Microfinance and Financial Inclusion in Karnataka: Emerging Role, Issues and Challenges

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Abstract:
Microfinance has emerged as an important instrument for extending financial services to economically weaker sections and promoting financial inclusion in India. Karnataka has played a pioneering role in the development of the Self Help Group–Bank Linkage Programme (SHG-BLP), particularly through the early NABARD–MYRADA initiatives. The present study examines the emerging role of microfinance in promoting financial inclusion in Karnataka, with particular emphasis on the status of the sector as on 31 March 2018. The study is based exclusively on secondary data collected from NABARD reports, Reserve Bank of India publications, Government reports and other relevant sources. The analysis indicates that Karnataka remained one of the leading states in India in terms of SHG credit linkage. As on 31 March 2018, about 10.75 lakh SHGs in Karnataka had savings bank accounts with various banks, while 7.44 lakh SHGs had outstanding bank loans amounting to approximately ₹11,126 crore. At the national level, 87.44 lakh SHGs had savings linkage and 50.20 lakh SHGs had outstanding bank loans of ₹75,598 crore. The study finds that microfinance has contributed not only to access to formal credit but also to savings mobilisation, women's empowerment, livelihood promotion and social inclusion. However, inadequate financial literacy, uneven credit linkage, inadequate institutional support, multiple borrowing, weak group quality, non-performing assets and limited opportunities for enterprise development continue to constrain the effectiveness of microfinance. The study concludes that strengthening SHGs, improving financial literacy, expanding digital financial services, enhancing enterprise-oriented credit and improving coordination among banks, government agencies, NGOs and SHG-promoting institutions are essential for achieving sustainable financial inclusion in Karnataka.

Keywords: financial inclusion, Karnataka, microfinance, self-help groups, SHG-Bank Linkage Programme.

I. INTRODUCTION

Financial inclusion refers broadly to ensuring access to appropriate and affordable financial services for individuals and households that are excluded or inadequately served by the formal financial system. Access to savings, credit, insurance, remittance and payment facilities enables economically weaker households to manage financial risks, invest in productive activities and improve their standard of living. In developing economies such as India, financial exclusion has historically been associated with poverty, inadequate banking infrastructure, low financial literacy and the absence of conventional collateral.

Microfinance emerged as an important institutional response to these constraints. It seeks to provide small-scale financial services to low-income households, particularly women and rural communities, who may find it difficult to obtain conventional bank credit. In India, the Self Help Group–Bank Linkage Programme pioneered by the National Bank for Agriculture and Rural Development (NABARD) became one of the principal mechanisms through which microfinance was integrated with the formal banking system.

The SHG-BLP began as a pilot programme in 1992 and subsequently expanded across the country. NABARD describes the programme as having evolved from a simple bank outreach mechanism into a broader instrument for financial, economic and social inclusion. Karnataka occupies a particularly important position in this development. The State was associated with the early NABARD–MYRADA experiment in SHG–Bank linkage and subsequently became one of the leading states in the country in terms of credit linkage. The programme has helped connect poor households, especially rural women, with formal financial institutions. The importance of microfinance should therefore not be understood merely in terms of the amount of loans disbursed. Its broader significance lies in creating a bridge between excluded households and formal financial institutions. SHGs encourage regular savings, internal lending, collective decision-making and financial discipline while enabling members to access bank credit. As on 31 March 2018, the scale of the SHG-BLP was considerable. At the all-India level, 87.44 lakh SHGs had savings linkage with banks, while 50.20 lakh SHGs had outstanding bank loans amounting to ₹75,598 crore. SHGs had savings of ₹19,592 crore with banks. During 2017–18, banks disbursed ₹47,186 crore to 22.61 lakh SHGs. Against this national background, Karnataka's performance deserves particular examination. The State had 10.75 lakh SHGs with savings bank accounts and 7.44 lakh SHGs with outstanding bank loans amounting to ₹11,126 crore as on 31 March 2018.

II. REVIEW OF LITERATURE

Harper (2002) discusses the significance of SHGs and microfinance as mechanisms for providing financial services to poor households. The collective nature of SHGs reduces transaction costs and substitutes social collateral for conventional physical collateral.

Kabeer (2005) links access to financial resources with women's empowerment, arguing that financial services can contribute to women's ability to participate in household and economic decision-making.

Karmakar (2008) highlights microfinance as an important component of rural development and poverty alleviation, while emphasising that credit must be accompanied by appropriate institutional and developmental support.

NABARD's *Status of Microfinance in India 2017–18* demonstrates the substantial growth of the SHG-BLP. During 2017–18, SHGs received ₹47,186 crore in bank loans, while the outstanding loan portfolio reached ₹75,598 crore by March 2018.

III. OBJECTIVES OF THE STUDY

1. To examine the concept and importance of microfinance in promoting financial inclusion.
2. To analyse the growth of the SHG-Bank Linkage Programme in India.
3. To examine the status of microfinance and SHG-BLP in Karnataka as on 31 March 2018.
4. To identify the major issues and challenges faced by microfinance institutions and SHGs in Karnataka.

IV. RESEARCH METHODOLOGY

The study is descriptive and analytical in nature and is based entirely on secondary data.The major sources include: NABARD, Status of Microfinance in India 2017–18. NABARD StateFocus/Potential Linked Credit Plan documents for Karnataka, Reserve Bank of India annual reports and publications, Government of India reports and Relevant books, research papers and journal articles relating to microfinance and financial inclusion.

V. RESULTS AND DISCUSSION

1. STATUS OF MICROFINANCE IN INDIA AS ON 31 MARCH 2018

Table 1: Progress of SHG-BLP in India

Particulars	2016–17	2017–18
SHGs with savings linkage (lakh)	85.77	87.44
Savings with banks (₹ crore)	16,114	19,592
SHGs receiving loans during year (lakh)	18.98	22.61
Loans disbursed during year (₹ crore)	38,781	47,186
SHGs with loan outstanding (lakh)	48.48	50.20
Loan outstanding (₹ crore)	61,581	75,598
Gross NPAs (₹ crore)	4,002	4,628
Gross NPAs (%)	6.50	6.12

(**Source:** NABARD, *Status of Microfinance in India 2017–18*.)

The table indicates substantial expansion during 2017–18. Savings-linked SHGs increased from 85.77 lakh to 87.44 lakh, while savings with banks increased from ₹16,114 crore to ₹19,592 crore. More importantly, the number of SHGs receiving bank loans during the year increased from 18.98 lakh to 22.61 lakh. Bank credit disbursement increased from ₹38,781 crore to ₹47,186 crore. This represents an increase of approximately 21.67 per cent. Loan outstanding increased by approximately 22.76 per cent, from ₹61,581 crore to ₹75,598 crore.

2. POSITION OF MICROFINANCE IN KARNATAKA

Karnataka has been one of the pioneering states in the Indian microfinance movement. The State was closely associated with the NABARD–MYRADA pilot initiative that contributed to the development of the SHG-Bank Linkage model. As on 31 March 2018, 10.75 lakh SHGs had savings bank accounts with various banks in Karnataka. Of these, approximately 7.44 lakh SHGs had outstanding bank loans amounting to ₹11,126 crore.

Table 2: SHG-BLP in Karnataka as on 31 March 2018

Indicator	Karnataka
SHGs having savings bank accounts	10.75 lakh
SHGs with outstanding bank loans	7.44 lakh
Loan outstanding against SHGs	₹11,126 crore
Position in India	Among leading states in credit linkage

(**Source:** NABARD)

The figures demonstrate the considerable scale of microfinance in Karnataka. The ratio of credit-linked SHGs to savings-linked SHGs was approximately **69.2 per cent**. This also indicates that although a large proportion of SHGs had access to savings accounts, not every savings-linked group had outstanding bank credit.

3. KARNATAKA'S CONTRIBUTION TO FINANCIAL INCLUSION

Savings mobilisation: SHGs encourage members to save regularly, even when individual savings are small. These savings provide an internal financial resource and also create a relationship between the group and formal financial institutions. The large number of savings-linked SHGs in Karnataka demonstrates the importance of collective savings as an entry point into the formal financial system.

Access to institutional credit: Traditional banking systems often require collateral, documentation and a formal credit history. Poor households may not possess these characteristics. The SHG mechanism provides an alternative based on group-based financial discipline and social collateral. The ₹11,126 crore outstanding bank credit against 7.44 lakh SHGs in Karnataka illustrates the substantial role played by banks in extending credit to economically weaker sections.

Women's financial participation: Women constitute a major proportion of SHG members. Consequently, microfinance creates opportunities for women to participate in savings, borrowing and collective financial decisions. The SHG model may also contribute indirectly to women's confidence, mobility, decision-making and participation in income-generating activities.

Livelihood promotion: Microfinance can support activities such as dairy, agriculture-related enterprises, petty trade, handicrafts, food processing, tailoring, livestock rearing and other small businesses. However, the mere availability of credit does not automatically generate sustainable livelihoods. Credit must be supported by skills, technology, market access and business development services.

Social inclusion: The SHG model creates a community-based institutional structure in which members meet regularly, maintain records and collectively address financial and social issues. Thus, the contribution of microfinance extends beyond financial transactions to social capital formation.

4. EMERGING ROLE OF MICROFINANCE IN KARNATAKA

4.1 Microfinance as a tool of poverty reduction: Access to small loans enables poor households to undertake productive activities and smooth consumption during periods of financial stress. SHG credit can reduce dependence on informal moneylenders, although the extent of this benefit depends upon the cost, adequacy and timeliness of formal credit.

4.2 Promotion of entrepreneurship: A major future role of microfinance is to facilitate the graduation of mature SHGs from small-scale borrowing to micro-enterprise development. The challenge is to move beyond repeated small loans for consumption and low-return activities towards investments that generate sustainable income.

4.3 Empowerment of women: Women-centred SHGs have the potential to improve financial independence and participation in household decision-making. Collective savings and credit also provide women with an institutional identity.

4.4 Strengthening formal banking linkages: Microfinance acts as a bridge between informal community institutions and formal banking institutions. SHGs that maintain savings and repayment records can gradually develop a financial history that supports larger credit requirements.

5. MAJOR ISSUES AND CHALLENGES

5.1 Gap between savings linkage and credit linkage: The existence of 10.75 lakh savings-linked SHGs compared with 7.44 lakh SHGs having outstanding bank loans indicates a significant credit-linkage gap. This may arise from inactive groups, inadequate group grading, documentation problems, weak repayment records or inadequate bank-level follow-up.

5.2 Quality and sustainability of SHGs : The numerical growth of SHGs does not necessarily guarantee quality. Some groups may become inactive after initial formation. Regular meetings, savings, bookkeeping, internal lending and repayment discipline are essential for sustainability. NABARD's Karnataka planning documents specifically identify the need to focus on the quality and sustainability of SHGs, including regular grading and capacity building.

5.3 Financial literacy: Limited financial literacy can affect members' ability to understand interest rates, repayment schedules, savings products, insurance and digital financial services. The RBI has recognised financial literacy as an important component of financial inclusion and has supported financial literacy initiatives aimed at vulnerable groups.

5.4 Non-performing assets: Asset quality remains a concern. At the national level, SHG-BLP gross NPAs stood at ₹4,628 crore, equivalent to 6.12 per cent of outstanding loans, as on 31 March 2018. Although Karnataka has historically performed relatively well compared with several other regions, repayment discipline remains essential for sustainable expansion.

5.5 Multiple borrowing: Multiple borrowing can arise when SHG members obtain loans from different institutions without adequate coordination. It can increase repayment pressure and create indebtedness.

5.6 Limited enterprise development: Many SHGs continue to depend on relatively small and low-return activities. Without appropriate market linkage, technology and skill development, increased credit may not necessarily result in increased income.

5.7 Inadequate handholding support: SHGs require continuing institutional support after formation. NGOs, SHG-promoting institutions, banks and government agencies must provide training in bookkeeping, financial management, enterprise development and marketing.

5.8 Inadequate bank-level monitoring: Regular monitoring and effective communication between banks and SHGs are necessary for timely credit renewal and appropriate assessment of credit requirements.

5.9 Dependence on government programmes: Excessive dependence on subsidies, interest incentives or loan waivers can weaken repayment discipline if not carefully designed. Microfinance programmes should encourage financial responsibility and long-term institutional sustainability.

VII. FINDINGS OF THE STUDY

1. Microfinance has become an important mechanism for expanding financial inclusion among rural and economically weaker households.
2. The SHG-BLP has achieved substantial scale in India, with 87.44 lakh savings-linked SHGs and 50.20 lakh SHGs having outstanding bank loans as on 31 March 2018.
3. Bank credit disbursement to SHGs during 2017–18 amounted to ₹47,186 crore, indicating strong institutional support for the programme.
4. Karnataka remained one of the leading states in SHG credit linkage.
5. As on 31 March 2018, 10.75 lakh SHGs in Karnataka had savings bank accounts, while 7.44 lakh SHGs had outstanding bank loans of ₹11,126 crore.
6. The difference between savings-linked and credit-linked SHGs indicates scope for further expansion of institutional credit.
7. Microfinance contributes to financial inclusion through savings mobilisation, institutional credit, women's participation, livelihood promotion and social capital formation.
8. The principal challenges include weak SHG quality, inadequate financial literacy, credit-linkage gaps, multiple borrowing, NPAs, inadequate handholding and limited market-oriented enterprise development.

VIII. CONCLUSION

Microfinance has emerged as an important pillar of financial inclusion in Karnataka. The SHG-Bank Linkage Programme has created a significant institutional connection between low-income households and the formal banking system. Karnataka's early association with the SHG movement and its substantial scale of savings and credit linkage demonstrate the State's important position in India's microfinance landscape. The position as on 31 March 2018 indicates that 10.75 lakh SHGs in Karnataka had savings bank accounts and 7.44 lakh SHGs had outstanding bank loans amounting to ₹11,126 crore. These figures demonstrate that microfinance had moved beyond a small experimental programme and had become an important mechanism for financial inclusion. Nevertheless, access to credit alone cannot ensure sustainable development. The next stage of microfinance should focus on the quality and sustainability of SHGs, financial literacy, enterprise development, digital financial services, market linkages and responsible lending. The experience of Karnataka demonstrates that microfinance can serve as a powerful bridge between financially excluded households and formal financial institutions. For the benefits to be sustainable, however, microfinance must move from a credit-centred approach towards a broader financial-inclusion and livelihood-development approach. Stronger SHGs, better bank linkages, improved financial literacy and effective institutional coordination can enable microfinance to make a greater contribution to inclusive economic development in Karnataka.

IX. LIMITATIONS OF THE STUDY

The study is based on secondary data and therefore depends on the accuracy and coverage of published sources. The analysis is restricted to information available with reference to 31 March 2018 and does not incorporate subsequent developments. The study primarily focuses on the SHG-Bank Linkage Programme and therefore does not provide a detailed institution-wise analysis of all Microfinance Institutions (MFIs) operating in Karnataka. Further, the study does not use primary survey data to assess the perceptions of individual SHG members.

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