Understanding the Micro Enterprise Lending Practices in India: Need for a Decisive Policy Intervention

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Abbreviations

APL	Above Poverty Line
BC	Business Correspondent
BF	Business Facilitator
BPL	Below Poverty Level
CAGR	Compound Annual Growth Rate
CGTMSE	Credit Guarantee Fund Scheme for Micro and Small Enterprises
DIC	District Industries Centre
FI	Financial Institution
FL	Financial Literacy
FLCC	Financial Literacy and Credit Counselling Centre
FY	Financial Year
GCC	General-purpose Credit Card
GDP	Gross Domestic Product
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
IFC	International Finance Corporation
KCC	Kisan Credit Card
KVIC	Khadi and Village Industries Commission
KYC	Know Your Customer
LDM	Lead District Manager
ME	Micro Enterprise
MFI	Micro Finance Institute
MFIN	Microfinance Institutions Network
MSME	Micro, Small and Medium Enterprise
MUDRA	Pradhan Mantri Micro Units Development and Refinance Agency
NABARD	National Bank for Agriculture and Rural Development
NBFC-MFIs	Non-Banking Financial Company -Micro Finance Institution
NCEUS	National Commission for Enterprises in the Unorganized Sector
NGO	Non- governmental Organization
NRLM	National Rural Livelihoods Mission
OECD	Organization for Economic Co-operation and Development
PMEGP	Prime Minister's Employment Generation Programme
PMMY	Pradhan Mantri Mudra Yojana

RBI	Reserve Bank of India
RUDSETI	Rural Development and Self- employment Training Institute
SFB	Small Finance Banks
SHG	Self-Help Group
SHG - BLP	SHG Bank Linkage Programme
SIDBI	Small Industries Development Bank of India
SKDRDP	Shree Kshetra Dharmasthala Rural Development Project
SLBC	State Level Bankers Committee
UTLBC	Union Territory Level Bankers Co

Executive Summary

The study provides an assessment of the various credit sources for microenterprises and micro entrepreneurs in India which include alternate channels of credit, it also understands the difficulty in accessing the credit from different sources. The chapters in the study begin with explaining the key characteristics of the microenterprises, based on both secondary and primary survey data. Following, it assesses the need of microenterprises for finance and contrasts it with the actual flow of finance. The study describes the predominant sources of finance, including informal sources and enumerates the stated purposes for which finance is used and tries to explore the issue of fungibility (interchangeability) between household cash flows and business cash flows of micro-entrepreneurs. It explores the difficulties faced by enterprises in raising finance and the difficulties expressed by bankers in extending credit to microenterprises. Delving into potential interventions it addresses the lack of access to formal finance for microenterprises.

Secondary data from the Economic Census (EC), 2014[1] indicates that there were 58.5 million economic establishments (the term used for enterprises in the EC), registering a growth of 41.7% from the Fifth EC (2005). The total includes 45.36 million (77.6%) non-agriculture-based enterprises while the remaining are agricultural enterprises. The total number of enterprises owned by women entrepreneurs was 8.05 million (13.8%). About a fifth or 18.44% of the establishments were outside the home but without any fixed structures like road side vendors. About 1.71% of the establishments were engaged in handloom or handicraft production activity.

These enterprises accounted for nearly 25% of all employment in the country at that time making them critical to the national goal of inclusive growth, considering the total employment was 12.8 crore persons of which 52% were in rural areas. The employment was a majority for household members and thus these are technically called own account enterprises. On the other hand, hired workers were about 45.7% which means nearly six crore workers were paid through these enterprises. Percentage of female workers was 25.6%. The growth rate in total employment over Fifth EC (2005) was 38.13%.

Factors such as lack of adequate and timely access to finance, shortage in market linkages and erratic supply of raw materials and power make it difficult for microenterprises to expand and cope with increasing competition, thus constraining the growth of the sector. To understand these better and make a judgment on the ground reality in providing policy recommendations, the study was largely based on a field survey.

The microenterprise survey was conducted in one district each of four states in different regions, Uttar Pradesh (Northern region, Varanasi district), Odisha (Eastern region, Ganjam district), Karnataka (Southern region, Bidar district) and Maharashtra (Western region, Chandrapur district). The districts were also selected for different levels of penetration of microfinance institutions which have become a significant alternative channel of formal financing. The research design followed a simultaneous use of quantitative and qualitative research methods. 813 samples from these four locations were drawn for representing the different types of microenterprises. The choice of districts was strategic and within these districts the selection of rural/semi-urban and urban sample was also strategic so that an adequate number of rural

[1] Report of Sixth Economic Census, MOSPI (2016)

districts were covered. The surveyed microenterprises were selected through stratified random sampling.

The survey dwelt on both the demand and the supply side factors affecting credit flow. On the demand side, nearly 78% of surveyed micro-entrepreneurs expressed the need for finance for their microenterprises, with the average amount required being close to Rs. 90,815. The main purpose of the requirement was to procure raw material (including 'saleable' goods for trading enterprises). Surprisingly, only 28% of the surveyed households expressed the need for financing household expenditure for consumption (main purpose), education, health, housing and social purposes, with the stated average need of Rs. 65,541.

On the supply side, while 91% of the sampled microenterprises reported to have got loans, around 70% of the loans had been taken for business purpose and another 8% for agricultural and allied activities. On an average a respondent had 1.5 loans, which showed that multiple borrowing was common. Micro entrepreneurs tended to rely on multiple sources because of the inadequacy of finance from one single source and to hedge their chances of getting finance. Remaining 22% of the loans were taken for the household purposes. Fungibility of the credit is a common phenomenon, i.e. a part of the credit taken for microenterprises is used for household purpose. In some cases, it is also used to repay other loans because of the difficult repayment schedule of the latter.

Of those who received loans, 47.4% bought raw materials, 9.3% utilised it for other long- term business needs, 4.3% for buying machinery and 3.7% to buy tools/equipment. The extent of finance accessed was Rs 76,700 on an average, which was 84% of the average need of Rs 90,815 for business purposes stated above. If household needs are also taken into account which is Rs 65,541, then the availability of finance was only 65% of the expressed need, showing a severe shortfall in 35% access to finance.

This study shows that the formal sources, accounted for around 60% in terms of both number of loans received and the amount financed. Among the formal sources, Self-Help Groups (SHGs) are the major source of finance (16.2%) followed by Microfinance Institutions (12.6%) and Private Sector Banks (9.4%). Public sector banks account for 7%. Among the informal sources, moneylenders are a major source of finance (17.4%) followed by friends and neighbours (9.7%) out of the total finance to the microenterprises. This is not necessarily an issue as the loans by these channels are more appropriately sized. For most microenterprises, 40% of the loans were from informal sources, accounting for 40% of the amount financed. Moneylenders play a dominant role in the category of informal sources as they lend 43% of total loans (and 61% of the amount financed) for financing enterprises, followed by 34% by family, friends and neighbours and 18% by input suppliers and output buyers out of the total number of loan financed by informal sources.

The alternative credit channels like MFIs and SHGs have been providing credit services to micro entrepreneurs; however, loan amount provided is often inadequate to meet the needs of the enterprise, thus there is an increasing dependence on the informal sources. Banks have created a network of BCs, however, their role is mostly restricted to account opening and saving transactions. Banks are currently offering only liability products and are yet to offer their asset-based products to their clients through the Business Correspondent (BC) points until then micro-entrepreneurs have to visit bank branch offices to access finance. Awareness among potential users of the BC model is limited to 18%. With respect to the BC's role of providing banking services at their doorstep only 5% reported taking loans through them. Wherever these channels have been established, moneylenders' share of credit has come down.

Financial literacy initiatives were taken up and content was developed to suit various target groups including micro entrepreneurs for training and orientations which were conducted by Financial Literacy Centres (FLCs), however the demand for financial education was expressed by 79.2% of the respondents. Over 80% were aware of SHGs while nearly 18% were aware of BCs, etc. The study, however, reveals that micro-entrepreneurs are not adopting banking in a big way, leave alone newer things like digital finance.

This is happening due to constraints in accessing finance from banks and limitations of the alternative channels of credit due to which many of the micro-entrepreneurs depend upon the informal sources to access credit/raw materials and some of them also accept to sell their produce to the input suppliers/output buyers who provide cash credit and/or raw materials in kind.

The financing gap in the microenterprise sector is a combined result of demand-side challenges such as lack of awareness, documentation requirements, inability to provide margin money, collateral and mixing up of household and enterprise cash flows, and supply-side issues, such as lack of translation of high level credit policies into appropriate processes for microenterprise borrowers, and incentives for field bankers to lend to micro entrepreneurs. Superficial understanding about microenterprise business among bankers is persistent, and due to their branch and desk-based orientation, they find it difficult to identify the right borrowers and instead lend to those who come to them, often through middlemen or recommendations of influential persons and who can at least on paper, meet the various requirements. Project appraisal, loan monitoring and default management are more for the purpose of reporting "action taken" rather than a job done in true spirit.

The study recommends policy interventions suitable to address the difficulties faced by micro entrepreneurs in accessing credit from their preferred sources and to address the constant inadequacy of credit.

- Enhancing awareness through information dissemination, training, hand holding, mentoring and establishment of the network for facilitating cross-learning and mutual help. The RBI has already taken many steps towards this through various banks but the outreach is extremely limited and perfunctory. This because most programs of financial literacy are based on holding face-to-face training programs in rural areas and low-income urban areas which are too labour intensive for the trainers and take too much time for the participants. Instead, mobile phone based training; short videos, mobile phone games (e.g. the ones designed by the ILRT, Hyderabad – www.ilrtindi.org) and mobile apps like Haqdarshak (www.haqdarshak.com) which indicate the eligibility of a person for a government program or loan, should be used. These can be supplemented by web-based e-learning modules such as www.dhangyan.com or Rupaya Paisa, a series of books developed by Pratham Books for children of classes 6 to 8. Vocational training courses to become professional Household Financial Advisors and Microenterprise Business Advisors should be offered as a part of the National Skill Qualification Program from class 9 to 12 so that eventually India will have lakhs of young people engaged in these professions.

- Reducing the complexity in documentation by replacing it with simple procedures, increased periodical monitoring, and further strengthening of DICs etc. In its movement towards digitisation, the Indian government should eliminate the need for any paper-based loan application and a physical visit by the borrower to a branch. Loan applications for loans up to the Shishu category should be fully digitized using mobile phone apps and tabs. These can be uploaded by anyone having access to the internet. If they need assistance in filling the application, lakhs of BC and CSC operators should be trained and authorised to do this for a fixed fee. If the mighty Life Insurance Corporation (LIC)could digitise its insurance policy application and issuing of cover notes, through a nationwide network of Common Service Centres (IT kiosks offering access to government services) in rural areas, there is no reason why the banking system should lag behind. Already significantly sized pilots are being conducted in Rajasthan by the United Bank of India and Sub-K (a BC company) for originating and approving microenterprise loans in a paperless manner using electronic tablets (Tabs).
- Worth mentioning in this regard is Streenidhi, (https://www.sthreenidhi.ap.gov.in) a wholesale lending institution for SHGs and SHG Federations, established by the Govt of Andhra Pradesh (AP) in 2012. The operations of Streenidhi are fully digitised and a woman applying for a loan to her SHG in rural AP gets a decision within three days and if the loan is approved the money credited in her bank account by the fifth day.
- The gap between policy pronouncement on credit to small borrowers and actual flow needs to be bridged differently than issuing more circulars by the RBI and the bank's head offices. The processes that a borrower has to go through should be subjected to a detailed scrutiny by business process reengineering professionals. Banks must be mandated to make all applications up to Shishu loans completely digital and paperless and not requiring any branch visit. Once an application is digitally uploaded, its appraisal, approval, disbursement and repayment must be digitally tracked. This must include a mandatory use of Aadhaar for e-KYC check and a credit history check of applicants, conveying of approval or rejection of loan application, including causes thereof by mobile SMS, and disbursement as well as repayment through their bank accounts electronically linked to the core banking system.
- Separately, the incentive system for field based bank staff must be changed to encourage Field Officers to move out of the branches and branch managers to occasionally leave their desks to interact with micro-entrepreneurs in their location. To monitor this, bankers must be asked to upload their photographs with applicants or borrowers along with the GPS location and date and time stamp, on the designated website of the bank. Field officers must not only be given adequate travel allowances but also incentives for originating loans by numbers, not amount, so that they can look for smaller borrowers. Repayment must be monitored and bankers should be rewarded for keeping NPAs below an acceptable target level, say 3%. Zero NPA should be rewarded.
- Banks should be encouraged to use alternative channels – like SHGs, MFIs and BCs who are already engaged in cash-in and cash-out transactions for bank accounts. Banks are using these channels but reluctantly and tend to do so when they get a government mandate and an operating subsidy for the channel costs (as in case of the SHG loans). In case of MFIs as well loan-originating BCs, banks tend to keep a much larger share of the net interest income that their proportion of operating costs plus risk. To correct this

situation the RBI should establish an Expert Committee to determine the efficiency level cost structure (including operating and risk costs) for each channel and the channels should then be paid accordingly. Banks should be allowed to price products in line with cost structures. Public Sector Unit (PSU) banks currently hesitate to mark-up the price to accommodate for BC costs thus ending up underpaying BCs.

- Banks need to innovate greatly on product features. The standard term loans with quarterly or monthly repayment instalments do not take into account the seasonality of microenterprise cash flows nor of the varying requirements of micro-entrepreneurs' households. Thus "cash-credit" products should be offered but with digital operations, so that deposit or withdrawal of small amounts frequently need not require the micro-entrepreneur to go to a bank branch or ATM. Term loans should be only given for purchase of equipment, machinery or other lumpy fixed assets and should be at least four year duration with one year moratorium or three years with a ballooning of instalments (higher amounts in the latter years). Even though they may be below the GST registration floor, microenterprises taking bank loans may be encouraged to use apps like GR4GST (get ready for GST) to channel as much of their input purchase and utility payment transactions through bank accounts as possible. Sale proceeds may be mostly still in cash but the bank must insist on a daily deposit of proceeds and a reminder should go out by SMS if it does not happen by 11am every morning. Even cash collection from the shop is now being offered as a reliable digitally recorded service by Indepay (www.indepay.com) and State Bank of India (SBI) is partnering with them for a pilot in the Delhi NCR region.
- Banks need to innovate greatly on product features. We have to recognise that for microenterprises, the business cash flows and the household cash flows are mixed up, and often entrepreneurs are forced to use business loans to meet other financing needs, medical care, children's education, housing, and social expenditure. In case of very low-income households, a part of the loan is even used for consumption.
- Thus it is important to offer a range of different products to meet these needs and allow one person or one household to have multiple, simultaneous loans (within overall repayment capacity) for different financing needs, with different interest rates and repayment terms. In this connection, the work done on household wealth planning by IFMR Capital, Chennai and the theoretical and policy work done by the recent RBI Committee on Household Finances need to be studied and put in action more widely.
- Though the RBI Technical Group, 2007, had recommended a selective and careful use of moneylenders, to enhance access to credit by micro borrowers, and even drafted model legislation for regulation of moneylenders who would then be linked with banks for wholesale finance, not much progress happened on it. The reasons for this are from both sides – moneylenders are reluctant to be brought under any formal controls, and banks are unwilling to lend to them in case the scheme backfires. Instead banks are more willing to use alternative channels like MFIs, SHGs and BCs, as they are more prone to being supervised. The study found that wherever the outreach of these channels was dense, the dependence on moneylenders was getting reduced. In summary, therefore, our recommendation is that informal channels should be allowed to slowly wither away as the alternate channels spread their outreach.

- Based on this experience, we are recommending the establishment by SIDBI of a Micro Entrepreneurs' Network for Training, Operational Support and Resource Mobilization (MENTOR). Under MENTOR, experienced micro entrepreneurs not only will provide guidance on local market demand, customer preferences, skill training and business training, but also help in operations such as identifying and linking with sources of raw materials or inputs, equipment, and any permissions or licenses needed, along with helping mobilize credit from MFIs or bankers by giving references and offering support in filling applications. All these services of MENTORs should be paid under the RBI approved scheme of business facilitators, by the bankers of the upcoming entrepreneurs, at about 3% of the loan value, 1% each when the loan was approved, when it was utilized and when it was repaid. Thus micro enterprise mentoring itself becomes a service sector micro enterprise while the trainee enterprises also see an increase in revenues and income.

1 Introduction

1.1 Background and scope of the study

The microenterprises play a crucial role in providing large employment opportunities. Since the merger of the Ministry of Small Scale Industries and Ministry of Agro and Rural Industries into Ministry of MSME, and since the execution of MSME Act, 2006, the scope of microenterprises in India has widened. The Sixth All India Census of MSME provides good insight into the status of MSMEs in India. The numbers of MSMEs are 512.99 lakhs. The number of employed is 1112.28 lakhs. As per the results of Sixth Economic Census 2013, non-agricultural enterprises constitute 77.6% or more than three-fourths of establishments in the country. The credit markets in India are characterized by the coexistence of both formal and informal sources of finance and the market is fragmented. It is assessed that the share of informal credit in total outstanding debt has been certainly decreasing over the period from 1950 to till date due to various financial inclusion initiatives of the Reserve Bank of India (RBI) and legislations of the various state governments to regulate moneylenders. But the inadequate and untimely credit along with procedural hassles from formal institutions has been the major problem of credit access by masses. Although formal microcredit programs exist in India, their scope and impact still remains limited creating room for a large informal credit market.

1.2 Microenterprises in India - Current status and growth

Institutional arrangements have posed hurdles to financing microenterprises. Since microenterprises fall in the 'missing middle' category that does not come under the purview of either MFIs or Banks, they have always found it difficult to meet their working capital requirement. The sub-group of the Planning Commission on MSME estimated the demand and supply of credit for MSME. The projection is for the entire five year period from 2012-2017. The estimation for microenterprises alone, done by Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ), is shown in the table.

Table 1: Estimation for Credit Demand by Microenterprise in India

Year	Working capital demand (Rs. trillion)	Term loan demand (Rs. trillion)	Total demand (Rs. trillion)
2014-15	8.6	1.9	10.5
2015-16	9.5	2	11.5
2016-17	10.5	2.3	12.8

In the study published by GIZ India, the demand of microenterprises for credit was about Rs. 7.9 trillion while the supply of loans from the banks was only estimated to be Rs. 1.5 trillion for microenterprises. Hence, there is a big gap to be filled with respect to the credit demand from microenterprises. Similar results have been shown in the study by IFC-Intellecap. The debt gap in the microenterprises sector Rs. 2.3 trillion, a majority share in the total gap of Rs. 2.9 trillion in MSME.

Table 2: Share of MSME sector in GDP and total manufacturing output

Manufacturing output at current Price			Share of GDP		
Year	MSME manufacturing output (Rs. In crores)	Share of MSME manufacturing output in total manufacturing output (%)	MSME Manufacturing Sector	MSME Service Sector	Total
2011-12	2,167,110	33.12	6.16	23.81	29.97
2012-13	2,385,248	33.22	6.27	24.13	30.40
2013-14	2,653,329	33.27	6.27	24.37	30.64
2014-15	2,783,433	33.40	6.11	24.63	30.74

Source: Annual Report 2016-17-Ministry of MSME (msme.gov.in)

The contribution of MSMEs in GDP is 6%, in manufacturing sector 33% and in exports 45%.

Table 3: Summary results of Fourth All India Census of MSME

S. No.	Characteristics	Establishments (6th EC)	Employment (6th EC)	Establishments (5th EC)	Employment (5th EC)
1	Total	58,495,359	131,293,868	41,253,630	95,054,007
2	Rural	34,795,754	67,895,421	25,146,177	16,107,453
3	Urban	23,699,605	63,398,447	50,374,053	44,679,954

Table 4: Growth rate of Non-Agricultural establishments and employment

Sector	Item	5th EC(2005)	6th EC(2013)	CAGR (%)	Total Growth (%)
Rural	Establishments	19,437,178	22,710,545	1.96	16.84
	Employment	40,198,855	46,838,101	1.93	16.52
Urban	Establishments	15,736,469	22,653,241	4.66	43.95
	Employment	43,941,551	61,573,266	4.47	40.13
Combined	Establishments	35,173,647	45,363,786	3.23	28.97
	Employment	84,140,406	108,411,367	4.12	28.85

The status of Microenterprises in India, in general, has been discussed based on the available data from the reports of Ministry of MSME. The unregistered category is the majority, within which the rural enterprises are lagging behind in registering their enterprises. This may be due to both lack of information and unwillingness of entrepreneurs, as they don't want to reveal details about their enterprises to avoid tax and regulatory process The above table gives the number of establishments and employment in last two economic censuses and inter-census growth rate of establishments in respect of rural, urban and combined over the period 2005-13. It is seen that the overall compound annual growth rate (CAGR) of establishments per year during 2005-13 was 4.46% per annum in urban areas was slightly more than the growth rate in rural areas. The total growth in the number of establishments during 2005-13 was 41.79%. As far as employment is concerned, overall CAGR of 4.12% was observed during 2005-13. The total growth in the number of workers during 2005-13 was 38.13%.

Few of the ready government schemes for boosting the credit flow are as follows,

Credit Guarantee Fund Scheme for Micro and Small Enterprises

It encourages member institutions to extend collateral free financing (both fund-based and non-fund-based) to the MSE segment with a maximum limit of INR 10 Million (USD 0.2 Million). For credit applications covered under the scheme, the trust extends guarantee cover up to 85% of the outstanding amount on default.

Prime Minister Employment Generation Programme (PMEGP) scheme

It is implemented by Khadi and Village Industries Commission (KVIC) functioning as the nodal agency at the national level. At the state level, the scheme is implemented through state KVIC Directorates, State Khadi and Village Industries Boards (KVIBs), District Industries Centres (DICs) and banks. In such cases, KVIC routes government subsidy through designated banks for eventual disbursal to the beneficiaries/entrepreneurs directly into their bank accounts. The maximum cost of the project/unit admissible in manufacturing sector is ₹ 25 lakhs and in the business/service sector, it is ₹ 10 lakhs.

However, by not registering their enterprises, they are missing out on the benefits like subsidies provided by the government. There is a need to create awareness on this front and to guide the entrepreneurs in such processes. Few other challenges faced by the banks to provide credit to micro entrepreneurs are identification of right borrowers, identification of right borrowers, documentation and disbursement, loan monitoring, delayed repayment and defaults.

The numbers of MSMEs as on date are 584.95 lakhs throughout the country and provide the employment to 1312.93 lakhs. As per the results of Sixth Economic Census 2013, non-agricultural enterprises constitute 77.6% or more than three- fourths of establishments in the country. Out of 58.5 million establishments, around 96.4% were under private ownership. More than one third (36.19%) of all establishments in the country are home -based establishments. The growth rate of employment since 2005 was of the order of 38.13%.

1.3 Objectives of the study

- All the data indicate facts that have been motivated to a large extent to study the financing of microenterprises and to understand the reasons for inadequate access to credit for microenterprise and the persistence of informal sources of credit in whatever access there is. The study will try to understand both supply side and demand side causes for the persistent inadequacy of credit and dependence of microenterprises on informal channels for credit.
- The study aims to examine various credit sources for microenterprises[2] and micro entrepreneurs in India including alternate channels of credit and understand the difficulty in accessing the credit from different sources. Further, based on the findings and micro-entrepreneurs' feedback, corrective measures would be suggested so as to help

[2] The intention for using the both the terms "Microenterprise and Micro entrepreneur" is, normally at Microenterprise, the household expenditure and enterprise requirements are mixed-up.

Note: This study will focus predominantly on Sishu and Kishor (up to Rs.2 lac credit required) micro enterprise segment as defined by GoI.

policy makers, regulators and credit providers – banks, financial institutions, NBFCs, and informal lenders including input suppliers and output buyers.

- To study the various sources of finance for microenterprises and micro entrepreneurs in India and understanding the difficulties in accessing the credit from different sources.
- Understand the reasons for persistence of overall inadequacy of credit to micro-enterprises.
- Understand the role of informal credit sources including moneylenders, input suppliers and output buyers in meeting the credit requirements of microenterprises and micro entrepreneurs.
- Assess the extent to which alternative channels such as NBFCs, MFIs, BCs and SHGs are meeting the credit requirements of microenterprises and micro entrepreneurs and the possibility of enhancing their role.
- Understanding the impact of Financial Literacy efforts on micro entrepreneurs in decision making for borrowing.
- To examine the suitability of proposals to establish a nationwide network of accredited credit counsellors to facilitate credit access by microenterprises and micro entrepreneurs from banks/FIs/NBFCs/MFIs etc.

2 Key Lessons from Earlier Studies and Programs

2.1 Demand Side: Financial needs of microenterprises

2.1.1 Micro Small and Medium Enterprise Finance Market in India

As per an IFC study, the sector's total finance demand, including debt and equity is estimated to be INR 32.5 trillion ($ 650 billion in 2009-10), with 80% of the demand originating from the informal sector. Micro and small enterprises have limited access to equity and, in many cases, their ownership structure prevents infusion of external equity. Information from sector associations suggests a debt-equity structure of 4:1.

The total finance gap in the sector, including debt and equity, but excluding entrepreneur's equity contribution, is INR 20.9 Trillion (USD 418 Billion). This is split between Micro (INR 16.25 Trillion; USD 325 Billion), Small (INR 3.9 Trillion; USD 77 Billion) and Medium (INR 0.78 Trillion; USD 15.4 Billion) enterprises. Following the exclusions already highlighted, the debt gap that is immediately addressable by formal financial institutions is estimated at INR 2.9 trillion ($ 58 billion) and the equity gap at INR 1.9 trillion ($ 38 Billion). The Microenterprises Debt Gap was estimated to be INR 2.3 trillion ($ 46 Billion) in 2009-10 by the IFC.

Banks adopt conservative policies that minimize both credit risk and cost of delivery; thus, they focus more on the less risky small and medium enterprises than on microenterprises. Small finance banks, non-banking finance companies, and microfinance institutions serve specific segments of the market. Lower regulatory overheads and nimble structure enable shorter turnaround time and targeted products. Most non-banking finance companies provide asset finance (primarily transport), and margin finance to the sector. They are rarely the primary source of finance to the sector, due to limited access to adequate growth capital, inadequate credit default support and no priority sector incentives. The following factors come in the way of additional bank financing:

- Microenterprises tend to be too large for microfinance institutions and too small for large commercial banks.
- Cost of acquiring and maintaining accounts is very high.
- Banks have limited information on microenterprises and no access to alternative tools for assessment.
- Micro-entrepreneurs lack adequate collateral.

Informal Finance is Predominant

Informal finance dominates the sector and 95% of it originates from non-institutional sources such as family, friends, relatives, and family business. Institutional channels, comprising trade credit, chit funds, and moneylenders tend to be expensive. Interest rates range from 25% - 60% per annum as compared to 20-25% per annum by non-banking finance companies and 13-16% per annum by commercial banks.

An ADB working paper, Finance for Micro, Small, and Medium-Sized Enterprises in India: Sources and Challenges,[3] tried to identify the factors that encourage financial access for start-up stage enterprises. It found that enterprises highlighted the need for loans without collateral, affordable interest rates, and loan guarantees provided by the government. They also reported the need for guidance by personnel from the financial institution and the need for a paradigm shift by which financial institutions view MSMEs as prospective customers rather than as interference. A few entrepreneurs emphasized that financiers should have faith in lending to businesses that had continued to operate in the same place for generations.

Requirements of Micro entrepreneurs at various stages of their business lifecycle

Survival stage: Enterprises asked for provision of quick finance and flexibility in the repayment schedule.

Growth stage: Enterprises emphasized the need for information on MSME finance schemes and the need for banks and other financial institutions to deliver the benefits prescribed through these schemes, especially those that involve minimal or no collateral. The role of a good relationship with a bank in securing access was also highlighted. Respondents also felt that approved or empanelled suppliers with long-term experience of supplying to the government must get preference over others while taking advantage of assistance through MSME finance schemes.

Sustenance stage: The primary concern reported by enterprises was the interest rate. Respondents felt that their relationship with public banks was better (because it was more personalized) compared with private banks. There was also concern regarding the time needed to process loan requests, with some enterprises resorting to taking gold loans for meeting immediate financial requirements.

Factors that Impede Financial Access Start-up stage[4]

The major concern was the delay in the processing of loan applications. Business owners also felt that it was not practical to frequently visit banks for clarifications and that the role of agents in the system needs to be minimized.

Survival stage: The primary concerns were complications in the process and the response of bankers.

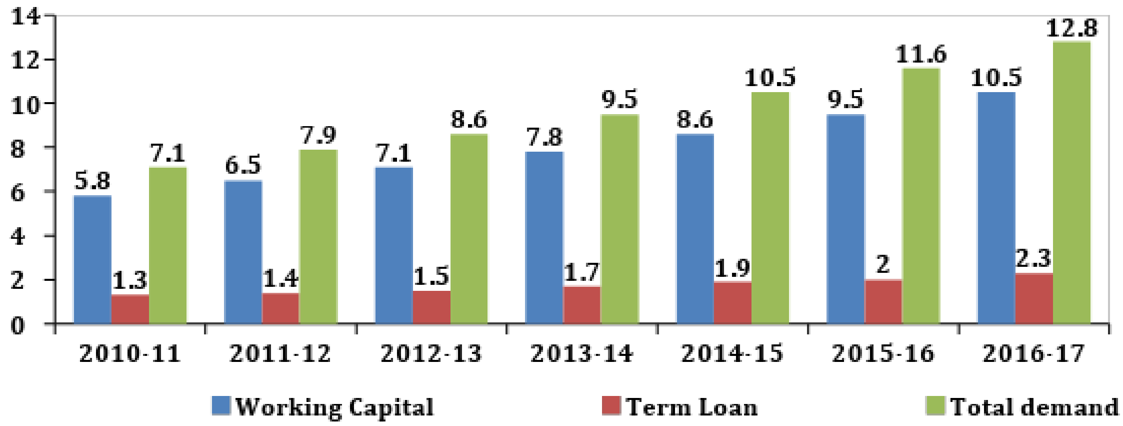
Growth stage: Enterprises reported that bank officials had a very bad attitude toward them because nonperforming assets of MSME schemes were increasing and managers were averse to considering their applications for finance. Two major issues were the long-overdue need to process applications and inadequate information provided about available government schemes. Owners also noted that small businesses were generally volatile in nature, which added to their vulnerability and meant that capital requirements varied throughout the year and that the nature of their operations was not recognized or factored into the lending decisions made by financial institutions.

Sustenance stage: Enterprises highlighted high interest rates as an impediment to financial access. Two other key issues that caused problems were (i) lack of understanding among financial institutions of the sector in which enterprises operated and the corresponding policies needed;

[3] Finance for Micro, Small, and Medium-Sized Enterprises in India: Sources and Challenges- ADBI Working paper series –https://www.adb.org/sites/default/files/publication/188868/adbi-wp581.pdf
[4] Singh and Wasdani, ADBI Working Paper 581.

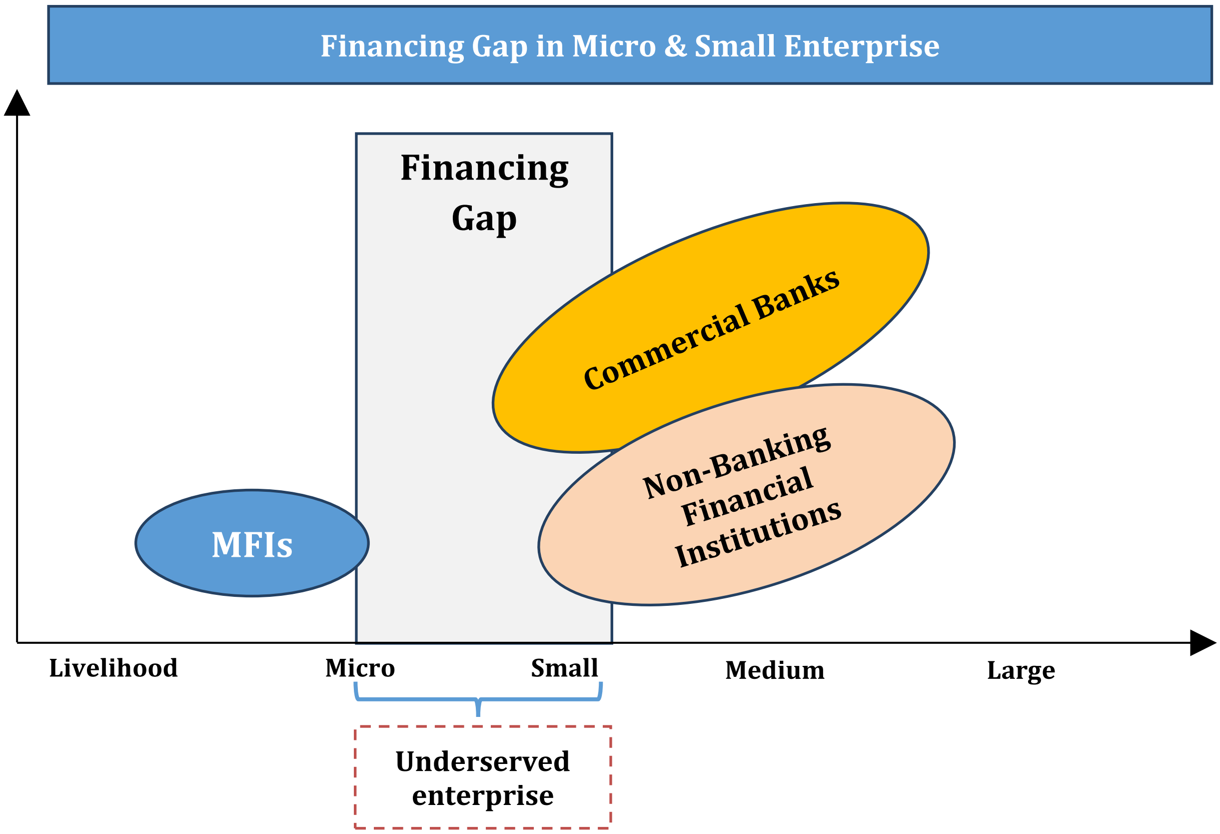
and (ii) red tape involved in hierarchical processing of loans (i.e., moving loan applications from one branch to another), thereby causing a loss of time. Enterprises also suggested that recovery of payments from customers must be enforced through proper implementation of laws.

Figure 1: Demand for credit for Microenterprises, INR trillion



Source: State of Financial Inclusion of Microenterprises: Missing Middle GIZ India

Figure 2: Financing Gap in Micro & Small enterprise



However, only 4% of such units get institutional finance. The MFIs are aggressively targeting the enterprises that require less than INR 50,000. Banks and NBFCs are lending more to small, medium and large enterprises. There is a huge financing gap for the enterprises that require credit ranges between INR 50,000 to INR 500,000. Despite of having a huge potential of credit off take by these enterprises, there are very few institutions in addition to banks that are serving this market with a limited portfolio exposure of 15%-20% (e.g. Vistaar Finance, Fullerton, Intellegrow, AU Financier, etc.) hence the formal source of fund supply is almost negligible to this sector resulting in increased dependency of these enterprises on informal sources.

2.1.2 Composite view of household financing needs

The RBI set up a Committee on Household Finance and its report was released by the Reserve Bank of India in 2017. The committee is an inter-regulatory group consisting of members from one major issue for a distorted assets and liabilities picture in Indian households is the lack of unified framework or guidelines to provide high quality and low-cost financial advice. The committee said that Indian households continue to have high levels of unsecured debt from informal sources like moneylenders, putting them at risk of falling into a debt trap, a study by a central bank-appointed panel has found. Such a dependence on unsecured loans leads to higher costs and traps households in a long cycle of interest repayments. It noted that this phenomenon has been well-documented over the decades, but remains stubbornly persistent.

The reason why these households prefer informal sources of funding is because they have a low nuisance factor, according to the committee. The average Indian household associates the formal banking system with a high administrative burden and complicated paperwork, it said. According to observations made in the report, Indian households need customised and cost-effective financial products. These products would need to be made available without any issues surrounding incentives to those providing it. The report also recommended that complicated paperwork and bureaucratic impediments be reduced, by ensuring that the terms and conditions of financial products are made simple and intuitive to the intended customers.

In the recommendations, the committee proposed a set of sector-specific recommendations to improve the functioning of mortgage, collateralised lending, insurance, pensions, and gold markets. It also proposed improvements to official survey data on Indian household finance, in an effort to spur more detailed analysis and research of these issues in the future, and to assist in the implementation of evidence-based policy.

The committee suggested a set of standardised norms across regulators for financial advice to be implemented in a phased and unified manner, supported with a fiduciary standard for financial advisors. It also proposed that the provision of financial advice be clearly separated from the distribution of financial products, and provided in a manner that avoids conflicts of interest.

2.2 Supply Side: Financing by formal channels

2.2.1 Pradhan Mantri Micro Units Development and Refinance Agency (MUDRA)

In April 2015, the Government of India launched the Pradhan Mantri Micro Units Development and Refinance Agency (MUDRA) to develop and refinance all banks and microfinance institutions (NBFC-MFIs) in the business of lending to micro/small business entities engaged in manufacturing, trading, and service activities. Later this was dubbed the Pradhan Mantri MUDRA Yojana and all loans given by banks to microenterprises were brought under its ambit. Thus, based on the existing portfolio of banks and its incremental growth, the numbers looked large, with banks sanctioning 3.97 crore loans and disbursing an amount of Rs 175,312 crore (1.75 lakh crore or 1.75 Trillion) in 2016-17 as can be seen from the PMMY website data reproduced below:

Table 5: PMMY overall performance

Category	Shishu (Loans up to Rs. 50,000)				Kishore (Loans from Rs. 50,001 to Rs. 5.00 Lakh)				Tarun (Loans from Rs. 5.00 to 10.00 Lakh)				Total			
	No of A/Cs	Sanctioned Amount	Disburseme nt Amount	Outstanding Amt.	No of A/Cs	Sanctioned Amount	Disburseme nt Amount	Outstanding Amt	No of A/Cs	Sanctioned Amount	Disburseme nt Amount	Outstanding Amt	No of A/Cs	Sanctioned Amount	Disburseme nt Amount	Outstanding Amt
General	14835512	35163.69	34615.71	26289.17	1896749	40820.62	39135.12	33416.74	468592	36600.85	35218.49	29508.15	17200853	112585.2	109032.3	89214.06
SC	6985508	15976.2	15774.74	10972.48	139982	2170.84	2040.03	1830.51	10134	750.79	709.32	604.4	7135624	18897.83	18524.08	13407.38
ST	1726857	3831.28	3763.66	2551.94	59987	1030.01	954.25	847.1	5658	411.5	387.64	320.03	1792502	5272.74	5105.55	3719.07
OBC	12949936	30129.63	29737.77	20593.76	566784	9523.67	8933.73	7830.89	55348	4119.52	3978.69	3444.15	13572068	43772.82	42650.19	31868.8
Total	36497813	85100.74	83891.88	60407.35	2663502	53545.14	51063.12	43925.22	539732	41882.66	40357.13	33876.74	39701047	180528.5	175312.1	138209.3
Out of above																
Women Entrepreneurs	28472344	66997.91	66185.86	46684.74	624925	9541.63	8733.38	15938.01	49625	3750.13	3330.54	2917.9	29146894	80289.68	78249.77	65540.65
New Entrepreneurs /Accounts	8110486	18720.64	18429.78	13250.49	1586010	31757.94	300001.99	25841.24	292974	22481.56	21542.19	18043.26	9989470	72960.14	69973.96	57134.98
Minority	4786834	11341.14	11186.68	7545	324071	5690.97	5380.82	4761.6	43646	3243.96	2906.7	2488.15	5154551	20276.07	19474.2	14794.75
PMJDY OD Account	1423715	417.64	312.62	168.12	0	0	0	0	0	0	0	0	1423715	417.64	312.62	168.12
Mudra Card	147371	386.14	356.44	318.06	27948	550.35	543.42	438.63	8605	628.12	615.98	512.24	183924	1564.61	1515.84	1268.93
NULM	5841	23.03	21.66	18.88	9870	155.43	138.98	124.03	117	8.31	7.94	7.25	15828	186.77	168.59	150.16
NRLM	73449	314.76	263.78	230.01	75634	1293.93	956.61	817.57	6437	395.74	166.71	134.87	155520	2004.42	1387.11	1182.45
Other Govt. Sponsored Prog.	1036913	2664.79	2623.55	1968.52	189658	3377.27	3140.73	2582.56	27414	2201.58	2086.45	1792.68	1253985	8243.64	7850.74	6343.76

Source: PMMY report

The data indicates there hardly has been any significant growth in the micro and small loan portfolio of the banking sector over the previous two years in spite of the refinance and credit guarantee support provided to banks by the government.

To the estimated credit demand of 11.54 trillion for microenterprise sector during 2016-17, the existing credit flow of bank to microenterprises along with incremental credit through MUDRA scheme is able to meet 15% of the total demand (1.75 trillion) with respect to disbursement and 77% with respect of no. of clients. This shows the credit flow to microenterprise through banking sector has barely grown in the last one year.

Table 6: Credit flow to microenterprise

MUDRA	FY 2015-16		FY 2016-17		Percentage Increase	
Category	**No. of Accounts (Lakh)**	**Amount Disbursed (Rs. Crore)**	**No. Of Accounts (Lakh)**	**Amount Disbursed (Rs. Crore)**	**No. Of Accounts**	**Amount Disbursed**
Shishu	324.02	62,028	364.97	83,891.9	13%	35%
Kishore	20.69	41,073	26.63	51,063.1	29%	24%
Tarun	4.1	29,854	5.39	40,357.1	31%	35%
Total	**348.81**	**132,955**	**397.01**	**175,312**	**14%**	**32%**

Source: PMMY report

State-wise Number of Accounts, Loan Sanction and Disbursement under Pradhan Mantri Mudra Yojana (PMMY) in India

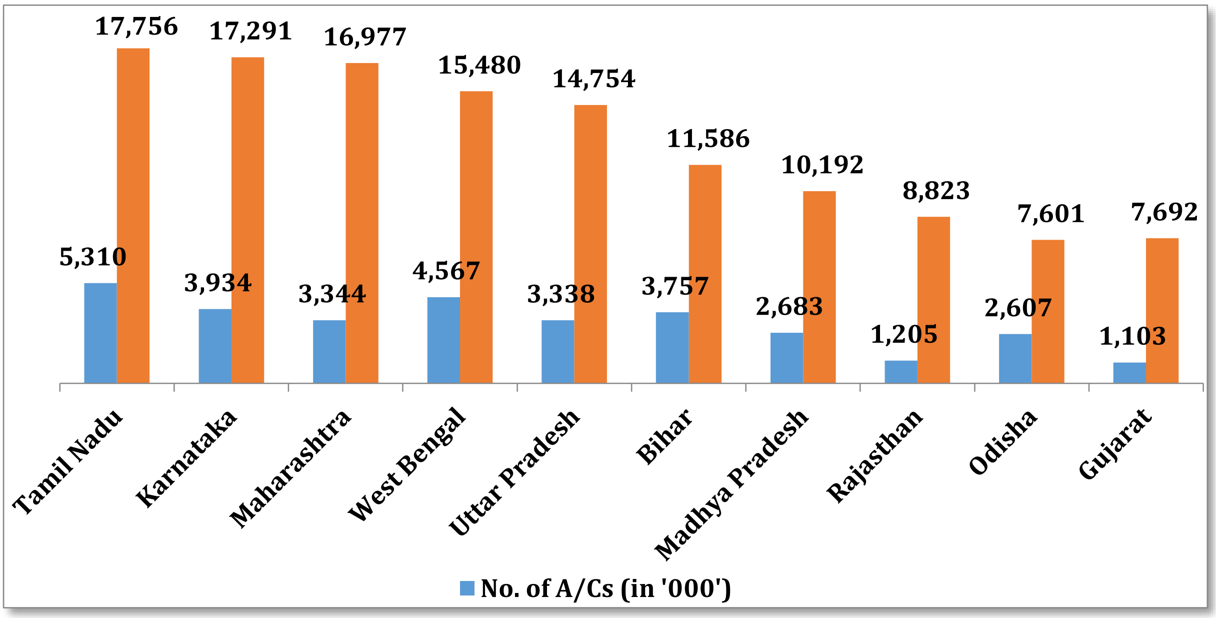
Table 7: State-wise PMMY performance

State/UT	No. of A/Cs	Sanctioned Amt. Rs. Crore	Disbursement in Rs. Crore	No. of A/Cs	Sanctioned Amt. Rs. Crore	Disbursement in Rs. Crore
Tamil Nadu	47,81,567	15,846	15,497	53,09,857	18,053	17,756
Karnataka	44,59,609	16,861	16,469	39,33,578	18,003	17,291
Maharashtra	35,35,065	13,806	13,372	33,44,154	17,287	16,977
West Bengal	26,28,548	8,034	7,740	45,66,505	15,695	15,480
Uttar Pradesh	33,45,382	12,276	11,881	33,37,547	15,283	14,754
Bihar	24,51,439	7,554	7,266	37,56,716	12,191	11,586
Madhya Pradesh	25,11,191	8,097	7,769	26,83,052	10,506	10,192
Rajasthan	11,59,819	5,485	5,248	12,04,837	9,025	8,823
Odisha	23,43,261	5,695	5,436	26,06,769	7,891	7,601
Gujarat	10,86,407	6,035	5,910	11,03,453	7,782	7,692
Kerala	8,30,411	4,858	4,727	9,82,260	6,289	6,140
Andhra Pradesh	7,95,688	6,104	5,791	5,87,569	6,078	5,732
Assam	4,27,272	1,818	1,728	12,55,754	4,908	4,825
Punjab	6,53,973	3,572	3,484	7,05,569	4,641	4,512
Jharkhand	8,72,868	2,944	2,846	10,23,593	4,004	3,909
Telangana	4,00,761	3,835	3,694	4,82,694	3,878	3,780
Haryana	7,45,535	3,259	3,153	7,16,622	3,844	3,698
Delhi	3,94,388	2,948	2,858	2,24,975	3,763	3,701

State/UT	No. of A/Cs	Sanctioned Amt. Rs. Crore	Disbursement in Rs. Crore	No. of A/Cs	Sanctioned Amt. Rs. Crore	Disbursement in Rs. Crore
Chhattisgarh	6,39,711	2,266	2,156	8,84,941	3,334	3,210
Uttarakhand	3,60,007	1,788	1,745	2,86,579	1,974	1,914
Jammu and Kashmir	57,974	1,185	1,152	89,712	1,845	1,664
Himachal Pradesh	85,564	999	966	82,851	1,282	1,214
Tripura	68,146	372	337	2,53,807	999	969
Puducherry	82,866	338	332	1,30,360	491	485
Goa	45,471	399	376	31,289	390	373
Chandigarh	22,605	212	205	19,039	229	221
Meghalaya	19,151	166	162	23,915	190	186
Manipur	24,021	131	120	21,865	156	142
Nagaland	5,134	86	77	11,051	114	104
Mizoram	7,772	87	78	6,973	101	90
Sikkim	6,889	60	55	19,865	100	97
Arunachal Pradesh	4,625	74	72	6,109	81	79
Andaman and Nicobar Islands	24,719	218	213	3,353	80	78
Dadra and Nagar Haveli	1,236	22	21	2,587	23	23
Daman and Diu	1,109	12	12	774	13	12
Lakshadweep	740	7	5	473	6	5

Source: IndiaStat

Figure 3: PMMY disbursement profile



2.2.2 Credit Guarantee Fund Scheme for Micro and Small Enterprises (CGTMSE)

The scheme encourages member institutions to extend collateral free financing (both fund-based and non-fund-based) to the MSE segment with maximum limit of INR 10 million (USD 0.2 million). For credit applications covered under the scheme, the trust extends guarantee cover up to 85% of outstanding amount on default.

Table 8: CGTMSE cover limits

Beneficiary Category	Value of the Credit Disbursed		
	Up to INR 0.5 million	INR 0.5 –INR 5 million	INR 5 –INR 10 million
Micro Enterprise Segment	85% of amount in default with maximum limit of INR 0.45 million	75% of amount in default with maximum limit of INR 3.75 million	INR 3.75 million with 50% of amount in default above INR 5 million with a maximum limit of INR 6.25 million
Women entrepreneurs and Enterprises in North East	80% of amount in default with maximum limit of INR 4 million		INR 4 million with 50% of amount in default above INR 5 million with a maximum limit of INR 6.5 million
Other Category	75% of amount in default with maximum limit of INR 3.75million		INR 3.75 million with 50% of amount in default above INR 5 Million with a maximum limit of INR 6.25 million

Source: Reserve Bank of India

2.2.3 Operational highlights of CGTMSE

Table 9: Operational highlights of CGTMSE

Period	No. of Active MLIs	No. of Credit Facilities Approved	Amount of Guarantees Approved (Rs. Million)	Cumulative Guarantees Approved (Rs. Million)
FY 2000-01	9	951	60	60
FY 2001-02	16	2,296	300	360
FY 2002-03	22	4,955	590	940
FY 2003-04	29	6,603	1180	2,120
FY 2004-05	32	8,451	2670	5,390
FY 2005-06	36	16,284	4620	10,010
FY 2006-07	40	27,457	7050	17,050
FY 2007-08	47	30,285	10,560	27,020
FY 2008-09	57	53,708	21,990	48,240
FY 2009-10	85	1,51,387	68,750	1,15,600
FY 2010-11	106	2,54,000	1,25,890	2,38,460
FY 2011-12	109	2,43,981	1,37,840	3,71,390
FY 2012-13	117	2,88,537	1,60,620	5,26,000
FY 2013-14	117	3,48,475	1,81,880	7,00,260
FY 2014-15	119	4,03,422	2,12,750	9,04,460
FY 2015-16	119	5,13,978	1,99,490	10,89,910

Source: Ministry of Micro, Small and Medium Enterprises

2.2.4 Prime Minister Employment Generation Programme (PMEGP)

The scheme is implemented by Khadi and Village Industries Commission (KVIC) functioning as the nodal agency at the national level. At the state level, the scheme is implemented through State KVIC Directorates, State Khadi and Village Industries Boards (KVIBs), District Industries Centres (DICs) and banks. In such cases, KVIC routes government subsidy through designated banks for eventual disbursal to the beneficiaries / entrepreneurs directly into their bank accounts. The maximum cost of the project/unit admissible in the manufacturing sector is Rs. 25 lakh and in the business/service sector, it is Rs. 10 lakh.

Table 10: State/Industry-wise number of projects setup under PMEGP in India

States/UTs	FY 2013-14	FY 2014-15	FY 2015-16	FY 2016-17	CAGR
Nagaland	419	416	623	1,018	34%
Goa	42	78	91	90	29%
Chhattisgarh	867	847	1,277	1,598	23%
Tripura	1,307	787	642	2,297	21%
Manipur	733	747	685	1,265	20%
Puducherry	43	58	65	66	15%
Gujarat	914	1,289	1,419	1,386	15%
Haryana	939	1,175	1,248	1,377	14%
Rajasthan	1,278	1,976	1,988	1,749	11%
Odisha	2,222	2,013	2,876	3,029	11%
Punjab	942	1,153	966	1,266	10%
Tamil Nadu	2,269	2,858	2,463	2,941	9%
Karnataka	2,760	2,431	2,140	3,575	9%
Telangana	-	604	660	664	5%
Maharashtra	2,118	3,469	2,343	2,325	3%
Uttarakhand	1,236	1,333	1,136	1,345	3%
West Bengal	3,273	3,397	1,873	3,528	3%
Kerala	1,505	1,344	1,369	1,584	2%
Bihar	3,121	1,639	2,430	3,234	1%
Uttar Pradesh	4,356	4,891	4,365	4,074	-2%
Andhra Pradesh	1,453	937	642	1,357	-2%
Chandigarh	55	36	43	47	-5%
Himachal Pradesh	1,112	1,244	1,077	941	-5%
Delhi	142	198	256	119	-6%
Andaman and Nicobar	237	161	119	195	-6%
Jammu and Kashmir	1,849	1,565	2,207	1,492	-7%
Meghalaya	414	555	603	329	-7%
Madhya Pradesh	2,463	2,737	1,979	1,940	-8%
Assam	8,279	5,015	3,483	6,028	-10%

States/UTs	FY 2013-14	FY 2014-15	FY 2015-16	FY 2016-17	CAGR
Mizoram	777	817	1,134	425	-18%
Jharkhand	2,612	1,699	1,839	1,300	-21%
Arunachal Pradesh	657	652	35	301	-23%
Sikkim	66	16	110	27	-26%
Lakshadweep	-	31	-	-	
India	**50,460**	**48,168**	**44,340**	**52,912**	**2%**

Source: IndiaStat

The above table indicates, the compound annual growth rate (CAGR) of 2% in the number of projects setup under Prime Minister Employment Generation Programme (PMEGP) in the last 4 years. Assam exceeds all the other states in supporting the number of projects under this scheme followed by Uttar Pradesh and Karnataka.

Table 11: State-wise margin money subsidy allocated, utilized, number of projects assisted and estimated employment generation under PMEGP in 2016-17

State	Subsidy Allocated Rs. Lakh	Subsidy Utilized Rs. Lakh	Percentage Utilization	No. of Projects
Andaman and Nicobar Islands	100	-	0%	195
Andhra Pradesh	2,337	2,388	102%	1,357
Arunachal Pradesh	500	149	30%	301
Assam	5,636	1,788	32%	6,028
Bihar	6,910	2,200	32%	3,234
Chandigarh	100	33	33%	47
Chhattisgarh	4,493	625	14%	1,598
Delhi	300	19	6%	119
Goa	372	-	0%	90
Gujarat*	5,398	1,707	32%	1,386
Haryana	3,371	457	14%	1,377
Himachal Pradesh	1,970	360	18%	941
Jammu and Kashmir	3,541	-	0%	1,492
Jharkhand	4,166	701	17%	1,300
Karnataka	4,942	5,355	108%	3,575
Kerala	2,446	1,193	49%	1,584
Lakshadweep	50	-	0%	-
Madhya Pradesh	8,527	1,741	20%	1,940
Maharashtra	6,111	1,070	18%	2,325
Manipur	1,742	740	43%	1,265
Meghalaya	1,748	151	9%	329
Mizoram	1,253	127	10%	425

State	Subsidy Allocated Rs. Lakh	Subsidy Utilized Rs. Lakh	Percentage Utilization	No. of Projects
Nagaland	1,752	135	8%	1,018
Odisha	5,202	1,730	33%	3,029
Puducherry	150	106	71%	66
Punjab	3,504	1,000	29%	1,266
Rajasthan	5,501	124	2%	1,749
Sikkim	200	2	1%	27
Tamil Nadu	5,291	2,382	45%	2,941
Telangana	2,005	911	45%	664
Tripura	1,579	1,748	111%	2,297
Uttar Pradesh	12,982	6,305	49%	4,074
Uttarakhand	2,141	195	9%	1,345
West Bengal	3,680	1,330	36%	3,528
India	**1,10,000**	**36,774**	**33%**	**52,912**

Source: IndiaStat

The above table indicates, only 33% of the allocated subsidy were utilised to serve the microenterprise sector by banks.

2.3 Supply Side: Enhancing access through alternative channels

Micro spread district level data for microfinance industry[5]

At an aggregated industry level (i.e. for all FIs put together), some of the key highlights of FY 16-17 at the state level are as under:

- The microfinance industry has business spread across 35 states and union territories.
- Largest states in terms of loan amount outstanding are West Bengal and Tamil Nadu, together accounting for 30% of the total industry loan amount outstanding.
- They are followed by Karnataka and Maharashtra, with loan amount outstanding of Rs. 9,903 Cr and Rs 9,674 Cr. Top 6 states in terms of portfolio, West Bengal, Tamil Nadu, Karnataka, Maharashtra, Bihar and Uttar Pradesh account for 64% of the total industry portfolio. Top 10 states account for 86% of the total industry portfolio.

2.4 Supply Side: Financing from informal sources

The National Commission for Enterprises in the Unorganised Sector (NCEUS), 2007, established a Task Force on Credit under the chairmanship Prof VS Vyas.[6] The Task Force report's main findings are reproduced below. It showed that in 2001-02, only 4.1 percent of all enterprises have

[5] MFIN publication in partnership with Equifax -Heat Map of Number of MFIs; as of 31st March 2017: MicroSpread District Level Data for Microfinance Industry (Limited Circulation)

[6] Report on Conditions of Work and Promotion of Livelihoods in the Unorganised Sector, The National Commission for Enterprises in the Unorganised Sector (NCEUS), 2007. http://nceuis.nic.in/condition_of_workers_sep_2007.pdf p.181

access to institutional credit, but within them, only 3.1 percent of the unorganised enterprises had access to institutional credit. The banks in the post reform period had turned away from lending to small borrowers – the loan amount to borrowers below Rs. 25,000 declined from 21 percent of the net bank credit in 1985 to 3.7 percent in 2005.

The study also revealed that despite the RBI guidelines to extend credit to micro-enterprises up to Rs. five lakh without collaterals, commercial banks are not willing to do so. Only 26 per cent of the micro-enterprises who received credit had got credit without collateral security. The cost of credit was high as half of the credit that micro-enterprises were getting was from non-institutional sources, including moneylenders, input suppliers and output buyers. The situation had not improved even after the growth decade of 1998-2008.

Figure 4: NCEUS Task Force on Credit

This report addresses itself mainly to that segment of non-farm unorganized enterprise whose investment in plant and machinery is less than Rs 0.5 million.

Key findings:

- 93.8% of the SSI investments in plant & machinery is less than Rs 0.5 million (3rd census of SSI)
- 97.4% of the non-farm enterprise employed not more than five persons (55th NSS round)
- 14.3% of the SSI unit is registered sector availed bank finance, while only 3.1% of the unregistered units had access to bank finance (3rd census of SSI 2001-02)
- almost equal number of enterprise (4.1%) had access to institutional credit and to non-institutional credit including those from relatives & money lenders (55th NSS round)
- the number of SSI accounts declined from 3.0% of the total to 1.2 % and the credit from 11.5% of the net bank credit to 4.1%
- the decline of SSI credit as percent of net bank credit from 15.34% in 1997-98 to 6.4% in 2005-06
- agriculture sector received only 11.9% of the bank credit against the stipulation of 18%
- insistence on collateral even on loan up to Rs. 0.5 million, in spite of the RBI guidelines to this effect
- the share of small loans (below Rs.25000) in the total outstanding of scheduled commercial banks declined from 21% in June 1985 to 3.7% in March 2005
- disinterested banks in advancing loans under credit guarantee scheme which is available for loans up to Rs. 2.5million
- the higher cost of credit for unorganized enterprise
- inadequate institutional infrastructure at field level

2.4.1 The All India Debt and Investment Survey-2012

The highlights[7] are given below. From the data on "incidence of indebtedness", a surrogate measure for access to credit, only 31.4 percent of all households had access to credit. Access to credit rose along with the asset ownership class. The lowest five deciles had access less than the

[7] Household Indebtedness in India, 70th Round of National Sample Survey, Ministry of Statistics and Program Implementation, Govt of India, 2013. http://mospi.nic.in/sites/default/files/publication_reports/nss_577.pdf

average, which itself was low enough. The table below indicates that the access to credit from formal institutions was even lower, with only 17.2 percent of all rural and 14.8 percent of all urban households getting access to formal institutions.

Table 12: Incidence of indebtedness to institutional & non-institutional credit

Decile class of HH asset holding	Incidence of Indebtedness (%)					
	Rural			Urban		
	IOI (%)	AOD per hh (Rs.)	AOD per indebted hh (Rs.)	IOI (%)	AOD per hh (Rs.)	AOD per indebted hh (Rs.)
1	7.9	14	19.6	3.4	6.5	9.3
2	7.4	17.1	22.3	6.2	10.1	14.6
3	10.8	19.1	27.1	10.6	11.9	20.2
4	12.4	18.2	27.5	12.5	14.4	24.2
5	13	21.9	30.9	12.1	12.6	21.7
6	16.9	21.6	33	14	12.7	23.4
7	19.1	19.3	32.7	15.7	11.6	23.8
8	22.2	21.6	37.3	18.9	10.1	25.4
9	29.2	22.1	42.6	25.6	7.1	29.4
10	32.6	15.3	41.3	29.1	5.7	31.7
All	17.2	19	31.4	14.8	10.3	22.4

2.4.2 Linkages between moneylenders and formal credit channels

The RBI had established a technical group on this topic which gave its report in 2007.[8] Various studies in India and abroad show that the informal sector is better at serving the sectors neglected by banks such as small businessmen, traders, poor transport operators, handloom weavers, small farmers, self-employed people and women. They are also better at recovering loans. They have a better market knowledge and lower transaction costs. They are flexible and can customize the products to suit the needs of individual borrowers. They respect the borrowers' privacy. On the other hand, the formal sector has strengths in terms of its access to low- cost funds, providing safe avenues for savings and access to the payments system. But their procedures and practices deter the poor.

Also both theoretically and empirically, linkages are at an embryonic stage in many countries. Issues of mechanism, design, institutions, and incentives are relatively new areas to explore. Furthermore, historically, policymakers have viewed moneylenders as exploitative. This adds a moral and equity dimension that acquires political weight. Indeed, in certain cases, banks may not find it worthwhile since normally, one bank would not like to provide another with borrower training and management skills gratis. Though no study provides an independent evaluation on the effectiveness of moneylenders with respect to non-moneylenders, if banks hire moneylenders, they need not expend resources on training since moneylenders are already

[8] Report of the Technical Group to Review Legislations on Money Lending Linkages between Moneylenders and Formal Credit Channel Chapter -5 https://rbi.org.in/scripts/BS_ViewBulletin.aspx?Id=10852

experienced in this field. Therefore, both commercial banks and the informal institutions would need additional incentives for these linkages. (Varghese 2004).

In India, initiatives have been taken to bridge the gap in lending by banks. Guidelines have been issued to the effect that the services of Banking Correspondent (BC)/Banking Facilitator (BF) model may be utilised by banks for expanding their outreach in rural areas and in previously unbanked areas. However, only a few banks have adopted these innovations, and there have been reservations in widely expanding/implementing the models. One of the reasons for the scheme not taking off is reported to be the restriction on the BC/BF to recover charges directly from the ultimate borrower.

The advantages of forging links with moneylenders for more efficient credit delivery according to the branch managers are:

- Better identification of prospective customers in view of better information with moneylenders.
- Better coverage of remote and unbanked rural areas.
- Facilitate better recovery.
- Increase in the portfolio of banks.
- Availability of credit at lower rates compared to what is presently being paid by borrowers to moneylenders.
- Help in avoiding multiple lending to same borrowers against same assets by both the banks as well as moneylenders.
- Save the time and effort of banks in credit appraisal, making pre-sanction visits, documentation processes, credit supervision, and recovery, etc., thereby facilitating better credit flow especially in the context of staff shortages at rural branches.
- Provision of services during the bank holidays as well as after banking hours, which would prove beneficial to people in need of funds in emergency situations.

The disadvantages are:

- The inability of the banks to enforce end-use of funds, reasonableness of interest rates and ensure fair recovery practices.
- The likelihood of monopolistic practices if banks withdraw and lend only through moneylenders.
- Scope for increased political influence.
- High interest rates, diversion of funds for furtherance of moneylenders' own businesses leading to further malpractices as more funds are made available to them.
- Adverse effect on direct lending and possibility of deterioration of the direct relationship between banks and customers and continuance of coercion in recovery, ultimately resulting in tarnishing the bank's image.

Most moneylenders felt they needed a commission of at least 6 percent to cover their transaction cost as they were dealing with very small loans. They were also concerned about the non-availability of relief/concessions in the event of non-wilful defaults. They feared that banks might not allow the facility of automatic rescheduling of the loan and they would be forced to repay on behalf of the farmer-borrowers as per the original repayment schedule, which might lead to recovery risk. They also apprehended that formal linkages might attract adverse attention from income tax and police authorities, and feared harassment from the co-operative department if registration under money lending were made compulsory for accessing bank finance; instead, some moneylenders preferred regulation/inspection by some outside agencies, such as NABARD.

The following policy recommendations were made by the RBI Technical Group –

i. Compulsory Registration of the moneylenders

Some of the moneylenders registered their business under the respective State Moneylender's act. The study shows that the moneylenders who registered under the act are charging less rate of interest compared to the unregistered moneylenders. However the number of registered moneylenders is very small relative to the unregistered moneylenders. The state government has to ensure all the moneylenders to be registered and abide by the rules and regulations of the act.

ii. Awareness on Moneylenders Act

Around 22 states of India have money lending laws.[9] However, it was observed that majority of the entrepreneurs are not aware of the respective State Moneylender's act and paying interest rate as demanded by the moneylenders. For e.g. As per the Karnataka Moneylenders and Pawn Brokers Act 1961 and Rules 1965,[10] the moneylenders supposed to charge interest rate 14% per annum (for secured loans) and 16% per annum for unsecured loans, but as per the entrepreneurs information the moneylenders are charging high interest rate compare to the rates prescribed by act. The maximum interest rate that can be charged by moneylenders should be notified by the state government from time to time.

iii. Bank loans to moneylenders for on lending to micro entrepreneurs

Formal banks are experiencing many microenterprise default cases due to several reasons including the bank staff do not have required information to identify the right borrowers, understanding about the type of enterprises they are engaged in, required time to loan appraisal, loan monitoring etc. On the other hand, moneylenders are successful in lending business because of the in-depth understanding of the local community, culture, socioeconomic conditions etc. Banks may use the local eligible (for e.g. education) moneylenders as their credit counsellors and provide loans to them for on lending to entrepreneurs.

iv. Use of Input Suppliers

The Government needs to explore how to mainstream and use the input suppliers to meet the credit needs of entrepreneurs.

2.5 Recent policy initiatives and guidelines

2.5.1 Revised priority sector lending guidelines

Priority sectors refer to those sectors of the economy such as agriculture, small enterprises and housing for poor people which, though viable and creditworthy, may not get timely and adequate

[9] List of Money Lending Laws in India.
https://rbi.org.in/scripts/PublicationReportDetails.aspx?UrlPage=&ID=513#sum

[10] Karnataka Moneylenders and Pawn Brokers Act 1961 and Rules 1965 http://sahakara.kar.gov.in/faqML&PB.html

credit in the absence of a special dispensation. The priority sector lending policy of the Reserve Bank envisages that banks extend credit to the priority sector as part of their normal business operations and not as a corporate social responsibility. Towards this end, pricing of all credit has been made free, though with the expectation that it will not be exploitative. Drawing upon the recommendations of an Internal Working Group set up by the Reserve Bank, revised guidelines on priority sector lending were issued in April 2015. The salient features are:

- Separate targets of 8% for small and marginal farmers (within the agriculture target of 18%) and 7.5% for microenterprises to be achieved by 2017. After a review in 2017, these targets will be made applicable to foreign banks with 20 branches and above from 2018. Coverage of the priority sector widened to include medium enterprises, social infrastructure and renewable energy (Bank loans of up to Rs. 150 million for solar-based power generators, biomass-based power generators, wind mills, micro-hydel plants, etc. For individual households, the loan limit is Rs. 1 million per borrower). Priority sector lending compliance to be monitored on a 'quarterly' average basis from 2016-17.
- Priority sector lending certificates (PSLCs) made an eligible tradable instrument for achieving priority sector targets. Educational loans (including loans for vocational courses) up to Rs. 1 million irrespective of the sanctioned amount made eligible for the priority sector. Export credit up to 32 per cent made eligible as part of the priority sector for foreign banks with less than 20 branches. For domestic banks and foreign banks with 20 branches and above, the incremental export credit over the corresponding date of the preceding year reckoned up to 2% of Adjusted Net Bank Credit (ANBC) or Credit Equivalent of Off-balance Sheet Exposure (CEOBE) (whichever is higher), made eligible as part of the priority sector, subject to certain conditions. Foreign banks with less than 20 branches required to achieve the total priority sector target of 40 per cent of ANBC or CEOBE, whichever is higher, in a phased manner by 2020.
- Priority sector lending certificates (PSLCs) the scheme of priority sector lending certificates (PSLCs) was operationalised on April 7, 2016 to facilitate the achievement of priority sector lending targets by banks. It simultaneously incentivises banks with surplus by making available a mechanism to sell their over-achievement, thereby enhancing lending to the categories under the priority sector. The PSLC scheme enables banks that have under-achieved their PSL targets to achieve them by purchasing PSLCs from banks that have overachieved the targets/ sub targets. Four types of PSLCs viz. General, Agriculture, Small and Marginal Farmers and Microenterprises can be bought/ sold by banks. The entities eligible for trading in PSLCs include public sector banks, private sector banks, regional rural banks, urban co-operative banks and small finance banks. The PSLC mechanism does not involve transfer of credit risk or underlying assets.
- Banks have been provided with an on-line anonymous trading platform through the Reserve Bank's Core Banking Solution (CBS) portal e-Kuber for trading in PSLCs. PSLCs have a standard lot size of Rs.2.5 million or multiples thereof and are valid till the end of the financial year, i.e., March 31, irrespective of the date of issuance. The total volume traded at the end of September 2016 was about Rs. 140 billion.

2.5.2 Phase III of Financial Inclusion Plan (FIP) of the RBI

With the conclusion of Phase II (2013- 16) of FIP in March 2016, all domestic scheduled commercial banks (including RRBs) were advised to set new board approved FIP targets for the next three years, viz. 2016-19. Recognising the important role of robust monitoring, banks were also advised to submit district-level data on the progress made under FIPs. A snapshot of the progress reported by banks under their FIPs for certain key parameters as on September 30, 2016, is given below:

The number of banking outlets in rural locations went up from 67,694 in March 2010 to 589,849 in September 2016. Urban locations covered through BCs went up from 447 in March 2010 to 91,039 in September 2016. The total number of Basic Savings Bank Deposit Accounts (BSBDAs) increased from 73.5 million in March 2010 to 495.2 million in September 2016. The surge in opening of the BSBDAs can be attributed to the push given by the Government of India under the Pradhan Mantri Jan Dhan Yojana. The total number of KCC issued went up from 24.3 million in March 2010 to 46.4 million in September 2016. General credit cards issued went up from 1.4 million in March 2010 to 11.5 million in September 2016. BC-ICT transactions recorded a considerable increase during these years. From 26.5 million transactions recorded for the quarter ended March 2010, it increased to 550.6 million in the quarter ended September 2016.

Progress made under financial inclusion plans – as on September 2016 (Scheduled commercial banks including RRBs) is below:

Table 13: Progress made under FI plans

Particulars	Year ended March 2010	Year ended March 2016	Half year ended September 2016
Banking Outlets in Rural Locations - Branches	33,378	51,830	52,240
Banking Outlets in Rural Locations - Branches less mode	34,316	534,477	537,609
Banking Outlets in Rural Locations - Total	67,694	586,307	589,849
Urban locations covered through BCs	447	102,552	91039
BSBDA - Through branches (No. in Million)	60	238	247
BSBDA - Through branches (Amt. in Billion)	44	474	538
BSBDA - Through BCs (No. in Million)	13.3	230.8	247.8
BSBDA - Through BCs(Amt. in Billion)	10.7	164	181.1
BSBDA - Total (Amt. in Billion)	73.5	469	495
BSBDA - Total (No. in Billion)	55	638.1	719
OD Facility availed in BSBDAs (No. in Million)	0.2	8	8.4
OD Facility availed in BSBDAs (Amt. in Million)	0.1	14.8	18.1
KCCs- Total (Amount in Billion)	24	47	46
KCCs- Total (No. in Billion)	1,240	5,131	5,543
GCCs- Total (No. in Billion)	1.4	11.3	11.5
GCCs- Total (Amount in Billion)	35	1,493	1,613
ICT -A/Cs BC Total no. of txns (in million)	27	827	551

Particulars	Year ended March 2010	Year ended March 2016	Half year ended September 2016
ICT -A/Cs BC Total no. of txns (in billion)	7	1,687	1,199

2.5.3 Accreditation of credit counsellors

Subsequent to the announcement in the first Bi-Monthly Monetary Policy Statement for 2016-17, Reserve Bank, after holding discussions with IBA, SIDBI and other stakeholders, finalised a framework for accreditation of credit counsellors, who can act as facilitators for entrepreneurs to access the formal financial system. Accordingly, the framework has been provided to SIDBI who have been assigned the task of rolling out the Certified Credit Counsellors scheme by acting as their registering authority.

2.5.4 Scaling-up the BC model

The Reserve Bank of India has prepared the framework for graded certification/training programme for BCs. BCs with a good track record who would undergo advanced training and receive certification shall be entrusted with more complex tasks such as handling/delivery of financial products that go beyond deposits and remittances. In order to have a tracking system of BCs, a framework for a Registry of BC agents covering all BCs, both existing and new, has been created. The registry is intended to capture basic details including the identity of a BC, location of fixed point BCs and nature of operations.

3 Methodology, Approach and Coverage of the Study

The study focused on understanding various sources of credit used by microenterprises and micro entrepreneurs from both formal and informal sources. A special focus was given in understanding the informal sources of credit including, why entrepreneurs availed loans from informal sources, despite having a choice of taking cheaper loans from formal financial institutions like banks. The study also reviewed credit features including interest rates, repayment conditions, documentation, processing time etc. The study examined both supply side and demand side causes for the dependency of the micro entrepreneurs on informal channels for credit. From supply side, the study also scanned various alternative channels/models of credit which are currently meeting the credit requirements of the microenterprises and their key features. The study aims at suggesting the possible way to formalize/ regulate the informal sources in India based on the primary survey and secondary research and finally come out with recommendations required for policy interventions and corrective measures for designing the policy/act for institutionalizing/mainstreaming the informal credit sources.

3.1 Selected districts and rationale for selection

Geographical location for study: Four districts (Varanasi, Chandrapur, Bidar and Ganjam) were selected to carry out the study. The districts were carefully (purposively) selected to represent various zones of the country and also based on the various parameters like migration, the degree of penetration of microfinance institutions' operations etc.

Table 14: Selected districts

Zone	State	District	Basis of Selection
North	Uttar Pradesh	Varanasi	High density of MFIs
South	Karnataka	Bidar	Low Density of MFIs
East	Odisha	Ganjam	High density of MFIs
West	Maharashtra	Chandrapur	Low density of MFIs and high density of informal credit channel

Note: High density and low density of MFI operational districts selected based on the data from; MFIN District Level Data of Microfinance Industry -31st March 2017

3.2 Data collection sources and Sampling:

The study aimed at collection of data from 900 respondents (800 respondents through Household Interviews of Microenterprise Owners and 100 respondents through Focus Group Discussions of Microentrepreneurs). The research teams also interviewed key informants from institutions like NABARD, bank branch managers, MFIs,[11] NGOs,[12] Enterprise related Training Centres etc. who are important stakeholders in the promotion and supporting the microenterprises and financial literacy. The sampled data microenterprises were across rural, semi-urban and urban areas

[11] Microfinance Institutions

[12] Non-Governmental Organisations engaged in promotion of Self Help Groups and Micro enterprise development

(proportion of sample drawn from areas varies across locations) and the sampling is random across these activity strata, thus we used stratified random sampling.

Table 15: Data Collected from field as part of the study

No. of MEs interviewed	No. MEs covered through FGDs	Key Informant Interviews conducted	Case Studies
813	106	28	6

3.3 Detailed methodology

3.3.1 Secondary Research

The secondary research involved reviewing various guidelines of legal and regulatory bodies like RBI, NABARD, Mudra Loan policy documents, study the experiments done in India on formalization of moneylenders activities/business etc. review studies done on access to credit sources to small borrowers, dependency on informal finance, alternative sources of credit available to small borrowers, initiatives taken by various institutions within India and other countries to formalize the money lenders under certain policy and framework and learnings from such initiatives.

3.3.2 Household Survey of Microenterprise and Micro Entrepreneurs

After identifying data elements to be collected, the questionnaire was designed, developed and finalised in consultation with SIDBI. An app was developed based on the questionnaire with technical assistance from a technology-based company. The field investigators were trained on how to fill the questionnaire and were also tested on a sample of microenterprises.

The survey questionnaire has the following structure: household details, microenterprise details, access to finance, microenterprise assets, and need for finance, sources of finance, and desired factor for finance, features of actual finance received, alternative channels of finance, preferred source of financing and financial literacy.

3.3.3 Focus Group Discussions (FGD)

To obtain information about objectives, a qualitative, semi-structured instrument called FGD was administered. Discussions were conducted with the sampled population in groups to understand the sources of credit they rely on, reasons, access and availability, and perceptions about different providers of credit.

3.3.4 Key Informant Interviews

The research team personally met the informants for key informant interviews and asked necessary questions regarding the subject of enquiry. The key informants interviewed are from lead banks of the district, other public and private sector banks, small finance banks, NBFCs, MFIs, and NABARD etc.

3.3.5 Case Studies

Based on discussions with clients, the team identified 1-2 clients in each of the states and developed case studies which are useful to understand the ground level situations like how clients are currently meeting their credit needs, managing their loan repayment obligations etc.

3.4 Survey implementation

Table 16: Study Design Methodology

Design → **Training** → **Data collection** → **Data Analysis & report writing** → **Submission of Report**

• Design Household Microenterprise/Micro entrepreneur level Questionnaire • Design tab based App • Design Focus Group discussion Guide	• Conduct Training for the Research Team • Field testing on sample microenterprises	• Data collection • Quality monitoring during data collection and support • Data downloading • Data cleaning • Data Analysis	• Submission of draft report • Submission of final report

3.5 Limitations of the Study

i. Respondents did not feel encouraged to provide accurate, honest answers on the total borrowings, especially from the informal sources like money lenders.

ii. As the surveys was Computer Assisted Personal Interviewing (CAPI) based that had mostly the closed-ended questions with only the anticipated options, the enumerators did not have the space to capture the responses (options) which were not anticipated before the study.

iii. There may be some sampling bias, for example in Varanasi, the number of women respondents is more – as the loans to the enterprises are rooted through women though both men and women- owned it; in Ganjam the urban sample is high.

4 Findings of the Survey

4.1 Profile of micro entrepreneurs covered in the survey

Table 17: Characteristics of the micro entrepreneurs

S. No	Variable	Particulars	Total		Varanasi		Bidar		Gangnam		Chandrapur	
			N	%	N	%	N	%	N	%	N	%
1	Gender	Male	506	62	29	14	167	84	184	92	126	63
		Female	307	38	184	86	33	17	16	8	74	37
		Total	**813**	**100**	**213**	**100**	**200**	**100**	**200**	**100**	**200**	**100**
2	Religion	Hindu	689	85	162	76	145	73	196	98	186	93
		Muslim	120	15	51	24	51	28	4	2	14	7
		Christian	4	1			4					
		Total	**813**	**100**	**213**	**100**	**200**	**100**	**200**	**100**	**200**	**100**
3	Area	Rural	293	36	112	53	95	48	49	25	37	19
		Urban	317	39	64	30	65	33	111	56	78	39
		Semi-Urban	203	25	37	17	40	20	40	20	85	43
		Total	**813**	**100**	**213**	**100**	**200**	**100**	**200**	**100**	**200**	**100**
4	Social Category	SC	116	14	61	29	46	23	2	1	7	4
		ST	93	11	3	1	33	17	0	0	57	29
		OBC	252	31	81	38	23	12	70	35	78	39
		Gen	330	41	17	8	46	23	124	62	22	11
		Others	22	3	51	24	52	26	4	2	36	18
		Total	**813**	**100**	**213**	**100**	**200**	**100**	**200**	**100**	**200**	**100**
5	Economic Category	APL	403	50	46	22	9	5	175	88	173	87
		BPL	390	48	166	78	175	88	25	13	24	12
		Others	20	2	1	0	16	8		0	3	2
		Total	**813**	**100**	**213**	**100**	**200**	**100**	**200**	**100**	**200**	**100**
6	Literacy Level	Illiterate	97	12	67	31	18	9	8	4	3	2
		Primary (1-7)	281	35	86	40	5	3	20	10	11	6
		Secondary (8-10th)	107	13	43	20	49	25	67	34	107	54
		Higher Secondary (11th-12th)	132	16	1	0	55	28	24	12	52	26
		UG and PG	102	13	8	4	35	18	53	27	7	4
		Vocational/ Technical	94	12	8	4	38	19	28	14	20	10
		Total	**813**	**100**	**213**	**100**	**200**	**100**	**200**	**100**	**200**	**100**
7	Types of Microenterprises	Manufacturing	320	39	62	29	42	21	109	55	107	54
		Trading	276	34	64	30	68	34	54	27	90	45
		Processing	58	7	25	12	24	12	8	4	1	1
		Servicing	133	16	54	25	51	26	27	14	1	1
		Mixed	26	3	8	4	15	8	2	1	1	1
		Total	**813**	**100**	**213**	**100**	**200**	**100**	**200**	**100**	**200**	**100**

S. No	Variable	Particulars	Total		Varanasi		Bidar		Gangnam		Chandrapur	
			N	%	N	%	N	%	N	%	N	%
8	Average age of micro entrepreneur	Mean	SD	Mean	SD	Mean	SD	Mean	SD	Mean	SD	Mean
		41.2	11.9	39.2	9.8	42.8	11.6	39.1	12.5	43.8	12.7	41.2
		Min	Max	Min	Max	Min	Max	Min	Max	Min	Max	Min
		15	87	20	65	17	80	15	70	19	87	15

4.2 Profile of microenterprises covered in the survey

Table 18: Characteristics of the Microenterprises

S. No	Variable	Particulars	Total		Varanasi		Bidar		Ganjam		Chandrapur	
			Mean (Yrs.)	**SD**	**Mean (Yrs.)**	**SD**	**Mean (Yrs.)**	**SD**	**Mean (Yrs.)**	**SD**	**Mean (Yrs.)**	**SD**
1	Average age of microenterprises		14	12	9	8	13	12	17	13	17	10
			Min	Max	Min	Max	Min	Max	Min	Max	Min	Max
			0	60	0	50	0	60	1	52	3	47
2	Avg. No. of HH members involved		1.3		1		1.8		1.7		0.7	
3	Avg. No. of hired labour		0.8		0.6		1.5		0.5		0.7	
			N	**%**	**N**	**%**	**N**	**%**	**N**	**%**	**N**	**%**
4	Seasonality of microenterprises	Seasonal	172	21.2	26	12.2	39	19.5	60	30.0	47	23.5
		Round the year	641	78.8	187	87.8	161	80.5	140	70.0	153	76.5
		Total	**813**	**100**	**213**	**100**	**200**	**100**	**200**	**100**	**200**	**100**
5	Skill development for ME	ME which require special skills	423	50.9	13	5.6	108	54	119	59.5	183	91.5
		ME which undergo training	58	13.7	8	61.5	24	22.2	19	16	7	3.8
			831		**231**		**200**		**200**		**200**	
6	Number of ME which received support	Government	30	3.6	6	2.6	9	4.5	14	7	1	0.5
		NGO/ company	22	2.6	1	0.4	21	10.5	0		0	0.0
		Total	**831**		**231**		**200**		**200**		**200**	

The interviewed microenterprises, on an average, are 14 years old; ranging from 0-60 years; around 79% of them operate all year round. Overall, around 51% of the interviewed micro entrepreneurs reported the need for training to operate the microenterprises, while only 13.7% of them underwent training.

4.3 Asset ownership of the microenterprises

Table 19: Ownership of Assets

Fixed Assets		
Asset	**%**	**Av. Value (Rs.)**
Land	22.9%	1,234,505
Machine	18.2%	91,418
Motor Vehicle	5.0%	91,325
Premises	24.6%	703,035
Tools	17.3%	30,217
Electricity meter	0.2%	3,000
Furniture	8.7%	22,770
Current Assets		
Stock-raw material	28.3%	74,524
Stock- work in process	1.1%	75,389
Stock- finished goods	18.9%	56,633
Receivables from clients	2.1%	58,482

About 25% of microenterprises reported to operate from their own premises.

5 Financial Needs of Micro entrepreneurs/enterprises and Difficulties Faced

5.1 Financial needs of micro entrepreneurs (ME)/enterprises

Out of the total micro entrepreneurs interviewed, 6.6% of the entrepreneurs need a loan for both personal and business need.

Table 20: Financial needs of micro entrepreneurs (ME)/enterprises

Personal financial needs		Need of finance for business	
% of ME expressed need for personal loans	Average amount needed (Rs.)	% of ME expressed need for business loans	Average amount needed (Rs.)
28%	65,541	78%	90,815

Nearly 78% of micro-entrepreneurs interviewed, expressed need for finance for their microenterprises, with the average amount required stated to be Rs. 90,815. The main purpose stated to be buying raw material (including saleable goods for trading enterprises) purchase. 22% of the micro entrepreneurs expressed the need of finance for household expenditure with average need being Rs. 65,541. The extent of finance accessed was Rs. 69,000 on an average, which was 75% of the average need of Rs. 90,815 for business purposes stated above.

Table 21: Personal financial and business needs

Personal financial needs											
	Buying durable items	Educational expenses	Meeting household consumption needs	House repair/ extension/ purchase	Medical expenses	Social expenditure (e.g. marriage/ death)	Buying crop inputs/ irrigation/ land for cultivation	Buying livestock / fodder	Total for Personal	% of ME who expressed need for personal loans	Average amount needed (Rs.)
Varanasi	1	0	11	1	2	2	5	17	**39**	**18.3%**	**60,059**
Ganjam	2	2	16	10	6	7	3	0	**46**	**23.0%**	**93,460**
Bidar	0	11	22	10	3	8	2	2	**58**	**29.0%**	**1,01,750**
Chandrapur	0	2	38	2	21	2	1	22	**88**	**44.0%**	**18,855**
Total	**3**	**15**	**87**	**23**	**32**	**19**	**11**	**41**	**231**	**28.4%**	**65,541**
Percentage	**1%**	**6%**	**38%**	**10%**	**14%**	**8%**	**5%**	**18%**			

Business financial needs										
	Giving advance to get finance or subsidy	Buying tools/ equipment	Buying machinery	Other –long-term	Other – short-term	Buying raw material for microenterprise	Building a work shed	Total for business	% of ME who expressed need for business loans	Average amount needed (Rs.)
Varanasi	7	13	18	81	3	63	1	**186**	**87.3%**	**65,890**
Ganjam	1	14	16	1	6	106	2	**146**	**73.0%**	**1,71,000**
Bidar	2	6	23	10	3	129	14	**187**	**93.5%**	**1,21,260**
Chandrapur	0	4	10	0	8	88	4	**114**	**57.0%**	**60,010**
Total	**10**	**37**	**67**	**92**	**20**	**386**	**21**	**633**	**77.9%**	**90,815**
Percentage	**2%**	**6%**	**11%**	**15%**	**3%**	**61%**	**3%**			

The micro-enterprises targeted in the study don't require huge capital investment. The establishment is primarily within the premises of their own house. It starts with a low investment in buying the raw materials and need fund to increase the raw material on up surging the demand. 61% of the microenterprises reported the requirement of loan for the purpose of buying raw material for their enterprise. About 2% of the micro entrepreneurs reported availing small size loan to meet the upfront fee and cost for availing the bigger loan. About 28% of the total micro entrepreneurs interviewed reported the need for finance for consumption purpose.

5.1.1 Working capital to stock raw material when it is cheap

The entrepreneurs tend to buy and stock the raw material when it is cheap to increase the margin. At the same time, the market is erratic and the price of the raw material fluctuates. During the interview with the micro entrepreneurs, it was reported that there is an urgency of immediate finance when the price of the raw material falls. In this situation, they buy the raw material in credit. For some of the cases when the raw material is not available on credit, they approach informal sources mainly moneylenders for a quick loan. Availability of cheaper and quick loans from banks to stock raw material when it is cheap would generate an additional income for them, however, entrepreneurs reported that banks take a long time for processing loan application.

5.1.2 Working capital to stock finished goods before peak demand

The micro entrepreneurs interviewed who were involved in the production (for e.g. Sari, Carpet making etc.) were selling their produce to the output buyers or in the market immediately after production at a lower price due to unavailability of capital to stock the finished goods. Invariably, they are losing money. The other reason highlighted by the respondents as to why they sell the finished good immediately is to arrange money for buying input. If they stock the finished goods, they have to avail loan from informal sources or to buy input on credit, either. In both cases, they will lose good margin.

5.1.3 Need to extend credit sales to expand customer base

Micro entrepreneurs are also facing a challenge in the expansion of their business as they cannot provide material on the credit. Some of the grocery shop owners shared that they know their customers are creditworthy as they live in the same neighbourhood but unable to provide material to their customers on credit as they have limited investment capacity. Due to this, they are unable to expand their customer base. Some of the enterprises having investment up to Rs. 200,000 reported operating in a rolling business manner. They need immediate cash to buy raw material and hence they do not sell the finished goods on credit despite they know it will enhance their customer base.

5.1.4 Capital for equipment to improve quality or increase production

Most of the micro entrepreneurs of manufacturing industry interviewed are still using conventional technologies for the production of goods though the latest technologies that are available. For e.g. the Bidri workers in Bidar districts reported the availability of equipment for carving and engraving but it is costly and they cannot afford to procure. This leads to low production and some of the flour mill owners interviewed reported that buying a packing machine will enhance their business as they can supply a variety of flour to the retail shops.

5.2 Actual borrowing patterns

5.2.1 Borrowing analysed by purpose

Table 22: No. of ME wise actual purpose of borrowing- personal purpose

	Buying durable items	Educational expenses	Meeting household consumption needs	House extension/ building new	Medical expenses	Social expenditure (e.g. marriage/death)	Buying fodder/ feed	Crop inputs and livestock	Total for Personal	% of ME who took personal loans	Average amount borrowed (in Rs.)
Varanasi	0	1	9	4	3	3	0	22	42	**15.5%**	33286
Ganjam	3	3	10	8	4	3	0	0	31	**16.4%**	110000
Bidar	0	9	43	16	5	23	0	29	125	**29.7%**	56000
Chandrapur	0	4	78	0	49	1	6	53	191	**41.9%**	20150
Total	**3**	**17**	**140**	**28**	**61**	**30**	**6**	**104**	389	**31.7%**	50400

Out of total 1,232 loans taken by 347 respondents (28.2%) were for personal purpose; out of which 27% were for agriculture & allied activities, and remaining for household consumption need.

Table 23: No. of ME wise actual purpose of borrowing- Business Purpose

	Giving advance to get finance or subsidy	Buying tools/ equipment	Buying machinery	Other – long-term (specify)	Other – short-term (specify)	Buying raw material for microenterprise	Building a work shed	Total for business	% of ME who took business loans	Average amount borrowed (in Rs.)
Varanasi	9	14	22	107	6	71	0	229	**84.5%**	30,650
Ganjam	0	21	9	3	10	117	1	161	**85.2%**	156,000
Bidar	1	7	9	5	12	164	1	199	**63.6%**	68,520
Chandrapur	0	4	13	0	18	232	0	267	**58.6%**	57,100
Total	**10**	**46**	**53**	**115**	**46**	**584**	**2**	856	**69.7%**	76,700

Out of the total loans used for business purpose, 68% were to buy raw material, 5% to buy tools/equipment, 6% to buy machinery and build a work shed.

Table 24: Amount wise actual purpose of borrowing

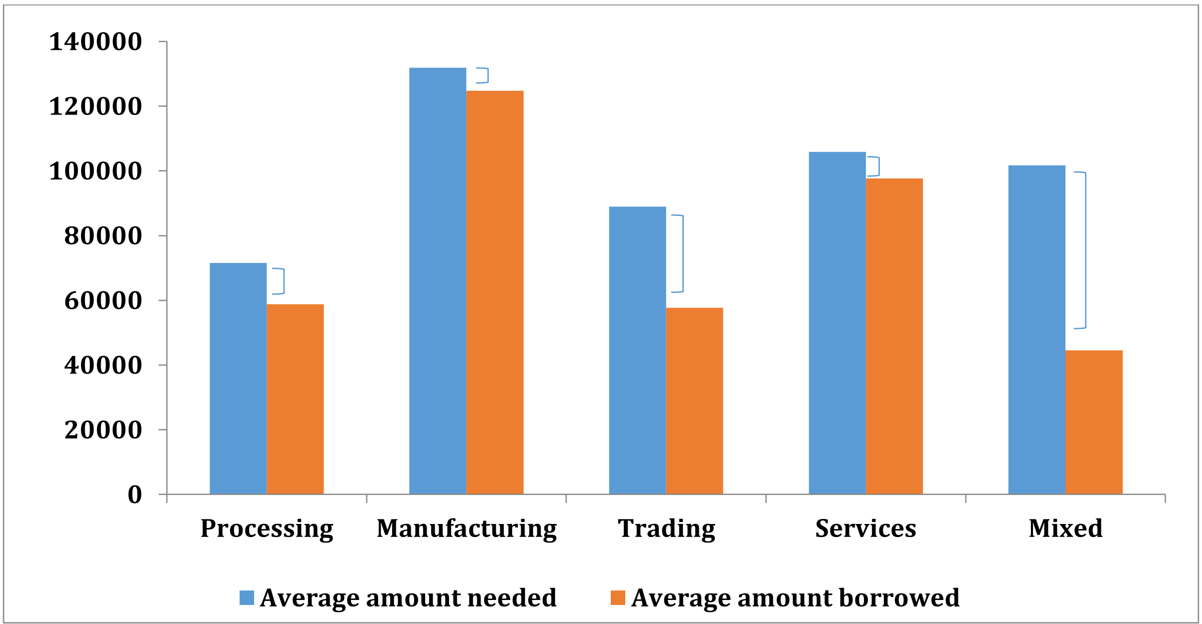
Purpose	Average	SD	Total borrowing	Share of borrowing sorted by amount
Business Purpose				
Buying raw material for microenterprise	79,403	1,74,975	463,71,110	55%
Buying tools/equipment	1,28,870	1,97,429	59,28,000	7%
Buying machinery	92,837	2,17,535	49,20,337	6%
Other –long-term (specify)	36,680	59,419	41,81,503	5%
Other –short-term (specify)	63,989	1,30,784	29,43,477	3%
Buying land for enterprise	2,37,500	2,63,688	14,25,000	2%
Giving advance to get finance or subsidy	20,100	10,913	2,01,000	0%
Building a work shed	57,500	42,500	1,15,000	0%
Total for business purposes			**660,85,427**	**78%**
Consumption Purpose				
House extension	3,12,188	5,54,105	49,95,000	6%
Social expenditure (e.g. marriage/death)	91,167	1,08,333	27,35,000	3%
Buying livestock	34,013	22,082	26,53,000	3%
Buying crop inputs	70,167	78,730	16,84,000	2%
Meeting household consumption needs	15,810	32,380	15,81,000	2%
House repair	1,66,250	1,35,249	13,30,000	2%
Medical expenses	20,048	38,066	12,22,900	1%
Mixed –consumption uses above	28,853	23,032	9,81,000	1%
Buying house/land for house	2,25,000	1,29,904	9,00,000	1%
Buying durable items	1,70,000	~	5,10,000	1%
Educational expenses	29,647	23,250	5,04,000	1%
Other –consumption (specify)	30,000	31,754	1,80,000	0%
Buying fodder	29,167	7,862	1,75,000	0%
For crop irrigation	80,000		80,000	0%
Leasing land for cultivation	70,000	~	70,000	0%
Total for consumption purposes			**196,00,900**	**23.1%**

In terms of amount, 78% of the existing borrowed fund by the microenterprises is utilized for the business purpose out of which the majority of the fund (55%) is utilized for buying raw materials followed by buying tools/equipment (7%). They rely on multiple sources because of the inadequacy of finance from one single source as well as to hedge their chances of getting finance, fungibility of the credit is a common phenomenon.

Table 25: Demand-supply mismatch – By ME type

ME type	Average amount needed (in Rs.)	Average amount borrowed (in Rs.)	Mismatch
Processing	71524.07	58779.6	17.8%
Manufacturing	131826.6	124786.7	5.3%
Trading	88903.63	57724.5	35.1%
Services	105911.7	97635.7	7.8%
Mixed	101708.3	44541.7	56.2%

Figure 5: Demand-supply mismatch – By ME type



As manufacturing enterprises require higher capital investment, the average loan requirement for these enterprises is more. Manufacturing enterprises emerge as the highest type for the fund requirement and inflow. And the demand-supply mismatch is smallest in this category. However, it may be observed that highest demand-supply mismatch is in trading.

5.2.2 Borrowing from different sources by microenterprise types

Table 26: Number of formal loans across type of ME

Type of Micro Enterprise	N	% of formal loans By firm type	% of ME by type in total sample	formal loans as % of all loans, by type of ME
Processing	8	4%	7%	14%
Manufacturing	87	45%	39%	27%
Trading	63	33%	34%	22%
Services	30	16%	16%	22%
Mixed	4	2%	3%	15%
Total	**192**	**100%**	**100%**	**100%**

5.2.3 Borrowing from different sources by microenterprise types

Table 27: Borrowing from different sources by microenterprise types

	Microenterprise type				
	N	**Percentage**	**Average**	**Loan amount**	**% (loan amount)**
	Banks				
Processing	15	28%	82,500	12,37,500	25%
Manufacturing	102	37%	2,40,440	245,24,880	60%
Trading	88	34%	1,57,400	138,51,200	52%
Services	59	46%	1,05,195	62,06,505	57%
Mixed	6	25%	45,000	2,70,000	26%
Total	270	36%	1,72,230	465,02,100	55%
	MFI				
Processing	19	36%	31,550	5,99,450	12%
Manufacturing	25	9%	36,950	9,23,750	2%
Trading	38	15%	46,000	17,48,000	7%
Services	29	22%	47,100	13,65,900	13%
Mixed	3	13%	33,300	99,900	9%
Total	114	15%	41,580	47,40,120	6%
	SHG				
Processing	8	15%	36,870	2,94,960	6%
Manufacturing	53	19%	40,080	21,24,240	5%
Trading	33	13%	32,310	10,66,230	4%
Services	10	8%	39,250	3,92,500	4%
Mixed	10	42%	19,300	1,93,000	18%
Total	114	15%	35,840	40,85,760	5%
	Informal				
Processing	11	21%	2,53,750	27,91,250	57%
Manufacturing	70	25%	1,71,540	120,07,800	29%
Trading	80	31%	97,620	78,09,600	30%
Services	29	22%	97,140	28,17,060	26%
Mixed	4	17%	1,10,750	4,43,000	42%
Total	194	26%	1,34,800	261,51,200	31%
	Credit				
Processing	-	0%	-	-	0%
Manufacturing	25	9%	62,000	15,50,000	4%
Trading	23	9%	85,820	19,73,860	7%
Services	2	2%	25,000	50,000	0%
Mixed	1	4%	50,000	50,000	5%
Total	51	7%	68,230	34,79,730	4%
Grand Total	743			849,58,910	

The service-based MEs are not borrowing much and they are pre-dominantly (45.7%) dependent on formal banking sources for borrowings. The highest per ME borrowing is recorded in the manufacturing-based ME which derive finance from both banks and informal sources, but quantum-wise most of the finance is taken from the banks (59.6%). Among the service-based MEs, land transport, hotels and restaurants are more dependent on formal sources than others; while among manufacturing-based ME, textiles, apparels and leather related MEs are also dependent on SHGs for finance. Furniture related MEs are mostly dependent on informal sources.

5.2.4 Borrowing from different sources by microenterprise sub types-wise

Table 28: Borrowing from different sources by microenterprise sub types-wise

	Banks			MFI			SHG			Informal			Credit from suppliers			Total ME
	N	%	Average (in '000')	N	%	Average (in '000')	N	%	Average (in '000')	N	%	Average (in '000')	N	%	Average (in '000')	
Processing	**15**	**0**	**82,500**	**19**	**0**	**31,550**	**8**	**0**	**36,870**	**11**	**0**	**2,53,750**	**-**	**-**	**-**	**53**
Manufacturing	**102**	**0**	**2,40,440**	**25**	**0**	**36,950**	**53**	**0**	**40,080**	**70**	**0**	**1,71,540**	**25**	**0**	**62,000**	**275**
Food products and beverages	22	0	1,35,500	9	0	39,200	10	0	27,000	17	0	1,16,125	5	0	1,72,000	63
Tobacco products	-	-		1	1	75,000	-	-	-	-	-	-	-	-	-	1
Textiles	19	0	1,14,300	4	0	30,000	18	0	24,700	5	0	1,79,500	2	0	36,000	48
Apparel	12	1	60,000	1	0	30,000	5	0	27,000	3	0	77,500	1	0	50,000	22
Leather	2	0	2,00,000	1	0	30,000	2	0	60,000	-	-	-	1	0	15,000	6
Wood	6	1	67,000	5	0	20,600	-	-	-	-	-	-	-	-	-	11
Paper/paper product	2	1	50,000	-	-	-	-	-	-	-	-	-	-	-	-	2
Publishing/printing	3	0	75,000	1	0	30,000	2	0	22,000	1	0	10,000	-	-	-	7
Rubber/plastic /chemicals	2	0	83,000	1	0	30,000	1	0	5,000	3	0	1,40,000	-	-	-	7
Non-metallic mineral product	4	0	5,50,000	2	0	1,50,000	3	0	40,000	-	-	-	-	-	-	9
Metal	14	1	1,45,500	-	-	-	-	-	-	4	0	2,80,000	1	0	2,00,000	19
Radio/TV/machinery/motor vehicle	1	1	60,000	-	-	-	-	-	-	-	-	-	-	-	-	1
Furniture	15	0	4,56,000	-	-	-	12	0	26,500	37	0	1,62,000	15	0	11,500	79
Trading	**88**	**0**	**1,57,400**	**38**	**0**	**46,000**	**33**	**0**	**32,310**	**80**	**0**	**97,620**	**23**	**0**	**85,820**	**262**
Wholesale trade	4	1	3,00,000	-	-	-	-	-	-	2	0	2,62,500	2	0	4,450	8

	Banks			**MFI**			**SHG**			**Informal**			**Credit from suppliers**			**Total ME**
	N	**%**	**Average (in '000')**	**N**	**%**	**Average (in '000')**	**N**	**%**	**Average (in '000')**	**N**	**%**	**Average (in '000')**	**N**	**%**	**Average (in '000')**	
Retail trade	79	0	1,52,500	38	0	36,150	31	0	51,200	69	0	1,56,400	20	0	75,500	237
Sale/maintenance/ repair of motor vehicle	5	0	80,000	-	-	-	2	0	45,000	9	1	94,200	1	0	1,15,000	17
Services	**59**	**0**	**1,05,195**	**29**	**0**	**47,100**	**10**	**0**	**39,250**	**29**	**0**	**97,140**	**2**	**0**	**25,000**	**129**
Hotel and restaurants	36	1	2,99,000	11	0	35,900	5	0	17,150	12	0	73,000	1	0	85,000	65
Land transport	10	0	2,04,000	3	0	28,300	3	0	20,000	5	0	98,750	1	0	40,000	22
Water transport	1	0	25,000	1	0	50,000	1	0	27,500	2	0	70,000	-	-	-	5
Supporting auxiliary transport services	5	0	1,28,000	11	1	56,500	-	-	-	3	0	1,83,000	-	-	-	19
Post/telecom	6	0	1,22,500	3	0	32,500	-	-	-	7	0	1,47,500	-	-	-	16
Financial intermediation	1	1	1,56,000	-	-	-	1	1	30,000	-	-	-	-	-	-	2
Mixed	**6**	**0**	**45,000**	**3**	**0**	**33,300**	**10**	**0**	**19,300**	**4**	**0**	**1,10,750**	**1**	**0**	**50,000**	**22**
Total	270	0	1,72,250	114	0	41,600	114	0	35,850	194	0	1,34,800	51	0	68,200	743

5.3 Difficulties faced by the micro entrepreneurs in accessing finance

Table 29: Difficulties faced by the micro entrepreneurs in accessing finance

Reported desired factors for financing	N	%
Easy physical accessibility	548	67.4%
Less processing time	526	64.7%
Lower interest rate	464	57.1%
Less paper work and formalities	408	50.2%
Friendliness of financier	380	46.7%
Adequate amount of finance	269	33.1%
No need for land title for mortgaging	259	31.9%
Repayment schedule which suits your cash flow	209	25.7%
Duration of finance suits you	195	24.0%
Lesser requirement of collateral security for finance	191	23.5%
Less cost of financing (other than interest)	168	20.7%
Flexibility of end use – the financier does not ask what we used for	70	8.6%
Availability of subsidy	62	7.6%
Chances of loan being waived	49	6.0%
Is the financing like a partnership with profit sharing	25	3.1%

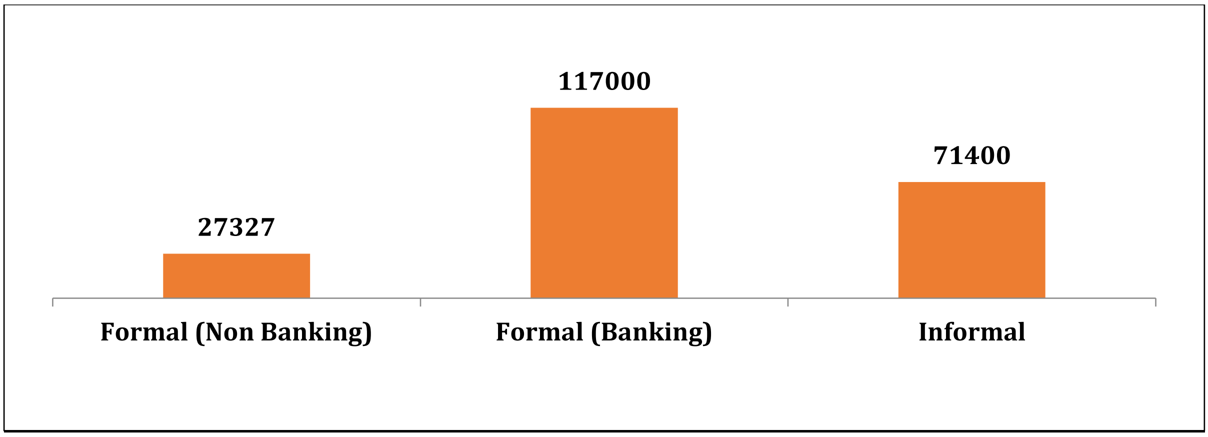
5.3.1 Lack of awareness of finance from banks

Majority of the respondent interviewed are unaware of the credit schemes of the government rooted through the banks. The unawareness mostly lies in the features and the benefits of the schemes. Even the banks are reluctant apprising the micro entrepreneurs on the schemes. The lack of awareness of government schemes is also leading to another loophole in the scheme and the reason for the inadequacy of credit. Micro entrepreneurs are highly dependent on intermediaries to approach a bank to avail loans.

5.3.2 Attitude of bank staff towards small borrowers

During discussions with entrepreneurs and bankers, it was observed that some of the bank staff discourages the small loan borrowers. As bank managers think that they need to spend equal time compare to the big size loan borrowers and the loan size below Rs.50, 000 is too small for them to document and monitor. Some banks experience loan defaulters from some of the microenterprise loans and decided not to entertain any small borrowers who want to take unsecured loans. Some of the banks blacklisted some villages/places and reject the small borrowers whoever comes from that particular village/area. Majority of the bankers interviewed say that they don't know required information about the viability of some of the microenterprises (for e.g. idol making enterprise, snack making etc.) and also have limited information about the clients as they don't have appropriate assessment tools. Bankers consider microenterprise loans as risky compared to the big size enterprises in terms of cost of delivery and security.

Figure 6: Formal to informal credit



Banks are insisting upon immovable collaterals to hedge against the risk of default especially in case of loans above Rs.50, 000. Some of the banks are demanding client asset related documents even for below Rs.50, 000 loans and are keeping with the client application, bank staff say that this is just to ensure credit discipline among the clients. Lack of collateral is major reasons many of the entrepreneurs not approaching banks.

5.3.3 Documentation and other requirements of banks

Bankers seeing microenterprise loans are riskier, compared to the big size enterprise in terms of cost of delivery and security. Banks are insisting up on immovable collaterals to hedge against risk of default especially in case of loans above Rs.50, 000. Some of the banks are demanding client asset related documents even for below Rs.50, 000 loans and are keeping with client application, bank staff say that this is just to ensure credit discipline among the clients. Lack of collateral is major reasons many of the entrepreneurs not approaching banks.

5.3.4 Need for margin money and under-financing

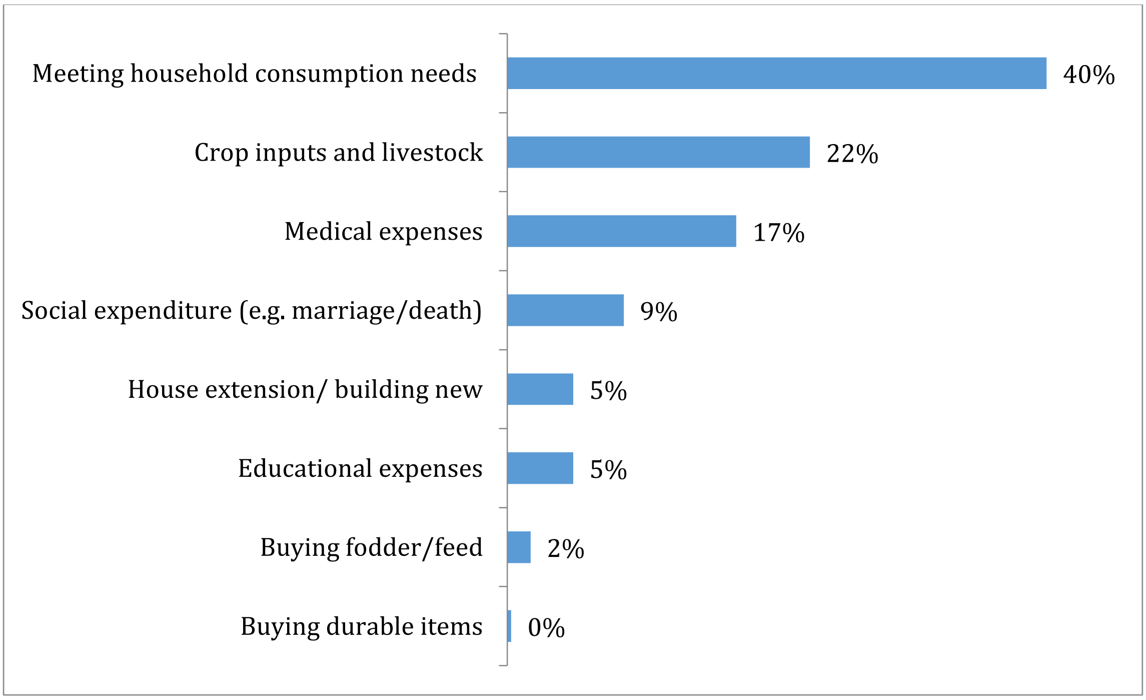
The study shows that some of the banks are asking micro entrepreneurs to make a fixed deposit (15%-25% of loan amount) in the bank for advancing credit to their microenterprises. Micro entrepreneurs take loans from Moneylenders/MFIs/SHGs to make the fixed deposit in the bank. During interaction with bankers, it was understood banks want to reduce the default risk by taking the fixed deposit from their clients.

The loans from MFIs and SHGs though easily available, reported to be of little assistance because of the inadequacy of loan amounts (mostly <Rs. 50000) to invest in enterprise, as a result the entrepreneur has to either adjust with available loan amount or has to take credit from another source.

5.3.5 Micro entrepreneurs' household and enterprise cash flows are mixed up

During interactions with the micro entrepreneurs, it was quite evident that even though they take the loan for the enterprise, some portion of the credit they use for consumption. Normally neither banks nor MFIs do not allow clients to divert their credit to consumption and instruct them upfront that the loan is only for the enterprise. However, entrepreneurs do not differentiate cash flows between home and enterprise and adjust based on the need. Micro entrepreneurs prefer financial service providers who do not keep conditions on use of credit between home and enterprise. The micro entrepreneurs of the weaving community said that they prefer to take credit from input suppliers as they provide both required raw materials and also cash loan for consumption and they need not hide anything from the input suppliers. In the similar way moneylenders also not impose conditions on the use of credit between household and enterprise and their focus more on other aspects like repayment capacity and character of the client.

Figure 7: Household needs where loan is used



Out of the total 28% of total borrowings used for consumption purpose, meeting household consumption need has emerged as the highest need followed by crop input and livestock.

6 Access to Formal Sources of Finance

6.1 Availability of different sources of finance

Table 30: Perception about availability of different sources of finance

	Few	Lot	Nil	Few	Lot	Nil	Few	Lot	Nil
PSUB			**MFIC**			**Big Farmer/Trader**			
Varanasi	9%	9%	8%	1%	14%	11%	0%	0%	26%
Ganjam	10%	10%	4%	9%	7%	9%	9%	3%	12%
Bidar	6%	11%	8%	2%	9%	13%	7%	1%	16%
Chandrapur	2%	9%	13%	0%	1%	24%	0%	2%	23%
Total	27%	40%	33%	13%	30%	57%	16%	7%	77%
RRB			**MFIV**			**Finance company agents**			
Varanasi	6%	6%	14%	0%	0%	25%	0%	0%	26%
Ganjam	10%	7%	7%	6%	1%	18%	7%	1%	16%
Bidar	5%	11%	8%	2%	13%	10%	8%	3%	13%
Chandrapur	1%	8%	15%	0%	1%	24%	0%	0%	25%
Total	23%	32%	44%	8%	15%	77%	16%	4%	80%
Private Banks			**Cooperative society**			**Business Partners**			
Varanasi	2%	2%	23%	0%	0%	26%	0%	0%	26%
Ganjam	9%	7%	9%	9%	3%	13%	8%	1%	16%
Bidar	4%	10%	11%	1%	9%	15%	3%	1%	21%
Chandrapur	0%	10%	14%	1%	3%	20%	0%	0%	24%
Total	16%	28%	56%	11%	14%	74%	10%	1%	88%
Small Financing Bank			**Chit Fund- Registered**			**Family Members**			
Varanasi	3%	12%	11%	0%	0%	26%	9%	2%	15%
Ganjam	5%	2%	18%	1%	0%	23%	7%	9%	8%
Bidar	4%	6%	14%	4%	1%	19%	1%	16%	7%
Chandrapur	0%	8%	17%	0%	0%	24%	0%	18%	7%
Total	12%	27%	60%	5%	1%	93%	18%	45%	37%
Cooperative Bank			**Raw material suppliers**			**Friends**			
Varanasi	0%	0%	26%	8%	6%	12%	1%	1%	24%
Ganjam	7%	4%	14%	9%	7%	8%	7%	10%	8%
Bidar	4%	7%	13%	6%	3%	15%	1%	17%	6%
Chandrapur	1%	8%	16%	0%	3%	22%	0%	20%	5%
Total	13%	18%	68%	24%	19%	57%	9%	47%	44%
FIs			**Output buyers**			**SHG- Bank linked**			
Varanasi	0%	0%	26%	2%	0%	25%	0%	6%	20%
Ganjam	1%	0%	23%	9%	4%	12%	11%	3%	10%
Bidar	2%	0%	22%	4%	0%	20%	2%	19%	3%
Chandrapur	0%	0%	25%	0%	6%	18%	0%	9%	15%
Total	4%	0%	96%	15%	10%	75%	14%	37%	49%
NBFCs			**Moneylender-registered**			**SHG-Not linked to bank**			
Varanasi	1%	1%	25%	0%	2%	24%	0%	23%	3%
Ganjam	7%	2%	17%	0%	0%	24%	9%	2%	14%
Bidar	7%	2%	16%	6%	3%	15%	2%	18%	4%
Chandrapur	0%	0%	25%	0%	0%	24%	0%	0%	25%
Total	14%	5%	82%	7%	6%	88%	11%	43%	46%

	Few	Lot	Nil	Few	Lot	Nil	Few	Lot	Nil
Moneylender-unregistered				Chits- unregistered					
Varanasi	2%	2%	22%	0%	0%	26%	-	-	-
Ganjam	9%	10%	5%	3%	1%	21%	-	-	-
Bidar	0%	17%	7%	4%	4%	16%	-	-	-
Chandrapur	0%	13%	11%	0%	0%	25%	-	-	-
Total	12%	43%	46%	7%	5%	88%	-	-	-

Friends, family members and moneylenders are the sources of finance which have the highest presence. Among formal sources, the top 3 institutions that have the highest presence are public sector banks, Bank-linked SHGs, NBFC-MFIs. Chit funds, business partners and finance company agent's presence have a very low presence.

6.2 Average borrowing across asset ownership

Table 31: Average borrowing across asset ownership

Asset Category	Banks				
	N	Percentage	Average	Loan amount	% (loan amount)
0-50000	51	23%	1,32,000	67,32,000	41%
50001-200000	68	30%	1,99,000	135,32,000	48%
200001-500000	60	47%	1,88,000	112,80,000	64%
500001-1000000	45	47%	1,77,000	79,65,000	57%
1000001-50L	41	58%	1,49,000	61,09,000	77%
Above 50L	5	63%	1,83,000	9,15,000	92%
Total	**270**	**36%**		**465,33,000**	**55%**
Asset Category	**MFI**				
	N	Percentage	Average	Loan amount	% (loan amount)
0-50000	24	11%	42,500	10,20,000	6%
50001-200000	29	13%	51,500	14,93,500	5%
200001-500000	21	17%	40,000	8,40,000	5%
500001-1000000	21	22%	34,000	7,14,000	5%
1000001-50L	17	24%	42,000	7,14,000	9%
Above 50L	2	25%	32,500	65,000	7%
Total	114	15%		48,46,500	6%
Asset Category	**SHG**				
	N	Percentage	Average	Loan amount	% (loan amount)
0-50000	47	21%	45,000	21,15,000	13%
50001-200000	32	14%	26,200	8,38,400	3%
200001-500000	16	13%	46,000	7,36,000	4%
500001-1000000	15	16%	26,300	3,94,500	3%
1000001-50L	4	6%	14,000	56,000	1%
Above 50L	1	13%	20,000	20,000	2%
Total	**114**	**15%**		**41,59,900**	**5%**

Asset Category	**Informal**				
	N	**Percentage**	**Average**	**Loan amount**	**% (loan amount)**
0-50000	71	32%	87,000	61,77,000	37%
50001-200000	76	34%	1,37,000	104,12,000	37%
200001-500000	26	20%	1,76,000	45,76,000	26%
500001-1000000	12	13%	3,33,000	39,96,000	29%
1000001-50L	9	13%	1,20,000	10,80,000	14%
Above 50L	0	0%	-	-	0%
Total	**194**	**26%**	**-**	**262,41,000**	**31%**
Asset Category	**Credit**				
	N	**Percentage**	**Average**	**Loan amount**	**% (loan amount)**
0-50000	26	12%	19,800	5,14,800	3%
50001-200000	18	8%	1,07,500	19,35,000	7%
200001-500000	4	3%	52,500	2,10,000	1%
500001-1000000	3	3%	2,74,000	8,22,000	6%
1000001-50L	0	0%	-	-	-
Above 50L	0	0%	-	-	-
Total	**51**	**7%**	**-**	**34,81,800**	**-**
Grand Total	**744**	**-**	**-**	**852,62,200**	**-**

For microenterprises with lesser assets, most of the borrowing comes from informal sources, which includes friends, family, moneylenders and raw material suppliers. The contribution of banking sources is higher only among enterprises with higher worth. The MEs with higher assets are capable of meeting the terms and conditions tied with the formal loans such as collateral. With ownership of higher assets, access to formal banking sources gets better, the dependence on informal sources seems to be reducing.

6.3 Loan-wise borrowing across different sources

Table 32: Loan-wise borrowing across different sources

	FORMAL													
	Banks								Cooperatives		MFI		SHG	
Loan Size	**PSU**	**Average**	**RRB**	**Average**	**Private**	**Average**	**SFB**	**Average**	**No.**	**Average**	**No.**	**Average**	**No.**	**Average**
>10000	-		-		-		-		-		1	10,000	28	7,152
10000-30000	-		7	20,500	70	25,000	66	22,863	13	16,334	131	23,799	141	21,254
30001-50000	39	47,500	20	49,667	17	50,000	27	41,334	2	50,000	13	44,462	17	37,643
50001-1L	26	90,000	5	79,167	6	78,000	1	60,000	6	90,667	7	78,000	7	70,909
100001-2L	16	1,88,334	4	1,75,000	11	1,70,000	-		4	1,75,000	-		6	1,75,000
200001-5L	10	3,63,637	2	5,00,000	11	3,93,273	-		4	3,75,000	-		-	
Above 5L	4	7,80,000	1	12,00,000	2	14,66,667	-		3	18,00,000	-		-	
Total	**95**	**1,94,915**	**39**	**1,15,415**	**117**	**2,07,475**	**94**	**26,891**	**32**	**26,891**	**152**	**29,474**	**199**	**31,450**

	INFORMAL							
	Moneylender		OPB		Family & Friends		Others	
Loan Size	**No.**	**Average**	**No.**	**Average**	**No.**	**Average**	**No.**	**Average**
>10000	14	8,750	44	1,675	63	6,070	-	
10000-30000	80	22,365	13	22,500	62	21,667	6	21,500
30001-50000	42	49,050	15	45,625	22	48,334	6	48,000
50001-1L	43	87,295	9	90,700	7	80,000	4	51,000
100001-2L	28	1,66,110	6	1,55,000	7	1,71,430	4	1,73,300
200001-5L	13	3,95,830	2	4,00,000	6	3,81,430	2	2,50,000
Above 5L	4	9,75,000	1	6,75,000	1	7,00,000	-	
Total	**224**	**1,42,010**	**90**	**79,726**	**168**	**88,085**	**22**	**1,03,684**

For the microenterprises who are borrowing very small amounts (< Rs.10, 000), the finance is provided by family or friends or they buy inputs on credit. For a slightly higher amount, their preferences of borrowing seem to be shifting towards MFIs, SHGs and small financing banks; which contribute more than 60% loans. While for the very high amount of borrowings (>Rs.1 Lakh), the microenterprises rely either on banks or informal sources; with latter dominating as 54% of the loans taken by ME and 36% are from banks. However, on comparing the quantum the difference is not so vast (39% and 46% respectively from banks and informal sources).

6.4 Features of lending sources

Table 33: Features of lending sources

Actual source for borrowing	Total ME		Interest rate		Average amount		Total amount	
Source	**N**	**%**	**Mean**	**SD**	**Mean**	**SD**	**Rs**	**%**
FORMAL SOURCES								
Banks								
PSU	97	7.8%	11	4	1,37,874	1,78,565	133,73,747	16.1%
Private	117	9.4%	21	6	1,09,709	2,98,174	128,36,000	15.4%
RRB	39	3.1%	10	6	1,08,385	2,00,613	42,27,000	5.1%
SFB	94	7.6%	23	3	28,484	10,450	26,77,500	3.2%
MFIs								
NBFC-MFI	116	9.3%	25	22	26,754	15,082	31,03,509	3.7%
NGO- MFI	37	3.0%	17	6	31,514	18,131	11,66,000	1.4%
NBFCs (non-MFI)	4	0.3%	11	~	2,10,000	~	8,40,000	1.0%
SHGs								
SHGs – bank linked	175	14.1%	26	9	25,220	28,459	44,13,500	5.3%
SHGs – not linked to bank	26	2.1%	23	4	20,208	22,444	5,25,417	0.6%
Cooperatives								
Bank- cooperative	26	2.1%	12	3	2,39,720	3,64,348	62,32,720	7.5%
Cooperative society	7	0.6%	14	10	37,571	29,563	2,63,000	0.3%
INFORMAL SOURCES								
Moneylender unregistered	216	17.4%	71	43	94,653	1,54,346	204,45,000	24.6%
Family members	50	4.0%	8	21	49,115	86,826	24,55,729	2.9%
Friends/ neighbours	120	9.7%	6	15	40,409	97,345	48,49,070	5.8%
Raw Material Suppliers	37	3.0%	4	11	82,676	1,13,461	30,59,029	3.7%
Output Buyers	55	4.4%	10	22	18,405	38,092	10,12,295	1.2%
Finance "company" agents	10	0.8%	30	10	83,000	81,829	8,30,000	1.0%

Actual source for borrowing	Total ME		Interest rate		Average amount		Total amount	
Source	**N**	**%**	**Mean**	**SD**	**Mean**	**SD**	**Rs**	**%**
Moneylenders (registered)	8	0.6%	34	3	51,250	34,709	4,10,000	0.5%
Chit funds (registered)	3	0.2%	29	~	58,333	35,198	1,75,000	0.2%
Employer	3	0.2%	0	~	50,000	~	1,50,000	0.2%
Chits (unregistered)	2	0.2%	27	~	53,667	36,791	1,07,333	0.1%
Big Farmer/ Trader	1	0.1%	24	~	1,00,000	~	1,00,000	0.1%
Total	**1243**	**100%**					**832,51,849**	**100%**

Interest rate and the average loan amount are higher for formal financial sources. Among the formal sources, public sector banks account for maximum exposure to microenterprises and among informal sources, moneylenders account for the highest exposure to microenterprises.

6.5 Loan conditions of various sources

Table 34: Loan conditions of various sources

Sources for borrowing		Finance duration (months)		Required guarantor		Required collateral		Processing time (days)
Source		**Mean**	**SD**	**N**	**%**	**N**	**%**	
Informal Sources	Moneylender unregistered	12.9	13.8	38	18%	47	22%	0
	Friends/ neighbours	6.3	10.03	11	9%	5	4%	2
	Output Buyers	12	0	0	0%	0	0%	0
	Family members	8.7	14.1	3	6%	4	8%	12
	Raw Material Suppliers	4.8	3.7	0	0%	0	0%	0
	SHGs – not linked to bank	15.7	9.1	21	81%	0	0%	7
	Finance "company" agents	17.3	10.4	8	80%	6	60%	2
	Moneylenders (registered)	11.2	7.4	0	0%	2	25%	4
	Employer	1.5	~	0	0%	0	0%	0
	Chits (unregistered)	11.7	~	3	150%	0	0%	0
	Big Farmer/ Trader	15	~	0	0%	0	0%	0
Formal Sources	SHGs – bank linked	17.1	9.7	85	49%	3	2%	30
	NBFC-MFI	18.32	7.3	80	69%	2	2%	8
	NGO- MFI	14	4.3	26	70%	0	0%	12
	Chit funds (registered)	7	~	3	100%	1	33%	0
	Bank – private sector	18	13.7	69	59%	19	16%	35
	Bank – public sector	35.2	27	38	39%	38	39%	45
	Bank – small finance	20.9	5.5	90	96%	0	0%	12
	Bank – regional rural	26	16.7	30	77%	19	49%	60
	Bank- cooperative	24.9	16.3	21	81%	19	73%	40
	Cooperative society	12.6	5.1	7	100%	4	57%	8
	NBFCs (non-MFI)	31.25	11.6	1	25%	0	0%	9

6.6 Preferred sources of finance

Table 35: Preferred sources of finance

	Varanasi	Ganjam	Bidar	Chandrapur	Total	Percentage
Family & Friend	0	116	81	278	**475**	**58.4%**
Bank – public sector	75	110	81	19	**285**	**35.1%**
Bank – regional rural	51	56	76	18	**201**	**24.7%**
SHGs – bank linked	24	2	61	63	**150**	**18.5%**
Bank – private sector	0	57	56	34	**147**	**18.1%**
Moneylenders	0	41	14	76	**131**	**16.1%**
Bank – small finance	81	9	6	12	**108**	**13.3%**
NBFC-MFI	73	14	5	5	**97**	**11.9%**
SHGs – not linked to bank	9	0	63	0	**72**	**8.9%**
Output Buyers	0	9	0	39	**48**	**5.9%**
NGO- MFI	4	1	36	1	**42**	**5.2%**
Bank- cooperative	0	9	7	15	**31**	**3.8%**
Business Partners	0	3	0	3	**6**	**0.7%**
Chits (unregistered)	0	0	5	0	**5**	**0.6%**
Chit funds (registered)	0	0	0	0	**0**	**0.0%**

The majority, 52.7% of the loans were from informal sources, accounting for 32% of the amount financed. Moneylenders play a dominant role as within the informal sources they lent 44% of total loans for financing enterprises, followed by 33% by family, friends and neighbours and 17% by input suppliers and output buyers.

Table 36: Use of bank accounts, distance to banks and borrowings by micro entrepreneurs

Place	Entrepreneurs having bank account
Varanasi	93.4%
Ganjam	98.5%
Bidar	93.5%
Chandrapur	95.5%
Total	95.2%

Sources for money withdrawal

Bank	BC Outlet	ATM	Do not withdraw
73%	1%	14.6%	5%

Distance to banks/ATM/BC outlet and last visit (in weeks)

	Distance (average: in Km)	time lag (last visit: in weeks)
Varanasi	2.3	20.2
Ganjam	2	4
Bidar	2.9	17.6
Chandrapur	5.6	5.8
Total	**3.2**	**12.5**

Borrowing

	Borrowing in the last 3 years	Borrowing for Microenterprise	Bought raw material on credit

Total	86%	77%	38%

Majority of the entrepreneurs who were interviewed were aware that the rate of interest on loans from banks is low compared to informal sources. However, very few of them approached banks to access loans to meet the credit needs of their enterprises.

The formal sources accounted for 47.3% of the number of loans received with 68% of the amount financed. Among formal sources, public sector banks were more prominent, followed by the non-banking formal channels NBFCs, NBFC-MFIs, NGO-MFIs, Bank linked SHGs and BCs, who accounted for 38% of the loans but only 12% of the amount.

Table 37: Reasons reported for preferring formal sources

Easy access	11.4%
Trust and transparency	5.4%
Lower interest rate	56.5%
Adequacy of the amount	12.7%
Suitable repayment	11.4%
Less processing time	1.7%
Availability of subsidy	1.0%

The major constraints faced by the entrepreneurs in accessing bank loans included the lack of knowledge about available schemes, difficulty in providing collateral or a guarantee, processing time for loan applications, and procedural complications. The opportunity cost for entrepreneurs is high for availing loans from banks. Lack of knowledge about available schemes hinders them to from choosing the most effective option for financial assistance. In some of the remote villages, entrepreneurs reported that the bank branches are far away and hence depend on informal sources to meet their credit needs. Thus proximity of the banks also plays a positive role in accessing loan from the banks as entrepreneurs can visit banks frequently.

6.7 Barriers/challenges in accessing credit from formal sources

Major challenges faced by the entrepreneurs in accessing credit from formal sources are:

Lack of knowledge about available credit schemes

Entrepreneurs do not know the credit schemes available with the banks to avail financial assistance from the banks, lack of knowledge about available schemes hinder them from choosing the right option to avail credit.

Table 38: Reasons for not preferring formal sources

Processing time	36.30%
Documentation and formalities	24.00%
Collateral and guarantor demands	12.00%
Lack of friendliness	9.90%
Lack of accessibility	8.90%
High interest rates	4.80%

Other charges (apart from interest)	4.10%

Lengthy process

Entrepreneurs stated that accessing loan from banks is very time consuming the average time as per the discussions with the entrepreneurs was 3-4 months if all required documents are submitted. Some of the entrepreneurs opined that the transaction amount they incur to access loan from banks is almost equal to excess interest amount what they pay to the moneylenders.

Procedural complications

Entrepreneurs stated that bank asks for “No objection certificate” from all banks in the area and licence for the enterprise. One of the entrepreneurs stated that he got No objection certificate from six banks but still he could not get the loan from the bank.

Need for collateral and a guarantee

The entrepreneurs from one of the districts reported that they need many documents to avail loan from banks. The documents required as per their report: Home Patta[13] (title deed), if Patta is available whether it is Grarabari or agriculture land patta, if it is Grarabaripatta or agriculture Patta whether it is fenced or not, if it is fenced then get the 25 years EC from Revenue Inspector and Tehasil office, after that they have to get 25 years EC (Encumbrance Certificate) from local Tehasil office and get the valuation of it from RI and lawyer. The banks also insist on appropriate guarantor as per the bank rules.

Lack of proximity of the bank and approachability

Entrepreneurs feel comfortable in visiting the bank branches which are nearby their locality or within their neighbourhood as it would give confidence in visiting branch office with one of their family members/friends. Entrepreneurs feel comfortable in explaining their ideas/plans about the starting new business or expanding their existing business and credit needs only if the branch manager/bank staffs approachable. This is one of the major reasons why entrepreneurs approach informal credit sources to avail the loans because they are more approachable compared to bank officers.

Negative attitude of the banker towards microenterprise loans

Many of the entrepreneurs in Bidar district reported that the bank officials had a very bad attitude towards them because of nonperforming assets of microenterprise portfolio is very high in the bank and as a result the bank officials reject their loan request without even listing to them.

Rejection of loan requests as one of the family members/ close relative is defaulter

Some of the entrepreneurs stated that they have taken a loan from informal sources as banks rejected their loan application as one of their family member’s was a bank defaulter and bank staff were averse to considering their applications for finance.

Uncertainty about the loan sanction

Despite submission of all required documents including collateral and mortgage of property (some cases) entrepreneurs were not sure about sanction of the loan. And even loan is sanctioned the timely credit is not sure. One of the entrepreneurs from Chandrapur District applied for a loan

[13] A Patta is a legal document issued by the Government in the name of the actual owner of a particular plot of land. It can also be issued for lands having buildings or individual houses etc. constructed on them.

to the bank as he got a huge order for idols few weeks before a festival, but he could not get the loan from bank to buy raw material and hence took loan from the moneylender at higher interest rate.

6.8 Challenges faced by the Banks to provide credit to Micro Entrepreneurs

6.8.1 Sourcing of borrowers

The microenterprise sector is highly diverse in nature in terms of geography, size, operation, employee strength, borrowing capacity, legal structure and seasonality. As a result, the cost of sourcing and serving microenterprise is high as the effort and the cost required to source a micro enterprise client is the same as that for a medium enterprise. Consequently, banks prefer to serve small and medium enterprises than microenterprises.

Banks have limited branch network in the remote locations due to which there is a limited lower interface between financial institutions and enterprises. Now days, banks have created a good network of BCs however their role is mostly restricted to account opening and saving transactions. To some extent, it has created confusion on the clarity of roles between bank and BCs. It was being reported by the respondents that if the BCs are taking longer time in offering services, they are approaching bank but have been referred to BCs again.

6.8.2 Project appraisal in the absence of written records

The key to financing the microenterprises lies in the ability of the financier to evaluate and manage business risks and offer customized product. In banks and other financial institutions, the underwriting process is similar in length and complexity regardless of size of enterprise or credit requirement. Banks and other formal financial institutions have a tendency to focus on Project Financing that involves diagnosis of financial performance of enterprises and assessment of risk associated with them. Information asymmetry in the microenterprises makes underwriting a challenging task for financial institutions. It was reported that, the microenterprises are taking assistance from the chartered accountants and other relevant peoples in drafting the project reports but unable to present it effectively before financiers. Moreover, the credit history of these borrowers is missing as they usually avail loan from informal sources. In the absence of complete and readily available financial information, banks find it difficult to assess the credit worthiness of these borrowers and tend to reject loan application. As per banks the entrepreneurship skill of people is lacking.

6.8.3 Documentation and Disbursement

Lack of any documented financial and legal information of the microenterprises is one of the major challenges for banks to lend these enterprises. Even if these enterprises present some documents, the authenticity of the information is difficult to ensure. Field insights reveal banks require legal documents such as shop establishment certificate, trade license, business plan, bank statement, cash flow details and tax filing documents. Due to this majority of microenterprises prefer to take loans under the Sishu category because it is easier and quicker (only requires documents such as Aadhaar, Election card, Ration Card), despite the inadequacy of the loans for their microenterprise.

6.8.4 Loan monitoring

Effective monitoring of portfolio quality and allowing for early warning of a potential default is essential to manage the asset quality and capture critical data that can be leveraged for future credit assessment of microenterprise clients.

Currently, the financial institutions use information technology platforms to monitor disbursal and repayments that may not be sufficient.

In fact, most of the loans have not been used for business and were used for household expenses, health and other one-time expenditures. When asked from banks about verification mechanism, they said that it is in place, however, when they go for verification and find out that the amount is not used for microenterprise, they cannot do anything because nothing has been specified in the guidelines. Even when people use it for microenterprise, the fungibility of the borrowed amount is a common phenomenon, especially in case of mudra loans and loans from small finance banks or MFIs.

> Mr Anil was planning on expanding his tailoring business. There are 4 to 5 tailors in the village. So the expansion of his business and giving better service is the only way he can earn more money and feed his seven members family. One day he saw a banner on 'Mudra loan' saying that the rate of interest is only 1% per month and the loan amount is repayable in five years (for the loan size up to Rs. 50,000). 'Mudra' seemed to be a dawn of new hope in his business. He immediately contacted Bank Manager of local RRB and the manager was supportive and explained the simple procedures to be followed to avail the loan under the scheme. He could get a loan of Rs. 40,000/- in a two months' time, but used the loan for consumption purpose. Anil repaid the first instalment of loan and stopped repayment for past one year, as many of the borrowers were not repaying the loan. Bank Manager (BM) was discouraged to advance further loans. BM said it is very difficult for him/his staff to monitor such loans.

6.8.5 Delayed repayment

The micro entrepreneur doesn't ensure the proper end usage of the loan and actual tracking of such loans are too difficult. Many of the clients use Mudra loans for consumption purposes. Some of them also use it for diversified purposes. According to most of the banks, SHGs lending is safe and the performance is better because liability is fixed on SHGs. Individual loans are mostly NPAs, mostly small loans. Frequent transfer of branch managers also creates difficulty in following up for recovery.

6.8.6 Default

Each bank is assigned a target to lend the microenterprises under various government schemes, but they have doubt on the people due to a large number of loan defaulters (unsatisfied repayment percent) in the area. Stress assets are going up, as a result banks are afraid to sanction further loans. Protracted and expensive default settlement also compels underwriters to take a more conservative approach in assessing risky assets. One of the bankers reported that as on date NPAs in Mudra loan portfolio are more than any other credit portfolios. There is also a mind-set among customers not to repay the loans availed through government schemes.

Table 39: Key features of the financing sources used by micro entrepreneurs

Source	% of ME take loan	Loan Duration (in months)		ME reported requirement of guarantor	ME reported requirement of collateral	Source wise Processing time
	%	Mean	SD	%	%	Days
Moneylender unregistered	17.4%	12.9	13.8	17.6%	21.8%	0
SHGs – bank linked	14.1%	17.1	9.7	48.6%	1.7%	30
Friends/ neighbours	9.7%	6.3	10.0	9.2%	4.2%	2
Bank – private sector	9.4%	18.0	13.7	59.0%	16.2%	35
NBFC-MFI	9.3%	18.3	7.3	69.0%	1.7%	8
Bank – public sector	7.8%	35.2	27.0	39.2%	39.2%	45
Bank – small finance	7.6%	20.9	5.5	95.7%	0.0%	12
Output Buyers	4.4%	12.0	0.0	0.0%	0.0%	0
Family members	4.0%	8.7	14.1	6.0%	8.0%	12
Bank – regional rural	3.1%	26.0	16.7	76.9%	48.7%	60
NGO- MFI	3.0%	14.0	4.3	70.3%	0.0%	12
Raw Material Suppliers	3.0%	4.8	3.7	0.0%	0.0%	0
Bank- cooperative	2.1%	24.9	16.3	80.8%	73.1%	40
SHGs – not linked to bank	2.1%	15.7	9.1	80.8%	0.0%	7
Finance “company” agents	0.8%	17.3	10.4	80.0%	60.0%	2
Moneylenders (registered)	0.6%	11.2	7.4	0.0%	25.0%	4
Cooperative society	0.6%	12.6	5.1	100.0%	57.1%	8
NBFCs (non-MFI)	0.3%	31.3	11.6	25.0%	0.0%	9
Chit funds (registered)	0.2%	7.0	~	100.0%	33.3%	0
Employer	0.2%	1.5	~	0.0%	0.0%	0
Chits (unregistered)	0.2%	11.7	~	150.0%	0.0%	0
Big Farmer/ Trader	0.1%	15.0	~	0.0%	0.0%	0

Table 40: Responses on consequences of delay of instalment payment

Source	Nothing	Reminder	Threats	Fine	Social cost
Big Farmer/ Trader	0.0%	0.0%	100.0%	0.0%	0.0%
Chit funds (registered)	0.0%	66.7%	0.0%	33.3%	0.0%
Chits (unregistered)	0.0%	100.0%	0.0%	0.0%	0.0%
Bank- cooperative	7.7%	69.2%	11.5%	3.8%	0.0%
Family members	30.0%	60.0%	0.0%	0.0%	4.0%
Finance “company” agents	0.0%	80.0%	10.0%	10.0%	0.0%
Friends/ neighbours	22.5%	74.2%	1.7%	0.8%	0.0%
NBFC-MFI	0.0%	87.9%	0.0%	0.0%	10.3%
NGO- MFI	0.0%	75.7%	0.0%	18.9%	0.0%

Source	Nothing	Reminder	Threats	Fine	Social cost
Moneylenders (registered)	25.0%	25.0%	50.0%	0.0%	0.0%
Moneylender unregistered	10.2%	66.2%	19.4%	0.0%	2.8%
NBFCs (non-MFI)	25.0%	0.0%	0.0%	0.0%	0.0%
Output Buyers	5.5%	72.7%	16.4%	0.0%	0.0%
Employer	0.0%	100.0%	0.0%	0.0%	0.0%
Bank – public sector	24.7%	48.5%	6.2%	3.1%	0.0%
Bank – private sector	7.7%	83.8%	7.7%	0.9%	0.0%
Raw Material Suppliers	37.8%	35.1%	2.7%	0.0%	0.0%
Bank – regional rural	7.7%	84.6%	0.0%	5.1%	0.0%
Bank – small finance	0.0%	98.9%	0.0%	0.0%	0.0%
SHGs – bank linked	4.6%	76.6%	6.3%	11.4%	0.0%
SHGs – not linked to bank	11.5%	53.8%	0.0%	0.0%	11.5%
Cooperative society	0.0%	71.4%	0.0%	114.3%	0.0%

Table 41: Reported responses on consequences of non-repayment

Source	Nothing	Threats	Court case	No further loan	Take away assets
Big Farmer/ Trader	0.0%	0.0%	0.0%	0.0%	100.0%
Chit funds (registered)	0.0%	0.0%	0.0%	0.0%	66.7%
Chits (unregistered)	0.0%	100.0%	0.0%	0.0%	0.0%
Bank- cooperative	3.8%	0.0%	80.8%	0.0%	7.7%
Family members	64.0%	6.0%	0.0%	10.0%	10.0%
Finance "company" agents	0.0%	10.0%	0.0%	10.0%	80.0%
Friends/ neighbours	46.7%	20.8%	0.0%	22.5%	6.7%
NBFC-MFI	1.7%	1.7%	4.3%	19.0%	63.8%
NGO- MFI	0.0%	64.9%	2.7%	13.5%	8.1%
Moneylenders (registered)	12.5%	12.5%	0.0%	0.0%	37.5%
Moneylender unregistered	6.0%	12.5%	0.5%	47.7%	30.1%
NBFCs (non-MFI)	0.0%	25.0%	0.0%	0.0%	75.0%
Output Buyers	9.1%	29.1%	0.0%	43.6%	12.7%
Employer	0.0%	0.0%	0.0%	0.0%	0.0%
Bank – public sector	15.5%	0.0%	44.3%	6.2%	15.5%
Bank – private sector	2.6%	0.9%	88.9%	1.7%	5.1%
Raw Material Suppliers	45.9%	8.1%	0.0%	16.2%	5.4%
Bank – regional rural	7.7%	2.6%	61.5%	10.3%	12.8%
Bank – small finance	0.0%	0.0%	1.1%	23.4%	75.5%
SHGs – bank linked	8.6%	5.7%	4.0%	49.7%	20.6%
SHGs – not linked to bank	15.4%	0.0%	0.0%	23.1%	23.1%
Cooperative society	0.0%	0.0%	42.9%	15.0%	28.6%

6.9 Access through alternative channels – MFIs, BCs, SHGs

The demand for financial education was expressed by 79.2% of the respondents, and over 80% were aware of SHGs while nearly 30% were aware of BCs, etc. The study, however, reveals that micro-entrepreneurs are not adopting banking in a big way, leave alone newer things like digital finance.

Table 42: Access through alternative channels

Preferences of Formal source of finance other than Banks	Lot
SHG-Not linked to bank	43%
SHG- Bank linked	37%
NBFC-MFI	30%
NGO-MFI	15%
Cooperative Society	14%
NBFC (non-MFI)	5%
Finance Company Agent	4%
Business Partners	2%

6.9.1 MFIs

MFIs are playing a significant role in meeting the credit demand of the microenterprises, however, the field reality divulges that, the loans from MFIs have quick processing time but with the existing legal compliances and requirement they are unable to replace the informal sources completely in a short run. Though NBFC-MFIs are aggressively working with the microenterprises, the loans reported being of little assistance because of the inadequacy of loan amounts (mostly <Rs.50000). This hasn't reduced their dependence on the informal credit sources, especially for the one-time-expenditures like weddings. One of the respondents said – "If we get enough amount from one source only, we wouldn't go to other sources. It will save us lot of effort and humiliation". Micro entrepreneurs also express social humiliation on availing loans from these institutions due to forced recovery.

Table 43: Preferences of NBFC-MFI and NGO- MFI

	NBFC-MFI			NGO- MFI		
	Few	**Lot**	**Nil**	**Few**	**Lot**	**Nil**
Varanasi	11	114	88	2	4	207
Ganjam	75	54	71	45	8	147
Bidar	19	73	108	15	104	81
Chandrapur	0	6	194	0	7	193
Total	**105**	**247**	**461**	**62**	**123**	**628**
Percentage	**12.9%**	**30.4%**	**56.7%**	**7.6%**	**15.1%**	**77.2%**

6.9.2 BCs

Banks have created a network of BCs, however, their role is mostly restricted to account opening and saving transactions. To some extent, it has created confusion on the clarity of roles between bank and BCs. The respondent reported that BCs are taking longer time in providing services and if they are approaching bank branches they have been referred to BCs. Few BCs are asking for a commission from people for the services.

Table 44: Role of business correspondents

Role of BC	Awareness		Financing		Benefits		Willing to consider taking it	
Location	**No.**	**%**	**No.**	**%**			**No.**	**%**
Varanasi	6	2.8%	4	1.9%	Understand needs	5	7	3.3%
Ganjam	0	0.0%	0	0.0%	Easy access	37	0	0.0%
Bidar	42	21.0%	8	4.0%	Convenience	9	19	9.9%
Chandrapur	97	48.5%	29	14.5%			81	47.4%
Total	145	**17.8%**	41	**5.0%**			107	13.9%

Community awareness is limited regarding the BC model they are not yet recognised BCs are the bank agents and can provide banking services at their door step. Banks currently offering only liability products and yet to offer their asset based products to their clients through the BC points especially in the districts where the study was conducted. Limited efforts were made to bring awareness about BC services among the community.

6.9.3 SHGs

To a great extent, the SHGs and the Federation of SHGs have created a good network among the women to do inter- lending which also resolves the issue of inadequacy as the network is not only restricted to their own SHG but the federation of 8-10 SHGs. This movement has reduced the dependency on informal credit and MFIs.

Table 45: Preferences of SHG- Bank linked and SHG-Not linked to bank

	SHG- Bank linked			SHG-Not linked to bank		
	Few	**Lot**	**Nil**	**Few**	**Lot**	**Nil**
Varanasi	3	49	161	1	184	28
Ganjam	91	24	85	71	16	113
Bidar	20	154	26	18	148	34
Chandrapur	0	74	126	0	0	200
Total	114	301	398	90	348	375
Percentage	**14.0%**	**37.0%**	**49.0%**	**11.1%**	**42.8%**	**46.1%**

6.10 Factors considered by micro entrepreneurs to choose a formal source of finance

Table 46: Preferences wise desired factors for financing

Ranking	Factors	% of ME preferred
1	Easy physical accessibility	67.40%
2	Less processing time	64.70%
3	Lower interest rate	57.10%
4	Less paper work and formalities	50.20%
5	Friendliness of financier	46.70%
6	Adequate amount of finance	33.10%
7	No need for land title for mortgaging	31.90%
8	Repayment schedule which suits your cash flow	25.70%
9	Duration of finance suits you	24.00%
10	Lesser requirement of collateral security for finance	23.50%
11	Less cost of financing (other than interest)	20.70%
12	Flexibility of end use – the financier does not ask what we used the finance for	8.60%
13	Availability of subsidy	7.60%
14	Chances of loan being waived	6.00%
15	Is the financing like a partnership with profit sharing or is it a finance to be returned	3.10%

Following are the top six factors micro entrepreneurs consider when choosing a financier

6.10.1 Easy physical accessibility

Refers to distribution and making sure that the product/service is available where and when it is wanted. This includes such options as field officers, business correspondents, local persons hired by banks to help them with the local community (for e.g. Bank Mitra who is liasoning between SHGs and Banks) working with the informal sector financial services etc. Entrepreneurs prefer the availability of the loan within their neighbourhood so that they need not lose their work and also expressed the need for contact person to be approachable for e.g. know their local language, local conditions, explain the services available with patience etc.

6.10.2 Less processing time

Microenterprises prefer loans that can meet their immediate demand. For banks and other financial institutions, the loan processing time and process is similar in length and complexity regardless of the size of enterprise or credit requirement. Even the loan sanctioning process is centralized for these institutions that require longer period.

6.10.3 Lower interest rate

Microenterprises prefer lower interest rate on loans. It was reported by the microenterprises that the interest rate of banks are less and are the preferred source for a loan but the opportunity cost is high due to the lengthy process of banks.

6.10.4 Less paper work and formalities

Micro entrepreneurs prefer less paperwork to avail loan. Field insights reveal, banks require legal documents such as shop establishment certificate, trade license, business plan, bank statement, cash flow details and tax filing documents. Majority of microenterprises interviewed prefer to avail loans under the Sishu category because it is easier and quicker (only requires documents such as Aadhaar, Election card, Ration Card), despite the inadequacy of the loans for their microenterprise.

6.10.5 Friendliness of financier

Friendliness of financier is the 5th desired factor indicated by the microenterprises. Micro entrepreneurs are scared to face and confront the bankers. They feel lending to a microenterprise is not a priority for bank rather a target oriented exercise. Micro entrepreneurs express that they face social humiliation on availing loans from MFIs and moneylenders due to forced recovery.

6.10.6 Adequate amount of finance

Micro entrepreneurs want the required amount of credit from the single source so that they do not have to approach many people/ institutions to meet financial requirements of their enterprise. Underfinance will lead to entrepreneurs being unable to provide required a range of services/products to their clients. Loans from other institutions except banks are of little assistance because of the inadequacy of loan amounts. As a result, their dependence on the informal credit sources, especially for the one-time expenditures like weddings have not reduced.

7 Access to Finance from Informal Sources

This study shows that 86% of the micro-entrepreneurs have borrowed money in the last three years. Out of the total entrepreneurs interacted, 77% of them have borrowed money for their micro-enterprises activities during last three years. During this period, entrepreneurs availed 43% of their loans from informal sources.

On analysis of the desired factors for financing, it was observed that easy physical accessibility, less processing time, less processing time, low interest rate, less paper work and friendliness of financer are the major four desired factors for financing. Out of these four factors credit from informal source does match with three factors which drive the micro-entrepreneurs to access credit from the informal sources.

This study shows the informal finance dominates the financial sources used by the micro entrepreneur sector and 43% of credit comes from informal sources such as family, friends, relatives, chit funds, moneylenders, input suppliers and output buyers.

The study team also probed to understand the reason for not preferring formal sources. The data analysis reflects that 36% of the micro-entrepreneurs don't prefer to avail credit from formal financial institutions because of the processing time and 24% of micro-entrepreneurs don't prefer it because of the documentation and formalities. One of such case is the story of Mr Ramesh from Karnataka state.

7.1 Friends and Relatives

Family, Friends and Relatives played a vital role in providing the credit to the entrepreneurs for the required capital to start the enterprise. They also provided credit for working capital until the business was established and able to access the credit from other sources. Micro entrepreneurs also avail credit from friends and relatives only for two consumption purposes i.e. marriage and emergency cases. Many entrepreneurs reported that the interest rate was in a very low range from 0% - 12% per annum. The entrepreneurs who have availed loan from friends and relatives prefer to get it from friends and relatives because they get the credit almost on the same day. The friends and relatives don't need collateral and information related to business.

More than 90% of entrepreneurs try to repay their loan as quick as possible to maintain their relationship. They repay their loan to their relatives and friends max within three or four instalments.

7.2 Moneylenders

Entrepreneurs avail loan for both business and consumption purpose from the moneylenders. Entrepreneurs reported that moneylenders provide credit immediately without collateral and waiting time. During the study, it was observed that respondents are hesitant to disclose the credit availed from the moneylenders as they do not want to spoil their long term relationships with these sources (who are essentially the lenders of last resort). There are many variations observed within the moneylenders some of them collect repayments on daily basis, some collect only interest on monthly basis, while most of them accept bullet payments along with interest payment. The loan amount given by moneylenders ranges between Rs.10, 000 – Rs.200, 000. The size of the loan depends upon the trust established between moneylender and the entrepreneur.

The places where higher number of formal players especially SHGs and MFIs exist, moneylenders have reduced their rate of interest to attract the clients. Entrepreneurs stated that some of the moneylenders keep a condition that their customers should not repay the principal amount immediately but have to pay the interest on monthly basis. Most of the entrepreneurs (44%) prefer money lenders over friends and relatives (33%) because they don't want to spoil their relationship with friends and relatives. In both the sources i.e. friends & relatives and moneylenders, repayment percentage is better than formal financial institutions particularly banks because of relationship and close monitoring.

Entrepreneurs reported that they know the rate of interest rate in the banks is less but they need to submit several documents including No objection certificate, collaterals, guarantor/s, licence for business, many visits to the bank for providing information and inquiring about status, and long waiting period made them to avail loans from informal sources like moneylenders. On other hand, banks discourage loan applications from microenterprises as they perceive them as risky and cost of monitoring is high and tend to provide loans to big size enterprises.

7.3 Input suppliers and output buyers

In some of the business activities, it was quite evident that input suppliers and output buyers play a key role in providing credit to the respondents. There are two categories of input suppliers. One category of input suppliers provides inputs on credit and purchase the output against the credit. Usually, it is the small micro entrepreneurs that depend on such input suppliers. The other category of input supplier is those who provide only the raw material on credit. The details of these categories and factors that are responsible for it mentioned in the next subsection. Respondents said that they are aware that they can get a little extra for their finished product (for e.g. sari) in the open market but still prefer to avail services from input suppliers as they provide required quality, colour and quantity and are flexible to the needs of the clients. Some of the respondents said that they also take cash loan from input suppliers to meet the consumption needs. Some of the snack business owners said that they prefer to take loans and inputs from input suppliers as they provide door step services and never reject loans based on the purpose of the loan (they also said that banks will not allow people to use part of the loan for consumption purpose).

To understand the dynamics of input supplier, we tried to understand different players and the volume of informal source of transactions and reasons for dependency on input suppliers in weaving cluster of Ganjam, Odisha.

Table 47: Input requirements in weaving cluster of Ganjam, Odisha

#	Information*	Unit	Quantity
1	Sale of colour thread per day by one raw-material supplier (Trader)	Kg	90
2	One dying unit caters the need of number of Handloom	No.	20
3	One dying unit caters the need of number of Power loom	No.	20
4	Number of raw-material supplier (Traders) in the Hinjlikatu cluster and Berhampur	No.	8
5	Number of raw-material supplier (Wholesaler) in Berhampur	No.	3
6	% of raw-material that comes back to raw-material supplier as finished product	%	50
7	Informal Credit Percentage of transaction from raw-material supplier to weavers who works on wage basis	%	100

#	Information*	Unit	Quantity
8	Credit Percentage of transaction from raw-material supplier to weavers who sale their product to other traders	%	50%
9	Quantity of thread in one kata	gm	220
10	No of kata (small rill) that can be produce from one kg thread	No.	5
11	Quantity of colour thread require to produce one gamuchha	gm	176
12	Quantity of colour thread require to produce one Dhoti (normal not the Berhampur Pata)	gm	704
13	Quantity of colour thread require to produce one Saree	gm	880
14	Percentage of gamuchha production	%	90%
15	Percentage of Dhoti production	%	10%
16	Price of 1 kg colour cotton thread (Raw-material to Weaver)	Rs.	200
17	Price of 1 gamuchha (lowest grade) from traders to wholesaler	Rs.	25
18	Price of 1 gamuchha (highest grade) from traders to wholesaler	Rs.	55

Figure 8: Demand for credit for Microenterprises, Rs. Trillion

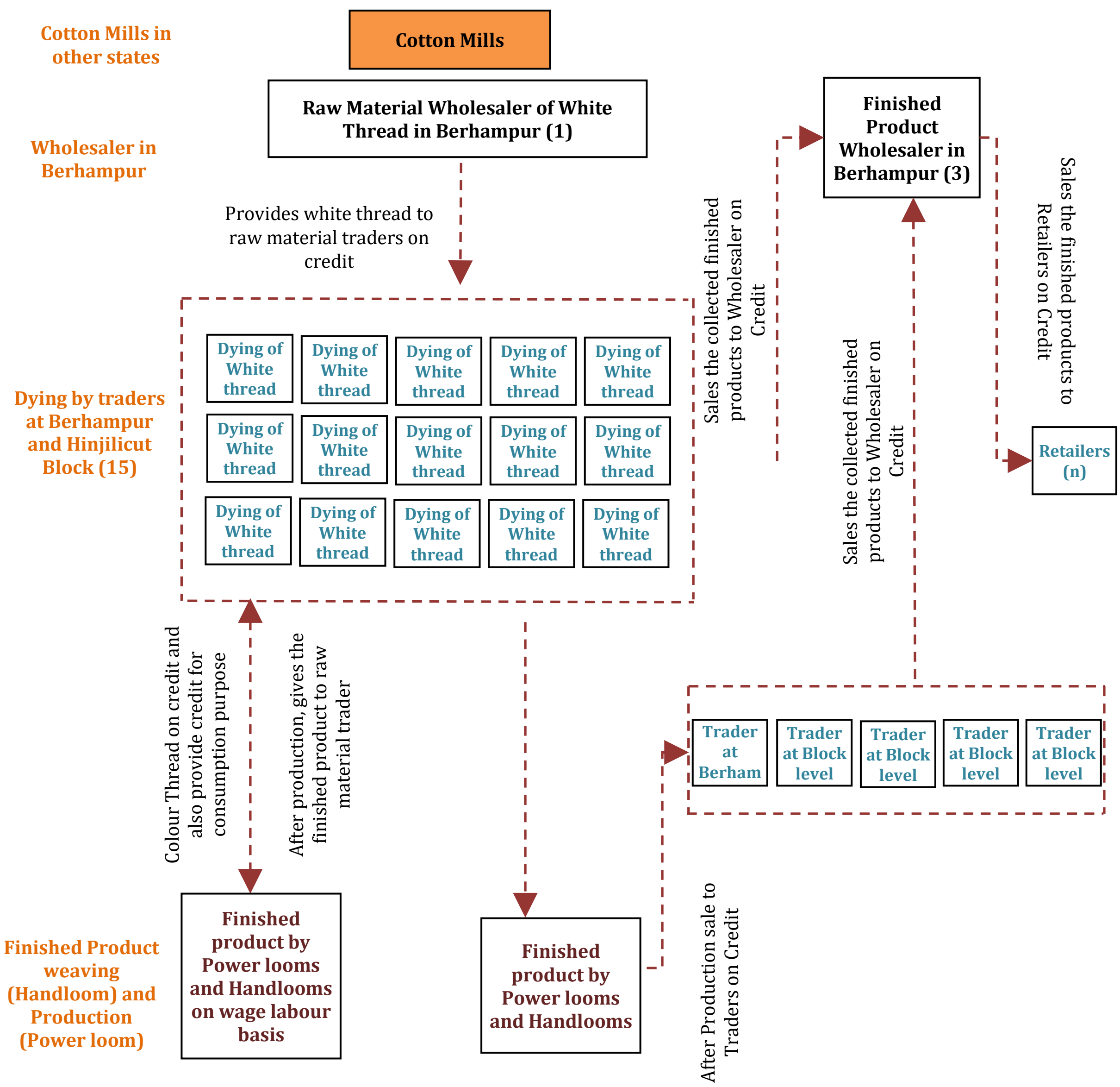


Table 48: Estimate of informal credit per day

Stakeholders	Unit	Quantity	Unit Rate	Total (INR)
Finished product (Gamuchha) that comes back to one raw material supplier from weavers per day	Kg	45	40	32,400
Finished product (Gamuchha) that comes back to wholesaler per day from raw material supplier (Trader) per day	Rs.			259,200
Finished product (Gamuchha) that comes back to wholesaler per day from Trader who only collects finished product from weavers per day	Rs.			259,200
Total amount of finished products (Gamuchha) that comes back to wholesaler in Berhampur per day	Rs.			518,400
Amount of Informal credit in the cluster for cotton products (excluding Berhampur patta) per day	Rs.			259,200

Reasons for Informal credit

We observe that the prevailing rate of interest from informal source credit in the Ganjam district is 24% to 36% per annum. Three years before it was 36% to 60% per annum. The reduction in rate of interest from informal source of credit is due to SHG bank linkage programme and mostly due to NBFCs. However, people are still availing the credit from informal sources and around 95% of the people know that they are paying higher interest rate. People don't mind to pay more to get the credit from informal source because they perceive that the ultimate credit cost from informal source is cheaper than the formal financial institutions. People don't opt to avail the credit from informal sources because it is easy for them to get it from informal source but because they find it difficult to complete the following process to access credit from formal financial institutions.

- No loan without mortgage
- Documentation (availability of home Patta, if Patta is available whether it is Grarabari or agriculture land patta, if it is Grarabaripatta or agriculture patta whether it is fenced or not, if it is fenced get the 25 years EC from RI and Tehsil office, If gets 25 years EC from Tehsil office, get the valuation of it from RI and lawyer)
- Long documentation process to submit the application
- Long waiting time even after submission of application documents
- Uncertainty about sanction of loan
- Those whose loan is approved get the loan after their purpose of availing loan gets over

Limitation of the analysis

It was difficult to collect information from traders on the amount of transaction. The amount was calculated based on the raw material being used per day by weavers in the area.

7.3.1 Factors considered to choose informal source of finance

Based on the data analysis, we found that following are the top five desired factors micro entrepreneurs consider when choosing a financier.

Table 49: Reasons reported for preferring informal sources

Easy access	28.6%
Less processing time	22.1%
Friendliness of the financier	14.6%
No paper work and formalities	13.1%
Low/No interest rate	9.5%
Adequacy of the amount	9.0%
Lack of formal sources in the vicinity	3.0%

Based on the sub-factors, the micro entrepreneurs can be classified into two categories. One which is start-ups and small volume and other category is already in the business for long time (more than 10 yrs).

Figure 9: Sub-Factors leading to selection of financers by micro entrepreneurs who are small and want to start

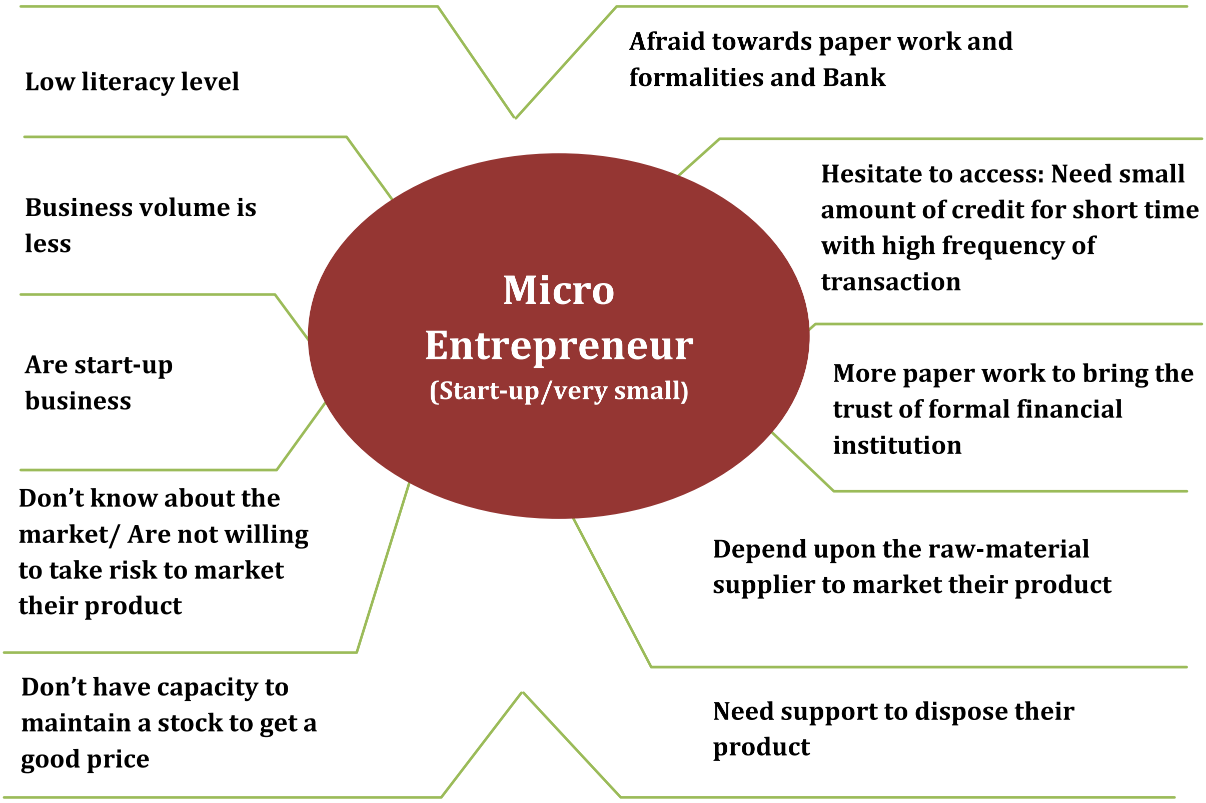
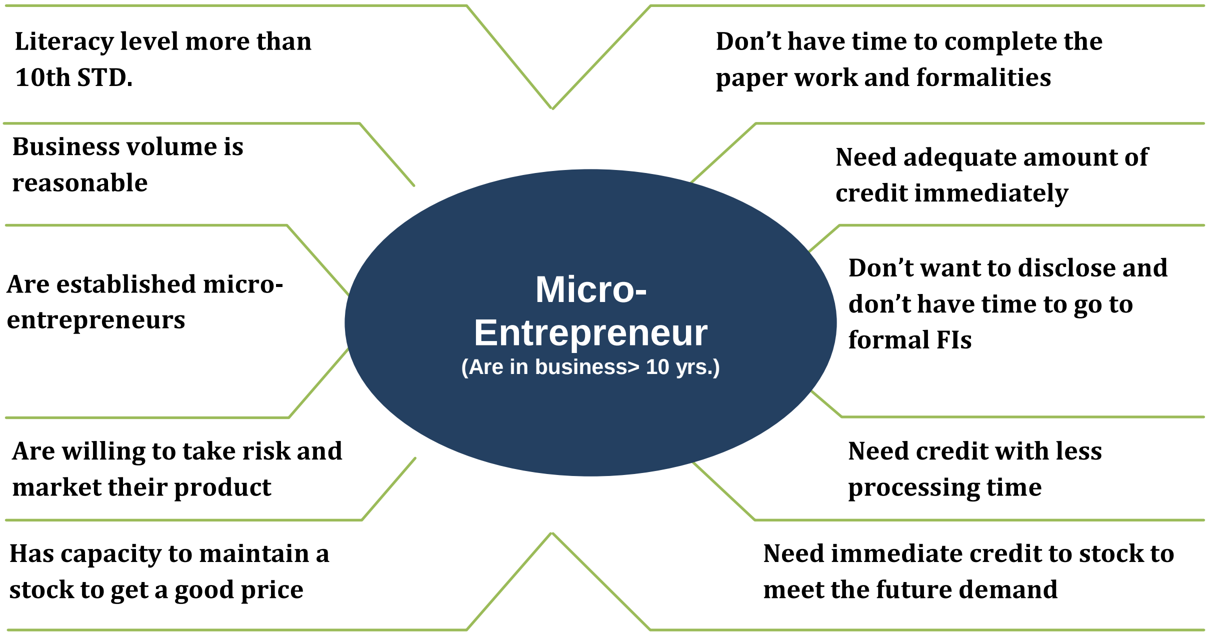


Figure 10: Sub-Factors leading to selection of financer by micro entrepreneurs who are in business for more than 10 yrs



The following case study reflects some of the above mentioned factors that are responsible for micro entrepreneurs not to access credit from formal financial institutions.

Box 1: Informal loan to Formal Loan: Case of two youths in Berhampur, Odisha

G Ashok Patro and M Shyam Sundar Rao are the two youths from Berhampur city, known as silk city of Odisha, known for its handloom sarees made from Tussar silk. Mr Ashok with no education started his career with a nearby doctor's clinic with Rs.30 per month and worked for 16 years. At the time of leaving his job, he was getting a remuneration of Rs.200 per month.

Shyam, 7th pass started working in a Kirana shop and at the time of leaving his job was getting Rs. 300 per month. Due to their stressed financial condition and increase in liability due to their marriage, they took a decision to start some trading business on fruits. They came in contact with each other and became close friends. They struggled to sell fruits as street vendors because fruits being a perishable product, each day they were losing some amount. No preservatives were available at that time to increase the shelf life of the fruits. Then they started street vending of snacks item on bicycle. With four years of observation from where they used to purchase the snacks, they decided to start their snacks (local name: Supulu, Dantikili) making unit in the year 2006 in a partnership.

They went to Andhra Pradesh and learned the skill to prepare the snacks and returned to Berhampur to start their own unit. They engaged 3 skilled workers from Andhra. The unit is in rented premises for which they are paying Rs. 4500 per month on rent plus electricity bill. Initially, the machine was purchased at Rs. 28,000. They brought skilled workers from Andhra Pradesh with basic skills requirement for the enterprise to mix grinded items properly and proportionately. The two partners took the 1st loan from a nearby moneylender in 2006. The loan amount was Rs. 0.1 million with 24% flat interest rate per annum.

They were able to pay only the interest to the money lender. In the year 2009, they decided to avail a loan from a bank to repay the total loan amount to the moneylender. They approached the then RRB-Rushikulya Garmin Bank (now known as Utkal Gramya Bank after the merger of RRBs in Odisha) and got the required support starting from filling up the application through the support of one of their relatives who was in the bank. The duo applied for a loan of Rs. 0.1 million to the bank. The amount was sanctioned for which they mortgaged their manufacturing unit land and they repaid the loan to the money lender. Now the enterprise employs 12 women and 4 male persons as labourer in the enterprise. The enterprise functions whole of the year except during strikes and during summer when sales go down. Over a period of time, turnover has increased. After production, they deliver it to the local shop owners and some of the traders also purchase it from their manufacturing unit. Now the transaction of the unit is around Rs. 2.5 million per annum. Now they have a cash credit of Rs. 0.2 million. In between, they had taken housing loan of Rs. 0.6 million and repaid the loan. They have constructed their house next to each other by purchasing a plot and share it among themselves. The bank allowed them to have cash credit of Rs. 0.2 million. Everything was going smoothly. All of a sudden the banks asked for revised collateral security. Initially they had submitted their land tittle which was on agriculture land, which was not converted to Gharabadi (change of land type from agriculture to house construction) and was accepted by the bank. Due to some new circular to the bank/audit issue, the bank asked to provide the land record (GharabadiPatta) as collateral. Both the partners repeatedly went to Tehsil office to convert their land which is yet to be materialised. Bankers told that it is not possible to advance cash credit. The banker suggested them to close their CC account if they fail to submit the required documents. After doing transactions for last 10 years partners they were forced to close the account recently. Now they are looking for a new bank for transaction. They are still interested to go to a bank because of less interest charge. They have heard that MUDRA loan is available only up to Rs. 50,000. Awareness on MUDRA is not very significant in the area.

It is quite evident that none of the formal sources provide immediate provision of finances as the informal lender does, even if the cost of finance from informal sources is exorbitant. Even when there is no actual cost of financing, there is a social cost – they may have to help them sometime in future. In cases where people have reported to have borrowed from family or friends and paid no interest, people are dreadful that non-repayment would involve damaging social connections. This may have long term effects such as exclusion from family or friends' network. In cases with moneylenders, there is social humiliation and threats. Thus, though there are excruciating costs associated with informal financing, there are factors which make its presence stronger and make its elimination from the "financing system" difficult. The ease with which people get a loan (which includes quick and easy processing, adequate amount, easy repayment schedule, less requirement of guarantor or collateral) makes it an attractive option despite its costs. And when the situation requires urgent finance (mostly in case of medical or social expenses like a wedding), informal sources are most relied upon due to the adequacy of the amount and quick provision.

Table 50: Perceived reduction in dependence on informal sources

	with banks		with SHGs		with MFIs	
	N	%	N	%	N	%
Varanasi	37	17.4%	136	63.8%	138	64.8%
Ganjam	48	24.0%	15	7.5%	11	5.5%
Bidar	52	26.0%	97	48.5%	56	28.0%
Chandrapur	10	5.0%	18	9.0%	8	4.0%
Total	**147**	**18.1%**	**266**	**32.7%**	**213**	**26.2%**

The above table shows that SHG movement is very effective in reducing the dependency of microenterprises on informal sources. The reason is easy accessibility, quick processing time and transparency. With door step presence and quick processing, MFIs also prove to be effective in reducing the dependency of microenterprises on informal sources.

8 Financial Literacy efforts and their Impact

8.1 Financial literacy efforts by various players

8.1.1 Establishment of FLCCs

As per the key informant interviews, LDMs are following the RBI guidelines in terms of organizing and implementing financial literacy programs for microenterprises through the facilitation centres. Rural Branches are also conducting Financial Literacy Camps. The branches are conducting required number of camps as per their plan. They are also conducting camps for focus groups like farmers, micro-entrepreneurs etc. However, there is a lot of scope to improve the quality of the program that can fulfill the objectives more effectively. All the key informants have indicated that large operational area and work load on existing bank staffs are the key factors behind it. Earlier banks used to provide only two type of service i.e. savings and credit. As per their business strategy, all the banks have expanded their financial services. This has led to less interaction with their customers.

8.1.2 Bank Branch Staff in conducting orientation to the community

The study found that each of the banks is conducting financial literacy camp every year. An average number of camps per year for every branch is 3-4. The number seems to be very small depending on the size of the service area (including urban, eemi-urban and rural area). The program is being conducted in the awareness mode. In association with NABARD, all the SLBCs have customised the standard RBI training module. The study team also got a chance to go through the customised training materials in bank branches. It was observed that the materials are mostly confined to the product flyers that are being distributed to the participants. Targeted customers for the FL were the villagers. The study team was not able to find out the functioning FLCC in the rural areas, where the largest sections of the financially excluded population reside. The schemes executed by NABARD and other government departments are also ensuring mass awareness generation.

It has been observed that wherever the bank management has goodwill, the BCs are working well and the micro entrepreneurs have better financial literacy. It was analysed that the awareness of the existence of FLCC among the local populace is limited. FLCCs are mostly serving walk -in clients, whereas outdoor literacy drives by FLCCs are exceptions. The literacy material available at FLCCs is generally the publicity material pertaining to various products of sponsor banks.

8.1.3 MFIs and NGOs efforts in mass education on financial literacy

Availability of wide variety formal credit sources and frequent interaction with MFI loan officers, NGO staffs led to improving their decisions on comparing the features of available credit. However, because of lack of similar mobilization by the banks the awareness about bank loans and government schemes rooted through banks is less. Awareness on Mudra Loans and other government schemes rooted through banks is low.

Table 51: Micro entrepreneurs willing to join financial literacy class

	ME	N	%
Varanasi	213	201	94.4
Ganjam	200	111	55.5
Bidar	200	157	78.5
Chandrapur	200	175	87.5
Total	**813**	**644**	**79.2**

SHGs and SHG federation emphasize on literacy and hence resulted in better financial literacy over time because of their internal operation on pooling of resources and fund management.

8.1.4 Use of communication channels Radio, TV, newspapers, wall paintings etc.

The team doesn't observe any wall painting on importance of financial literacy in the visited locations. The bank branches have displayed posters on financial literacy only within the premises of their branches.

8.2 Impact of financial literacy efforts

8.2.1 Awareness about credit Bureau

Only 24% of respondents are aware of the Credit Bureau. It was generally observed that the locations where MFIs are predominant, the awareness about credit bureau is high as this is the part of the training that MFI provides to the client.

Table 52: Awareness about credit bureau

Places	% of respondent aware about credit bureau
Uttar Pradesh – Varanasi	74.2%
Odisha – Ganjam	3.5%
Karnataka – Bidar	9.5%
Maharashtra – Chandrapur	7.0%
Total	24.4%

However 79% of total respondent are interested to join the financial literacy training, if it is provided to them. Most of the key informants have a view that the communication channels talks about the financial literacy but it should emphasise more on the benefit of the repayment.

8.2.2 Increased use of bank accounts for savings

The study reflects that 95.2% of the micro entrepreneurs have bank account whereas only 30% of the micro entrepreneurs are accessing loan from banks.

Table 53: Increased use of bank accounts for savings

Sources for money withdrawal				
	Bank	**BC Outlet**	**ATM**	**Do not withdraw**
Varanasi	84.5%	0.0%	9.4%	6.1%
Ganjam	52.0%	0.0%	45.5%	2.5%
Bidar	72.5%	3.5%	15.5%	8.5%
Chandrapur	81.0%	1.0%	13.5%	4.5%
Total	**72.7%**	**1.1%**	**20.8%**	**5.4%**

8.2.3 Use of banks for access to credit

As mentioned in previous section, more than 95% of micro entrepreneurs have bank account but only 30% of the micro entrepreneurs are accessing credit from banks (including SFBs). Due to increased awareness and availability, entrepreneurs started using the banks, SHGs and MFIs and therefore a reduced dependency on informal sources perceived by entrepreneurs.

Table 54: Perceived reduction in dependence on informal Sources

Perceived reduction in dependence on informal sources			
	with banks	**with SHGs**	**with MFIs**
Varanasi	17.4%	63.8%	64.8%
Ganjam	24.0%	7.5%	5.5%
Bidar	26.0%	48.5%	28.0%
Chandrapur	5.0%	9.0%	4.0%
Total	18.1%	32.7%	26.2%

9 Policy recommendations

The financing gap in the microenterprise sector is a combined result of demand-side challenges such as lack of awareness, documentation requirements, inability to provide margin money, collateral and mixing up of household and enterprise cash flows, and supply-side issues, such as lack of translation of high level credit policies into appropriate processes for microenterprise borrowers, and incentives for field bankers to lend to micro entrepreneurs. Superficial understanding about microenterprise business among bankers is persistent, and due to their branch and desk-based orientation, they find it difficult to identify the right borrowers and lend to those who come to them, often through middle men or recommendations of influential persons and who can at least on paper, meet the various requirements. Project appraisal, loan monitoring and default management are more for the purpose of reporting "action taken" rather than to actually do it in spirit.

The study recommends policy interventions suitable to address the difficulties faced by micro entrepreneurs in accessing credit from their choice preference and to address the persistence of overall inadequacy of credit.

- Banks need to innovate greatly on product features. The standard term loans with quarterly or monthly repayment instalments, do not take into account the seasonality of microenterprise cash flows nor of the varying requirements of micro entrepreneurs' households. Thus "cash-credit" products should be offered but with digital operations, so that deposit or withdrawal or small amounts frequently need not mean the micro entrepreneur has to go to a bank branch or ATM. Term loans should be only given for the purchase of equipment, machinery or other lumpy fixed assets and should be at least for four year duration with one year moratorium or three years with a ballooning of instalments (higher amounts in the latter years). Even though they may be below the GST registration floor, microenterprises taking bank loans may be encouraged to use apps like GR4GST (get ready for GST) to channel as much of their input purchase and utility payment transactions through bank accounts as possible. Sale proceeds may be mostly still in cash but the bank must insist on a daily deposit of proceeds and a reminder should go out by SMS if it does not happen by 11 am every morning. Even cash collection from the shop is now being offered as a reliable digitally recorded service by, for example, Indepay (www.indepay.com)and SBI is partnering with them for a pilot in the Delhi NCR.

Banks need to innovate greatly on product features. We have to recognise that for microenterprises, the business cash flows and the household cash flows are mixed up, and often entrepreneurs are forced to use business loans to meet other financing needs medical care, children's education, housing, and social expenditure. In case of very low income households, part of the loan is even used for consumption. Thus it is important to offer a range of different products to meet these needs and allow one person or one household to have multiple, simultaneous loans (within overall repayment capacity) for different financing needs, with different interest rates and repayment terms. In this connection, the work done on household wealth planning by IFMR Capital, Chennai and the theoretical and policy work done by the recent RBI Committee on Household Finances need to be studied and put in action more widely.

9.1 Enhance financial awareness using technology

Enhancing awareness through information dissemination, training, handholding, mentoring and establishment of a network for facilitating cross- learning and mutual help. The RBI has already taken many steps towards this through various banks but the outreach is extremely limited and perfunctory. This because most programs of financial literacy are based on holding face-to-face training programs in rural areas and low income urban areas which are too labour intensive for the trainers and takes too much time for the participants. Instead, mobile phone based training short videos, mobile phone games (e.g. the ones designed by the ILRT, Hyderabad – (www.ilrtindi.org) and mobile apps like Haqdarshak (www.haqdarshak.com) which indicate the eligibility of a person for a government program or loan, should be used. These can be supplemented by web-based e-learning modules such as www.dhangyan.com and Rupaya Paisa series of books developed by Pratham Books for children of classes 6 to 8. Vocational training courses to become Household Financial Advisors and Microenterprise Business Advisors should be offered as a part of the National Skill Qualification Program from class 9 to 12, so that eventually India has lakhs of young people engaged in these professions.

Additional recommendations include, adequate and timely information about MSME schemes needs to be actively disseminated through advertisements in newspapers and magazines and on television. The government could consider starting a dedicated TV channel to address MSMEs' need for information and to communicate policies. More systematic training on financial literacy; financial Institutions require to organise more accounting/finance training programmes; cluster level awareness for both bankers and micro entrepreneurs need to be organised. Engaging more credit counsellors and increasing the commission/incentive of credit counsellors and also fixing accountability on recovery

9.2 Enhance promotional support to microenterprises - MENTOR

The all-round reluctance or inability of the so-called promotional institutions to serve micro-enterprises in general and within those, service sector enterprises, in particular, requires to be handled with a totally new approach, which was being suggested here. The idea was to use successful micro entrepreneurs to mentor upcoming micro entrepreneurs, taking care that they are from slightly different areas so that the established ones do not see the new ones as competitors. Basix has successfully tried this methodology in its "inter-borrower exchange program". Under this program, those micro-entrepreneurs who were rated high in their line of business (such as grocery store, plastics goods shop, hardware shop, rice mill, bakery, wood or metal workshop, etc. by Basix field staff, were requested to organize training programs for 5-10 others in the same business but not from the same village/town so that they are not competitors. Proper techniques of storage, display, inventory management, customer handling, account keeping and financing were discussed by an experienced trainer.

Based on this experience, we are recommending the establishment by SIDBI of a Micro Entrepreneurs' Network for Training, Operational support and Resource mobilization (MENTOR). Under MENTOR, experienced micro entrepreneurs not only will provide guidance on local market demand, customer preferences, skill training and business training, but also help in operations such as identifying and linking with sources of raw materials or inputs, equipment, and any permissions or licenses needed, as also in helping mobilize credit from MFIs or bankers by giving references and offering support in filling applications. All these services of MENTORs should be paid under the RBI approved scheme of business facilitators, by the bankers of the upcoming entrepreneurs, at about 3% of the loan value, 1% each when the loan was approved, when it was utilized and when it was repaid. Thus micro enterprise mentoring itself becomes a service sector micro enterprise. The trainee enterprises also see an increase in revenues and income.

To support the MENTORs, a permanent agency was needed and it would too distant if it would be located at the district level like the not very useful District Industries Centres (DIC). Instead, non-governmental social enterprises should be asked to set up block level Self-Employment Promotion Agencies (SEPA), staffed by at least three professionals, one each from the field of business management, agriculture or animal husbandry or forestry and community development/social work/training. These professionals should train and guide the MENTORs and link them with the outside world for knowledge, financial resources, skills and markets for inputs and outputs. The SEPA could be paid partly by the MENTORs and partly by the state governments.

9.3 Reduce documentation – go digital for micro loans

Reduce the complexity in documentation by replacing it with simple procedures, increased periodical monitoring, and further strengthening of DICs etc. In its movement towards digital India, the GoI should eliminate the need for any paper- based loan application and a physical visit by the borrower to a branch. Loan applications for loans up to the Shishu category should be fully digitized using mobile phone apps and tabs. These can be uploaded by anyone having access to the internet. If they need assistance in filling the application, the BC and CSC operators should be trained and authorised to do this for a fixed fee.

If LIC with a huge customer base could digitise its insurance policy application and issuing of cover notes, through a nationwide network of Common Service Centres (IT kiosks offering access to government services) in rural areas, there is no reason why the banking system should lag behind. Already significant sized pilots are being conducted in Rajasthan by the United Bank of India and Sub-K (a BC company) for originating and approving microenterprise loans in a paperless manner using electronic tablets (Tabs). Another effort worthy of mention in this regard is Streenidhi, (https://www.sthreenidhi.ap.gov.in) a wholesale lending institution for SHGs and SHG Federations, established by the Govt of Andhra Pradesh in 2012. The operations of Streenidhi are fully digitised and a woman applying for a loan to her SHG in rural AP gets a decision within three days and if the loan is approved then she gets the money credited in her bank account by the fifth day.

The processes that a borrower has to go through should be subjected to a detailed scrutiny by business process re-engineering professionals. Banks must be mandated to make all applications up to Shishu loans completely digital and paperless and not requiring any branch visit. Once an application is digitally uploaded, its appraisal, approval, disbursement and repayment must be digitally tracked. This must include a mandatory use of Aadhaar for e- KYC check and Credit Bureau for credit history check of applicants, conveying of approval or rejection of loan application, including causes thereof by mobile SMS, and disbursement as well repayment through their bank accounts electronically linked to the core banking system.

Relaxation of some norms is required. MUDRA application in many cases rejected showing Service area approach. This need to be considered, service area approach is only for Govt.

sponsored programme. MUDRA cases reporting/monitoring/follow up-should be done weekly once (Credit proposal and disposal-MIS monitoring-weekly). Fund Utilization –self certificate by entrepreneurs should be enough. In Ganjam, the study team found that houses are attached to each other and bankers do not mortgage these houses because of legal issues, BDA approval of house. Banks should not involve their advocates to deal with the customers, particularly SBI. Majority of entrepreneurs are unhappy with SBI.

9.4 Introduce incentives for responsible lending to microenterprises

The incentive system for field- based bank staff must be changed to encourage field officers to move out of the branches and branch managers to occasionally leave their desks to interact with micro-entrepreneurs in their location. To monitor this, bankers must be asked to upload their photographs with applicants or borrowers along with the GPS location and date and time stamp, on the designated website of the bank. Field officers must not only be given adequate travel allowances but also incentives for originating loans by numbers, not amount, so that they can look for smaller borrowers. Repayment must be monitored and bankers rewarded for keeping NPAs below an acceptable target level, say 3%. (Zero NPA is a fantasy).

Other recommendations that emerge were simplifying documentation requirement from entrepreneur; reducing bank charges for processing fee and insurance; reducing charges for 3 months verification done by Bankers, RRBs of Rs.250. It is difficult for fresh entrepreneurs to provide documents like IT return and land deed. Rigidity approach of bankers needs to be changed and a minimum three years' tenure in one branch may help. Frequent and early transfer results in more NPAs. Bankers focus should shift from existing established traders to fresh entrepreneurs

9.5 Encourage banks to enhance use of alternative channels

Banks should be encouraged to use alternative channels – like SHGs, MFIs and BCs who are already engaged in cash-in and cash-out transactions for bank accounts. Banks are using these channels but reluctantly and tend to do so when they get a government mandate and an operating subsidy for the channel costs (as in case of the SHG loans). In case of MFIs as well loan-originating BCs, banks tend to keep a much larger share of the net interest income that their proportion of operating costs plus risk.

To correct this situation the RBI should establish an Expert Committee to determine the efficiency level cost structure (including operating and risk costs) for each channel and the channels should then be paid accordingly. Specific recommendations for the BC channel include

- The BC model can be extended beyond microfinance to meet other financing needs of low income communities, such as micro-businesses, micro-housing, small vehicles, agri and SHG loans.
- Lending BCs may be brought under direct supervision of RBI similar to P2P and NBFC-MFIs so that same standards will apply to all players and customer interests would be better protected.
- BC compensation and risk sharing parameters should be better defined so that accountability and risk-return balance are fairly distributed between the bank and BC.

- Banks should be allowed to price products in line with cost structures. PSU banks currently hesitate to mark-up the price to accommodate for BC costs thus ending up underpaying BCs.
- BCs should be allowed to access UIDAI, NPCI and Credit Bureaus directly in order to ensure efficient flow of information and to encourage cashless transactions.
- BCs may be given access to public database for analysing customer profiles and managing risk better.
- To improve supervision of BCs, the BC Federation of India (BCFI) may be conferred the status of a Self-Regulatory Organisation (SRO) with due authority and accountability.

9.6 Let moneylenders slowly fade away

Some experiments were tried by Basix in this regard, in 1996, using Arhatiyas (commission agents) in the Raichur agricultural market yard. The experiment showed some positive results – in terms of enhancing outreach to a large number of small farmers, and the repayment was hundred percent. But by the third year, it was found that the Arhatiyas were lending at a much higher rate than specified and the scheme was closed. Similar lessons were learned by Basix in lending in Mahaboobnagar district to input suppliers (seed, fertiliser and pesticide dealers) as well output buyers (cotton seed production organisers).

Though the RBI Technical Group, 2007, had recommended a selective and careful use of moneylenders, to enhance access to credit by micro borrowers, and even drafted model legislation for the regulation of moneylenders who would then be linked with banks for wholesale finance, not much progress happened on it. The reasons for this are from both sides – moneylenders are reluctant to be brought under any formal controls, and banks are unwilling to lend to them in case the scheme backfires. Instead, banks are more willing to use alternative channels like MFIs, SHGs and BCs, as they are more prone to being supervised. The study found that wherever the outreach of these channels was dense, the dependence on moneylenders was getting reduced.

In summary, therefore, our recommendation is that informal channels should be allowed to slowly fade away as the alternate channels spread their outreach. In this connection, we must caution that a new generation of digital moneylenders may crop up and the RBI needs to keep an eye on the new digital lending initiatives including person to person (P2P) lending platforms, from the point of view of consumer protection.

10 Way Forward

It is obvious from the study that the formal institutions have made a significant impact on microenterprises through financing that led to the reduction of dependency on informal sources but at the same time the informal sources are the vital players for the microenterprises that cannot be completely replaced from the market due to their unique service proposition.

The study also points out that there is a huge finance demand -supply gap for microenterprises that compel them to approach informal sources. The latest government schemes focussing on financial services to microenterprises proved to be very effective in terms of reaching out. Going forward, the formal financial sources have to focus on

- Efficient distribution system backed with technology, customised product and services and good relationship management, reduce the transaction cost and risk profile of microenterprises
- Leveraging local distribution channel added with non-conventional way to acquiring business detail result in scaling up the business
- Increasing ability of the financier to evaluate and manage business risks and offer customized product. Cash flow based appraisal & future cash flow of the enterprises would be estimated to derive the credit requirement and instalment. Examination of the special peculiarities of the business like seasonality, business margin, selling pattern, buying pattern, trend analysis to arrive at conclusion
- Customized underwriting procedures backed with technology result in faster and effective loan processing through anticipating cash flow of the enterprise & their overall participation in value chain
- Integrating into the supply chain of the microenterprises would help the financier to evaluate the client effectively.

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Annexures

Annexure 1: About BASIX Consulting

BASIX Consulting and Technology Services Ltd. (BASIX Consulting) is **an ISO 9001:2015 Certified Company.** It is a subsidiary of Bhartiya Samruddhi Investments and Consulting Services Ltd. (BASIX), the holding company of BASIX Social Enterprise Group (BASIX SEG). BASIX SEG is a conglomeration of 12 institutions. Consulting projects were executed as a division within the holding company from 1996 to 2010. A separate entity BASIX Consulting and Technology Services Ltd was registered in 2010 to exclusively handle consulting projects.

Drawing from the vast experiences and expertise gained over the years in microfinance operations and livelihood promotion, BASIX Consulting offers advisory services on Banking, Microcredit, Pensions, Insurance, Remittances, Information Technology and Livelihood Promotion. It provides practical and customized solutions to microfinance and financial institutions, and addresses their constraints of governance, management and operations to enhance their capability and expand their operations.

As on date BASIX Consulting has undertaken 250+ Consulting Assignments, strengthened the internal capacity of 170+ institutions ultimately benefiting 1.5 million+ Customers. BASIX Consulting's geographical reach is over 39 countries spanning the regions of Africa, South Pacific, South Asia and South East Asia. It has experiences of working in some of the most challenging environments in the above regions.

A.1.1: Range of Consulting Services

- **Inclusive Financial Sector Development Services (IFSD)** – for building an inclusive financial sector through undertaking research and evaluation studies, financial literacy programs, design and development of pro-poor financial products, capacity building of financial institutions engaged in providing financial services to the poor.

  Insurance being the risk mitigation mechanism, it has been an integral part of the inclusive financial services. BASIX has developed experience and expertise in the domains of Agriculture, Health, Livestock and Climate Change related Micro insurance solutions. BASIX Consulting offers following services Studies/Surveys, Technical Assistance, Training and capacity building and Facilitation services.

- **Institution development and Livelihood Promotion Services (IDLP)** - to various organizations engaged in microfinance and livelihood promotion including MFIs, NGOs and community based institutions like Farmer producer organizations (FPOs) and Self Help Groups (SHGs), SHG Federations. The services include institutional assessment, institutional strengthening through design of organizational structure, systems and processes, strategic business planning and capacity building, and project evaluation and Impact assessment.
- **Information Technology and Advisory Services (ITAS)** – Support the organizations engaged in microfinance and livelihood promotion on information technology solutions to improve operations, management and regulatory compliance. The services include undertaking system requirement studies and develop/implement appropriate specialized software solutions to suit these institutions. The product offering internally developed by BASIX and its collaborators include Delphix Nano as Core Enterprise Solution for microfinance institutions (MFIs), BANKSOFT as Core Banking Solution for Banks & MFIs, ViTranSP as Agent/ Branchless Banking Solution, BINDAS as Micro Insurance Solution and Customized Web-Portals (M & E Applications, Soil Testing, Product Warranty Tracking Systems etc.). BASIX also provided technical assistance to MFIs in acquiring and implementing third party MIS solutions – such as CBS and Branchless Banking solutions, including setting up of Data Centre and training IT resources of MFIs.
- **Technology to Market (T2M) -** T2M services include explore, understand, customize, test and productize technologies which have impact on the livelihoods and overall wellbeing of community. Some of the examples of such technologies include sub-surface irrigation system, decentralized production of bio-pesticides, soil testing through portables kits and web-portal (miitidoctor.com), safe drinking water at affordable cost in rural areas and production of low cost sanitary napkins through SHG federations.

A.1.2: Geographic Outreach

BASIX Consulting has executed consulting assignments in 17 states in India and in 39 countries across Asia, Pacific and Africa.

- **South Asia:** India, Bangladesh, Bhutan, Maldives, Rwanda and Sri Lanka
- **South East Asia**: Cambodia, China, Indonesia, Lao PDR, Malaysia, Myanmar, Timor-Leste and Vietnam
- **Central Asia**: Tajikistan
- **Pacific**: Fiji, Samoa, Solomon Islands, Papua New Guinea, Vanuatu
- **Africa**: Burkina Faso , Burundi, Cameroon, Ethiopia, Ghana, Kenya, Madagascar, Malawi, Mali, Mozambique, Nigeria, Rwanda, Senegal, South Africa, South Sudan, Tanzania, Uganda, Sierra Leone and Zambia.

A.1.3: Notable Clients and Associates:

International Agencies

- World Bank
- International Finance Corporation (IFC)
- Asian Development Bank (ADB)
- Department for International Development (DFID)
- Canadian International Development Agency (CIDA)
- International Fund for Agricultural Development (IFAD)
- Consultative Group to Assist the Poorest (CGAP)
- Développement international Desjardins (DID)
- UN Agencies (UNDP, UNOPS, UNCDF, UN Women)
- International Labour Organization (ILO)
- Kreditanstalt für Wiederaufbau (KfW)
- International Livestock Research Institute (ILRI)
- United States Agency for International Development (USAID)
- German Technical Cooperation (GTZ)

National level

- Ministry of Rural Development, India
- Ministry of Finance, India
- Government of India
- State Governments

Annexure 2: Household Questionnaire to interview microenterprise/ micro entrepreneurs

1. **Name of the respondent:** ______________________________

2. **Religion: 1. Hindu** ☐ **2. Christian** ☐ **3. Muslim** ☐ **99. Others** ☐ **Specify:** __________

3. **Caste*: 1. SC** ☐ **2. ST** ☐ **3. OBC** ☐ **4. GC** ☐ **99. Others** ☐ **Specify:** __________

   [*SC-Scheduled Caste; ST-Scheduled Tribe; OBC-Other Backward Caste; GC-General Caste*]

4. **Economic category of the household by govt. Norm**

   1. BPL ☐ **2. APL** ☐ **3. U.Poor** ☐ **99. Others** ☐ **Specify:** __________

   [*BPL-Below Poverty Line; APL-Above Poverty line; U.Poor-Ultra poor (Antyodaya)*]

Household Details

Background of the household members:

1	2	3	4	5	6	7	8
Sl. No.	**Name of the household members#**	**Sex (*Code*)**	**Age**	**Marital status (*Code*)**	**Education/ Use 77 for literate without schooling**	**Primary Occupation***	**Income PM (Approx.)**
1	**Respondent**						
2							
3							

3: Sex	**5: Marital status**	**7: Primary Occupation:**	
Female 1	*Unmarried 1*	*Non-Farm Activity*	*1*
Male 2	*Married 2*	*Agriculture*	*2*
	Widow/widower/ separated/divorced 3	*Agri. labour*	*3*
	Others (specify) 99	*Non-agri. labour*	*4*
		Petty business	*5*
		Business (other than petty business)	*6*
		Private job	*7*
		Govt Job	*8*
		Livestock rearing	*9*
		Other (specify)	*99*

*Mark head of the household by underlining her/his name.

*Primary occupation: The occupation which gives the highest income. Always it will be one (not more than one).

Distance of the bank branch/BC outlet/ATM may be stated as under

1. 0 – 2 km **2**. 2.1 – 4 km **3**. 4.1 to 6 **4**. 6.1 and Above

Did you borrow any money in the past three years? 1. Yes, 2. No

Source of money can be mentioned here

Did you borrow any money for your micro-enterprise in the past three years? 1. Yes, 2. No

Source of money can be mentioned here

1. Access to Finance		
Do you have bank account?	Yes	1
	No	0
Name of bank, branch name and IFSC code (if available)	Name of bank	
	Name of branch	
	IFSC code	
From where do you usually withdraw your savings?	Bank Branch	1
	BC Outlet	2
	ATM	3
What is the distance of the bank branch/BC outlet/ATM from your home? (in KMs)	Bank Branch	
	BC Outlet	
	ATM	
How many weeks ago did you last withdraw money from or deposit in your bank account?		
Did you borrow any money in the past three years?	1. Yes, 0. No	
Did you borrow any money for your micro-enterprise in the past three years?	1. Yes, 0. No	
Did you take any raw materials on credit from any supplier in the past three years	1. Yes, 0. No	

2. Microenterprise Assets			
Type of fixed-assets	**Number of unit**	**Year of Purchase**	**Value in Rs '000**
Land			
Premises			
Tools			
Machinery/Equipment			
Motor vehicles			
Electrical connection/meter			
Water connection/tank			
Others (specify)			
Type of current assets	**Number of units**	**Value in Rs '000**	

2. Microenterprise Assets		
Stock – raw material 1		
Stock – raw material 2		
Stock – raw material 3		
Stock – work-in-process		
Stock – finished goods 1		
Stock – finished goods 2		
Stock – waste material		
Receivables from clients		

3. Need for Finance			
Question	**Choice**	**Code**	**Rs in 000**
What are the main purposes for which you need finance (whether you get or not)? (This is a multiple choice question; please fill NIL or amount you need in Rs 000 for each choice. For things like crop inputs which are used every year, note the amount on a per annum basis)	Meeting household consumption needs	HHCN	
	Medical expenses	MEDX	
	Educational expenses	EDUX	
	House repair	HSGR	
	Buying house/land for house	LANH	
	House extension/ building new	HSGX	
	Buying durable items	CDUR	
	Social expenditure (e.g. marriage/death)	SOCX	
	Pilgrimage	PILG	
	Migration for work	MIGW	
	Other –consumption (specify)	SOCC	
	Mixed –consumption uses above	MIXC	
	Total for Personal	TOTB	
	Buying crop inputs	CROP	
	For crop irrigation	IRRI	
	Buying fodder/feed	FEED	
	Leasing land for cultivation	LEAS	
	Buying land for crop cultivation	LAND	
	Buying livestock	LSTK	
	Buying raw material for microenterprise	RAWM	
	Giving advance to get finance or subsidy	ADVL	
	Buying land for enterprise	LANB	
	Buying tools/equipment	EQPT	
	Buying machinery	MCHY	
	Building a work shed	SHED	
	Other –short-term (specify)	OTST	
	Other –long-term (specify)	OTLT	
	Total for Business	TOTB	

4. Sources of Finance			Q 5.1	Q 5.2
Questions	**Sources**	**Code**	**LOT/FEW/NIL**	**NIL or Amt. in Rs. 000**
4.1. What are the main sources of finance in your area? (This is a multiple choice question; please indicate LOT/FEW/NIL for all the sources)	Bank – public sector	PSUB		
	Bank – regional rural	RRB		
	Bank – private sector	PVTB		
	Bank – small finance	SFB		
	Bank- cooperative	COOP		
	FIs (KVIB/ SFC/ SIDBI)	FIGO		
	NBFCs (non-MFI)	NBFC		
	NBFC-MFI	MFIC		
4.2. Which of these have you borrowed from in the last three years and how much in Rs 000? (This is a multiple choice question; please fill NIL or amount borrowed in nearest thousand rupees for all the sources)	NGO- MFI	MFIV		
	Cooperative society	SOCC		
	Chit funds (registered)	CHFR		
	Raw Material Suppliers	RMS		
	Output Buyers	OPB		
	Moneylenders (registered)	MLR		
	Moneylender unregistered	MLU		
	Big Farmer/ Trader	BFT		
	Finance "company" agents	FINC		
	Business Partners	BIZP		
	Family members	FAMY		
	Friends/ neighbours	FREN		
	SHGs – bank linked	SHGB		
	SHGs – not linked to bank	SHGU		
	Chits (unregistered)	CHFU		
	Other (specify)	OTH		
Total amount borrowed in last three years				

5. Desired Factors for Financing			
	Response	**Code**	**IMP/ABIT/NOT**
5.1. What are the factors you consider while choosing the financier?	Easy physical accessibility	1	
	Friendliness of financier	2	
	Is the financing like a partnership with profit sharing or is it a finance to be returned	3	
	Less paper work and formalities	4	
	Less processing time	5	
	Less cost of financing (other than interest)	6	
	Lower interest rate	7	
	Adequate amount of finance	8	
	No need for land title for mortgaging	9	
Rate each factor on importance : Important, ABIT & NOT important	Lesser requirement of collateral security for finance	10	
	Flexibility of end use – the financier does not ask what we used the finance for	11	
	Repayment schedule which suits your cash flow	12	
	Duration of finance suits you	13	
	Availability of subsidy	14	
	Chances of loan being waived	15	
	Any others	16	

6. Features of Actual Financing Received			
For the three largest finances taken in last three years	**Finance 1**	**Finance 2**	**Finance 3**
What was the purpose for which you took the finance (please select from codes in 4)			
Who did you take the finance from? (Please select from codes used in 5.2)			
What is the amount taken by you?			
Was it a partnership finance or a loan?			
If partnership finance, state how your partner was agreed to be compensated (sales share/ profit share/ fixed return)			
What is the annual rate of interest charged?			
What was the agreed finance duration? (in months)			
What is the amount of instalment you pay?			
What is the interval of instalment payment? W/F/M/Q/HY/Y/AS			
Did you need to give any collateral security for this finance?			
Did you have to have a guarantor for this finance?			
Did you have to join a group (SHG/JLG/other) to get this finance?			
How long did it take to get the finance after you applied for it? (in months)			
What was the processing fee? (Write “0” if none)			
What were the other charges? (write the write of charges with amount; Write “0” if none)			
Are there any other conditions/eligibility tied with the finance?			
What would happen if you delay the repayment of an instalment? (Nothing/Reminders/ Threats/other (specify))			
What would happen if you did not repay the finance at all? (Nothing/Threats/Court Case/ No further loan/Will take away other assets/other (specify))			
For the three largest finances taken in last three years	**Finance 1**	**Finance 2**	**Finance 3**
Based on your experience, please suggest the three most preferred source of financing? (Use codes in 4.1)			
Please state a reason for your preference.			
Based on your experience, please suggest the three least preferred source of financing? (Use codes in 4.1)			
Please state a reason for your preference.			
Did you depend less on informal sources of finance after banks came to your area? If yes, give details			
Did you depend less on informal sources of finance after SHGs came to your area? If yes, give details			
Did you depend less on informal sources of finance after MFIs came to your area? If yes, give details			
Have you heard of a credit bureau (use names like High Mark? Equifax and CIBIL t explain credit bureau)			

Will you support anybody who says loans taken should not be repaid?
If yes, then how do you expect to get loans in future as no one will lend?
If no, then what according to you, should be done about those who do not repay?
Will you be willing to join a financial literacy class if it is free?
Summary of any open ended comments by the respondent to be recorded here.

7. New channels of finance (e.g. Business Correspondents of banks / Business Facilitators of Banks, Peer to Peer (P2P), Digital finance					
	Response)	**BC**	**BF**	**P2P**	**Digital**
Are you aware of it?	Code (Yes=1, No =0)				
Did you get finance from it?					
What are the benefits of availing it?	Specify benefits in each source used				
What are the disadvantages of availing it?	Specify benefits in each source used				
Will you consider taking from it?	Code (Yes=1, No =0)				
If No, provide reason for not availing the credit from alternative channels?	Not sure of hidden issues HI				
	No scope for face to face negotiation NF				
	Other (specify)				
Name of survey investigator and signature with date					
Found suitable for analysis without any clarifications /corrections Yes/No					
If no then specify questions that need to be back checked					
Space for clarifications/corrections					
Name of supervisor and signature with date					

Annexure 3: Focus Group Discussion Guide

Focus Group Discussion Guide to discuss with Clients

Study on Financing Microenterprises in India

Date	Location:	No. of participants
Moderator	Assistant Moderator	Rural/Urban/Semi –Urban

Microenterprise profiling in the particular area

Major microenterprises in the area (rank them by prominence)	

Individual Profiling

Name	M/F	Age	Edu	Marital status	Religion	caste	Economic category	Primary occupation	Income per month	Loan 1		Loan -2		Loan -3	
										Source	**Amt Rs.**	**Source**	**Amt. Rs**	**Source**	**Amt. Rs**

FGD Questions

Key Questions	Enquiry	Notes
1. What are the different sources of credit for people in the community?	List down both formal and informal sources of credit available in the community, e.g. Banks, MFIs, Moneylenders, Chits, Pawnshops, SHG, input suppliers, output buyers etc.	Formal Informal
2. Major reasons for use of credit	Probe the reasons for use of credit a) Demand side (investment in business, existing loans inadequate, family obligation/basic household expenditures, repayment of other loans, seasonal expenditures, etc.) b) Supply side (easy availability of loans, influence of field staff, influence of group members/friends/community leaders)	
3. What are the factors that you considered before loan application?	Accessibility, Interest rate, processing time, collaterals requirement, loam amount, formalities, etc.	
4. Do you aware about the loan features?	Loan products, instalment size, interest rates, credit bureau check. (probe do they know that implication of non-repayment of loans) Who tells you about these features? Does this understanding help you in comparing the loans?	
5. Major pain points in accessing loans	Probe around documentation, long waiting time, conditions for not using the loan for other than the enterprise, repayment is not align with cash flows, high interest rates, need of guarantors, assets to mortgage/collateral , unethical repayment collection practices, inadequacy of loan etc.	Formal Informal
6. What are the prominent credit source you use to meet your enterprise credit requirements and why?	Probe top 3 credit sources and purpose to use the sources for e.g. establishment of enterprise, working capital Top 3 reasons why people like you use these credit sources	
7. Two years back what were the Prominent credit source you use to meet your enterprise credit requirements	Probe top 3 credit sources and purpose to use the sources for e.g. establishment of enterprise, working capital	
8. >2 -5 years back what were the Prominent credit source you use to meet your enterprise credit requirements	Probe top 3 credit sources they used (used by community) and purpose to use the sources for e.g. establishment of enterprise, working capital	
9. If there is a change in use of credit sources over a period of time?	Probe reasons for change in use of credit sources are it because of increase financial literacy, availability of credit through alternative channels etc. Is there any difference in availability of credit sources over the time? (To cater supply side of loan-market)	

Key Questions	Enquiry	Notes
10. What are the major alternative credit sources you are using to meet enterprise credit requirements	Probe around BC, BF, P2P, and Fintech companies etc. Community is aware about such alternative credit sources? If No, reasons for not using the alternative credit sources If yes, are they started using such credit sources Major suggestions to alternative credit sources to become more prominent	
11. Loan utilization Pattern	Client's response about how a member used his/her loan and it is consistent with loan size. Check if the loans are used for productive or non-productive (consumption) purpose [ask purpose of each loan such as working capital for business, purchase of asset, education, etc.] Probe if loan is used as per the stated purpose • Probe if the loan is given only business based on the project appraisal and not allowed to use for consumption purpose • if Loan Utilisation Checks (LUCs) were conducted by concerned institutions • Check the loan use pattern of client – want to use/used some portion of credit to meet household expenses. {The objective of this question is to see who exactly is the ultimate beneficiary or user of the loan}	
12. Use of loans from Moneylenders	Probe if respondents use loans from moneylenders If yes, why did they take loan from moneylenders When banks are available to give loans why they still want to take loans from moneylenders Major advantages and disadvantage of availing loans from moneylenders Suggestions from respondents on making moneylenders more customer friendly – probe around should moneylenders should be formalised/regularised, should banks use them as mediators to provide loans at reasonable interest rates, should there be any regulations to follow ethical repayment collection mechanisms etc.	
13. Respondents understanding about Mudra loans available from FIs	Probe do they know about Mudra loans If yes what are key features of Mudra Loans they know Is Mudra loan is sufficient to establish his/her enterprise? If no what is other source they take loan to establish enterprise. Did they avail Mudra loans? If No what are the major reason for not using Mudra Loans? If yes what is their experience in use of Mudra loans? What are their major recommendations to make Mudra loans to become more prominent use of credit	

Key Questions	Enquiry	Notes
	Probe around use of mediators (accredited credit counsellors) between bank and clients to understand the product details, fulfilling the documentation requirements, project appraisals etc.	
Any suggestions to Regulators/Government to ensure Micro entrepreneurs to get better information, easy access, and hassle free loans at affordable price.		

Annexure 4: Financial Literacy efforts and their Impact

Excerpts from the Report on Trend and Progress of Banking of India – Financial Inclusion: Policy and Progress – December 2016 [14]

5.1 Providing universal access to banking services and improving the forms of credit delivery, especially for the weaker sections of the population, form the basis of the Reserve Bank's financial inclusion agenda. With a view to achieving sustainable and scalable financial inclusion, multiple strategies are being used such as appropriate relaxations in guidelines, provision of new products and other supporting measures. I. Financial inclusion: policy approach and interventions The Reserve Bank has since the last decade made the following policy interventions in the area of financial inclusion. Allowing correspondent banking

5.2 The Reserve Bank permitted banks to utilise the services of intermediaries in providing banking services through the use of business facilitators and Business Correspondents (BCs). The BC model allows banks to do 'cash in-cash out' transactions at a location much closer to the rural population, thus addressing the problems of last mile reach. Providing banking services in villages with population more than 2,000

5.3 In order to provide door step banking facilities in all the unbanked villages in the country, a phase wise approach has been adopted. During Phase-I (2010-13), all unbanked villages with population more than 2,000 were identified and allotted to various banks (public sector banks, private sector banks and regional rural banks) through State Level Bankers' Committees (SLBCs) for coverage through various modes – Branch or BC or other modes such as ATMs, mobile vans, etc. During Phase-I, as reported by SLBCs, banking outlets have been opened in 74,414 unbanked villages with population more than 2,000. Such newly opened banking outlets comprised of 69,589 outlets opened through BCs and 2,332 by other modes, apart from 2,493 branches. Opening banking outlets in unbanked villages with population less than 2,000

5.4 After the completion of the first phase of the roadmap, the second phase (2013-16) to provide banking services in unbanked villages with populations less than 2000 was rolled out. About 4,90,298 unbanked villages with population less than 2000 have been identified and allotted to various banks (public sector banks, private sector banks and regional rural banks) through SLBCs across the country for coverage in a time bound manner. As on June 30, 2016, as reported by SLBCs, 4,52,151 villages have been provided banking services; 14,976 through branches, 4,16,636 through BCs and 20,539 by other modes viz. ATMs, mobile vans, etc. thereby achieving 92.2% of the target

5.5 Financial inclusion plans all domestic Scheduled Commercial Banks (SCBs) – both in the public sector and private sector – were advised to draw up board-approved Financial Inclusion Plans (FIPs) as an integral part of their business strategy based on their competitive advantage. FIPs are submitted to the Reserve Bank and are implemented over blocks of three years. These plans broadly include self-set targets with respect to: opening rural brick and mortar branches; Business Correspondents (BCs) employed; coverage of unbanked villages through branches/ BCs/ other modes, opening of Basic Savings bank deposit accounts (BSBDAs) including through BC-ICT; issuance of Kisan Credit Cards (KCC)

[14] Financial Inclusion: Policy and Progress: December 2016: https://www.rbi.org.in/scripts/PublicationsView.aspx?id=17412

and General Credit Cards (GCC) and other specific products aimed at the financially excluded segments

5.6 In April 2011, domestic SCBs were mandated to open at least 25 per cent of the total branches opened during a year, in unbanked rural (Tier-5 and Tier-6) centres. Subsequently, in 2013, banks were advised to front-load the opening of branches in unbanked rural centres over a 3-year cycle co-terminus with their FIPs for the period 2013-16. With a view to accelerating the progress in opening of bank branches in rural areas, 'credit' was given for opening more (in excess of 25 per cent in a year) branches in unbanked rural centres while allowing for the 'credit' to be carried forward to the subsequent year of the FIP. Relaxed know your customer (KYC) requirements

5.7 Recognising that the KYC requirements and related documentation may potentially become a hindrance in encouraging sections of the population in opening bank accounts, KYC for opening bank accounts was simplified to the extent possible. Consequently, small accounts could be opened with self-certification in the presence of bank officials. Further, Aadhaar, the unique identification number allotted by the Unique Identification Authority of India (UIDAI), Government of India was allowed to be used as one of the eligible documents for meeting KYC requirement for opening a bank account. In September 2013, banks were allowed to provide e-KYC services based on Aadhaar thus paving the way for bank accounts to be opened by all and facilitating easy access to banking services

Committee on medium-term path on financial inclusion

5.14 The Committee on Medium-term Path on Financial Inclusion (CMPFI) constituted by Reserve Bank of India submitted its report in December 2015. Among the various recommendations made by the committee, some of the important ones that have been implemented include:

Framework on BC Registry and BC Certification issued to Indian Banks' Association (IBA). Introduction of Movable Asset Registry. Universal crop insurance and satellite imagery for crop mapping and damage assessment as a part of the Pradhan Mantri Fasal Bima Yojana (PMFBY). Registration of mobile numbers through ATMs connected with NFS. Celebration of financial literacy week at regional offices

Some of the recommendations that are under implementation include introduction of a system of professional credit intermediaries/advisors for MSMEs, a survey for assessing the level of financial literacy and inclusion across the country, a pilot project for installing kiosks (30 interactive and 70 non-interactive) at 100 locations to encourage self-learning by people newly inducted into the financial system, impact assessment of the financial literacy camps and preparing a curriculum for training programmes for lead literacy officers by the College of Agricultural Banking (CAB), Pune. Financial Inclusion Advisory Committee (FIAC)

5.16 The Reserve Bank had set up the Financial Inclusion Advisory Committee (FIAC) in 2012 to review Financial Inclusion (FI) policies on an on-going basis and to provide expert advice on additional efforts under FI. Considering the need for convergence of the FI efforts of various stakeholders, FIAC was reconstituted in July 2015 with representation from the Government of India, SEBI, IRDA, PFRDA with renewed focus on review and monitoring of FI and financial literacy (FL) policies and progress; impact evaluation and preparing a national strategy for financial inclusion (NSFI). Roadmap for opening brick and mortar branches in villages with population more than 5,000 without a bank branch of a scheduled commercial bank

5.17 For increasing banking penetration and financial inclusion, brick and mortar branches are an integral component and hence it has been decided to focus on villages with population above 5000 without a bank branch of a scheduled commercial bank. Therefore, SLBC Convener Banks have been advised to identify villages with population above 5000 without a bank branch of a scheduled commercial bank in their State. As reported by SLBCs, 6,593 villages were identified and allotted among SCBs (including RRBs) for opening branches. The opening of brick and motar branches under this Roadmap is to be completed by March 2017. Streamlining the flow of credit to micro and small enterprises

5.18 In order to provide timely financial support to Micro and Small Enterprises (MSEs) facing financial difficulties during their life cycles, banks were advised in August 2015 to review their existing lending policies to the MSE sector. Accordingly, these policies were required to be modified by incorporating therein, among others, the provisions for sanctioning of a standby credit facility in case of term loans, additional working capital limits, a midterm review of regular working capital limits and timelines for credit decisions. Framework for the revival and rehabilitation of micro, small and medium enterprises

5.19 To provide a simpler and faster mechanism to address stress in the accounts of Micro, Small and Medium Enterprises (MSMEs), in March 2016, a 'Framework for Revival and Rehabilitation of Micro, Small and Medium Enterprises' was issued to banks, in consultation with Government of India. Under this framework, the revival and rehabilitation of MSME units having loan limits up to ₹250 million would be undertaken

National Mission for Capacity Building of bankers for financing the MSME sector

5.20 With a view to develop entrepreneurial sensitivity amongst banks' field-level functionaries for lending to the MSME sector, in August 2015, the Reserve Bank rolled out a capacity building programme named as 'National Mission for Capacity Building of Bankers for Financing the MSME Sector' (NAMCABS) in collaboration with CAB, Pune, which involves: (i) Training programme for MSME division in charges of commercial banks. (ii) Training the trainers of commercial bank owned training colleges. (iii) Capacity building for in-charges of specialised branches for MSMEs

Financial literacy initiatives

5.21 In India, financial literacy has been regarded as a process that provides demand side support for financial inclusion. To assess the extant level of financial literacy and inclusion, a pan-India survey is being conducted by the Reserve Bank. Target-specific content for five target groups' viz. farmers, small entrepreneurs, self-help groups (SHGs), school students and senior citizens is also being designed for tailored financial literacy programmes conducted by Financial Literacy Centres (FLCs). A pilot project for setting up 100 Centres for Financial Literacy (CFL) at the block level to scale up the existing FLC infrastructure has been initiated. Functioning of financial literacy centres (FLCs)

5.22 Guidelines for banks' financial literacy centres and the operational guidelines for conducting camps by FLCs and rural bank branches were revised in January 2016. Banks have been advised to put in place board approved policies for stronger FLC architecture in terms of providing basic infrastructure to FLCs as well as appointing FLC counsellors. As on

March 2016, 1,384 FLCs were operational. During 2015-16, 87,710 financial literacy activities (outdoor camps) were conducted by FLCs. Pilot project on setting up Centres for Financial Literacy (CFLs)

5.23 Given the challenges of skewed distribution of existing FLCs in a few states, limited outreach and to have an exclusive focus on financial literacy at the ground level, the Reserve Bank is encouraging banks to set up CFLs at the block level on a pilot basis in a few states. The key elements of this block level CFL project are: a) Area based approach (block) b) Schedule of camps c) Skilled workforce d) Partnerships with NGOs e) Use of technology f) Common name and logo 'Moneywise Centre for Financial Literacy'

5.24 The pilot project to set up 100 CFLs across 10 states with support from the Financial Inclusion Fund has been initiated. Possibilities of partnerships with eligible NGOs/institutions are being explored to bring in innovative and more efficient approaches/ methods for conducting financial literacy activities

Technical group on financial inclusion and financial literacy

5.25 A Technical Group on Financial Inclusion and Financial Literacy of the FSDC sub-committee was set up to co-ordinate the efforts on financial inclusion and literacy at the policy level. The group is chaired by the Deputy Governor, Reserve Bank of India and has representatives from all regulators and the Finance Ministry. A National Centre for Financial Education (NCFE), comprising representatives from all financial sector regulators has been set up to implement the National Strategy on Financial Education (NSFE). NCFE's main role is to create material on financial education and conducting financial education campaigns across the country. Some of the initiatives undertaken under the aegis of the Technical Group are: Kiosk project

5.26 About 100 kiosks (30 interactive kiosks and 70 non-interactive LFDs) are being set up in five states on a pilot basis in public places like banks, post offices, collector's offices and primary health centres to promote financial awareness. The kiosks will display messages in different languages controlled from a central location. Financial education in school curriculum

5.27 In collaboration with CBSE, NCFE has prepared financial education workbooks for classes VI to X; these are in the process of getting CBSE's final approval. Meanwhile, NCFE and the Reserve Bank are pursuing with state education boards for the adoption of the financial education workbooks in the school curriculum in their jurisdictions by appropriately integrating them with different subjects. Four state governments viz. Goa, Meghalaya, Jammu and Kashmir and Mizoram have agreed in principle to include financial education topics in state board school curricula. Talks with other state governments are at different stages. III. The way forward improving financial literacy levels.

Going forward, Reserve Bank envisages further steps for improving the financial literacy levels which include, among others, designing and implementing capacity building programmes for FLC counsellors and bank branch heads in rural areas and conducting surveys for obtaining insights on financial knowledge, attitudes and behaviour of the people.

Submitted by

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