

# Chapter 19

## Role of Microfinance in Financial Inclusion in India

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### ABSTRACT

*The purpose of this chapter is to critically evaluate the status of microfinance in India, the types, characteristics, and modes of operation of MFIs. It also highlights the main differences between commercial banking and microfinance institutions and examines the extent to which banks fulfill financial requirements and of whom? This chapter presents a linkage among microfinance institutions, financial inclusion, and economic development on a country. The study reveals that MFIs contribute in the upliftment of the society leading to economic benefit to the country as a whole. It makes the reader realize the importance of microfinance in the economic development of a country which cannot be realized just by uplifting the structured and most sophisticated banking sector. Handholding of the poor and rural population is required in order to accelerate the process of financial inclusion and thereby reaching the goal of economic development.*

### INTRODUCTION

Microfinance concept started with the idea of providing financial services to the poor who are otherwise considered un-bankable or credit-unworthy. Pioneered by Nobel Laureate Dr. Mohammad Yunus, modern microfinance concept revolves around the activities of the Grameen Bank. The initial success of Grameen Bank in alleviating poverty brought this concept into the global limelight and has led to micro-finance being populated as a panacea for poverty and under-development across the world. The basic principle of microfinance is that a group of individuals is more bankable than a single individual. Micro financing loans are small loans granted to the basic sectors, on the basis of the borrower's cash flow and other loans granted to the poor and low-income households for their microenterprises and small businesses to enable them to raise their income levels and improve their living standards. Loan is granted to poor without the requirement of any collateral security.

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## ***Role of Microfinance in Financial Inclusion in India***

Setting up of MFIs (Microfinance Institutions) in India has been instrumental in efforts taken to address poverty issues. The rural population, which does not have access to otherwise available alternate sources of finance like banks and other financial institutions, get access to financial loans for their personal, business or family uses. Financial inclusion talks about making financial services accessible to lower income group people who do not have access to banking facilities. The goal of financial inclusion is to make the banking facilities available to all the unbanked areas and to each and every household. Microfinance has proved to be a bridge between rural population and financial resources. Through SHGs (self-help groups) a microfinance institutions help in making financial products reach every house hold and benefit the under privileged. MFIs indirectly fulfill the purpose of financial inclusion. They help in the following areas (to name a few) (i) Ease of access to financial services as against traditional banking services; (ii) Customer education and training (iii) Relaxation in loan repayment rules; and many more. Thus, microfinance enables financial inclusion through the medium of micro credit provided to the lower income segment.

## **MICROFINANCE INSTITUTIONS IN INDIA**

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Microfinance includes a broad range of financial services such as deposits, loans, payment services, money transfers and insurance products to the poor and low-income households, for their microenterprises and small businesses, to enable them to raise their income levels and improve their living standards. It also includes micro-credit, micro-savings, micro-insurance and a host of other financial services. In India the maximum quantum of loan that can be granted through micro credit is around Rs 45000/-. Credit unions and lending cooperatives have been around hundreds of years. In the context of microfinance, Dr. Mohammad Yunus, began experimenting with lending to poor women in the village of Jobra, Bangladesh during his tenure as a professor of economics at Chittagong University in the 1970s. He founded Grameen Bank in 1983 and won the Nobel Peace Prize in 2006. The UN Year of Micro-credit in 2005 indicated a turning point for Microfinance as the private sector began to take a more serious interest in what has been considered the domain of government. The Consultative Group to Assist the Poorest (CGAP) estimated that microfinance probably reaches to fewer than 5 per cent of its potential group. Microcredit is the essence of microfinance business models, and has a number of distinctive features. Microcredit provider usually caters to low-income clients, both the underemployed and the entrepreneur with an informal family business. Borrowers are generally in a limited geographic area, social segment or entrepreneurial undertaking. Loans granted are of small, short term in nature and unsecured. The

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