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Research Paper

Road ahead for MFI's in Telangana

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ABSTRACT: *The CGAP (Consultative Group to Assist the Poor) defines "Microfinance or micro credit is the provision of financial services to low-income people."*
The Micro Finance Institutions (MFI's) have made inroads into the nook & corner of the country and more so into many of the unchartered territories where the reach of formal banking sources is negligible. MFI's have established themselves as an industry with loan portfolio in excess of Rs. 25000 cr. Few MFI's in their pursuit to make more profits have resorted to pushing of credit down the throat of borrowers with out properly assessing or diluting the loan appraisal processes. The loans have been bundled with articles like water purifiers, mobile phones, term insurance , weather policies which encouraged consumption trends rather than productive usage of loans. The Andhra Pradesh Micro Finance Institutions (Regulation of Money Lending) Act, 2010 has put the entire sector to a standstill. No business is happening. The Reserve Bank Of India has set certain guidelines for the conduct of this business.This paper tries to study the ramifications of this Act for the business and tries to explore the ways in which this business can be resumed to usher in new loans .
Keywords: *Micro Finance Institutions, Reserve Bank Of India, CGAP ,Porfolio , Appraisal, Credit*

I. INTRODUCTION

Micro Finance-"The term microfinance refers to provision of small-scale financial services and savings in rural , semi –urban and urban areas to the unbankables ,who are too poor to be served by regular banks , in most cases because they are unable to offer sufficient collateral."

Micro finance clients are often just below or above poverty line. Micro Finance Institutions (MFI's) had been the front runners in catering to the financial needs of unbanked sections of the society in our country. The sector has steadily progressed through initial hiccups and catapulting into a major industry till it hit a road block, bringing in a steep decline in its fortunes. Hyderabad had been the hub of MFI's in the country. The erstwhile Andhra Pradesh has contributed close to 40% of portfolio & 50% of borrowers of all major MFI's in the country.

MFI's had been contributing tremendously in the financial inclusion mission, rivaling the Government agencies doing similar activities. The business had blossomed & withered and it has to bloom again in the state of Telangana, albeit with treading the road more cautiously and conduct themselves as a responsible businesses. As the business crippled on account of Government intervention, it is for the Government to foster conditions conducive for resumption of business for the benefit of for banking deprived sections of the society.

The MFI's had been pioneers in taking financial services to the door steps of, hitherto sections who are in a way excluded from the gamut of formal financial services. The MFI's have aggressively traversed the length & breadth of the country venturing into many unchartered territories.

Let us glance through the business model of MFI's .

a. Grameen Model –Loan is advanced to a group of 20-30 members.
b. Joint Liability Group – Loan is advanced group of 3-6 members.

These both models rest on the principle of group liability i.e. "One for all & all for One".

MFI's had been doing brisk business with a portfolio of close to Rs. 25,000 cr & having borrowers exceeding 3cr no's. (State Of Sector Report , MFI , 2010) The micro-finance has been characterized by tiny loan sizes ranging from Rs. 3000- Rs. 50,000.The USP of these loans is with flexible repayments structures varying from weekly, fortnightly, monthly, half yearly etc.The striking feature of these MFI's is their high rate

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of recovery percentage in excess of 99%.This is one industry which is not prone to any sorts of economic recession. MFI's had been promoting economic empowerment with their focus on women members only. The Group itself is responsible for repayments as the group is formed by themselves. I.e. one member is responsible for the payments of rest of all members of his/ her group & vice –versa.

The distinctive feature of MFI's is the associate rendering services at the door steps of borrowers for loan application, appraisal, loan disbursement and repayment collections.The industry had not slowed down in the economic recession of 2008. This led to the focus of Corporates on this sector as it offers a decent rate of ROI and also satisfaction that they are associated with helping the cause of entrepreneurship ans empowerment. The direct benefits to the borrowers are least dependency on money lenders, banks who charge higher rates of interests and entail slow delivery process.The business has attained a massive scale with effective leverage on technology.As the business flourished, MFI's have drifted from their policy of lending to the borrowers helping them with access to financial services to profiteering.As the borrowers are from lower social hierarchy levels the business as a result led to meteoric rise in no of MFI's vying for same slice of the market.

As the MFI's in their greed to shore up loan no.'s and huge book size's have resorted to multiple lending to same borrowers. The borrowers ended up only to "borrowing from Paul to pay Peter".The credit appraisals were diluted, the loan sizes were inflated and the credit was pushed down the throat of borrowers. All this had an adverse impact with surge in loan defaults and MFI's adopting coercive practices for loan recovery, led to few borrowers ending life which erupted into a major, concerted resentment on part of borrowers to refuse payments. The political parties jumped on to the bandwagon urging borrowers to default. The Government too had its share in the collapse of this business. The national average loan out-standing is Rs. 7700=00 per borrower vis-a- vis Rs.65000=00 in Andhra Pradesh (Source :Micro Finance In India -Sector Overview: IFMR).

The then Andhra Pradesh Government brought out an ordinance APMFI Regulation , 2010 which regulated this sector with near impossible rules for MFI's to conduct business in Andhra Pradesh. The once citadel of MFI's of the Andhra Pradesh has crumbled with business coming to a grinding halt.

The Reserve Bank Of India intervened & constituted Malegam Committee which framed certain rules which has to be adopted for resuming business the prominent among them being.

a. Interest rate capping at 26% p.a.
b. Not more than two loans to a borrower at a time with loan outstanding not > Rs 50,000.
c. Credit bureau establishment

All this steps will ensure stream lining of business, but the major hindrance for MFI's in Telangana are.

1. The irrepairable damage caused to the repayment culture of MFI borrowers. No MFI is ready to test waters and burn a hole in their pockets , as already their enter portfolio in Andhra Pradesh has become a Non Performing Asset.(NPA).
2. Aggressive and arrogant nature of borrowers indulging in beating up MFI staff, burning of their offices.
3. Dragging about repayments.
4. Repayment evasive attitudes.

There is lot of demand for MFI loans among borrowers but proper harnessing is important. MFI's have to restart business and meticulously lend smaller loan amounts ,engage communities and build an ecosystem conducive for their business.

Shift from other activities like marketing, insurance to focus on stand alone loan portfolio & not insist on bundling of loan with other policies ,switch over from profiteering to profit making ,avoid poaching Self Help Group members. Proper credit appraisals to estimate borrowing & repayment abilities of loan applicants. Avoid over lending . Financial literacy programs to borrowers .

Proper training to staff in prudent behaving with women borrowers.

If above all steps are taken up there is a good scope for resurrection of MFI business in Telangana and MFI's too have to 'reinvent the wheel' of doing business in a transformed environment.

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