RESEARCH WORK ON IMPACT OF MICROFINANCE ON DEVELOPMENT OF MICRO AND SMALL ENTERPRISES

ABSTRACT

Microfinance emerged as a noble substitute for informal credit and an effective and powerful instrument for poverty reduction among people, who are economically active, but financially constrained and vulnerable in various countries. Microfinance covers a broad range of financial services including loans, deposits and payment services and insurance to the poor and low-income households and their micro enterprises. Microfinance institutions have shown a significant contribution towards the poor in rural, semi urban or urban areas for enabling them to raise their income level and living standards in various countries.

In developing countries like India the structure of economy is dualistic. The rich get richer and the poor get poorer. This worsens the access of poor to economic opportunities and reaches for formal financial services. Small enterprises in India suffer from a great deal of indebtedness and are subject to exploitation in the credit market through high interest rates and lack of convenient access to credit. They need credit to fund their working capital needs on a day-to-day basis as well as long term needs like emergencies or other income related activities. So the need for financial assistance and business development services for the micro and small enterprises is essential to alleviate poverty for consistent economic growth. The focus of the study is to find out whether these micro and small enterprises in and around Coimbatore city of Tamil Nadu were able to access Micro Finance Institutions (MFIs) for capital loans and services and utilize it for their growth and development.

INTRODUCTION

Microfinance is not a new concept. It dates back in the 19th century when money lenders were informally performing the role of now formal financial institutions. Over the past two decades, various development approaches have been devised by policymakers, international development agencies, non-governmental organizations, and others aimed at poverty reduction in developing countries. One of these strategies, which have become increasingly popular since the early 1990s, involves microfinance schemes, which provide financial services in the form of savings and credit opportunities to the working poor (Johnson and Rogaly, 1997).
From the year 2000, Microfinance institutions in and around Coimbatore city have grown dramatically in terms of branches, groups, loan disbursement, number of loans, loans collected, savings clients etc. Microfinance has penetrated into rural areas of Coimbatore and Pollachi.

CONCEPT OF MICROFINANCE

Microfinance enables the poor and excluded section of people in the society who do not have an access to formal banking to build assets, diversity livelihood options and increase income, and reduce their vulnerability to economic stress. In the past, it has been experienced that the provision for financial products and services to poor people by MFIs can be practicable and sustainable as MFIs can cover their full costs through adequate interest spreads and by operating efficiently and effectively. Microfinance is not a magic solution that will propel all of its clients out of poverty. But various impact studies have demonstrated that microfinance is really benefiting the poor households (Littlefield and Rosenberg, 2004).

Microfinance is defined as a development tool that grants or provides financial services and products such as very small loans, savings, micro-leasing, micro-insurance and money transfer to assist the very or exceptionally poor in expanding or establishing their businesses (Robinson, 1998).

In addition to financial intermediation, some MFIs provide social intermediation services such as the formation of groups, development of self confidence and the training of members in that group on financial literacy and management (Ledgerwood, 1999). There are different providers of microfinance (MF) services and some of them are; Non Governmental Organizations (NGOs), savings and loans cooperatives, credit unions, government banks, commercial banks or non banking financial institutions. The target group of MFIs are self employed low income entrepreneurs who are; traders, seamstresses, street vendors, small farmers, hairdressers, rickshaw drivers, artisans blacksmith etc (Ledgerwood, 1999).

EVOLUTION OF MICROFINANCE

Microfinance as an industry evolved in all the third world countries almost at the same time span. World over, it was getting widely recognized that improving income levels of low income community is essential to improve their well-being. During the 1970s and 1980s, the microenterprise movement led to the emergence of Non-Governmental Organizations (NGOs) that provided small loans for the poor. One of the significant events that helped it gained prominence in the 1970s was through the efforts of Mohammad Yunus, a microfinance pioneer.
and founder of the Grameen Bank of Bangladesh. In 2006, Prof. Yunus was awarded Nobel Peace prize for his efforts to create economic and social development.

Microfinance in India started in the early 1980s with small efforts at forming informal Self Help Groups (SHGs) to provide access to much-needed savings and credit services. From this small beginning, the microfinance sector has grown significantly in the past decades. National bodies like the Small Industries Development Bank of India (SIDBI) and the National Bank for Agriculture and Rural Development (NABARD) are devoting significant time and financial resources to microfinance. The strength of the microfinance organizations (MFOs) in India is in the diversity of approaches and forms that have evolved over time.

STRUCTURE OF EXISTING MICROFINANCE INSTITUTIONS IN INDIA

Indian Microfinance Institutions are predominantly NGOs i.e., nearly 80 % of the Microfinance Institutions operate under the Society/Trust form which is for the not-for-profit sector with a clear development agenda. Apart from this, other important legal forms are being used by Indian Microfinance Institutions. 10 % of organizations operate under the company structure; 5% are section 25 companies (Section 25 of the Indian Companies Act, 1956); 2% as Cooperatives; 2% as Non Banking Finance Companies (NBFCs); and 1% as Local Area Banks (LAB). The Organization Structure of existing Micro Finance Institutions in India is given below (http://www.nabard.org/microfinance/ mf_institution.asp) accessed on June 25, 2012

a) Not for Profit Microfinance Institutions
   a.) NGO - Microfinance Institutions - 400 to 500 – Registered under Societies Registration Act, 1860 or similar provincial Acts Indian Trust Act, 1882
   b.) Non-profit Companies - 10 – Registered under Section 25 of the Companies Act, 1956

b) Mutual Benefit Microfinance Institutions
   a.) Mutually Aided Cooperative by State Government Societies (MACS) and similarly set up institutions - 200 to 250 – Registered under Mutually Aided Cooperative Societies Act enacted by State Government

c) For Profit Microfinance Institutions
   a.) Non-Banking Financial Companies (NBFCs) - 6* - Registered under Indian Companies Act, 1956 Reserve Bank of India Act, 1934
MICRO AND SMALL ENTERPRISES

The major barrier to the development of Micro and Small Enterprises is access to credit. These enterprises differ in the level in which they are and the products and services offered to them by the MFIs. The micro and small enterprises need to be financed differently and the financing is determined by whether the firm is in the start-up phase or existing one and also whether it is stable, unstable, or growing. Stable survivors are those who benefit in having access to the financial services provided by MFIs to meet up with their production and consumption needs. Unstable survivors are groups that are considered not credit worthy for financial services to be provided in a sustainable way and Growth enterprises are Micro and Small Enterprises with high possibility to grow.

In identifying the market, MFIs consider whether to focus on already existing entrepreneurs or on potential entrepreneurs seeking for funds to start up a business venture. Working capital is the main hindrance in the development of already existing SMEs and to meet up, the borrow finance mostly from informal financial services which have high interest rates and services offered by the formal sector or not offered by these informal financial services.

The business activity of a microenterprise is equally as important as the level of business development. There are three main primary sector where an enterprise may be classified; production, agriculture and services. Each of these sectors has its own risk and financing needs that are specific to that sector.

PRODUCTS AND SERVICES BY MICROFINANCE INSTITUTIONS

Products and services offered by microfinance institutions in and around Coimbatore for the development of Micro and Small Enterprises are basically classified as two i.e. Financial Intermediation and Enterprise development services.

Financial intermediation: Providing financial assistance for small business groups in the form of business loans and those loans can be utilized for further investment in the existing business or setting up new tiny business ventures. Since the rate of interest and the repayment schedule are
formulated to suit the requirements of the loan takers, there exists enormous demands for this product. MFI s extends such microloans ranging from Rs.5000/- to Rs.25,000/- for such income generating activities and few MFI s categorized their clients activities as farm based activities which includes Agriculture, Poultry, Sheep-rearing, Goat-rearing, sericulture, mushroom cultivation etc and non – farm based activities which includes Petty-shop, Catering, Provision shop, Tailoring, Embroidery work, Beauty shop Vegetable vendor, Fruit Vendor, Textile shop, Xerox machine, Brick making, Gold covering work, Jewelers work and others etc. The loans are taken by poor households directly as well as through groups to meet their diverse needs.

**Enterprise development services:** MFI s provides cost efficient microfinance coupled with knowledge and information services that raise human capacity and organizational capability and create open access to markets resulting in more productive loans. MFI s provide skill development services, business training, marketing and technology services to their clients based on their occupation which helps them use their resources more productively.

**GROWTH AND DEVELOPMENT OF MICRO AND SMALL ENTERPRISES**

The term growth in this context can be defined as an increase in size or other objects that can be quantified or a process of changes or improvements. The firm size is the result of firm growth over a period of time and it should be noted that firm growth is a process while firm size is a state (Penrose, 1995). The growth of a firm can be determined by supply of capital, labour and appropriate management and opportunities for investments that are profitable. The determining factor for a firm’s growth is the availability of resources to the firm (Ghoshal, Halm and Moran, 2002.)

MFI s considering the growth of Micro and Small enterprises developed large-scale operations by offering a few highly standardized products with few advantages like Streamlined loan administration, Simplified decision-making for field staffs, Reduced information requirements from clients, Low operational costs, Simplified repayment obligations. But this standardization also had its own disadvantages. So MFI s paid closer attention to product flexibility. Individual need-based loans are more suitable as they can be designed to cater to the specific requirements of the clients.

**REVIEW OF LITERATURE**
Maruthi Ram Prasad, Sunitha and Laxmi Sunitha (2011) conducted a study on Emergency and Impact of Micro-Finance on Indian Scenario. After the pioneering efforts by Government, Banks, NGOs, etc the microfinance scene in India has reached in take off stage. An attempt could be initiated to promote a cadre of new generation micro-credit leaders in order to strengthen the emergence of Micro-Finance Institution (MFIs), so as to optimize their contribution towards the growth of the sector and poverty alleviation. Each Indian state could consider forming multi-party working group to meet with microfinance leaders and have a dialogue with them about how the policy environment could be made more supportive and to clear up misperceptions. With one state leading the way, we need to build on a successful model. By unleashing the entrepreneurial talent of the poor, we will slowly but surely transform India in ways we can only begin.

Idowu Friday Christopher (2010) conducted a study to find the Impact of Microfinance on Small and Medium-Sized Enterprises in Nigeria. The fundamental objective of this study is to assess the impact of Microfinance on Small and Medium Enterprises (SMEs) in Nigeria. Simple random sampling technique was employed in selecting the 100 SMEs that constituted the sample size of the research. Structured questionnaire was designed to facilitate the acquisition of relevant data which was used for analysis. Descriptive statistics which involves simple percentage graphical charts and illustrations was tactically applied in data presentations and analysis. The findings of the study reveal that significant number of the SMEs benefitted from the MFIs loans even though only few of them were capable enough to secure the required amount needed. Interestingly, majority of the SMEs acknowledge positive contributions of MFIs loans towards promoting their market share, product innovation achieving market excellence and the overall economic company competitive advantage. Other than tax incentives and financial supports, it is recommended that Government should try to provide sufficient infrastructural facilities such as electricity, good road network and training institutions to support SMEs in Nigeria.

Chiyah Boma Ngehnevu Forchu Zachary Nembo (2010) conducted a study on The Impact of Micro Finance Institutions (MFIs) in the Development of Small and Medium Size Businesses (SMEs) in Cameroon Microfinance is a term used by many in different domains to fight poverty. Poverty is a syndrome that is affecting the developing countries and especially in sub Saharan Africa. This thesis is focused on three specific objectives: The first of them is to
investigate whether CamCCUL helps its members and/or customers in developing their small or medium size businesses. The second aim is to find out whether rural SMEs can secure micro-financing with ease and on reasonable terms. Lastly, to determine if there are underlying factors, such as size of operation, securable wealth, or gender of application, is a factor in getting a loan. In order to accomplish the task, we had to gather data from primary and secondary sources in the rural areas of Cameroon. The primary sources were from questionnaires and interviews. The population was drawn from two different groups; the members of CamCCUL and the credit unions constituting CamCCUL league. We made use of closed and open ended questions. The responses were analysed using percentage frequency tables.

From the information that we have, it is realized that CamCCUL has a positive impact in the development of the members’ businesses. CamCCUL provide its members with financial and social intermediation services to help improve their businesses. Securing micro-financing by SMEs is determined by the stage or level of development in which the business is. Businesses that are viewed as growing had it easy to get a loan. But the main criteria used were the ability to pay back and to meet the set requirements to obtain a loan. The main requirement is fixed tangible assets such as land.

We noticed that the poorest of the poor were not included in designing and implementing their policies. The entry requirements are difficult for the poorest to meet thus they do not enjoy the services of CamCCUL. We can say that the poorest are those who are not involved in any income generating activities.


Results of this study find several interesting issues, such as Microfinance has positive impact to improvement of MSE’s Performance Indicated by sales, the difference of regional characteristic of MSE is also play role in determining its business scale. Since doubling amount of loan has negative impact to the performance, it’s very Important to allocate the loan to the productive activities, such as investment, in the way to improve the business opportunity.
Sam Afrane (2002) conducted a study on Impact Assessment of Microfinance Interventions in Ghana and South Africa Synthesis of Major Impacts and Lessons. Delivery of microcredit to operators of small and microenterprises (SMEs) in developing countries is increasingly being viewed as a strategic means of assisting the so-called “working poor” (ILO, 1973). Over the past decade, a considerable amount of multi- and bilateral aid has been channeled into microfinance programs in the Third World with varying degrees of success. Like all development interventions, donors, governments, and other interested parties demand evaluations and impact assessment studies to ascertain the achievements and failures of these programs. This paper reviews two such studies conducted in Ghana and South Africa that focused mainly on impact results. The outcomes of the two case studies have established that microfinance interventions have achieved significant improvements in terms of increased business incomes, improved access to life-enhancing facilities, and empowerment of people, particularly women.

Bhasin and Akpalu (2001) conducted a study on Impact of Micro-Finance Enterprises on The Efficiency of Micro-Enterprises in Cape Coast.

It has been observed that the NBSSI has been performing very well as far as the training services are concerned. As far as the provision of credit is concerned, NBSSI has not performed well according to the expectations of hairdressers, dressmakers and wood-processors because of lack of funds. It has been observed that the informal sector caters for the needs of these micro-enterprises and they generally take loans from their friends/relatives and suppliers/clients. There exist many variations in the efficiency of hairdressers, dressmakers and wood-processors within each group and across these groups, which indicates that there is ample scope for raising the level of efficiency in these micro-enterprises. The most significant determinants of technical efficiencies of hairdressers, dressmakers and wood-processors are the age of operator, business experience, level of education, training programmes, credit, and contact with the lender.

SIGNIFICANCE OF THE STUDY

To justify the importance of the current study, it is important to mention this area of study is very important for the development of socio economic activities in developing countries like India and its contribution to the development of micro and small enterprises. The study of this
nature is essential to identify the role of MFIs products and services in small and microenterprises sector. This will enhance to indentify MFI’s and their contribution to the rural population in accessing to financial services in their localities to boost their living standards in a sustainable manner.

OBJECTIVES OF THE STUDY

The specific objectives of the study are to:

- To analyze the total capital invested by micro and small enterprises and to identify the contribution of financing through MFIs.
- To study the effective utilization of capital loans provided by MFIs to micro and small enterprises.
- To investigate whether capital loans and services of MFIs to micro and small enterprises lead to the growth and development of the organization.

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I seek opinion from the reviewer on the following areas

- Scope of this study in future
- Availability of data for the study
- Opinion on research objectives
- Any other relevant information

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