Mains Practice Question

Q. Microfinancing was introduced in India as a solution to poverty and to empower Self Help Groups (SHGs). Despite its strong potential, the microfinance sector faces challenges related to accessibility in India. Analyse. (250 words)

19 Apr, 2022 GS Paper 2 Social Justice

Approach

- Begin with a brief introduction
- Analyse the potential of microfinance sector
- Discuss various challenges faced by them
- Suggest measures to combat these challenges

Introduction

Microfinance is a type of banking service provided to those who have difficulty in accessing formal financial services. It is targeted at the low-income and unemployed fraction of the population. The institutions supporting microfinance offer services such as lending, setting up bank accounts and providing micro-insurance products.

Microfinance institutions (MFIs) in India are set to address two most important gaps – first, in terms of creating access to a formal banking system, and second, in building confidence among self-help group (SHG) women to access the formal system.

Body

Potential of microfinance sector

- Today, the sector serves around 6 crore unique customers with a combined portfolio size of Rs 2,31,000 Crore across 620 districts in 28 states and 8 UTs.
- Microfinance institution’s vast network can be leveraged to deliver other goods and services to the rural masses.
- The sector can generate significant employment opportunities not only by hiring from the hinterland but also enabling its customers provide employment opportunities to others via financial support extended.

Challenges faced by the microfinance sector related to accessibility in rural India

- The microfinance delivery models fail to focus on people who are below the poverty level as they are deemed to be risky. There is a bias whilst selecting beneficiaries for the scheme. To run the programme successfully and to attain higher repayment rates, the operators of the scheme select economically stable individuals as the programme beneficiaries.
- The coverage of microfinance programme is low in those states where a large percentage of the population lives in poverty.
- Borrowers are interest-sensitive, so the capacity of borrowing decreases with an increase in interest rates. Thus, high-interest rates are counterproductive and weaken the economic status of

poor clients.
- India has a low literacy rate, which is still more moderate in its rural areas. A large chunk of the Indian population fails to understand the basic financial concepts. There is a severe lack of awareness of financial services provided by the microfinance industry among the masses. This lack of adequate knowledge is a significant factor that keeps the rural population from accessing MFIs for easy credit to meet their financial needs.

Way forward

- Microlenders are majorly dependent on commercial banks for debt and equity funding. The sector must develop partnerships with private donors like foundations, NGOs, development agencies, venture capital and social impact investing through corporate social responsibility (CSR) funds, global trust funds and other financial sources.
- Microfinance players should look to provide curated financial products which are focused towards individual needs like crop insurance and equipment leasing facilities with repayment terms catered to specific agricultural growth and output cycles.
- In order to provide last-mile services in unpenetrated geographies, microfinance players can look to leverage government initiatives and enter into new partnerships to drive financial inclusion efforts.
- Holistic transformation of the microfinance sector can only be achieved by financially empowering women,who form a major portion of microfinance borrower. Efforts should also be made towards promoting a culture of entrepreneurship among them and enabling them to set up viable businesses,s, like Kerela’s Kudumbshree scheme.

PDF Refernece URL: https://www.drishtiias.com/mains-practice-question/question-1225/pnt