

A STUDY ON ISSUES AND CHALLENGES OF MICRO FINANCE IN KARNATAKA – AN OVERVIEW

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ABSTRACT

This paper studies microfinance as a unique economic development tool that was introduced to support low-income families and women who aim to work their way out of poverty and its challenges and prospects. The microfinance industry in India, which has helped to bring financial inclusion in India in 2005 by the RBI providing basic no frills banking accounts for making and receiving payments and other financial products to millions of rural families and women. MFI has become a dominant player when it comes to extending smaller credit limits, with Karnataka alone seeing 1 core loan accounts with a portfolio of Rs.46000 cores outstanding as of March 2023, as per a report by the Association of Karnataka microfinance institutions, the loan portfolio of microfinance institutions stood as 3.48 lakh cores with 7 core borrowers. The sector has also been serving a crucial purpose in the Indian economy, which has been driven by many factors. Meanwhile, the Govt of Karnataka and RBI have been closely examining the sector to protect borrowers and lenders as a high level of financial risk is involved. Karnataka stands fifth in the country in the share of clients who opt for microfinance lending at the end of March 2022 the state had 9.4 million loan accounts covering 5.4 million unique clients as per the report by NABARD, the districts of Mysore, Belagavi, and Tumakuru, Mandaya and Hassan were on top in terms of the number of loan accounts held with MFI'S.

Keywords: Women, NABARD, RBI, Banking, MFIs, Karnataka.

INTRODUCTION

Micro Finance refers to providing financial credit and other product related services to enable the poor in rural semi-urban or urban areas to increase their income levels and improve their standard of living. Microfinance is defined as financial services such as a savings account, insurance funds and debt provided to poor and low income clients, thereby helping to increase their income improving their standard of living. Micro Savings Accounts allow entrepreneurs to maintain a savings account with minimal balance. These accounts help users to maintain financial discipline and develop savings interest for the future. These accounts do not bind people to manage their accounts with a certain amount of fixed money. Micro insurance is a type of coverage provided to microloans borrowers these insurance programs have lower premiums than traditional insurance policies. MFI's provide loans and financial services without any securities and enable the needy group to develop economically. This gives a better overall loan repayment rate than a traditional banking product. This is a sustainable process that increases the likelihood of future investment of economic household and business concerns critics often point to some of the ills of micro credit that can create indebtedness, higher interest rates, less awareness of financial services in the economy etc many studies have tried to assess its impacts and prospects to assist the ever growing Indian population

The year 2022-23 was the first year with RBI's new uniform regulations, applicable to all players in the micro finance sector. The fact that the industry is back on track with an

indication that the new regulations have been positive for the sector. The support of the RBI, the Central Government and the State government has been crucial. The industry has got back to normalcy after COVID disruptions, with healthy repayment collection rates for loans given and good growth of portfolio. Microfinance sector has the potential to serve 10 to 15 per cent of the population living in India's rural areas and is likely to build infrastructures to serve up to 30 per cent of the populations in the future. Microfinance will play a major role in India's rural economic growth MFIs don't just offer loans but bring the most vulnerable people into the mainstream of Indian economy which is going to scale new heights over a few years' time from now. Financial inclusion is the way to have inclusive growth in our country; Microfinance Institutions have been playing a very crucial role in providing various financial services to the poor and low income household in Urban and Rural India. Reaching out to more than 2.67 Cores households with a loan portfolio of around 46,000 Cores outstanding, the Micro finance industry's contribution to the economy has been significant.

REVIEW LITERATURE

Vipin Kumar, Monu Chauhan, Ritesh Kumar (article on the microfinance sector) - India 70% of the population live in villages and 60% of their income comes from the agricultural sector. Thus, microfinance plays an important role in providing loans and financial assistance to the poor. The objective of this study is to understand the current situation of microfinance and its role in the economic growth of the country. Thus, microfinance plays an important role in improving the standard of living of the poor and helping them earn money. It is an effective tool to reduce poverty and the socio- economic conditions of the country. Therefore, the Indian government should focus on microfinance to ensure sustainable and inclusive economic growth.

Susy Cheston (2002) explores how microfinance can have a powerful impact on women's empowerment. Although microfinance does not always empower all women, most women experience some degree of empowerment as a result. Licensing is a complex change process, and everyone experiences then a slightly different way. Women need, want and benefit from credit and other financial services. Strengthening women's economic base and their economic contributions to their families and communities is an important part of their empowerment. Product design and program design must consider the needs and strengths of women. By increasing awareness of the potential impacts of their programs, MFIs can design products, services, and service delivery mechanisms to reduce negative impacts and increase positive impacts.

METHODOLOGY

This current article focuses on the requirements of the study objectives. The research design used for the study was descriptive. This research design was adapted to have in-depth analysis of research studies based on available secondary data. The investigator collects the necessary data through a secondary survey method, various papers, books and annual reports, articles published in various journals, essays and discussion with scholars and website information focusing on various aspects of microfinance institutions in Karnataka.

OBJECTIVES OF MICROFINANCE

The objectives of microfinance go beyond providing small loans. Here are the primary objectives, offering a clearer understanding of what is microfinance.

1. **Poverty Alleviation:** Microfinance's main goal is to reduce poverty by giving low-income people access to financial services.

2. **Financial Inclusion:** Microfinance aims to bring the unbanked population into the formal financial system.
3. **Entrepreneurship Promotion:** By offering microloans, microfinance encourages entrepreneurship, enabling individuals to start and grow their businesses.
4. **Women Empowerment:** Microfinance has a strong focus on empowering women, offering them financial independence and the ability to contribute to household income.
5. **Community Development:** Microfinance aims to foster community development by improving the economic well-being of individuals, which in turn, benefits the community at large.

ISSUES & CHALLENGES OF MICRO FINANCE

Microfinance in India has played a crucial role in providing financial services to the economically marginalized sections of society, particularly in rural areas. However, like any financial system, it has faced various issues and challenges. Here are some of the key issues and challenges associated with microfinance in India:

Over-Indebtedness: One of the major challenges faced by microfinance borrowers in India is over-indebtedness. In some cases, individuals take loans from multiple microfinance institutions (MFIs) to repay existing loans, leading to a debt trap. This situation can result in financial distress and defaults.

Interest Rates: The interest rates charged by some MFIs have been a subject of criticism. While microfinance is intended to be an affordable source of credit for the poor, high-interest rates can make it difficult for borrowers to repay loans, leading to a cycle of poverty.

Regulation and Governance: The microfinance sector in India has faced issues related to regulation and governance. There have been instances of malpractices by certain MFIs, including coercive recovery practices and lack of transparency. This has led to the need for stricter regulation and better governance.

Lack of Financial Literacy: Many microfinance borrowers, especially in rural areas, lack financial literacy. This makes it challenging for them to understand the terms and conditions of the loans, resulting in mismanagement of funds and potential defaults.

Limited Product Diversification: The microfinance sector in India has primarily focused on providing credit, with limited emphasis on other financial products and services. There is a need for product diversification to address the diverse financial needs of the poor, such as savings, insurance, and micro-investment options.

Dependency on Joint Liability Groups (JLGs): Microfinance institutions often rely on Joint Liability Groups, where individuals in a group are jointly responsible for the repayment of loans. However, the effectiveness of this model has been questioned, and there is a need for exploring alternative group lending mechanisms.

Sustainability of Microfinance Institutions: Some MFIs face challenges in achieving financial sustainability. The social mission of reaching out to the poor sometimes conflicts with the financial viability of the institutions. Striking a balance between social impact and financial sustainability is an ongoing challenge.

Impact Assessment: Assessing the real impact of microfinance on poverty alleviation is a complex task. While success stories exist, there is a need for comprehensive and unbiased impact assessments to understand the effectiveness of microfinance interventions.

External Shocks: Economic and environmental factors, such as natural disasters and economic downturns, can have a significant impact on the ability of microfinance borrowers to repay loans. This vulnerability highlights the need for risk mitigation strategies.

Technological Challenges: The adoption of technology in microfinance has been uneven. While some MFIs have embraced digital tools for operations and transactions, others face challenges in implementing and adapting to technological changes, limiting their efficiency.

Addressing these challenges requires a collaborative effort involving policymakers, regulators, microfinance institutions, and other stakeholders to ensure the sustainable and responsible growth of microfinance in India. Striking a balance between financial inclusion and the well-being of borrowers is crucial for the long-term success of microfinance initiatives.

LIST OF MICROFINANCE INSTITUTIONS IN INDIA

India has a vast network of microfinance institutions (MFIs) operating across the country. Below is a list of some prominent microfinance institutions in India:

1. **Bandhan Bank** Bandhan Bank is one of the leading microfinance institutions in India, offering a range of financial services including microloans.
2. **SKS Microfinance** Also known as Bharat Financial Inclusion Ltd., SKS Microfinance is a well-established MFI that provides microloans and other financial services.
3. **Spandana Sphoorty Financial Ltd.** Spandana Sphoorty is one of the largest MFIs in India, providing financial services to underserved populations, particularly women.
4. **Ujjivan Financial Services** Ujjivan focuses on providing financial services to the unbanked and underserved sectors of society, particularly in rural areas.
5. **Equitas Small Finance Bank** Equitas offers microloans and savings accounts, and it has grown to become one of the prominent MFIs in India.

OPPORTUNITIES FOR GROWTH & DEVELOPMENT

- **Expanding Digital & Fintech Integration:** The use of Artificial Intelligence (AI), machine learning (ML), and data analytics can improve credit assessment, reduce risks, and enhance operational efficiency.
- The rise of UPI, Aadhaar-linked banking, and digital KYC has already streamlined microfinance processes.
- **Focus on Rural & Agricultural Financing:** With the government's emphasis on rural development and financial inclusion, MFIs can expand their services to agriculture, allied activities, and rural businesses, providing customized financial products for farmers and small traders.
- **Women-Centric Microfinance Models:** Women make up a significant portion of microfinance borrowers.
- Strengthening women-centric lending models, self-help groups (SHGs), and women entrepreneurship programs can drive social and economic empowerment.
- **Sustainable & Impact-Driven Microfinance:** MFIs can diversify into green finance, supporting renewable energy, water conservation, and sustainable farming initiatives.
- It aligns with the global focus on impact-driven finance.

- **Strengthening Risk Management & Credit Bureau Coordination:** Enhanced coordination with credit bureaus (like CIBIL and Equifax) can prevent over-indebtedness, ensuring responsible lending.
- Risk-based pricing models and AI-driven credit monitoring can further reduce defaults.

GOVERNMENT & POLICY SUPPORT

- **Regulatory Support:** The Reserve Bank of India (RBI) regulates NBFC-MFIs, ensuring fair practices and stability in the sector. The introduction of the Microfinance Institutions (Development and Regulation) Bill has further strengthened the industry.
- The government passed the **Microfinance Institutions (Development and Regulation) Bill in 2012** to provide regulatory oversight and recognition to MFIs, ensuring transparency and accountability.
- The **RBI and Microfinance Institutions Network (MFIN)** have introduced stricter lending norms to mitigate risks and ensure sustainable growth, and protect the interests of borrowers.
- **New RBI Framework (2022):** To harmonize microfinance lending across different categories of lenders.
- **The Malegam Committee report** and subsequent regulatory framework helped restore stability of MFIs.
- **Financial Inclusion Initiatives:** Government schemes like Pradhan Mantri Jan Dhan Yojana (PMJDY), Micro Units Development & Refinance Agency (MUDRA Yojana), M SVANidhi and SHG-Bank Linkage Programme have boosted microfinance outreach.
- Other key initiatives are Stand-Up India Scheme, National Rural Livelihood Mission (NRLM) – Aajeevika, Credit Guarantee Fund for Micro Units (CGFMU), Interest Subvention Scheme for Women SHGs, and Deendayal Antyodaya Yojana – National Urban Livelihoods Mission (DAY-NULM) etc.

CONCLUSION

Microfinance is vital for increasing financial inclusion and reducing poverty in India. By providing services like small loans, savings, and insurance, microfinance institutions help people, especially women, improve their financial situations. Understanding “what is microfinance” reveals how these services positively impact the economy and the lives of millions. As India continues to grow, microfinance will remain an important tool for supporting low-income communities and boosting economic development.

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