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**ROLE OF MICRO FINANCE IN RURAL DEVELOPMENT (WITH SPECIAL  
REFERENCE TO UTTARAKHAND)**

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**Abstract**

Micro Finance is the provision of a broad range of financial services such as deposits loans, payments, money transfers and insurance to the low income households and their micro enterprises. The basic purpose of micro finance is to provide access to financial assistance, including credit to the poor to enable them to start/expand micro enterprises to break out of poverty. Microfinance enables the poor people to be thriftily and helps them in availing the credit and other financial services for improving their income and living standards.

Micro finance is needed in two vital areas of national development mainly on alleviation and poverty and women's empowerment products and services and micro finance are targeted to the poor who make up nearly half of the total population. Focusing especially on women is another important need as women represent approximately 90 percent of the total participant enrolled in microfinance programmes.

Uttarakhand came into existence in year 2000. Women of Uttarakhand played a pivotal role in its struggle for existence. They are the backbone of Uttarkhand with their contribution in all economic and social sectors, still the women of this state face extremely difficult condition like ill-literacy, poverty, poor sanitation, poor nutrition, male bias etc. Micro finance can play a very important role in improving the condition of women in Uttarakhand by giving them financial independence.

## Introduction

Micro finance originally established to impel the money lender out of business and to bridge the capital gap apparently unfilled by the rural cooperatives and commercial banks. It is a collection of banking practice built to provide small loans and accepting saving or borrowing takes and important place for everyone, regardless of their income. Microfinance the service of time shifting, borrow money today to solve today's problem and paying the money bank in future, or saving money today for an event in the future. According to Otero (1999) Microfinance creates access to productive capital, which together with two others forms of capital-human capital addressed through education and vocational training and social capital built through creating representative, local organization building promoting democratizing systems and strengthening human rights enables people to move out of poverty. Micro Finance enables poor self employed people to create productive capital, to protect the capital they have, to deal with risk and to avoid the destruction of capital. It attempts to build assets and create wealth among people who lack becomes a liquidity tool that helps smooth their consumption pattern and to reduce their level of vulnerability.

Micro Finance is the provision of broad range of financial services to low income micro enterprises and households. The range of financial services to usually includes savings, loans, insurance, leasing and money transfers. On the other hand microcredit emphasizes on providing credit to low income clients. Microcredit is often associated with an insufficient appreciation of the value of saving services to the poor. Microfinance models usually refer to the products and services provide as well as the method in which they are provided. Internationally the most well known microfinance models include the Grameen Bank Model, the latin American solidarity group, community owned villages banks, savings and loan associations credit union and self help groups.

According to institutionalist, a significant impact on poverty can be achieved only if MFO's are financially self sufficient and independent from any subsidize funding from donor of government. Example of MFO's operate under institutionalist approach includes, Bank RabyatIndonasia, Bank Solidariode Ecuador and Uganda Microfinance Union.

On the other hand welfarist focuses on immidiate improvement of economic safety for the poor. They focused on providing at sub-sidized interest rate. MFO' who fall under his approach are heavily reliant on government subsidiary and grants as well as donor subsidiaries. Saving mobilization is not a part of the lending process in the approach e.g. of MFO' operate under institutionalist approach includes Gramin Bank Bangladesh, FINCA in Latin America and most of the MFO's in Africa and Asia.

Acc. to Noble Prize winner Dr. Mohammad Yunus MFO's are just like any other bank, but doing a completely different kind of job with a very different methodology. Once government framework for microcredit, banks and set up regulatory commission to supervise them, they can run like any other enterprises'.

MFO's typically offer a variety of loan products and saving services as well. MFO's are become financially viable moving towards self sustainability and essential to the communities in which the resources and expand services to client. The ability of most MFO's to leverage capital and manage external resources is generally by borrowing from formal financial institutions or large institutional and individual investors or accepting limited deposited from the public.

Ownership of microfinance organizations can be many types, such as owned by borrower themselves owned by borrower and private investors, owned by non-government organizations (NGO) and Co-operatives.

### **Objectives of Micro Finance**

Micro finance program is typically viewed as an economic development strategy where disadvantage groups basically not benefitted from involvement with the formal economic activities. MFO's are designed to improve access of the rural poor to financial services make them bankable clients and promote savings mobilization among them.

The primary objective of MFO's following welfarist approach is to alleviate poverty according to supporter of welfarist approach Doocy (2005) mentioned that 'the primary goal of most microfinance institutes is improving the economic status of segment of the population, most services provider aim for broader impact of enhanced well being, on the other hand institutionalist proponents argue that the primary objective of microfinance is financial deepening, the creations of a separate system of sustainable intermediation for the poor.

Another objective of microfinance is impact which is concerned. With what kind of impact MFO's have in their clients, their micro enterprise their household and their community. The objective of institutionalist is to achieve financial sufficiency.

Uttarakhand, a state spread over an area of around 53.4 thousand Km and dominated, by mostly hilly and mountain areas, is one of the most socio economically under developed states in India. The state is inhabited by about 8.5 million population. The agriculture and allied, activities including animal husbandry constitute the economic base and the main source of livelihood and employment for the people.

Moreover the concentration of labour force in agriculture sector continued to be dominantly for past several generations, though its proportions is considerably declining and shifting towards non-agricultural activities. The worker participation rate in the state constitutes at much higher level as compare to national average which makes up around 37%, 46% and males & 27.09% for females of the total workforce employed in different economic activities around 58%, comprising 44% among men and 84% among women are alone engaged in the farm sector.

In terms of contribution of different sectors towards state income, agriculture contributes around, 67% manufacturing activities 20.8% forestry & logging 8.78% and mining and quarrying 4.27. However the dominance of agricultural sector has been recognized losing its ground in terms of its share into the generated from non-agricultural sector has been appreciably increasing during the recent past periods. The consequence of declining share of income from agriculture sector have resulted the increasing shifts of over 3% of workers into non farm sector activities annually.

Uttarakhand the newly formed 27<sup>th</sup> state is still in transitional phase. The people of U.K. especially of backward rural hilly areas now expect that their problems of unemployment, illiteracy among rural people, poverty, agricultural problems, lack of infrastructural facilities migration would be looked upon in their own state.

Microfinance can prove to be a appropriate tool to solve the problems of rural areas of Uttarakhand. The study is descriptive nature therefore the work is based on secondary data.

The state of Uttarakhand which came into being as the 27<sup>th</sup> state of the Union of India on 9 Nov. 2000 has a population of 8,489 million. The density of population is less than 51 persons per sq.km. in upper Himalaya and 51 to 200 persons in Midel Himalaya and more than 200 persons per sq.km. in Shivalik & Terai regions of the state. Overall population density is less than 159 per sq. k. 58% of the work force in the state depend on agriculture dominated by small and fargmented land holdings. Per capita income of the state is Rs. 15,186 (US\$337). 36.4% of the state's population lives below poverty. The level of poverty varies extensively from district to district being as low as 17.6% in Haridwar district and as high as 68.5% in Uttarakhand district.

The formal banking structure in Uttarakhand is made up of mix of nationalize banks (1097 branches), regional rural banks (176 branches), 9 private banks (38 branches), 10 district cooperative banks (184 branches) and cooperative agriculture and rural development banks (20 branches). Of the total networks of branches, 56 percent are located in rural areas, 25 percent are in semi urban areas and 19 percent are in urban areas. Uttarakhand has one of the lowest credit-deposit ratios in India- only 20% of the total deposit of Rs. 155,210 million (US\$345 million) was lent in the region. The loan disbursement to weaker sections was only Rs. 4799 million in 2002-03. As on 31<sup>st</sup> March 2005, the average population per branch in the state was 7739, which compares well with all India average of 15,438. Within the state is varied between 5938 in Pauri Garhwal to 12060 in Haridwar District. The Agricultural Credit availability on per ha basis is similarity estimated at Rs. 9455 in the state as against the all India average of Rs. 7438 during 2004-05.

After the formation of Uttarakhand, vigorous efforts have been made to promote self-help groups with a view to tackle a myriad of Uttarakhand's problems. NABARD estimates that about 26,000 SHGs have been formed in the state (2005) and 5,550 about SKGs have

been credit linked with banks as on 31 March 2006. 79% of these SHGs were formed under the Swarna Jayanti Gram Swarojgar Yojana (Village Self Employment Plan) by District Rural Development Agency. Externally aided projects such as Uttaranchal Diversified Agriculture Support Project (6.67%), Swashakti (5%) and SWAJAL (4%), contributed to growing number of SHGs.

Though SHG movement has taken roots in all districts of the state. The spread, however, is uneven, Dehradun, Nainital, Tehri Garhwal and U.S. Nagar has 70% of the SHGs formed and linked with the banks. The average loan disbursement size is highest with the lead banks (SBI, Punjab National Bank, and bank of Baroda) and lowest among Cooperative banks.

#### Progress under SHGs Linkage with Banks as on March 2006

	No. of Banks	Groups formed	Linked	Amount Disbursed, million Rs.	Avg. amount disbursed Rs.	Amount outstanding as % amount disbursed
Lead Banks	3	3259	2785	203.24	72.977	212%
Non Lead Banks	21	587	481	39.44	81.996	289%
Regional Rural Banks	5	928	383	36.11	94.283	221%
Cooperative Banks	2	4003	1901	58.8	30.931	176%
Private Commercial Banks	10	0	0	0	0	0
Total All Banks	41	8777	5550	337.59	60827	217%

Source : Unpublished Report from Sachivalya

At present 37 NGOs have been extended a total grant assistance of Rs. 4.5 million for promotion and credit linkage of 2370 SHGs from NABARD on an add on basis since 2000-01. The IFAD – assisted Uttaranchal Livelihoods Improvement Project for the Himalayas (ULIPH)- Ajeevika in Hindi-will promote SHG among the ultra-poor in 17 blocks of the state. The projects livelihood finance arm will set up a Social Venture Capital Company (SVCC) with a view to promote enterprise in Uttarakhand using cooperatives. SIDBI has recently approved term loans for Pahal, Kotdwar, and ATI-sponsored Uma Matt is Uttarakhand.

The participatory Research in Asia (PRIA) purposively selected Himalayan Action Research Center (HARC) in Uttarakhand to study the SHGs in their areas. This Voluntary Development Organizations (VDOs) promoted and mobilized the SHGs for political participation. Indeed, promoting SHGs is part of its large programmatic goal of reforming local level governance.

### **Problems of Micro Finance**

Most microfinance institutions outsource a substantial part of their transaction tasks to their clients through some form of group intermediation. The groups are not remunerated for providing these services.

Despite their growing visibility, MFIs have not been successful in reaching the very poor. This is because their survival depends on significant scale and the management of large, low-cost loan portfolios.

One of the key failures of microfinance has been in its limited outreach to remoter areas and poorer people in them. NGO's that have worked in these areas mobilizing community groups with savings and credit activities have often produced poor financial performance and run the risk of making people poorer.

The number of SHGs is growing faster than targeted, the social and empowerment effects are not as a wide spread or as long lasting as perhaps hoped for the poor are included but not exclusively, and on the financial side, account keeping is weak.

A relatively small proportion of microfinance loans are used to finance crop farming enterprises most are taken to finance farming and processing activities, for livestock or for consumption.

MFI interest rate is high as 30-36 percent per annum plus in the initial years to mainly in the range of 20-24 percent per annum now. Several informed person politicians, bureaucrats, bankers and intellectuals find it hard to accept that the poor can pay interest rates in this range.

MFI find it difficult to achieve financial sustainability as they have to cover their costs, which include the market rate of funds plus transaction costs plus bad debit risk.

The pattern of ownership of MFIs and good governance are crucial to their sustainability. Ownership can be by charitable persons who do not personally benefit the MFI in any way (like NGOs), of member users (as cooperatives) or of investors (as in companies). Each ownership pattern has its problems and plus points.

MFIs grow & try to become like mainstream institutions, they lose their focus on serving poorer customers and move to serving the entrepreneurial poor or just those non-poor households which lack access to financial services.

### **Conclusion**

Microfinance originally established to impel the money lender out of business and to bridge the capital gap apparently unfilled by the rural cooperatives and commercial banks. It is a collection of banking practice build to provide small loans and accepting tiny saving or borrowing, takes in important place for everyone, regardless of their income. Microfinance is needed in two vital areas of national development mainly on alleviation of poverty and woman's empowerment.

The Indian experience has demonstrated that microfinance can be a participatory exercise and the banking system can deliver it sustainability. Instead of creating new institutions to deliver microfinance, it has enable linkage of groups of poor with the existing banking infrastructure. Though there are emerging issues which need to be addressed to make it sustainable in the long run, it shows that by involving voluntary organizations in social mobilization and creating an enabling policy environment, which offers flexibility, autonomy and the space for innovations, microfinance can achieve a vast scale and can become a national movement.

Many of these weakness are already being addressed, new savings products are being introduced and regulations are being changed to allow MFIs to offer them, some successful poverty alleviation interventions have been introduced; and a small number of institutions are typing down to bones to broaden their offerings by including other forms of assistance and to move 'up-market' in order to finance enterprises that create jobs rather than marginal forms of self-employment. Such initiatives are still few and far between, however, and they almost inevitably conflict with the need to be 'sustainable' and to squeeze out subsidies.



## Suggestions

- It is important to study the reasons behind the causes for low level of literacy of rural people in spite of them having high level of participation in terms of SHG movement.
- Government should take necessary steps to bring more number of educated persons in self help group.
- NGOs and Government should inculcate saving habits to self help group members.
- Self help group members are properly trained before launching their venture.
- It is widely spoken that Self help group members fail in many areas; they must be concentrated and proper guidance and counselling programmers to be arranged.
- Mostly uneducated people joint in self help group to avail loan from the bank to utilize mere subsidy granted by Government this habit must be avoided.
- Self help group review meeting should be conducted periodically.
- Literacy is tool for development. The affective participation always depends upon the educational background there is need to create learning environment and impart political and social knowledge among rural people in the SHG movement. They will help rural people the welfare schemes provided by the government and in turn help active participation.
- Evolve suitable training needs environment building on social awareness and factors of barriers for effective women participation in mainstream of the society.
- The banks, particularly private banks, should extend linkages with SHGs.
- Nationalized bank may support emerging MFI's in the state with near market loan and credit for on lending.
- The state government should publish on-line full contact addresses of all SHGs that exists in the state which will help development agencies to establish direct links with SHGs.
- The Government may assist in developing innovative financial products and services suitable for mountain communities, carbon copying MFIs of the plains cannot address the unique requirements of Uttarakhand. Set minimum performance standards for MFIs.
- To order to maintain financial sustainability the MFI source of funds should largely be deposits rather than borrowing.

- To minimize cash transactions by borrowers MFIs should heavily invest in computerization for reaching poor household like smart cards or e-cash.
- To reduce bad debt costs MFI's should offer a suite insurance to cover the various risks that borrowers face to their lives and livelihood-such as death of the borrower or a family member or if livestock, or crop failure, In such cases, insurance can be claimed and part of its can be used to repay the loan.
- The MFI should attract capital from mainstream investors. It should either let this market be taken over by banks and insurance companies, while the MFI become the servicer/partner.

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