

## ► CHIDAMBARAM HOPEFUL OF EARLY PASSAGE OF MICROFINANCE BILL



Finance minister P Chidambaram with UN resident coordinator and UNDP resident representative in India Lise Grande at the Microfinance India Summit 2012 in New Delhi on Tuesday. Expressing hope that the microfinance Bill would be introduced in Parliament soon, he said its enactment would lead to a framework for the sector. Responsible financing by way of transparency, interest rate rationalisation and a respectable recovery procedure must be followed by MFIs, he added. ■ P8 ■ Edit: Reviving microfinance, P6

### Reviving microfinance

Despite negative reporting, MF industry holds promise

It is no secret that, in the last two years, microfinance in India, especially after the Andhra government's legislation (that heavily regulated the sector), has suffered. According to the recent *State of the Sector* report by Access Development Services, the customer base for the industry has shrunk from a peak of 76.7 million in 2010-11 to 68.2 million in 2011-12, whereas the outstanding loan portfolio for the industry, which grew four times between 2007-08 and 2010-11 to 21,556 crore, has declined to 20,913 crore in 2011-12. In 2010, a spate of suicides allegedly triggered by excessive indebtedness in rural Andhra Pradesh had Andhra's government acting populist by forbidding MFI officials to visit households to recover loans, and by requiring MFIs to register each of the operations with a local authority. This led to massive difficulties in recovering loans, as numerous borrowers took advantage of the law to refuse repayment, in a state which was responsible for almost a third of the industry's \$5.3 billion loans. And it didn't help when RBI followed suit by recommending a cap on interest-spreads.

So, is the industry, which promised to empower women and unleash the entrepreneurial energy of large swathes of poor in South Asia, a failure and all set for a stop? Perhaps not, because micro-credit continues to hold definitive advantages. For one, lending to the poor from an MFI is more preferable than lending from the only other alternative for the poor—local moneylenders and loan-sharks, who, thanks to the riskiness of poor folk and of administering their loan, charge interest rates as high as 1-2% a day (as compared to 25% a year for most MFIs). Moreover, the empirical evidence of the effect of microcredit proves the point. Abhijit Banerjee and Esther Duflo, in a critically acclaimed book *Poor Economics*, display the findings of a study they conducted on the effects of microcredit in poor neighbourhoods of Hyderabad. The results were encouraging—a significant increase in households starting businesses, and no sign of reckless spending—but not radical, with barely any difference in women's control over household spending and virtually no radical start-ups. In short, microfinance was "not miraculous. But it was working". This significant but not radical impact of this industry should be a good enough reason to encourage this sector. The recent *State of the Sector* report shows "nascent recovery" following the disaster inflicted by Andhra government's legislation. The central government would do well to not discourage the industry by putting in place unnecessary restrictions.

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