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INSTITUTIONAL CREDIT AND POVERTY ERADICATION

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ABSTRACT

For a long time, the State and its planners have prioritized the eradication of poverty. These attempts to reduce poverty through state-driven credit supply programs only yielded less than ideal outcomes. Enough provisions must be created for the distribution and delivery of credit to the rural poor in order to make effective use of these programs. One of the most hotly contested topics among academics and decision-makers is the reduction of poverty. The goal of the poverty reduction program from the 1950s to the 1980s was to improve macroeconomic performance in order to promote the involvement of the poor in the economy. Although academics have recognized the impoverished segment of the population that is mostly employed in the informal sector1, this segment has not been included in economic models or government policy. The World Bank's establishment in 1944 marked the institutionalization of poverty reduction. Through governments and organizations, the World Bank provided loans to developing nations through programs known as structural adjustment. These programs were a complete failure, causing the poorer segments of society to become dependent on aid with minimal assistance. This failure brought on by mistrust of formal institutions marks the start of a change in development theory that eventually gives rise to microfinance. Supporting the unorganized sector by giving people credit to assist them escape poverty is the main goal. These unofficial microbusinesses benefit from microfinance through microcredit. "The provision of small loans to individuals, usually within groups, as capital investment to enable income generation through self-employment" is the microcredit method to poverty reduction. Poor people's unofficial companies are referred to as an example of an unmet credit demand. Market failure is thought to be the cause of poverty. Microfinance would address this issue by giving the underprivileged access to credit. Credit would help the impoverished escape poverty by generating economic power that in turn would produce social power.

KEYWORD: Eradication, Poverty, Economy, Microcredit, Government Policy

1. INTRODUCTION

The main driver of microfinance innovations has been the official credit institutions' inability to satisfy the credit needs of the impoverished in rural areas. Serving modest loans and providing credit to the unreached and uncared for thus far—that is, an acceptable amount at the correct time with minimal paperwork requirements—is the most difficult issue facing the rural credit delivery system. In this regard, the Self-Help Group (SHG), a non-formal organization that provides credit to the underprivileged, may prove to be a viable adjunct to the official credit system. As a result, SHGs were established as tools for rural residents' socioeconomic advancement. It demonstrates how easy access to and effective microcredit provision may help the impoverished manage their risks, smooth their consumption, progressively increase their assets, grow their microbusinesses, increase their ability to earn income, and live better lives. In addition, microfinance services can aid with market expansion, resource allocation, and the adoption of improved technology, all of which support economic growth and development.

The provision of financial services to low-income clients—such as consumers and independent contractors—who typically do not have access to banking and associated services is known as microfinance. In a broader sense, the movement aims to create "a world in which as many poor and near-poor households as possible have permanent access to an appropriate range of high quality financial services, including not just credit but also savings, insurance, and fund transfers." The prevailing belief among proponents of microfinance is that it will enable impoverished individuals to escape poverty. Microfinance may be easily separated from charity and is regarded as a tool for socio-economic development. Charity should be given to families who are so impoverished that they are unlikely to be able to produce the cash flow needed to pay back a loan. Financial institutions are the ones who benefit others the most.

In order to give the impoverished access to credit, India's microfinance sector was established in the 1970s. It is now in charge of meeting the basic financial needs of the society's poorest members. People's centuries-old social conventions of seclusion have been shattered by this industry, which has also been quite successful in bringing them closer to the mainstream. The UN proclaimed 2005 to be the International Year of Microcredit in order to demonstrate the potential of microfinance as a significant weapon in the fight against poverty. The Noble Committee also believed that people may escape poverty with the aid of microfinance. In any developing nation, reducing poverty is regarded as a socially acceptable objective. The core poor are falling into the grip of poverty thanks to the inclusive microfinance policy, which makes it simple for them to obtain insurance, credit, savings, and other services.

2. STATEMENT OF THE PROBLEM

The goal of microfinance is to expand the boundaries of financial service delivery by offering financial services to the underprivileged who are not catered to by traditional formal financial institutions. Such financial services necessitate the use of creative distribution methods and channels. the demand for financial services that enable consumers to manage their resources more effectively and seize opportunities. One useful instrument among several for reducing poverty is microfinance. It should be utilized carefully, though, as despite recent assertions, there is no clear-cut relationship between microfinance and reducing poverty because poverty is a complicated issue with numerous barriers that the poor must overcome. We must comprehend when and how microfinance is suitable for the most impoverished; the technique, goods, and distribution channel are all interconnected and impact the potential and promise of reducing poverty.

For the impoverished, formal banking services are difficult to get. The primary obstacle faced by the impoverished when attempting to obtain loans from official financial institutions is the requirement for collateral that these organizations demand. Furthermore, obtaining a loan involves a number of bureaucratic steps that increase transaction costs for the underprivileged. They are not incentivized to receive loans from formal financial institutions. Formal financial institutions generally favor large-scale over small-scale transactions, non-agricultural over agricultural loans, and urban over rural sectors.

3. REVIEW OF LITERATURE

Olivares and Polance (2005) as a dependent variable along with other explanatory factors such as gender, competition, sustainability, lending methodology, and institution age. According to their findings, there is a negative correlation between loan size and age, indicating that smaller loans are provided by older MFIs. The average loan amount is a key indicator of helping the most impoverished members of society, according to another study by Mersland and Strom (2009). They discover a significant correlation between average profit and average loan size, suggesting that larger loans reflect MFIs' increased desire for profit. Christen and Drake (2002) demonstrate that profitability and depth outreach, as determined by average loan size, are positively correlated. Their research provides actual evidence that MFIs in Latin America are the most profitable due to a combination of three factors: rules, competition, and huge loan sizes.

Wagenaar (2012) has conducted research on mission drift and institutional change in microfinance organizations. He claims that donors put a lot of pressure on microfinance organizations to turn a profit. Some MFIs have changed from being non-profit to profit-oriented organizations as a result of this. He contends that achieving financial sustainability could result in less assistance for the most impoverished. The findings indicate a much higher loan amount and a smaller proportion of female borrowers in changed MFIs. This demonstrates how outreach is impacted by transformation, leading to a departure from the social mission in favor of business.

Cull et al. (2011) look into microfinance organizations that are regulated and those that are not. The findings indicate that licensed MFIs have larger loan amounts than unregulated NGO-style microfinance organizations. Lending to the poorer sector results in a fall in loan size and a rise in operating costs. In an effort to reduce or absorb these operating costs, MFIs are reportedly more inclined to serve wealthy clients, limit their outreach to the underprivileged, and raise loan amounts. Therefore, compared to non-regulated NGO-type institutions, regulated microfinance institutions are more likely to deviate from their social objective.

Rashid et al. (2011), microfinance has a beneficial effect on reducing poverty. They demonstrate how microfinance became crucial and successful in reducing poverty due to its larger funding, reduced interest rates, and easily accessible financial services. Zacharias (2008) demonstrated in another study that efficiency and average cost are inversely correlated. He has examined the topic of microfinance institutions' economics of scale and discovered evidence of scale efficiency. His research, which focuses on the relationship between size and operational costs, indicates that lesser costs are linked to larger firms. According to the study, average loan size and average cost have a negative correlation, which implies that increasing average loan and company size lowers operating costs.

Robert et al. (2011) investigate the trade-off between MFI efficiency and outreach. They discover that MFIs are more effective when they operate in nations with strong financial development. They discover that efficiency and outreach have a negative relationship, indicating that MFIs with lower loan amounts are less effective. Their results demonstrated that efficiency can only be attained when MFI shifts its attention away from the underprivileged sector.

Cull et al. (2007), there is no meaningful correlation between loan size and profitability. Results for individual lenders show that greater profits result in less outreach, which pushes away less wealthy customers. Village microbanks, which have high average costs and higher subsidies, concentrate primarily on making modest loans to the really poor. Few individual lending institutions realize their ultimate promises by aiming for both greater outreach to the impoverished and profitability, but these are unusual exceptions. Ultimately, their findings demonstrated that MFIs with more earnings tend to have poorer outreach and exclude the really poor from financial programs.

4. RESEARCH METHODOLOGY

This study's primary goal is to investigate how microfinance organizations are fulfilling their responsibility to combat poverty. Outreach to the poor and institutional financial sustainability—long-term anticipated outreach to reduce poverty—are among the goals of microfinance institutions.

The number of impoverished people who take part in microfinance programs is indicated by the scope of outreach. It is anticipated that increased outreach and greater service to the lowest people will result from a bigger number of borrowers. The current study uses the number of active borrowers to measure the scope of outreach. Based on the idea that outreach should be measured not only by the total number of borrowers but also by the number of poor borrowers, since their relative level of poverty is also taken into account, the depth of outreach measures the value of a borrower's net gain as a customer of the MFI program. When all else is equal, smaller loans show that poorer borrowers are served. The average loan size has been used as a stand-in for the scope of outreach. This study uses a mixed-method approach, integrating literature assessments of previous research and policy papers with quantitative data analysis. Data sets from governmental and international organizations are used to assess policy frameworks like the Priority Sector Lending (PSL) and Integrated Rural Development Program (IRDP) in order to conduct objective correlation and trend analysis.

5. RESULT AND DATA INTERPRETATION

Because credit lines to SHGs are dependent on a specific multiple of SHG members' bank savings accounts, they are severely constrained. Though the lack of aggregated savings among SHGs limits their potential, the collective savings of SHGs may provide a low-cost source of money for on-lending. Due to their informal status, SHGs are not eligible for commercial equity investments.

By obtaining funds from banks and other organizations and providing loans to people or members of SHGs or JLGs, Micro Finance Institutions (MFIs) play a crucial role in providing financial services to the nation's microfinance industry. Obtaining bulk loans from banks and other financial institutions is one of the ways that MFIs have been permitted to mobilize resources. Even while the SHG-Bank linkage program was well established before the majority of MFIs joined the microfinance space, the latter's operations expanded far more quickly than the former's. Compared to the official banking system, MFIs are more creative and active in their efforts to serve the impoverished in rural areas through efficient distribution channels. Based on the recommendations of the Malegam Committee, the Reserve Bank of India released guidelines for MFI lending operations. A new type of financial institutions known as NBFC-MFIs has been established, subject to meeting requirements pertaining to the amount of capital to be used, member lending, interest rate cap, margin retention, etc. Bank loans to MFIs are eligible under the priority sector category. MFIs have grown astronomically over the past three years as a result of RBI's updated rules and guidelines on NBFC-MFIs and banks' inclusion of loans to MFIs under priority sector.

TABLE-5.1: PROGRESS UNDER MFI-BANK LINKAGE

Particulars	2010-2011		2011-2012		2012-2013	
	No.MFIs	Amount	No.MFIs	Amount	No.MFIs	Amount
Loans disbursed by banks to MFIs	545	10282.49 (31.16%)	581	15190.13(47.73%)	647	20795.57 (36.90%)
Loans outstanding against MFIs as on 31 March	2422	16517.43 (14.50%)	4662	22500.46 (36.22%)	2020	25580.84 (13.69%)
Loan Outstanding as % of Fresh Loan		160.64		148.13		123.00

Source: NABARD Report 2012-2013

Table 5.2 Progress under Microfinance - Savings of SHGs with Banks Region-Wise Position as on 31 March 2013

Region	Commercial Banks		Regional Rural Banks		Co-operative Banks	
	No. of SHGs	Saving Amount	No. of SHGs	Saving Amount	No. of SHGs	Saving Amount
Northern Region	154137	26059.08	120455	11782.03	118883	7172.93
North Eastern Region	107737	7609.42	271305	9713.27	50781	1703.64

Eastern Region	694646	88910.82	553014	86688.88	452446	72752.08
Central Region	324838	51811.44	452386	29941.31	38429	2355.92
Western Region	476739	52221.90	155687	10159.21	385623	43322.75
Southern Region	2382014	676776.11	703964	100143.43	459918	90014.79
Total	4140111	903388.77	2256811	248428.13	1506080	217322.11

Source: NABARD Report 2012-2013

TABLE 5.3 PROGRESS UNDER MICROFINANCE - BANK LOANS DISBURSED TO SHGS AGENCY-WISE POSITION DURING 2012-13

Name of the Agency	Loans disbursed to SHGs by Banks during the year		Out of Total -Under SGSY		Out of Total –Exclusive Women SHGs	
	No. of SHGs	Loan disbursed	No. of SHGs	Loans disbursed	No. of SHGs	Loans disbursed
Commercial Banks	1132281	2518497.23	511745	1137201.78	972524	2296692.09
Regional Rural Banks	470399	916492.88	271423	482639.00	456352	900746.18
Co-operative Banks	229643	293699.98	32364	58737.52	199795	243703.67
Total	**1832323**	**3728690.09**	**815532**	**1678578.30**	**1628671**	**3441141.94**

Source: NABARD Report 2012-2013

In India, microfinance has changed dramatically in recent years, both conceptually and practically. In India, microfinance has become a solid foundation for financing rural and development projects throughout time. Microfinance is accompanied by several drawbacks. In India, formal sector banks have historically only provided loans to middle-class and upper-class consumers, meeting the demands of the business sector. Similarly, because of the perceived dangers of lending to this sector, HFIs have not developed a loan product to meet the demands of the very low income segment in the housing market. The majority of current microfinance institutions are having trouble finding trained labor, which is needed for accounting at the local level. There is a high rate of trained staff turnover.

6. CONCLUSION

Microcredit and microfinance have been widely acknowledged as a means of achieving economic empowerment and the elimination of poverty. The majority of the world's poorest people reside in rural areas, therefore microfinance is a means of combating poverty there. Poor people can start their own small businesses by obtaining small amounts of finance at affordable interest rates. Numerous studies demonstrate that those in poverty have greater payback rates than regular borrowers and are trustworthy. People in poverty can increase their income, accumulate assets, and protect themselves from outside shocks when they have access to financial services. By investing in improved housing, health, education, and nutrition, low-income households use microfinance to transition from daily survival to long-term planning.

Due to a lack of robust organizations offering such services, the majority of impoverished individuals are unable to obtain adequate financial services that satisfy their demands. Reputable organizations must charge enough to pay for their expenses. Recovering costs is not a goal unto itself. Instead, it is the sole means of achieving scale and influence that go beyond what contributors can afford. Other measures, such as infrastructural upgrades, job and training programs, or minor grants, will frequently be more effective at reducing poverty. Such services ought to be combined with construction savings whenever feasible. It demonstrates how easy access to and effective microcredit provision may help the impoverished manage their risks, smooth their consumption, progressively increase their assets, grow their microbusinesses, increase their ability to earn income, and live better lives. Additionally, microfinance services can aid with market expansion, resource allocation, and the adoption of improved technologies; as a result, microfinance supports economic growth and development.

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