from a traditional rotating savings and credit group (ROSCA) or other locally initiated grouping. According to Chankova S, Goldberg N & et al, (2004), the predominant financing model for SHGs is one in which the MFIs act as facilitator between banks and SHGs.

The process of formal ‘linkage’ to an MFO or bank usually goes through the following stages, which may be spread over many years or which may take place within a few months:

- The SHG members decide to make regular savings contributions. These may be kept by their elected head, in cash, or in kind, or they may be banked.
- The members start to borrow individually from the SHG, for purposes, on terms and at interest rates decided by the group themselves.
- The SHG opens a savings account, in the group’s name, with the MFO or bank, for funds that are not needed by members, or in order to qualify for a loan from the bank.
- The MFO or bank makes a loan to the SHG, in the name of the group, which is then used by the group to supplement its own funds for on-lending to it members. The SHG need never go through all these stages; it may satisfy its members’ needs quite effectively if it only goes to the second or even to the first stage, saving money and possibly not even withdrawing it
- The SHG carries out all the same functions as those required by the Grameen system, but they do this on their own behalf, since the SHG is effectively a micro-bank, carrying out all the familiar intermediation tasks of savings mobilisation and lending. The members have their accounts with the SHG, not with the MFO or bank, and the MFO or bank does not have any direct dealings with the members. The MFO or bank may assist the SHG in record-keeping; they may also demand to know who the members are and impose certain conditions on the uses of the loan which they make to the SHG. The various other differences between the two models can be seen as from the following table

6.2 Bank Guarantees: As the name suggests, a bank guarantee is used to obtain a loan from a commercial bank. This guarantee may be arranged externally (through a donor/donation, government agency etc.) or internally (using member savings). Loans obtained may be given directly to an individual, or they may be given to a self-formed group.

Bank Guarantee is a form of capital guarantee scheme. Guaranteed funds may be used for various purposes, including loan recovery and insurance claims. Several international and UN organizations have been creating international guarantee funds that banks and NGOs can subscribe to, to onlend or start microcredit programmes.

6.3 Village Banks: Village banks are community-based credit and savings associations. They typically consist of 25 to 50 low-income individuals who are seeking to improve their lives through self-employment activities. Initial loan capital for the village bank may come from an external source, but the members themselves run the bank: they choose their members, elect their own officers, establish their own by-laws, distribute loans to individuals, collect
payments and savings. Their loans are backed, not by goods or property, but by moral collateral: the promise that the group stands behind each individual loan.

6.5 The Grameen system: The Grameen model emerged from the poor-focussed grassroots institution, Grameen Bank, started by Prof. Mohammed Yunus in Bangladesh. It essentially adopts the following methodology:

A bank unit is set up with a Field Manager and a number of bank workers, covering an area of about 15 to 22 villages. The manager and workers start by visiting villages to familiarise themselves with the local milieu in which they will be operating and identify prospective clientele, as well as explain the purpose, functions, and mode of operation of the bank to the local population. Groups of five prospective borrowers are formed; in the first stage, only two of them are eligible for, and receive, a loan. The group is observed for a month to see if the members are conforming to rules of the bank. Only if the first two borrowers repay the principal plus interest over a period of fifty weeks do other members of the group become eligible themselves for a loan. Because of these restrictions, there is substantial group pressure to keep individual records clear. In this sense, collective responsibility of the group serves as collateral on the loan.

Potential clients are asked by the MFO to organise themselves into ‘groups’ of five members which are in turn organised into ‘centres’ of around five to seven such groups. The members make regular savings with the MFO, according to a fixed compulsory schedule, and they also take regular loans. They each have individual savings and loan accounts with the MFO, and the main function of the groups and centres are to facilitate the financial intermediation process, through performing tasks such as:

- holding regular and usually weekly meetings which are supervised by an MFO worker, where savings and repayments are collected and handed over to the MFO worker who maintains the records;
- organising contributions to one or a number of group savings funds, which can be used by the group for a number of purposes, usually only with the agreement of the MFO which maintains the group fund accounts; guaranteeing loans to their individual members, by accepting joint and several liability, by raising group emergency funds and by accepting that no member of a group will be able to take a new loan if any members are in arrears; arising from the above, appraising fellow-members’ loan applications, and ensuring that their fellow-members maintain their regular savings contributions and loan repayments.

6.6 Community Banking: Community Banking model essentially treats the whole community as one unit, and establishes semi-formal or formal institutions through which microfinance is dispensed. Such institutions are usually formed by extensive help from NGOs and other organizations, who also train the community members in various financial activities of the community bank. These institutions may have savings components and other income-generating projects included in their structure. In many cases, community banks are also part of larger community development programmes which use finance as an inducement for action.

6.7 Cooperatives: A co-operative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-
owned and democratically-controlled enterprise. Some cooperatives include member-financing and savings activities in their mandate.

6.8 Credit Unions: A credit union is a unique member-driven, self-help financial institution. It is organized by and comprised of members of a particular group or organization, who agree to save their money together and to make loans to each other at reasonable rates of interest. The members are people of some common bond: working for the same employer; belonging to the same church, labor union, social fraternity, etc.; or living/working in the same community. A credit union's membership is open to all who belong to the group, regardless of race, religion, color or creed. A credit union is a democratic, not-for-profit financial cooperative. Each is owned and governed by its members, with members having a vote in the election of directors and committee representatives.

6.9 Individual: This is a straightforward credit lending model where micro loans are given directly to the borrower. It does not include the formation of groups, or generating peer pressures to ensure repayment. The individual model is, in many cases, a part of a larger 'credit plus' programme, where other socio-economic services such as skill development, education, and other outreach services are provided.

6.10 Intermediary: Intermediary model of credit lending positions a 'go-between' organization between the lenders and borrowers. The intermediary plays a critical role of generating credit awareness and education among the borrowers (including, in some cases, starting savings programmes). These activities are geared towards raising the 'credit worthiness' of the borrowers to a level sufficient enough to make them attractive to the lenders. The links developed by the intermediaries could cover funding, programme links, training and education, and research. Such activities can take place at various levels from international and national to regional, local and individual levels. Intermediaries could be individual lenders, NGOs, microenterprise/microcredit programmes, and commercial banks (for government financed programmes). Lenders could be government agencies, commercial banks, international donors, etc.

7. Case studies of some MFIs: Many institutes have been consulted for getting an in-depth view about the subject. Among these institutes, Sambodhi is an initiative catering to research & allied service needs in social sector for design & development of state of art & knowledge ware products. Currently, Sambodhi is working on many Projects such as World vision (India), USAID, Rural livelihood project (MP) and Pilot projects. It advances market research methods for restructuring of micro finance products. On the other hand, Streebal is a community center that focuses on the empowerment of women. It provides courses in tailoring, beautician training, Childcare and health services. The main challenges this institute face are related to English language, Computer Literacy and more markets for their products. ICICI Bank, on the other hand, provides loan funds and technology. It lends directly to clients with risk sharing by NGO / MFI. The Bank decides pricing and risk sharing on historical data and undertakes loan origination, monitoring and collection. It focuses on the Microfinance activities through the MFI Model and lends money for that purpose.

7.1 Case study I. Deepalya: DEEPALYA is a Non-Government Development Organization working on issues affecting the urban and rural poor, with a special focus on
children. The organization believes that “Every child deserves a chance and thus working towards making that possible. The founders are Mrs. Grace Thomas, Mr. C.M. Mathai, Mr. Punnoose Thomas, Mr. T.K. Mathew.

It is the largest operational NGO in Delhi. It was started on July 16, 1979, with five children, two teachers and with the investment of Rupees 17,500/. DEEPALYA is currently working in more than 30 projects and its main focus is distributed to the areas like education, differently-able people, health issues and gender equality.

7.2 Case study II. Pradhan: Pradan is a NGO that works only as a Promoter. It implements Short-term Projects & the Focus is on livelihood of the people. It merely acts as a Motivator and guides the people to work for their benefits. Pradan, firsts, tries to link people with the SHG and then it tries to establish links between the SHG and the Banks. Pradan, basically, follows, a three-tier model that can be seen from the figure below -:

Fig. 2 Three tier model of Pradhan.

These three levels can be described as follows -:

1. **SHGs**: These are group of people consisting of 10 to 20 people and the focus is on saving some amount of money on weekly/monthly basis. The maximum limit of Loan amount that can be given is decided as 3 to 4 times of the Savings. 539 SHGs groups have been made till now. These groups have regular meetings on weekly basis & focus is also on to resolve any sort of Personal & Social issues of the Members.

2. **Clusters**: Cluster is a group of 10 to 12 SHGs. It acts as a mediator between SHG & Federation & the meetings are done regularly on monthly basis. The Meeting is to be attended by the representatives of each of the SHGs (normally 2 from each of the SHG). Social issues & Govt. Policies are also discussed within the Cluster.

3. **Federation**: It is the upper most level of the existing Model and covers around 6800 people. It is controlled & managed by Community People. Federation facilitates sales, inter loaning system and management of books of accounts.

In lieu of having Practical Exposure, a collected report of “nupi marup” (a Federation) Imphal has been made. It is a unit of 59 peoples and they meet regularly on monthly basis. The meeting is to be attended by a representative of each of the village. For becoming the representative, a person needs to be the member of the cluster also. Discussions on Community related social issues are taken care off by this association. Also, communication of any special government policies to individuals is made through the meeting.
From the report, it has been revealed that people there are better off now after the establishment of Pradan, but then also there are problems like lack of adequate number of schools, inadequate water supply and lack of infrastructure. The people are making efforts, through the federations, for solving all these problems, but in any case, improvement is being made in the livelihood of these people and still a long way to go through this initiative of microfinance.

8. Weaknesses of Existing Microfinance Models: One of the most successful models discussed around the world is the Grameen type. The bank has successfully served the rural poor in Bangladesh with no physical collateral relying on group responsibility to replace the collateral requirements. This model, however, has some weaknesses. These are as follows:

- It involves too much of external subsidy which is not replicable. Grameen bank has not oriented itself towards mobilising peoples' resources.
- The repayment system of 50 weekly equal instalments is not practical because poor do not have a stable job and have to migrate to other places for jobs. If the communities are agrarian during lean seasons it becomes impossible for them to repay the loan. Pressure for high repayment drives members to money lenders.
- Credit alone cannot alleviate poverty and the Grameen model is based only on credit. Micro-finance is time taking process. Haste can lead to wrong selection of activities and beneficiaries.

Another model is Kerala model (Shreyas). The rules make it difficult to give adequate credit (only 40-50 percent of amount available for lending). In Nari Nidhi/Pradan system perhaps not reaching the very poor. Most of the existing microfinance institutions are facing problems regarding skilled labour which is not available for local level accounting. Also, Drop out of trained staff is very high that again creates major problems in this field. One alternative for reducing this overdependence can be suggested as automation, which is not looked at as yet. In addition to it, all the models lack in appropriate legal and financial structure & thus transparency can be a big issue over here.

Thus, there is a need to have a sub-group to brainstorm on statutory structure/ ownership control/ management/ taxation aspects/ financial sector prudential norms & thus a forum/ network of micro-finance (self regulating organization) is desired.

Most of the demands of the rural credit are of fragmented in nature. Moreover most MFIs are managed by community and they don’t follow a particular model of providing credit to various poor people. Communities are not aware of the right and responsibilities of themselves. The existing regulations focus more on the formal service providers. The informal service providers which occupy an important place in the market are not regulated by any authority. Moreover sometimes different regulators have multiple and conflicting policies of regulating a particular MFI. Moreover many MFIs are surviving on grant provided by various financial institutions.

9. Constraints to growth and Challenges Remain: The major constraints identified as to Microfinance in India are greater and more diverse sources of funding, a meaningful set of poverty impact indicators in order to make meaningful statements about social impact, and lack of an enabling policy environment for microfinance.

In terms of an enabling policy environment, the main thing that MFIs can do is to work together with regulators to ensure that there is an understanding about the needs and challenges of MFIs. MFIs in India, have also formed an association and self-regulatory body,
Sa-Dhan, which provides a platform for communicating ideas jointly to the Reserve Bank of India and other authorities. The more that the government and central bank understand the nature of the business and what constrains growth, the better they will be able to strike the balance between enabling growth and protecting the poor.

This might be done by setting a minimum standard of regulation for MFIs but refraining from restrictive and inflexible regulation such as interest rate caps or prohibitive restrictions on foreign investment. Positive regulation such as liquidity requirements and capital requirements can sometimes ensure that MFIs are not taking on risk so as to jeopardize continuing operations. Some minimum regulation creates a sense of accountability for MFIs, placing them on a common platform and creating incentive to better manage risk. This can make a big difference to the quality of the services offered the poor and thus, the potential microfinance as a field has for really improving the lives of the poor.

A World Bank study assessing access to financial institutions found that amongst rural households in Andhra Pradesh and Uttar Pradesh, 59% lack access to deposit account and 78% lack access to credit. Considering that the majority of the 360 million poor households (urban and rural) lack access to formal financial services, the numbers of customers to be reached, and the variety and quantum of services to be provided are really large. It has been estimated that 90 million farm holdings, 30 million non-agricultural enterprises and 50 million landless households in India collectively need approx US$30 billion credit annually. This is about 5% of India's GDP and does not seem an unreasonable estimate.

A tiny segment of this US$30 billion potential market has been reached so far and this is unlikely to be addressed by MFIs and NGOs alone. Reaching this market requires serious capital, technology and human resources. However, 80% of the financial sector is still controlled by public sector institutions. Competition, consolidation and convergence are all being discussed to improve efficiency and outreach but significant opposition remains; for example, the All India Bank Employees Association has threatened to strike if the Government proceeds with its policy of reducing its capital in public sector banks, merging public sector banks or even enhancing Foreign Direct Investments in Indian private banks.

Also, in the Microfinance India conference, many speakers talked about the significant and growing gap between surging growth in South India, which contrasts with the stagnation in Eastern, Central and North Eastern India. Microfinance on its own is unlikely to be able to address formidable challenges of underdevelopment, poor infrastructure and governance.

The Self Help Group movement is beginning to focus on issues of quality and there were some interesting discussions on embedding social performance monitoring as a part of the regular management information systems. At the time of the conference, a leading and responsible MFI was being investigated by the authorities for charging "high" rates of interest. Per unit transaction costs of small loans are high but many opinion leaders still persist with the notion poor people cannot be charged rates that are higher than commercial bank rates.

The reality of the high transaction costs of serving small customers, their continuing dependence on the informal sector, the fact that most bankers shy away from retailing to this market as a business opportunity, and the poor quality of services currently provided does not figure prominently in this discourse. While the central bank has deregulated most interest
rates, including lending to and by MFIs, interest rates restrictions on commercial bank for retail loans below US$5,000 (all microfinance and beyond) remain and caps on deposit rates also discourage sharing transaction costs with customers. But most conference participants accepted the imperatives to build sustainable institutions.

There is still lot of policy focus on what activities are and are not allowed and not enough operational freedom as yet for banks and financial institutions to design and deliver programmes, and be responsible for their actions. Prescriptions and detailed circulars often limit organizational innovation and market segmentation. If the right indicators are monitored and operational freedom and incentives are clear, both public and private banks have the capacity to reorient their strategy to address the remaining challenges.

10. Future Prospect of Microfinance: Microfinance is a widely accepted & important term & it is much more than Micro credit & can be stated as, "Provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi-urban and or urban areas for enabling them to raise their income levels and improve living standards".

According to M-Cril Review (2009), India has the fastest growing micro finance sector in the world and is rapidly moving towards having the largest micro finance as well. The Self Help Group promoters emphasize that mobilizing savings is the first building block of financial services. For many years, the national budget and other policy documents have almost equated microfinance with promoting SHG links to the banks. The central bank notification that lending to MFIs would count towards meeting the priority sector lending targets for Banks offered the first signs of policy flexibility towards MFIs.

Fig. 3.Growth of fastest MFIs in India (Source: M-Cril Review, 2010)

One could argue that MFIs are small and insignificant, so why bother. The larger point is about policy space for innovation and diversity of approaches to meet large unmet demand. The insurance sector was partially opened to private and foreign investments during 2000.
Over 20 insurance companies are already active and experimenting with new products, delivery methodologies and strategic partnerships.

Microfinance programmes have rapidly expanded in recent years. Some examples are:

- Membership of Sa-Dhan (a leading association) has expanded from 43 to 96 Community Development Finance Institutions during 2001-04. During the same period, loans outstanding of these member MFIs have gone up from US$15 million to US$101 million.
- The CARE CASHE Programme took on the challenge of working with small NGO-MFIs and community owned-managed microfinance organisations. Outreach has expanded from 39,000 to around 300,000 women members over 2001-05. Many of the 26 CASHE partners and another 136 community organisations these NGO-MFIs work with, represent the next level of emerging MFIs and some of these are already dealing with ICICI Bank and ABN Amro.
- In addition to the dominant SHG methodology, the portfolios of Grameen replicators have also grown dramatically. The outreach of SHARE Micro fin Limited, for instance, grew from 1,875 to 86,905 members between 2000 and 2005 and its loan portfolio has grown from US$0.47 million to US$40 million.

The 2005 national budget has further strengthened this policy perspective and the Finance Minister Mr P. Chidambram announced "Government intends to promote MFIs in a big way. The way forward is to identify MFIs, classify and rate such institutions, and empower them to intermediate between the lending banks and the beneficiaries."

Fortunately, the 2005 Budget opened a small window in this area and the central bank annual policy recently confirmed discussions on this: "As a follow-up to the Budget proposals, modalities for allowing banks to adopt the agency model by using the infrastructure of civil society organizations, rural kiosks and village knowledge centers for providing credit support to rural and farm sectors and appointment of micro-finance institutions (MFIs) as banking correspondents are being worked out."

Thus, it can be deduced that microfinance itself has a long way to go and there is a lot of scope available for doing innovations and tapping a huge rural market. Many institutions have already started exploring this field and others are planning to do it. Hence, Microfinance has a great future prospect and it offers great opportunities.

11. Conclusions and recommendations: Various important conclusions can be drawn from the study of microfinance operation. Whatever may be the reason, the ultimate benefit is for the poor people. Provide the easy access to the credit, the poor people are ready even to repay at higher interest than commercial banks. Moreover the concept of joint liability in SHG and grameen model motivate MFIs to release loans to poor people easily due to low default rates.

The poor people who don’t have the habit of savings are also encouraged to engage in savings. From these two findings we can conclude that providing banking facilities to the poor can be a profitable business. However attaining financial viability and sustainability is the major institutional challenge.

Some of the business models of microfinance adopted by MFIs in India are a huge success. But still some of them have flaws. The MFIs should identify the different loopholes of a particular model and try to make some amendments in its implementation in order make it more successful.
One of the important conclusions is that microfinance activities can contribute to solving various problems of poor people like housing, infrastructure, schooling, water supply etc which are an integral part of the poverty alleviation vision. The challenge lies in finding the level of flexibility in the credit instrument that could make it match the multiple credit requirements of the low income borrowers without imposing unbearably high cost of monitoring its end use upon the lenders. A promising solution is to provide multi-purpose loans or composite credit for income generation, house improvement and consumption support.

Consumption loan is found to be especially important during the gestation period between commencing a new economic activity and delivering positive income. Careful research on demand for financing and saving behavior of the potential borrowers and their participation in determining the mix of multi purpose loans are essential in making the concept work.

Eventually it would be ideal to enhance the creditworthiness of the poor and to make them more "bankable" to financial institutions and enable them to qualify for long-term credit from the formal sector. Microfinance institutions have a lot to contribute to this by building financial discipline and educating borrowers about repayment requirements.

Based on the study, a new paradigm that emerges is that it is very critical to link poor to formal financial system, whatever the mechanism may be, if the goal of poverty alleviation has to be achieved. NGOs and CBOs have been involved in community development for long and the experience shows that they have been able to improve the quality of life of poor, if this is an indicator of development.

The four pillars of microfinance credit system are supply, demand for finance, intermediation and regulation. Whatever may the model of the intermediary institution, the end situation is accessibility of finance to poor.

![Fig. 4. Four pillars of micro finance credit system](Source: International Journal of Information Technology and Knowledge Management, July-Dec, 2010)

The strength and weakness of existing NGOs/CBOs and microfinance institutions in India indicate that despite their best efforts they have not been able to link themselves with formal
systems. It is desired that an intermediary situation is required between formal financial markets and grass root. The intermediary should encompass the strengths of both formal financial systems and NGOs and CBOs and should be flexible to the needs of the end uses. There are however certain unresolved dilemma regarding the nature of the intermediary institutions. There are arguments for both for and against each structure. These dilemmas are very contextual and only strengthen the argument that no unique model is applicable for all situations. They have to be context specific.

According to the recent Malegram committee Report, the rules and regulations of MFIs have become stricter and every MFI has to adhere to it. The MFI sector’s growth is likely to remain subdued over the medium term especially in regions with high micro finance penetration because of proposed regulatory restrictions on multiple lending, loan size and ease usage of loans. This will provide an impetus for consolidation in the sector. To comply with the new regulations, MFIs will have to enhance the robustness of their internal systems and processes, strengthen their monitoring mechanism and invest in training their employees. In this way, the now the issue arises is, “Can MFIs survive if they follow such strict rules and regulations that has been proposed by Malegram Report of RBI? The scenario has been changed a lot. The investors who were readily happy to invest more in MFIs are becoming more skeptical. If we see the present scenario, there has been a setback in way how the MFIs have been progressing in the last few years, the main reason being lack of funds from various financial institutes. The scenario is even worse in North Eastern states of India, where the investors have to think so many times even before declining a funding proposal by one of the MFI. This poses a challenge of extinction of mainly the MFI s having small and medium size portfolios. However regulatory jurisdiction for MFIs remains unclear. While RBI has created a new category of non banking financial companies to regulate the MFI sector, multiple regulators continue to oversee the sector. A clearer regulatory framework will remain critical to instill greater confidence in the sector.

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