

Micro lenders face collapse as RBI steps in

INDIA MAY have to step in to avert collapse of the \$6.7-billion microfinance industry, a leading ratings body warned on Friday, as lenders once hailed as saviours of the poor faced a major crisis. The Microfinance Institutions Network or MFIN, which represents 44 leading Indian microfinance lenders, has said commercial bank loans to the sector are drying up and borrowers are reneging on their debts.

Pioneered on the sub-continent by Nobel prize winner Muhammad Yunus of Bangladesh, microfinance was conceived to free the poor from the clutches of greedy moneylenders by giving them small, cheaper loans, but has been hit by sharp criticism from politicians and scrutiny of its loan recovery methods.

Before the crisis, the sector boasted repayment rate of 99%

"It could come to a systemic banking crisis — that is why I feel the central government won't let it go that far, it will have to take action," said Sanjay Sinha, managing director of M-CRIL or Micro-Credit Ratings International Ltd, a New Delhi-based leader in rating the sector.

The financial numbers involved are too great, he said. The warning came as the Reserve Bank of India (RBI) announced a committee to examine the debt recovery methods of microfinance institutions and their interest rate charges.

The head of MFIN, Vijay Mahajan, warned the industry could face collapse and was not at all out of the woods. The commercial bankers and everyone else are hoping against hope that things will improve, said Mahajan, a pioneer of lending to the poor who also heads a top microfinance institution, BASIX.

The sector was thrown into turmoil when the government of Andhra Pradesh, the hub of small loan activity, cracked down on microfinanciers. The state government said on Thursday it was investigating 56 suicides blamed by local politicians on aggressive debt collectors and high interest rates of up to 36 per cent.

After news of the suicides surfaced in mid-October, India's leading microlender SKS said 17 were among its borrowers, but rejected responsibility, saying our ethical way of doing microfinance has not caused these tragedies.

SKS staged a share offer in August which focused the spotlight on the millions of dollars being made in the sector by microfinance firms. The Andhra government introduced a measure earlier this month aimed at halting harassment of borrowers, imposing penalties of up to three years in jail and ₹1,00,000 (\$2,000) in fines for attempting to coerce borrowers.

The state also ordered the suspension of debt collections. The

order was later overturned by a court but industry officials said debt recovery agents were still being blocked. Andhra Pradesh's share of outstanding microfinance loans accounts for around 35 per cent of the sector's total \$6.7-billion portfolio. Before the crisis, the sector boasted loan repayment rates of 99 per cent.

Critics of the for-profit microfinanciers say borrowers should go to state-sponsored self-help groups which offer subsidised loans for as low as three per cent.

Finance minister Pranab Mukherjee said this week the government was in talks with the state to ease the situation in Andhra Pradesh for microlenders but also urged the industry to develop a code of conduct to help curb interest rates and prevent the use of coercive recovery methods.

AFP



SORRY STATE OF AFFAIRS: Andhra Pradesh's share of outstanding microfinance loans accounts for around 35% of the sector's total portfolio of \$6.7 billion.

THE MAKING OF A BUBBLE

Pioneered in the sub-continent by Nobel prize winner Muhammad Yunus of Bangladesh, microfinance was conceived to free the poor from the greedy moneylenders by providing cheap loans

PROBLEMS

- The sector has been hit by sharp criticism from politicians and scrutiny of its loan recovery methods
- Andhra Pradesh, the hub of small loan activity, cracked down on microfinanciers while investigating 56 suicides
- Local politicians blamed it on aggressive debt collectors and their high interest rates of up to 36%

SOLUTIONS

- Andhra govt introduced a measure aimed at halting harassment of borrowers and imposing penalties
- Critics say borrowers should go to state-sponsored self-help groups, which offer subsidised loans for 3%
- FM Pranab Mukherjee urged the industry to develop a code to help curb interest rates and prevent coercive recovery methods