RE DEFINING MICRO FINANCE

By

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Finance is one field where we have witnessed significant innovations in recent decades. Earlier, we could only visualize social change in rural India because villages were so deeply mired in caste conflicts. These conflicts had engendered local tyrannies and subverted the social order, resulting in bondage and servitude for significant portions of the population for generations. In the 1970s, the locus of change shifted to other areas, which worked in leveling caste divisions and neutralizing feudal overlords. Finance was the pivot of this process of change.

When I began life as a rural banker in the 1970s, outsiders rarely visited the villages. Those who did, other than the occasional anthropologist, government extension officer, family planning staff of the government or census worker, were missionaries of various religions. Over the years, I noticed that the balance shifted from outsiders bringing religion to outsiders bringing finance. Of course, those who lived in the villages already had both. As an ancient Indian proverb has it, a village can be formed wherever there come together a river, a priest, and a moneylender. This gradual change in the profile of visitors and reformers was my first introduction to the then-embryonic revolution in development finance which later grew into the niche of social banking.

With globalization and liberalization, a shift from the socialist to the capitalist approach was evident. Banks had bled badly in the government-mandated programs for eradication of poverty. They realized that age-old nostrums of finance could not be compromised; a new way had to be found to engage with the poor. Development finance emerged as the much-touted miracle for combating poverty. The eventual arrival of microfinance further strengthened the efforts .An important tool of development finance is microfinance .But in contrast to the microfinance model of public banks where the interest rates are reasonable, the rates of private microfinance operators are quite steep, being in the band of 20%-26%

In nearly three decades of academic work and grassroots involvement as an administrator of financial programs in local rural development, my experience is that microfinance programs that are run on the principle of building huge returns for investors most often spell the death of the local economy. Microfinance institutions were meant to free villagers and urban slum dwellers from the moneylenders' grip. But lack of regulatory oversight, unbridled political cynicism and the myopic herd-like mentality of the private sector combined to threaten pushing India's poor in the arms of the moneylenders again. Microfinance institutions have to re-jig their agenda: moderate profit, re-infuse the spirit of social responsibility and restrain their greedy impulses. They still enjoy enormous client support and if their mission remains clear and they remain true to it, no politician can dare challenge them. The electorate has demonstrated that it can't be swayed by populism and sloganeering. It wants development and transparency in administration. We are a vibrant democracy with a sense of maturity and robust common sense even amongst the poor. Had it not been for this, the poor would not have been able to bring such a powerful microfinance lobby, with international support, to its feet.

The narrow idea that capitalism is only about creating value for shareholders, that business is only about profits and the excesses to which the story has led around the world, is badly broken. Adam Smith, the father of capitalism, understood that capitalism works only when people tell the truth and have a sense of justice. Ethics and business go together at the core of capitalism. “Business is a very beautiful mechanism to solve problems, but we never use it for that purpose. We only use it to make money. It satisfies our selfish interest but not our collective interest,” states Muhammad Yunus. “I’m not against making money, but I am saying we can do both. We have designed a capitalist system wrong. We assume human beings are one-dimensional—all they do is make money—so we’ve created a money-centric world. Money commands everything because that’s our interpretation of capitalism … what kind of world is that? It’s a very uncomfortable interpretation of a human being. We have been turned into robots. Yes we are selfish, but also selfless, but we don’t allow that to be brought out.”

In some ways the microfinance that is seen is today is not recognizable as the one that was there in the initial days. The sector must change with passage of time. While products and processes can change (hopefully for the better), can the concern for the customer change? Microfinance players justified their existence on the argument that banks do not finance the poorest and are not empathetic to their requirements. Is the MFI sector better able to deal with poor customers today than the banks? Many MFIs started financing the poor but somewhere they lost the customer focus and along with that the mission too. The goals do not any more seem to be making credit access affordable; nor is it accompanying the livelihoods of people. It is no more about improving income generation in the hands of the customers. Book value multiples, price to earnings ratios and enterprise valuations dominate the discussion. High interest rates are justified as necessary to find more mainstream funds for further growth.

The biggest disadvantage of the MFI model is that it is less participatory and empowering, since the “banking” functions and procedures are taken care of entirely by field staff of the MFI, who disburse and collect loans. In

It may appear that the naysayers are ready to sound the bugle and shout out “The king is dead, long living the king”, that microfinance can no longer be relevant to the poor. But there is its hope; microfinance may once more redefine itself and in its new avatar be a leaner, more modest business with lesser interest rates and moderate profit that yet continue to be profitable. Only time will tell.