Role of Microfinance in Socio-Economic Development in Nepal

Shiv Narayan Chaudhary, Lecturer, Department of Management, M.M.A.M, Campus, Biratnagar

Email : chaudharishivanarayan02@gmail.com

Abstract

No systematic effort to map the distribution of microfinance has yet been undertaken. A benchmark was established by an analysis of 'alternative financial institutions' in the developing world in 2004. The authors counted approximately 665 million client accounts at over 3,000 institutions that are serving people who are poorer than those served by the commercial banks. Of these accounts, 120 million were with institutions normally understood to practice microfinance. Reflecting the diverse historical roots of the movement, however, they also included postal savings banks (318 million accounts), state agricultural and development banks (172 million accounts), financial cooperatives and credit unions (35 million accounts) and specialized rural banks (19 million accounts). Regionally, the highest concentration of these accounts was in India (188 million accounts representing 18% of the total national population). The lowest concentrations were in Latin America and the Caribbean (14 million accounts representing 3% of the total population) and Africa (27 million accounts representing 4% of the total population, with the highest rate of penetration in West Africa, and the highest growth rate in Eastern and Southern Africa Considering that most bank clients in the developed world need several active accounts to keep their affairs in order, these figures indicate that the task the microfinance movement has set for itself is still very far from finished. This paper attempts to study the role of Micro-Finance in socio-economic empowerment.

Keywords: Grameen bank, Microfinance, Socio-economic Development

Articles information Manuscript Receive : 20/10/2023, Review Date : 05/06/2024 Date of Acceptance : 23/09/2024, Publisher : TUTA, Mahendra Morang Adarsh Multiple Campus, Biratnagar Unit

Introduction

By type of service, "savings account in alternative finance institutions out number loans by about four to one. This is a worldwide pattern that does not vary much by region. An important source of detailed data on selected microfinance institutions is the Micro Banking Bulletin, which is published by Microfinance Information Exchange. At the end of 2009, it was tracking 1,084 MFIs that were serving 74 million borrowers ($38 billion in outstanding loans) and 67 million savers ($23 billion in deposits).

Another source of information regarding the environment of microfinance is the Global Microscope on the Microfinance Business Environment publication, prepared by the Economic Intelligence Unit (EIU), the Inter-American Development Bank, and others. The 2011 report contains informations on the environment of microfinance in 55 countries among two categories, Regulatory Framework and the Supporting Institutional Framework.

This publication, also known as the Microscope, was first developed in 2007, focusing only on Latin America and the Caribbean, but by 2009, this report had become a global study.

As yet there are no studies that indicate the scale or distributions of 'informal' microfinance organizations and informal associations that help people manage costs like weddings, funerals and sickness. Numerous case studies have been published however, indicating that these organizations, which are generally designed and managed by poor people themselves with little outside help, operate in most countries in the developing world. Help can come in the form of more and better-qualified staff, thus higher education is needed for microfinance institutions.

The micro credit era that began in 1970s has lost its momentum, to be replaced by a 'financial systems' approach. While microcredit achieved a great deal, especially in urban and near-urban areas and with entrepreneurial families, its progress in delivering financial services in less densely populated rural areas has been slow.

The new financial systems approach pragmatically acknowledges the richness of centuries of microfinance history and the immense diversity of institutions serving poor people in developing world today. It is also rooted in an increasing awareness of diversity of the financial service needs of the world's poorest people, and the diverse settings in which they live and work.

Brigit Helms in her books' Access for All: Building Inclusive Financial Systems', distinguish between four general categories of microfinance providers, and argues for a pro-active strategy of engagement with all of them to help achieve the goals of the microfinance movement.

Informal Financial Service Providers

These include moneylenders, pawnbrokers, savings collectors, money-guards, and input supply shops. Because they know each other well and live in the same community, they understand each other's financial circumstances and can offer very flexible, convenient and fast services. These services can also be costly and the choice of financial products limited and very short-term. Informal services that involve savings are also risky; many people lose their money.

Member-Owned Organizations

These include self-help groups, credit unions, and a variety of hybrid organizations like 'financial service association and CVECAs. Like their informal cousins, they are generally small and local, which means they have access of good knowledge about each other's financial circumstances and can offer convenience and flexibility. Grameen Bank is a member-owned organization. Since they are managed by poor people, their costs of operation are low. However, these providers may have little financial skill and can run into trouble when the economy turns down or their operations become too complex. Unless they are effectively regulated and supervised, they can be 'captured' by one or two influential leaders, and the members can lose their money.

NGOs

The Microcredit Summit Campaign counted 3,316 of these MFIs lending to about 133 millions clients by the end of 2006. Led by Grameen Bank and BRAC in Bangladesh, Prodem in Bolivia, Opportunity International and FINCA International, headquartered in Washington, DC, these NGOs have spread around the developing world in the past three decades; others, like the Gamelan Council, address larger regions, They have proven very innovative, pioneering banking techniques like solidarity lending, village banking and mobile banking that have overcome barriers to serving poor populations. However, with boards that don't necessarily represent either their capital or their customers, their governance structures can be fragile, and they can become overly dependent on external donors.

Formal Financial Institutions

In addition to commercial banks, these include state banks, agricultural development banks, savings banks, rural banks and non-bank financial institutions. They are regulated and supervised, offer a wider range of financial services, and control a branch network that can extend across the country and internationally. However, they have proved reluctant to adopt social missions, and due to their high costs of operations, often can'tdeliver services to poor or remote populations. The increasing use of alternative data in credit scoring, such as trade credit is increasing commercial banks' interest in microfinance.

With appropriate regulation and supervision, each of these institutional types can bring leverage to solving the microfinance problem. For example, efforts are being made to link self-help groups to commercial banks, to network member-owned organizations together to achieve economies of scale and scope, and to support effort by commercial banks to 'down-scale' by integrating mobile banking and e-payment technologies into their extensive branch networks.

The impact of microcredit is a subject of much controversy. Proponents state that it reduces poverty through higher employment and higher incomes. This is expected to lead to improved nutrition and improved education of the borrower's children. Some argue that microcredit empowers women. In the US and Canada, it is argued that microcredit helps recipients to graduate from welfare programs.

Critics say that microcredit has not increased incomes, but has driven poor households into a debt trap, in some cases even leading to suicide. They add that the money from loans is often used for durable consumer goods or consumption instead of being used for productive investments, that it fails to empower women, and that it has not improved health or education.

The available evidence indicates that in many cases microcredit has facilitated the creation and the growth of business. It has often generated self-employment, but it has not necessarily increased incomes after interest payments. In some cases it has driven borrowers into debt traps. There is no evidence that microcredit has empowered women. In short, microcredit has achieved much less than what its proponents said it would achieve, but its negative impacts have not been as drastic as some critics have argued. Microcredit is just one factor influencing the success of small business, whose success is influenced to a much larger extent by how much an economy or a particular market grows.

Role of Foreign Donors

The role of donors has also been questioned. CGAP recently commented that "a large proportion of the money they spend is not effective, either because it gets hug up in unsuccessful and often complicated funding mechanisms (for example, a government apex facility), or it goes to partners that are not held accountable for performance. In some cases, poorly conceived programs have retarded the development of inclusive financial systemsby distorting markets and displacing domestic commercial initiatives with cheap or free money."[5]

Working Conditions in Enterprises Affiliated to MFIS

There has also been criticism of micro lenders for not taking more responsibility for the working conditions of poor households, particularly when borrowers quasi-wage labourers, selling crafts or agricultural produce through an organization controlled by the MFI. The desire of MFIs to help their borrowers diversify and increase their incomes has sparked this type of relationship in several countries, most notably Bangladesh, where hundreds of thousands of borrowers effectively work as wage labourers for the marketing subsidiaries of Grameen Bank or BRAC. Critics maintain that there are few, if any, rules or standards in these cases governing working hours, holidays, working conditions, safety or child labour, and few inspection regimes to correct abuse.[6] Some of these concerns havebeen taken up by unions and socially responsible investment advocates.

Use of Loans

Practitioners and donors from the charitable side of microfinance frequently argue for restricting microcredit to loans for productive purposes—such as to start or expand a microenterprise. Those from the private-sector side respond that, because money is fungible, such a restriction is impossible to enforce, and that in any case it should not be up to rich people to determine how poor people use their money.

Microfinance and Poverty

In developing economies and particularly in rural areas, many activities that would be classified in the developed world as financial are not monetized: that is, money is not used to carry them out. This is often the case when people need the services money can provide but do not have dispensable funds required for those services, forcing them to revert to other means of acquiring them. In his recent book The Poor and Their Money, Stuart Rutherford cites several types of needs:[7]

- Lifecycle Needs: such as weddings, funerals, childbirth, education, homebuilding, widowhood and old age.
- Personal Emergencies: such as sickness, injury, unemployment, theft, harassment or death.
- Disasters: such as fires, floods, cyclones and man-made events like war or bulldozing of dwellings.

- Investment Opportunities: expanding a business, buying land or equipment,improving housing, securing a job (which often requires paying a large bribe),etc.

Poor people find creative and often collaborative ways to meet these needs, primarily through creating and exchanging different forms of non-cash value. Common substitutes for cash vary from country to country but typically include livestock, grains, jewellery and precious metals. In the 2000s, the microfinance industry's objective is to satisfy the unmet demand on a much larger scale, and to play a role in reducing poverty. While much progress has been made in developing a viable, commercial microfinance sector in the last few decades, several issues remain that need to be addressed before the industry will be able to satisfy massive worldwide demand. The obstacles or challenges to building a sound commercial microfinance industry include:

- Inappropriate donor subsidies.
- Poor regulation and supervision of deposit-taking MFIs
- Few MFIs that meet the needs for savings, remittances or insurance.
- Limited management capacity in MFIs.
- Institutional inefficiencies.
- Need for more dissemination and adoption of rural, agricultural microfinancemethodologies.

Historical Development of Microfinance in Nepal

Institutionally, micro credit program, an example of micro financing, was first introduced in Nepal in April 1956 when credit co-operative was established in Rapti Valley of Chitwan. Then, gradually the establishment of the co-operative bank and the Agriculture Development Bank were established in 1962 and 1986 respectively. We have already seen execution of many microfinance programs such as Small Farmer Development Program (SFDP) by Agriculture Development Bank Ltd. Production Credit for Rural Women (PCRW), Micro Credit Project for Women (MCPW), Garib Sanga Biseswar etc by Government. Rural Selfreliance Fund Project (RSRF) also provides credit for the microfinance. Rural Micro Finance Development Centre (RMDC) was also established to provide wholesale loan fund for microfinance. The Ninth Plan (1997-2002) and the Tenth Plan (2002-2007) accepted poverty reduction as their only objective. The current Interim Three Year Plan (2007-2009) has also given priority to the poverty alleviation and has focused on employment and equity and equality through social inclusion and targeted programs for the poor, recognizing the need to enhance accessibility of finance to the rural poor to promote their access to income generating activities. The government has started various 13 microfinance programs in Nepal . The main purpose of such programs is to empower them, enhance their capacity, increase their per capita income through self- employment activities and inspire and encourage small entrepreneurs by providing credit to them without any tangible collateral.

Conclusion

As proven by the success of the Grameen Bank, microloans can help reduce poverty and thereby promote realization of fundamental human rights. However, as with any new industry, there are twin dangers of both ignoring growing problems and over- reacting to the recent abuses. In order to avoid losing the benefits of microlending, national legislators should use international standards and comparative state practice to create more well informed and effective regulations. An attempt could be initiated to promote a cadre of new generation micro-finance leaders to strengthen the micro-finance institutions (MFIs) to optimise their contribution towards the sector's growth. Thus, with some renewed effort, substantial progress may be made in taking MFIs to the next orbit of significance and sustainability. This needs close monitoring of the on-going microfinance initiatives, suitable modification or formulation of innovative and forward-looking policies, based on the ground realities of successful MFIs in India. This, combined with a commercial approach from the MFIs in making micro-finance financially sustainable, will make this sector vibrant and help in achieving its single-minded mission of alleviating poverty through providing financial services to the poor.

References

Khandker, Shahidur R.: Fighting Poverty with Microcredit, Bangladesh edition, The University Press Ltd, Dhaka, 1999, p. 78.

Christen, Rosenberg & Jayadeva,: Financial Institutions with a double-bottom line : Implications for the future of Microfinance, CGAP/World Bank, Occasional Paper, July 2004, Washington, D.C Pp5–6.

Brigit, Helms.: Access for All: Building Inclusive Financial Systems. CGAP/World Bank, Washington D.C., 2006, pp. 35-57.

"State of the Microcredit Summit Campaign Report 2007", Microcredit Summit Campaign, Washington, 2007."

Brigit Helms.: Access for All: Building Inclusive Financial Systems. CGAP/World Bank, Washington D.C., 2006, p-97.

Chowdhury, Farooque: The metamorphosis of the micro-credit debtor, New Age, Magazine, June 24, 2007, P.7

Rutherford, Stuart: The Poor and Their Money. Oxford University Press, New Delhi, 2000, p. 4.