

**MICRO FINANCE:  
The Pillars of a Tool to Socio-Economic Development**

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**Introduction:**

Micro enterprises make an important contribution to economic output and employment in developing economies. While estimates vary greatly depending on definitions, recent work by the World Bank suggests that almost 30 per cent of employment in low-income countries is generated by the informal economy, while an additional 18 per cent is provided by (formal) small and medium enterprises. Together these two groups contribute 63 per cent of the GDP (Ayyagari, M., T. Beck and A. Demirguc-Kunt, Small and medium enterprises across the globe: A new database, World Bank Policy Research Working Paper). Finance is lifeblood of any enterprise irrespective of its size. Micro enterprise faces more problems in raising finance, as the provider of finance may not find the return on investment interesting as compared to large enterprise, and also investor is more skeptical about repayment.

Entrepreneurs compete in rapidly changing markets and must respond to the challenges of globalization, technological advance and other factors. Micro enterprise has limited resources at its disposal while competing with giant enterprises. At the same time they have special pool of business where micro enterprise is more competitive. To be able to work out of poverty, to survive and to grow, entrepreneurs need access to a range of services. Broadly, these are categorized as (1) financial services and (2) non-financial, or business development services (BDS), such as market information, management and vocational skills training and business advice. (Merten Sievers and Paul Vandenberg, Synergies through Linkages: Who Benefits from Linking Finance and Business Development Services?). Non-financial services are equally important to design, develop & market product or services. Micro enterprise has edge over large enterprise in various products; traditional knowledge and better control over business are unique strength.

Ignoring substantial population suffering from poverty may be costly for any economy and it is not prudent not to utilize strengths vested in such poor lot. Socioeconomic development as well as macroeconomic and financial sector stability is important components in ensuring an enabling environment for continued growth of overall economy as a whole and the micro finance industry in specific. Supporting micro enterprise is therefore necessary policy – socially & economically.

**What is Micro Finance?**

The dictionary meaning of 'finance' is management of money. The management of money denotes acquiring & using money. Micro Finance is buzzing word, used when

financing for micro entrepreneurs. Concept of micro finance is emerged in need of meeting special goal to empower under-privileged class of society, women, and poor, downtrodden by natural reasons or man made; caste, creed, religion or otherwise. The principles of Micro Finance are founded on the philosophy of cooperation and its central values of equality, equity and mutual self-help. At the heart of these principles are the concept of human development and the brotherhood of man expressed through people working together to achieve a better life for themselves and their children. (V. Sapovadia, Micro Finance – A tool for socio-economic development & Women Empowerment)

The business of financing is based on very simple theme 'the timing difference', one class in the society has surplus money than their current need while other class require more money than their current balance. Those who need money for business purpose, if create earning for themselves and supplier of money; the deal to provide finance to such entrepreneur may be mutually beneficial. Financing agency helps individuals to plan their differing needs of finance at differing points in time by an intervention that helps to balance. In essence the intermediation offers a mechanism of meeting the demand for finances of a person by the person's own supply. This is done by putting away some money (savings) to be used at a future point in time or using the money in the current point with a promise to replace it in future (loans). In either case - the service of intermediation is usually used to manage the time differences. (M.S. Sriram, Information Asymmetry and Trust: A framework for studying micro-finance in India). For micro enterprise, the intermediary should be socially sensitive. Also mechanism for acquiring & investing money is on different footing. Thus micro finance has different set of characteristics.

Micro enterprises are working in informal sector. Within the communities from where micro entrepreneur comes have suppliers of money. Such moneylenders may be exploiting the needy. Since full information about who is willing to supply money and who is willing to borrow is not easily available, there is asymmetry. A person might have greater amount of information about the needs and reliability of a small circle of people with whom s/he might have regular dealings. There require social institutions like cooperatives, Self Help Group, Micro Finance Institutes who can manage financing with special care of so-called micro clients.

Micro finance means providing very poor families with very small loans (micro credit) to help them engage in productive activities or grow their tiny businesses. Over time, micro finance has come to include a broader range of services (credit, savings, insurance, etc.) as we have come to realize that the poor and the very poor that lack access to traditional formal financial institutions require a variety of financial products.

Traditionally micro finance was focused on providing a very standardized credit product. The poor, just like anyone else, (in fact need like thirst) need a diverse range of financial instruments to be able to build assets, stabilize consumption and protect themselves against risks. Thus, we see a broadening of the concept of micro finance--- our current challenge is to find efficient and reliable ways of providing a richer menu of micro finance products. Micro Finance is not merely extending credit, but extending credit to

those who require most for their and family's survival. It cannot be measured in term of quantity, but due weightage to quality measurement. How credit availed is used to survive and grow with limited means.

### **Who are the clients of micro finance?**

The typical micro finance clients are low-income persons that do not have access to formal financial institutions. Micro finance clients are typically self-employed, often household-based entrepreneurs. In rural areas, they are usually small farmers and others who are engaged in small income-generating activities such as food processing and petty trade. In urban areas, micro finance activities are more diverse and include shopkeepers, service providers, artisans, street vendors, etc. Micro finance clients are poor and vulnerable non-poor who has a relatively unstable source of income.

Access to conventional formal financial institutions, for many reasons, is inversely related to income: the poorer you are, the less likely that you have access. On the other hand, the chances are that, the poorer you are, the more expensive or onerous informal financial arrangements. Moreover, informal arrangements may not suitably meet certain financial service needs or may exclude you anyway. Individuals in this excluded and under-served market segment are the clients of micro finance.

As we broaden the notion of the types of services micro finance encompasses, the potential market of micro finance clients also expands. It depends on local conditions and political climate, activeness of cooperatives, SHG & NGOs and support mechanism. For instance, micro credit might have a far more limited market scope than say a more diversified range of financial services, which includes various types of savings products, payment and remittance services, and various insurance products. For example, many very poor farmers may not really wish to borrow, but rather, would like a safer place to save the proceeds from their harvest as these are consumed over several months by the requirements of daily living. Central government in India has established a strong & extensive link between NABARD (National Bank for Agriculture & Rural Development), State Cooperative Bank, District Cooperative Banks, Primary Agriculture & Marketing Societies at national, state, district and village level.

### **Pillars of Micro Finance:**

At last the series of these articles would like to focus on the pillars of micro finance. As discussed earlier the need, means, objective, instruments & parties in micro finance are specific & different, and hence it becomes imperative to design pillars of micro finance that it can fulfill the aspirations of those who are involved and more specifically of the micro enterprises. The paper will explore ideas whether Financing & Non-financing services required by micro enterprise in formal & informal organization should be uniform or it should be area/region specific, product specific or time specific or a community specific.