

**BUSINESS MODELS OF MICRO FINANCING INSTITUTIONS  
NEED HOLISTIC CHANGE TO ACHIEVE THE DESIRED  
OBJECTIVE OF EMPOWERING POOR TO ATTAIN CAPABILITY  
AND CONFIDENCE TO EARN THEIR LIVELIHOOD WITH  
DIGNITY AND EASE**

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The recent spurt of suicides of farmers in various states of India particularly in Andhra Pradesh where MFIs have blossomed and provided a role model for other states to develop and nurture such institutions in their respective states to outreach poor people for alleviation of poverty and empowering them to undertake sustainable business and or farming. In fact in recent years these institutions have been highly acclaimed as most effective and sustainable institutions to outreach poor to fund them without any collateral to undertake some productive activities and also to assist them to meet some of their constant consumption expenditures also. In fact MFIs are gradually attaining the status of 'messiah of poor people' in some of the developing countries of the world. However models adopted were not always akin to each other. For example Grameen Bank model as developed in Bangladesh and in many other developed and developing countries of the world and widely acclaimed as poor man's bank has not been adopted by Indian MFIs.

There are formal and informal models developed over the years of purveying micro finance to the disadvantaged poor people. It may be interesting to note that most successful models so far developed are informal models. These informal models are conceived around 'group' of members residing in a village and agree to guarantee payment in case of default of any member for one reason or the other. Such groups work better when they voluntarily come together to resolve their credit and savings problems. Grameen Bank is most illustrious example of this model. It was started by Dr Mohd. Yunus to fund wives of landless farmers in Bangladesh. Over

the years it proved to be a very successful model as the groups were cohesive, receptive, voluntarily formed and extended loans for even consumption needs. Its success led it to become formal banks to garner savings of the poor and lend them without any collateral adequate funds to meet their emergent consumption and production needs.

Another informal mode called as 'NGO' has been developed in India, Ghana and Gambia to outreach poor women to fund them without any collateral at a rate of interest decided by the group forming the NGO. The rate of interest charged though quite high but definitely lower than usurious rate charged by the moneylenders. However these institutions largely depended on donor funds and savings of the groups. It is obvious therefore that these informal institutions succeeded well where donors were available and quality of service provided was comparable to any successful financial institution.

Similarly another informal group called Self Help Group has been conceived and nurtured by NABARD. These groups were formed by women mostly to undertake some business to supplement their family income. These were funded by the commercial banks and refinanced by NABARD. In recent years these are also getting finance directly from NABARD.

Over the years many formal institutions have also been developed to alleviate the poverty of the poor. MFIs are one of the latest and generally considered as one of the most successful model so far developed for the alleviation of poverty of disadvantaged people in our country. In fact its rapid and successful growth almost convinced most of us that at last we have been able to conceive and develop an appropriate model to serve our poor. But the fact was that all successes proclaimed by these institutions were not true as most of successes could be traced from unhealthy practices followed by them both while giving and collecting loans. In fact these institutions not only charged very high rate of interest but also adopted coercive and dubious ways to collect their dues. All these remain under the carpet as these institutions have been operating almost free from any oversight by the regulatory authorities or the government.

SIDBI in India has been designated to fund MFIs and also help these institutions to upgrade their technology to enable them to outreach poor people with least cost and maximum convenience. However despite these MFIs in general continue charging very high interest rates as they claimed that they source fund at high rates and undergo high risk as they lend money without any collateral.

Their main deficiency in management was very poor attention and efforts they provide to assess their risk. In fact risk assessment framework of MFIs was never been structured and formally designed with the help of latest methodology available in this regard. It appears it has been designed to protect the institution from downside risks and to reap advantages arising from upside risks. It did not introduce any systematic process to identify measure and monitor different types of risks that they may have to undergo while operating with a new class of borrowers whose financial literacy is almost nil and management skill is also not up to the mark. In fact it has to be conceived and developed with the application of innovative and imaginative skill of the management. The most essential need is to develop a feedback loop with the help of technology instead of depending upon manual feedbacks which not only get distorted while passing from one executive to the other but also imposes a heavy load of cost on the institution. However it would be needless to emphasize that there should be an in built internal culture of self supervision. In such a case threats and coercion would not be needed which unfortunately is very much prevalent in most of the MFIs in India. Risk apprehension could be minimized by consciously training and apprising as well as appraising various types of risks that MFIs have to undertake like other financial institutions—may be little more as these institutions lend without any collateral. In fact governance risk like inefficient oversight, inadequate knowledge with regard to borrowers are more serious and costly and therefore require better supervisor and technology to conduct the same with little cost and time. In this regard ASA has laid down some simple rules as stated below that would be worth practising to achieve the desired objective:

1. Develop simple products and standardize all procedures;
2. Introduce a strong credit culture within and outside the institution;
3. To develop alert signals and take instant action to avert impending risks;
4. To have the culture of transparency in all dealings; and
5. To introduce well documented oversight system with continuous feedback data from the field.

Besides strategizing to capture risk to avoid loss it would be necessary for these institutions to develop a participatory model so that poor people may not remain only a borrower from such institutions but also be a part of their management both in running these financing institutions but also to share the profit these institutions earned through lending to them. In fact such

participatory models not only benefit the borrowers but also the lending institutions as borrowers in such cases would not be wilful defaulters and they would also draw on the expertise and management skill of their lending institutions. In any case there would not be any coercion and outsmarting each other. The most healthy partnership could be formed in between public sector banks, MFIs and borrowers as a cluster group or groups created on the basis of trade and such other commercial activities as farming , food processing and tailoring with or without embroidery work and weaving etc.,

It is therefore very much painful to read the latest paper of Vijai Mahajan justifying the high rate of interest charged by the MFIs. It has been accepted by gullible poor borrowers and financially illiterate common people but it has obviously raised one pertinent question that how could he ignored the risks undertaken by poor borrowers as traders, artisans or farmers. These borrowers do not have steady income as has been assumed by him. Like MFIs they also face several types of risks that may seriously jeopardise their expected flow of income. It is further painful to read the observations of Akula that in case MFIs are forced to reduce rate of interest most of them would collapse. Akula himself has very successfully developed and taken full advantage of such growth personally should not have come out with such a statement. But perhaps this is most prevalent norms of our society as could be seen from the various schemes like NAREGAetc..

Indeed thee is need for paradigm change and not the knee jerk policy models that are under consideration by the RBI and Govt. of India. In fact RRBS, MFis and SHGs should work as partners and empower villagers to run their trade, business and farms without any hassle for fund and market support as well as market intelligence.