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RESEARCH ARTICLE

SOURCES OF FINANCE TO THE POOR ALONGWITH MICROFINANCE.

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Abstract

Before MFIs and NGOs, people had already been accustomed with other sources of finance and now both MFIs and NGOs are trying to fill up the gap that was created by these sources. Credit cooperatives, postal unions, savings banks, and government sponsored subsidized credit schemes predate microcredit and continue to exist. Even though these sources are still prevalent in many society MFIs and NGOs are trying to remove the ill effects of these sources and create a more positive financial atmosphere for the rural poor.

Introduction:-

Finance is an important aspect in fulfilling the basic needs of the human being. But when it comes to the rural poor section of the society sources of finance becomes limited and hence they are unable to come out of their state. Before MFIs and NGOs, people had already been accustomed with other sources of finance and now both MFIs and NGOs are trying to fill up the gap that was created by these sources. Even though these sources are still prevalent in many society MFIs and NGOs are trying to remove the ill effects of these sources and create a more positive financial atmosphere for the rural poor.

Financial support other than microfinance:-

To say that microfinance provides the poor with access to finance would be misleading. The poor already have a variety of ways to borrow. Contrary to popular images of informal finance, the moneylender is only one source of informal credit. Others include friends and family, the middlemen that provide them with access to the market and the community general store where they make their routine purchases.

In fact, borrowing between family members, neighbors and friends is so common that a study of rural Nigeria found that on average a typical household was 2.5 times more a borrower and a lender among themselves (Urdy 1994). Similarly, obtaining merchandise or supplier credit is standard business practice in the informal economy, though access can depend on non- economic criteria, such as ethnicity (Biggs, Raturi and Srivastava 2002). For example Jain diamond merchants in India usually obtain supplier credit from their own community as it is easier for them to trust people in their own community (Biggs, Raturi and Srivastava 2002). It even suggests that currently active microcredit clients routinely tap into multiple sources of informal credit.

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Of course, credit is not the only informal financial service. Some form of informal savings clubs or rotating savings and credit associations (ROSCAs)[1], are available in most regions of the global South, and average participation rates are reported to be exceptionally high, ranging between 50 to 95 percent in countries such as Nigeria, Kenya and the Ivory Coast (Bouman 1995). Roscas have traditionally been viewed as a savings mechanism for individuals with no access to formal savings or credit products (Levenson and Besley 1996). But new evidence suggests that even when formal mechanisms are available, individuals, especially women, continue to use roscas for different reasons, such as protecting their money from their husbands (Anderson and Baland 2002).

Thus, the poor regularly get into a varied network of financial services. The literature on financial access and microfinance does not include these informal financial services within the microfinance umbrella. In fact, it considers informal finance to be a less than ideal mode of financial service delivery that is assumed to automatically disappear as soon as formal microfinance arrives on the scene.

Microfinance seeks to distinguish itself from informal finance by arguing that it provides non-exploitative, predictable and transparent access to finance (Roodman 2012). Critics of informal credit say that it is an unpredictable source of finance, it can be exploitative, and if the poor are borrowing from members of their own community then their lenders are likely to be poor also, which implies that the amount borrowed is limited to how much the lender can afford to give (Collins, et al. 2009).

But the prevalent microcredit narrative against informal finance centres on the image of a threatening moneylender who charges such high rates of interest that the debt sometimes becomes impossible to be paid back in full. While this is true of a good number of moneylenders across the globe, where pay-day loan shops and credit card companies are considerably huge and prevalent, it is certainly not true of the entire spectrum of informal finance. In fact, a study of rural finance in China finds that borrowing from friends and family does not bear any interest at all, which has made it hard for rural credit cooperatives to penetrate in the region. The authors of the study predict that these same social networks will also crowd out registered MFIs. (Turvey and Kong 2009)

Scholars argue that informal credit is easy to access, is available in small denominations, for very short periods, and involves highly flexible loan agreements that are subject to change even during the duration of the loan depending on the borrower's circumstances (Srinivas 1993). In one study, Banerjee and Duflo(2011) looked at various slums in Hyderabad, India and discovered that even in areas with an active microfinance presence, only one-fourth of families were borrowing from microfinance institutions, though more than 50 percent remained clients of the local moneylender, despite having to pay higher rates of interest to the latter. They concluded that the moneylender's flexibility on repayment made him a more popular choice.

Similarly, it is also misleading to imply that before microfinance there were no other formal mechanisms to provide the poor with credit. Credit cooperatives, postal unions, savings banks, and government sponsored subsidized credit schemes predate microcredit and continue to exist (Roodman 2012). For instance, the World Council of Credit Unions reports that there are currently 55,952 credit unions across 101 countries (2012). This data does not include China, where the government runs an estimated 40,000 rural credit cooperatives (Ong 2013).

A rotating savings and credit association or ROSCA, is a group of individuals who agree to meet for a defined period in order to save and borrow together, a form of combined peer-to-peer banking and peer-to-peer lending.

Figure 1:-Financial support other than microfinance.

But critics contend that government sponsored interventions are generally corrupt, inefficient and most of the credit does not reach the poor because of political connections and bribery (Roodman 2012) (Braverman and Gausch 1986). In comparison, as a private sector intervention microfinance is expected to be less susceptible to these problems. In the study by Guha and Ghosh(2015), it is seen that micro-entrepreneurs (MEs) accrue more economic gains if they borrow from the microfinance institutions (MFIs) instead of informal moneylenders and earn high level of profit per sale ratio if they invest high start-up capital, bear low costs per month and borrow from any type of MFI. The younger MEs have a higher chance of achieving higher profit per sale ratio. In terms of asset ownership, it was found that there is a significant difference between the micro-enterpreneurs (MEs) of the Annapurna Mahila Multi State Co-operative Credit Society Limited (AMCCSL) and a community- based MFI and the Svasti Microfinance Private Limited (SMFPL), a NBFC–MFI. A higher proportion of MEs of the AMCCSL own financial assets, land assets and capital assets than the MEs of the SMFPL. In this context, the study concludes that community-based MFI like the AMCCSL are a more suitable institutional structure of MFI that helps clients to achieve higher economic gain in terms of accumulation asset (Guha and Ghosh 2015).

Poverty reduction is a top priority of Microfinance Institutions (MFIs). MFIs operate under the assumption that with access to credit, the poor can create stable sources of income that enable them to escape poverty. MFIs also recognize that microfinance is not by itself sufficient to reduce poverty, but it is a necessary tool that bridges the gap between macroeconomic development efforts, mainly in larger cities, and rural development, which is rarely targeted by macroeconomic development programs. Understanding MFIs goals and limitations will greatly facilitate understanding the literature in the correct context: its relevance to assessing MFIs as a tool to aid poverty alleviation, not as miraculous solution to global poverty.

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