Financial Inclusion through Microfinance: Evidences from Kerala

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Abstract

Financial inclusion is viewed as the most powerful instrument to accomplish inclusive growth and sustainable development. Microfinance has been perceived and acknowledged as an effective tool for attaining greater financial inclusion. The present study seeks to evaluate the capacity of the microfinance programmes in guaranteeing financial services to the poor households in Kerala. The study highlighted the ability of the microfinance programmes to extend financial inclusion to unbanked vulnerable sections of the population. Due to the intervention of microfinance, almost all the clients could access banking services substantially which empowered them to free from the clutches of money-lenders. Moreover, Microfinance programme inculcated a habit of regular savings for all the clients. The variables such as age of the client, social class of the client, economic class and years of active participation in microfinance programme, are found to be significant determinants of degree of financial inclusion made through microfinance.

Key Words: Financial inclusion, Kerala, Kudumbashree, Microfinance, NGOs.

Introduction

Financial inclusion is viewed as the most powerful instrument to accomplish inclusive growth and sustainable development. Financial inclusion visualises low-cost banking services to the financially excluded population and regions of the country. A society can be regarded as financially inclusive when all sections of the society have access to timely and adequate volume of formal credit and other financial services. The Committee on Financial Inclusion, Government of India, has defined "Financial inclusion as the process of ensuring access to financial services and timely and adequately credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost" (The Committee on Financial Inclusion, 2008). Financial inclusion focuses on bringing the unbanked households into the financial mainstream (Teki and Mishra, 2012). The essence of financial inclusion is to guarantee delivery of financial services which incorporate - opening up of bank accounts, easy access of credit, insurance facilities, etc. (Nair, 2005). The connection between inclusive growth and financial inclusion has been perceived in India's development strategy. Greater financial inclusion is a catalyst for speeding up the inclusive growth. Financial inclusion can create win-win environment for both clients as well as financial institutions in an economy (Thorat, 2006).

Microfinance has been perceived and acknowledged as a effective tool for attaining greater financial inclusion. The Task Force on Supportive and Regulatory Framework for Microfinance set up by NABARD defined microfinance as the "provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi-urban and urban areas enabling to raise their income levels and to improve their living standards". Under the microfinance programme there is a shift of emphasis from individual lending to group lending. Group lending shifts the responsibilities, namely, of screening and selection of borrowers, monitoring to borrowers, and guaranteeing repayment of credit, from the lenders to the borrowers. The group lending is done in light of the standard of joint obligation, where the clients guarantee each other's credits. Since joint liability mitigates the necessity of security to get credit, poor people with no collateral can easily access credit under microfinance (Yunus, 2001). Microfinance gives an entryway to the poor to get adequate volume of credit easily to undertake any income generating activities. It additionally guarantees the option to save and which works for bringing the poor into mainstream (Dos, 2003).

The microfinance programme in India formally began in India through NABARD pilot project entitled as 'SHG-Bank Linkage' programme in 1992. This project linked initially 500 SHGs (Self-Help Groups) with banks and upgraded it to a regular banking programme in 1996. The SBL programme has gained exceptional headway in India since its origin as far as the number of SHGs linked with banks and amount of bank credits advanced to SHGs. The strategy of connecting SHGs to banks, at first through savings and later through credits, has been intended to bring financial inclusion of the hither to excluded segment of the society. (Teki and Mishra, 2012). SHG movement in India is leveraging the strength of formal banking system and in offering adequate financial services to the poor (Thimmaiya, 2011).

In Kerala, the NGOs, as well as the state government have been effectively occupied with microfinance programmes. The government of Kerala launched a microfinance programme called 'Kudumbashree' (KDS) in 1998. Kudumbashree is introduced as a participatory-women-based programme for wiping out poverty from the state through micro-financing. It organizes the poor women into a Community Based Organizations under the initiative of Local Self-Governments. NGOs are the fore-runners of microfinance programmes in the State. Both the state government and NGOs assumed a critical part in promoting and spreading microfinance programmes all through the State (Oomen, 2008).

Review of Literature

Those clients with bigger land property and less number of income earners in a family were bound to be the major recipients of microfinance programmes of BRAC in Bangladesh (Zaman, 1996). Most of the rural poor in India did not receive any formal banking services, which gave a solid need for promoting microfinance programmes to fulfil the credit requirements of the rural poor (Basu and Srivastava, 2005). Kudumbashree project has been identified as powerful instrument for the socio-economic, political, personal, and familial empowerment of the poor in Kerala (Ruby, (2008). The active involvement of clients in the microfinance programmes brought a significant improvement in their knowledge and social awareness, leadership qualities, communication skills, social status and a better role in the family. All these positive changes paved the way for their economic well-being (George, 2008). The review of available literature indicated that most of the studies focused on the effect of microfinance on poverty and women empowerment and none of the studies assessed financial inclusion capacity of the microfinance programme. Henceforth, this study seeks to evaluate the ability of the microfinance programmes in ensuring financial services to the unbanked sections of the populations in Kerala.

Research Issues

- To what extent the microfinance programmes contribute to financial inclusion among the poor in Kerala? And, what are the crucial factors influencing their level of financial inclusion?
- What is the effect of microfinance on the poor in terms of accessing banking services, the pattern of borrowings, and savings?

Objectives

To examine the extent to which microfinance programmes have contributed to financial inclusion among the poor in Kerala and to identify the main determinants of their level of financial inclusion.

- To assess the impact of microfinance programmes upon the poor in terms of accessing banking services, pattern of borrowings and savings.

Methodology

The present study is both empirical and analytical in nature. The study is based on both primary and secondary data. The primary data were collected randomly from 375 respondents from Kottayam, Idukki, and Wayanad districts of Kerala. The sample size comprised of 300 microfinance clients (180 Kudumbashree beneficiaries and 120 NGOs clients) and 75 non-members of microfinance programme. Secondary data have been gathered from books, journals, Government reports, internet, and yearly reports of Kudumbashree projects, NGOs, etc. The study employed both econometric model and descriptive statistics to analyse the data.

Results and Discussion

1. **Extent of Financial Inclusion through Microfinance Programme**

The extent of financial inclusion through microfinance programme estimates the proportion of clients, who had no access to formal financial services previously, now accessed financial products through the microfinance programme. The study examines the depth of outreach as the ability of microfinance programmes in reaching the poor and extending them required banking services.

Table 1: Composition of Microfinance Clients & Financial Inclusion

Variable	No. of Microfinance Clients	Percentage
No formal credit	195	65
No formal savings	298	99
SC/ST category	34	11
OBC category	121	40
State BPL list	300	100
Female-headed	42	14

Source: Primary data

It is obvious from Table 1 that the vast majority of the microfinance clients (65%) did not have access to formal banking services in the pre-microfinance period. Now almost all the clients could access banking products through the intervention of microfinance. Moreover, the proportion of clients belonging to SC/ST and OBC categories accounted for more than half of the microfinance clients (51%), which clearly indicates the active participation of vulnerable segments of the society in the microfinance programme to access the banking services. The capacity of microfinance programme to reach the poor is evident as all the clients were from the state BPL list before they join in the microfinance programme.

2. **Determinants of Level of Financial Inclusion**

The level of financial inclusion of clients in the microfinance programme is represented by the total volume of credit accessed from the microfinance programme. It is determined by a number of variables, namely, age of the clients, their educational attainment, social class (caste), size of the family, economic class (BPL/APL), female-headed family, and years of active participation in microfinance programme. The factors influencing the level of financial inclusion of clients are estimated by employing the econometric model of Pitt and Khandker:

$$\mathbf{L_{ij}} = \boldsymbol{\beta_l} \mathbf{X_{ij}} + \boldsymbol{\varepsilon_{ij}}$$

Where, $\mathbf{L_{ij}}$ is the total amount of credit accessed from microfinance programme.

$\mathbf{X_{ij}}$ is the vector of personal and household characteristics such as age of the clients, their educational attainment, social class (caste), size of the family, economic class (BPL/APL), female-headed family, and years of active participation in the microfinance programme.

$\boldsymbol{\beta_l}$ is the unknown parameter

$\boldsymbol{\varepsilon_{ijc}}$ is the stochastic error term.

Seven dummy variables are used in the model to represent the level of education and social class of the clients. The four dummies representing the level of education are:

i. edndum1 (1 to 5 years of schooling); ii. edndum2 (6 to 10 years of schooling); iii. edndum3 (+2/pre-degree), and iv. edndum4 (Degree and above).

The social class of the clients is given by:

i. SCSTdum (SC/ST category); ii. OBCdum (OBC category), and iii. GENdum (General category).

Table 2: Determinants of Level of Financial Inclusion

Independent Variables	Regression Co-efficient	't' value	Significance
Constant	102317.4	6.153	.000
Age of the clients	-633.744	-4.516	.000
edndum1	-4511.823	-.341	.734
edndum2	-6567.142	-.542	.579
edndum3	-298.384	-.023	.972
SCSTdum	-38296.4	-5.622	.000
OBCdum	-27590.8	-5.357	.000
Economic class (BPL/APL)	-28390.9	-4.735	.000
Size of family	-1994.673	-1.246	.328
Female-headed family	1043.328	.269	.885
Years of participation	8668.561	13.586	.000
$\mathbf{R^2}$	.611		
No. of observations	300		

Source: Primary data; Dependent variable: Total credit accessed

The regression estimates reveals that the variables such as age of the client, social class of the client, economic class and years of active participation in microfinance programme, are found to be significant at 1% significance level. The age of the client has a negative impact on total borrowing, signifying that higher age of client decreases total credit obtained from microfinance programme. The social class of the client is seemed to be a constraint to the volume of credit accessed by the clients. The volume of credit received by clients belonging to the SC/ST and OBC categories is substantially lower than the clients from the general category. The total credit accessed by the core poor clients is reported to be lower than that of the economically better off clients by Rs. 28,391. It signifies that the economically better-off clients reaped larger benefits from the microfinance. Further, each additional year of active participation in the microfinance programme enhances the total credit received by Rs.8, 669. The coefficient of multiple regression, R^2 is 0.611, indicating that 61.1 percent of variations in total credit accessed the clients is explained by the explanatory variables included in the model.

3. Access of Credit through Microfinance Programme

Microfinance empowers its members, particularly the poor to access easy credit without any collateral. They can access mainly three types of loans such as thrift loan dispensed out of the pooled savings of the SHGs, bank linkage loan and loan taken from banks for starting income generating activities (IGAs). The delivery of these credits enables them to fulfil much of their credit requirements.

Table 3: Total Borrowing through Microfinance

Amount of Loan (in Rs.)	Type of Loan								
	Thrift Loan			Linkage Loan			IGA Loan		
	NGO	Kudumbashree	Total	NGO	Kudumbashree	Total	NGO	Kudumbashree	Total
No loan	Nil	Nil	Nil	9 (7.5%)	38 (21.1%)	47 (15.7)	Nil	Nil	Nil
Upto 20000	9 (7.5%)	53 (29.4)	62 (20.67%)	11 (9.26%)	63 (35%)	74 (24.7%)	60 (50%)	54 (30%)	114 (38%)
20001-40000	58 (48.3%)	77 (42.8%)	135 (45%)	37 (30.8%)	47 (26.1%)	84 (28%)	45 (37.5%)	87 48.3%)	132 (44%)
40001-60000	29 (24.2%)	34 (18.9%)	63 (21%)	39 (32.5%)	21 (11.7%)	60 (20%)	9 (7.5%)	6 (3. 3%)	15 (5%)
60001-80000	21 (17.5%)	11 (6.1%)	32 (10.7%)	16 (13.3%)	3 (1.7%)	19 (6.3%)	3 (2.5%)	11 (6.1%)	14 (4.7%)
Above 80000	3 (2.5%)	5 (2.8%)	8 (2.6%)	8 (6.7%)	8 (4.4%)	16 (5.4%)	3 (2.5%)	22 12.3%	25 8.4%
Total	120 (100%)	180 (100%)	300 (100%)	120 (100%)	180 (100%)	300 (100%)	120 (100%)	180 (100%)	300 (100%)

Source: Primary data

The figures in Table 3 reveal that every one of the members of the microfinance programme got both thrift loan and loan for IGAs. The highest proportion of them (44%) have received credit amounting to Rs.20,001 – 40,000. Another important finding is that a few clients did not get any bank linkage loan so far. This was because of their respective SHGs/NHGs failed to satisfy the eligibility conditions of NABARD to secure linkage loan from banks. The average amount of loan obtained by the microfinance clients is reported to be Rs. 33869. Two sample 't' test for equality of means is used to confirm whether the average amount of loan of the microfinance clients is significantly higher than that of the non-members.

Table 4: Two Sample 't' Test for Equality of Means

Category	No. of Observations	Mean Loan (in Rs.)	Std. Deviation	't' value	Significance
Participant household	300	30,869	65173.74	5.009	.000
Non-participant household	75	8,508	14592.18		

Source: Primary data

The test result confirms that there is a significant difference between the microfinance clients and the non-members in terms of mean amount of credit received at 1% level of significance. The mean amount of loan secured by the clients is more than three times higher than the non-members (Table 4).

3.1 Pattern of Borrowings

The pattern of borrowings of microfinance clients is totally changed after joining the microfinance programme. In the pre-microfinance period, a significant majority of the clients (69%) met their credit needs from the money-lenders. Now, due to greater financial inclusion through microfinance enabled the clients to reduce their reliance on money-lenders to 3 percent. And SHGs/NHGs and banks became main source of borrowing for a significant majority of the clients (83%) in the post-microfinance period (Table 5).

Table 5: Pattern of Borrowings of Clients during Pre and Post Microfinance Periods

Borrowing Source	No. of clients	
	Pre-microfinance period	Post-microfinance period
No loan	48 (16%)	Nil
Banks	41 (13.67%)	Nil
Money-lenders	141 (47.33%)	Nil
Banks & money-lenders	65 (21.67%)	Nil
SHGs/NHGs	Nil	42 (14%)
SHGs/NHGs & banks	Nil	248 (82.6%)
SHGs/NHGs & money-lenders	Nil	10 (3.33%)
Total	300 (100%)	300(100%)

Source: Primary data

3.2 Utilization of Loan

The actual utilisation of credit is a critical factor which determines the level of economic benefits reaped by the clients and also its repayment. It can be evident from Table 6 that majority of the clients (54%) utilized borrowed fund for productive purposes. Unproductive use of credit is more pronounced among the clients of the Kudumbashree group. The association between productive use of credit and microfinance type is statistically significant, as the value of chi-square statistic is 69.879, which is significant at 1% level.

Table 6: Utilization of Loan

Utilization of Loan	No. of Clients
Productive	168 (54 %)
Unproductive	132 (46%)
Total	300 (100%)

Source: Primary data

3.3 Repayment of Loan

The success of microfinance programme depends upon the repayment of loan disbursed to the clients. It is apparent from Table 7 that a vast majority of the clients repaid their loan promptly. The loan defaulters accounted for 7 percent of the total borrowed clients. This may be due to low level of earning from the IGA undertaken and the unproductive use of credit obtained.

Table 7: Repayment of Loan

Repayment	No. of Clients
Prompt	279 (93%)
Default	21 (7%)
Total	300 (100%)

Source: Primary data

3.4 Fulfilment of Credit Needs

People require credits for different purposes. It is, therefore, important to assess to what extent the credit needs of the clients are fulfilled through microfinance programme. An overwhelming majority of the client's loan needs (83%) were fully satisfied through their microfinance programme. The proportion of clients, whose credit requirements were not completely fulfilled, was reported to be more from the Kudumbashree groups (Table 8).

Table 8: Fulfilment of Loan Requirement

Fulfilment of Credit Needs	No. of Clients		
	NGO	Kudumbashree	Total
Yes	106 (88%)	142 (79%)	248 (83%)
No	14 (12%)	38 (21%)	52 (17%)
Total	120 100%)	180 (100%)	300 (100%)

Source: Primary data

4. Savings

Microfinance promotes regular savings among its clients in their respective SHGs. This collected saving is used to provide loans to its clients. The volume of credit delivered to a client determined by her total savings in the SHGs. The amount of linkage loan from banks by each SHG also depends on the size of total savings of the group. Owing to the intervention of microfinance, all the clients could make some savings out of their current income.

Table 9: Saving Trend during Pre and Post Microfinance Periods

Category	Household Savings					
	Pre-microfinance period			Post-microfinance period		
	Yes	No	Total	Yes	No	Total
Clients	5 (2%)	295 (98%)	300 (100%)	300 (100%)	Nil	300 (100%)
Non-members	-	-	-	8 (11%)	67 (89%)	75(100%)

Source: Primary data

Table 10 Two Sample 't' Test for Equality of Means

Category	No. of Observations	Average Savings (in `)	Std. Deviation	't' value	Significance
Clients	300	21420	36613.69	9.196	.000
Non-members	75	1064	3164.385		

Source: Primary data

The data shown in Table 9 indicates that almost all the clients (98%) had no savings in before joining the microfinance programme. However, all the clients have savings in the post-microfinance period. The average total savings of the microfinance clients is reported to be Rs.21420. A significant majority of the clients (63%) save in post office or chitty or both, in addition to their savings in SHGs. The ability of the microfinance programme to inculcate a habit of thrift among its clients is evident as the proportion of the non-members with savings is very low with 11 percent. The clients made these savings out of their earnings from the IGA undertaken. Two sample 't' test for equality of means is used to verify whether the average total amount of savings of the microfinance clients is significantly higher than that of the non-members (Table 10). The conclusion derived from the test is that the average total savings of the clients is significantly higher than the non-members at 1% significance level..

Conclusion

The foregoing analysis indicates that microfinance programme is very successful in reaching the poor and the vulnerable sections of the population and delivering them financial services. The respective SHG of clients and banks became the chief source of borrowing in the post-microfinance period; previously they borrowed mainly from informal sources, i.e., money-lenders. It is a clear proof for the ability of the microfinance programme in extending financial inclusion among the poor. Moreover, Microfinance programme inculcated a habit of regular savings for all the clients. The variables such as age of the client, social class of the client, economic class and years of active participation in microfinance programme, are found to be significant determinants of degree of financial inclusion made through microfinance. However, microfinance can function as a still better tool for financial inclusion if the State Government and NGOs focus greater attention to extend further their level of outreach to the poor and the vulnerable segments of the population as some of the non-members belonged to SC/ST and OBC categories, and also by intensifying the monitoring and follow-up and guaranteeing benefits this programme to the core and moderate poor. Otherwise, the potential capacity of microfinance in bringing more financial inclusion cannot be reaped on a sustainable basis.

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