THE POVERTY EFFECTS OF MICROFINANCE UNDER SELF-HELP GROUP BANK LINKAGE PROGRAMME MODEL IN INDIA

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IIM INDORE

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ATUL MEHTA

A THESIS
SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE
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ABSTRACT

Financial sector development (FSD) affects the poor. The relationship between FSD and the poor has received much attention from academics, practitioners, and policymakers in recent times The existing literature on the finance-poor nexus discusses the indirect effect of financial development on the poor through economic growth channel and its direct effect through access to finance channel. Economic growth benefits the poor by creation of more jobs, reduction in wage differentials between skilled and unskilled workers at a certain phase of development, increased tax revenues which result in higher social spending which allows poor to invest in human capital and increased capital accumulation that facilitates availability of more funds for investment for the poor.

Similarly, poor people's access to financial services strengthens their asset base and improves their productivity. However, access to formal financial services by the poor in developing countries is very limited forcing them to use informal sources of finance which are expensive as well as risky. Information asymmetry and high fixed costs of borrowing act as the key barriers to poor people's access to formal finance. Their inability to actively participate in formal financial market prevents them from increasing their income and consumption levels and contribute to the growth process.

The present study proposes that formal financial services by banks are primarily availed by non-poor and urban population and hence acts as a medium-direct channel to affect the poor whereas the semi-formal finance, i.e., microcredit, by microfinance institutions specifically target the poor and act as a direct channel. It examines the effect of direct (microcredit), medium-direct (bank credit) and indirect (through economic growth) channel of FSD on poor in rural India using state-wise annual data from 1999-00 to 2011-12. We conduct a panel data analysis for a sample of 15 major Indian states and provide an empirical evidence for the effect of FSD on rural-urban consumption ratio, rural poverty, rural income inequality, and rural poverty gap index in India. It is the first ever study to use state-wise data on microcredit disbursed under Self-help Group Bank Linkage Programme to assess the direct impact of FSD on poor. The study finds that finance is pro-urban in nature with microcredit being partially effective in benefitting the poor. The poorest of the poor seem to be at the greatest disadvantage. The robustness of the estimated results is checked for by using the log transformation of the dependent variables.

Keywords: Financial sector development; Poverty; Inequality; Bank credit; Microcredit; Economic growth

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