How New Regulations of Micro Finance Sector Transform the Old Ones and Its Impact

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Abstract

Old and new regulations in the microfinance industry in India are compared in this paper. For providing financial services to small businesses and low-income individuals, the microfinance sector plays a significant role. Over time, for ensuring consumer protection and addressing the emerging challenges appropriately the regulatory framework governing the microfinance industry has evolved. Including broader applicability for various regulated entities, introducing new regulations has brought about significant changes. The aim of conducting this research is to analyze the transformations in regulations along with their impact on the microfinance industry. The paper initiated an introduction to the microfinance industry and its importance in India. The requirements for the regulatory reforms are highlighted within the problem statement section, while the study objectives are outlined clearly in the research purpose section. The significance of understanding the regulatory change's impact on industry functioning is emphasized within the relevance and significance section. To guide the study effectively there are three research questions well formulated in this paper. The barriers and issues associated with the old regulations are discussed during the study and for providing a comprehensive understanding of the subject, the literature review is conducted. The approach used for the collection and analysis of data is clearly outlined within the methodology section. The empirical data is provided within the research findings, analysis, and results section. The valuable insights into the impact of new regulations are provided clearly within this section. The key findings and recommendations for policymakers are summarized in the conclusion section.

Keywords: Microfinance, Consumer Protection, Old regulations, New regulations, financial services

1. Introduction

The microfinance industry in India has become a critical component of the country's financial ecosystem and has witnessed substantial growth in the market. As a vital sector, the microfinance industry in India has emerged for providing financial services to small-scale and underprivileged entrepreneurs (Al-Azzam et al., 2022). The microfinance industry aims to empower individuals and address the financial inclusion challenges for enhancing economic circumstances through providing savings accounts, small loans, and other financial services. As the microfinance industry grew, so that for ensuring fair practices, maintaining the sector stability, and securing consumer interests the requirement for a regulatory framework has arisen. Over the years there are huge transformations made by the regulatory environment governing microfinance in India. In 2012, the microfinance institutions bill is introduced along with subsequent amendments (Al-Azzam et al., 2022). To assess the impact on sector functioning the old and new regulations in the microfinance industry in India are compared in this paper.

The transformations in regulations are well analyzed, and the financial sustainability of the microfinance industry and the interest rate regulations are also well analyzed (Bajde et al., 2022). In the year 1970, the India microfinance journey has been initiated when various self-help groups and non-governmental organizations recognize the microcredit potential in facilitating poverty reduction. For microfinance, the foundation for a more structured approach has been laid from these grassroots initiatives. The regulations are put in place for ensuring the stability and efficient functioning of this sector. However, in addressing emerging challenges the old regulations become outdated (Bajde et al., 2022). To shed light on improvements and the transformations that are introduced by new guidelines the old and new regulations in the microfinance industry are compared in this paper. The impact on industry practices is assessed by understanding the evolution of regulations.

1.1 Problem Statement

For providing financial services to enable the poverty alleviation and low-income segment, the microfinance industry plays an essential role. Due to the outdated regulations, various challenges are recognized in the microfinance industry which fails in addressing the microfinance operations dynamic nature appropriately (Behl & Singh, 2014). The lack of clarity in defining microfinance loans, the limited regulation applicability, the issues related to loan pricing, and the subjective assessment of household income are identified as a few of the challenges with old regulations. To reach the evolving requirements of the target market the microfinance industry growth in India has been hindered by these challenges. The aim of conducting this study is to address these problems by comparing both the old regulations with the new regulations. Identifying the barriers that are associated with old regulations and examining the effectiveness of the new guidelines in overcoming these challenges helps in addressing these challenges effectively (Behl & Singh, 2014). There is a pressing need for regulatory reforms for addressing the old regulation limitations and this ensures in enabling the microfinance industry to operate more efficiently.

1.2 Purpose of Research

The purpose of conducting this study is to provide a comprehensive understanding of the transformations that are made by new regulations in the microfinance industry along with providing its impact (Iqbal et al., 2019). How the revised regulations influenced the credit evaluation criteria, loan disbursement process, and the methods of risk assessment are analyzed efficiently by comparing the old and new guidelines. The study aims to evaluate the regulatory change's impact on microfinance institutions leading practices along with comparing old and new regulations. The impact on interest rates charged on microfinance loans will be explored by examining the pricing policy framework which is introduced by the new regulations. The research also aims to recognize the regulatory changes significance which is introduced by new guidelines in the microfinance sector (Iqbal et al., 2019). By achieving these research objectives, the values of the effectiveness of the new regulations in the microfinance industry are provided in this study.

1.3 Research Questions

1). How the leading practices of microfinance institutions are impacted by the new regulations?

2). How the innovation and technology adoption in the microfinance industry facilitated by the new regulations?

3). What type of challenges will be faced by the microfinance sector in the light of new regulations?

1.4 Barriers and Issues

The transition from old to new regulations in the microfinance industry is not exempt from the potential hurdles and in a few cases, there is a possibility to arise few barriers and issues. Microfinance and other regulated entities require to invest in systems and for ensuring compliance, there is a necessity to provide staff training (Radhakrishnan, 2015). For smaller institutions with limited resources, these additional costs may pose challenges. To reach the new regulatory requirements the regulated entities require to enhance both their capabilities and capacity. This might involve implementing robust monitoring, developing policies and procedures, and needs to involve in training staff. There is a requirement of both time and resources for building this capacity. With any regulatory transformations, there is a necessity for the interpretation of specific provisions in the new regulations. Confusion and challenges in implementation might be created if inconsistencies in guidelines are identified. For ensuring successful implementation there is a necessity to ensure new regulations enforcement and ensure effective monitoring (Singh & Kapoor, 2019). While supervising the diverse range of regulated entities there is a possibility to face challenges by the regulatory bodies. For addressing these challenges there is a necessity to provide adequate resources and coordination among the regulatory authorities.

2. Literature Review

To provide financial services for the economically disadvantaged and underserved populations microfinance institutions play an essential role. For exploring several microfinance aspects extensive research has been conducted over the years and this includes the social performance measurement, management information systems, and the impact of external factors such as sustainability and COVID-19 (Zamore et al., 2019). The main aim of conducting the literature review is to generate valuable insights into the major key findings and contributions of selected articles in the microfinance field. According to Behi and Singh(2014), for enhancing the performance of MFIs the significance of efficient MIS requires to be emphasized. During this study, a critical analysis has been conducted on the management information systems of selected Indian MFIs. While adopting the MIS and highlighting the requirement for tailored information systems to suit unique microfinance operations requirements there are various challenges are raised (Behl & Singh, 2014). So for enhancing the overall effectiveness of MFIs, it is required to enable well-designed MIS.

Based on the viewpoints of Bibi et al. (2018), the impact on social well-being and poverty reduction is evaluated by focusing more on measuring the MFI's social performance and presenting new approaches. During the study, the traditional financial indicator which integrates social outcomes is highlighted effectively (Bibi et al., 2018). The study contributes to the ongoing debate on evaluating the microfinance intervention's social impact and generates valuable insights for both policymakers and practitioners. Whereas on the other side, Chakravarty and Pylypiv (2015), investigated the legal status of MFIs on the loan repayment rates. During this study, the author examined both the organizational status and subsidization role on the microfinance borrower repayment rates (Chakravarty & Pylypiv, 2015). Based on the findings it is noticed that on repayment rates the subsidies have a positive effect and based on the subsidy type the impact will be varied.

According to the perception of Czura et al. (2022), by considering the factors such as default rates, loan approval rates, and loan size the changes in loan officer behavior and performance during the pandemic are investigated. During the study, the author identified that while approving loans the loan officers became more cautious which lead to a decrease in loan approval rates (Czura et al., 2022). However, for mitigating the risks associated with uncertain economic conditions the loan officers tended to grand smaller loans. During the crisis, the research provides valuable insights into the challenges faced by the MFIs. To unforeseen circumstances, the recommendations are offered for adapting microfinance operations.

Based on the standpoints of Garcia-Perez et al. (2017), due to the academic interest in the research subject microfinance has grown exponentially since early microcredit programs up to the present (García-Pérez et al., 2017). The aim of conducting the study is present a comprehensive microfinance literature survey from the sustainability level perspective. During the study, the major key dimensions are identified and a wide range of studies are reviewed related to microfinance sustainability. Based on three sustainability levels such as social, financial, and economic the literature is categorized during the study (García-Pérez et al., 2017). While achieving social and economic objectives the long-term viability of MFIs is considered by highlighting the requirement for a balanced approach.

According to the viewpoints of Gutierrez-Nieto and Serrano-Cinca (2019), although with ups and downs, microfinance has moved from a promise to a reality in the last 20 years (Gutiérrez-Nieto & Serrano-Cinca). For performing the scientometric analysis of the microfinance field there are nearly 1874 papers published from 1997 to 2017 have been reviewed in this paper. The evolution of research themes that are employed in microfinance studies has been analyzed during this study. Along with highlighting the significance of information management in addressing these gaps, the major key research gaps are identified (Gutiérrez-Nieto & Serrano-Cinca). For enhancing the microfinance operations sustainability the role of information systems is emphasized in this study.

3. Approach/ Methodology

Qualitative Research Methodology is selected for performing a study on the topic of comparisons of Old and New regulations in the Microfinance sector. This methodology is more suitable which mainly aims to acquire a detailed understanding regarding the experiences and perspectives through the collection of the data from participants (Gietzen, 2017). In this methodology, interviews are conducted with randomly selected participants. Mainly experienced candidates related to the topic are selected for gathering information related to the topic. All the gathered data is recorded and also that data is undergone the analysis process for ensuring the accuracy of the information collected (Gietzen, 2017). Through this Qualitative research, all the valuable insights are acquired into the complex procedures, and also the implications that are present due to the introduction of new regulations in the microfinance sector are known.

Qualitative research mainly enables an exploration of the diverse perspectives of different stakeholders including all the regulators, policymakers, experts in the industry, affected groups, or individuals (Godfroid et al., 2022). Through conducting interviews and surveys all the rich data is obtained regarding how various stakeholders have awareness regarding new regulations and also how they view the old regulations transformation. The implications that can be there due to the transformation of the old regulations to new regulations are also clearly experienced. Through the application of this methodology, in-depth explorations can be made (Godfroid et al., 2022). The consequences that can be there either negative or positive due to the transformation of old regulations to new regulations are known.

The selected methodology is well suitable for the research topic why because this mainly assists in getting the real-time experiences of the participants. The impacts are there due to the transformation of old regulations into new regulations (Goodell et al., 2020). By the application of certain techniques namely case-study or interviews, there will be an in-depth understanding of how these regulations have impacted the microfinance sector. Through performing this study it is well known that the adoption of the new regulations in the microfinance sector, there are positive impacts (Goodell et al., 2020). The advantages that are thereby introducing the new regulations are also clearly addressed through the Qualitative Methodology.

Under the illustrative process of research, certain interview questions are framed. For all the interview questions that are framed, the participants will be providing the necessary answers.

Through this methodology, the benefits that are gained from the new regulations are addressed. The data which is collected from the participants can be stored and also can be utilized for further research (Godfroid et al., 2022). All the data that is given by the participants are based upon their personal experiences. This data is also ensured with data integrity. All the data that is provided by the participants is kept highly confidential.

4. Research Findings

The main findings from this research are that compared to the old regulations of the micro-finance sector new regulations have increased the concentration towards consumer protection (Iqbal et al., 2019). Certain provisions are present in the new regulations which mainly aim to protect microfinance borrowers' interests making sure that there are fair practices, and there is transparency maintained in the terms and conditions disclosure. From this research study, it is also clearly understood that the new regulations include certain measures present for the mitigation of over-indebtedness. The research addresses that there are positive implications for these consumer protection measures (Iqbal et al., 2019). These implications are mainly for the well-being of the clients of microfinance and also ensure financial stability.

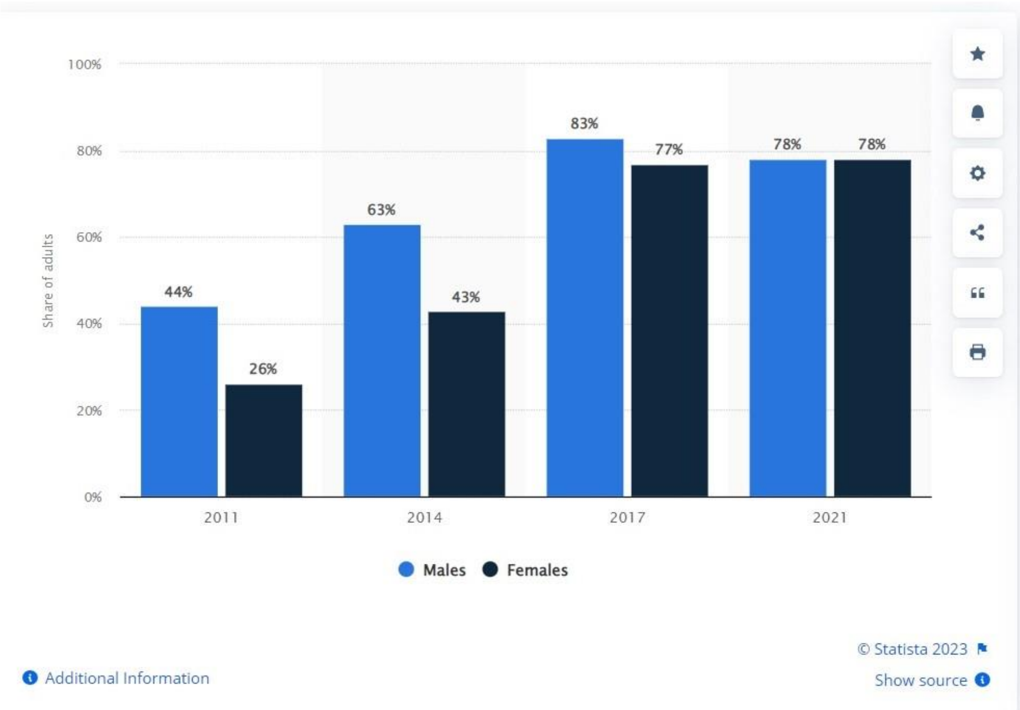

Figure 1. Financial inclusion rates in the year 2011-2021

Source: Statista.

The above image represents the financial inclusion rates after the implementation of new regulations in the microfinance sector. The X-axis indicates the years whereas in the Y-axis there is a representation of the percentage of adults who are accessing the financial services (Bajde et al., 2022). The above bar graph indicates two colors. The black bar is the percentage of females whereas the blue graph is the percentage of males. It is evident that with the implementation of the new regulations access to financial services has greatly increased by about 78% for males and females in the year 2021. It is also understood that there is no kind of discrimination in accessing financial services and there is an equal opportunity provided for males and females to access the financial services.

Certain other comparisons are listed by performing a detailed research study. Through this study, it is also known that old regulations are having very less emphasis on risk management and governance whereas new regulations is having a stronger concentration on the structures of governance, assessment of risks, and all the mechanisms are well monitored (Chakravarty & Pylypiv, 2015). It is also clearly understood from this research that through these new regulations there is an elimination of the regulatory arbitrage. New regulations are more effectively protecting customers from all unethical practices. There are positive impacts from the new regulations. Old regulations in the microfinance sector consist of limited measures for financial inclusion promotions but for the new regulations, there are flexible policies of lending and simplified norms of KYC (Chakravarty & Pylypiv, 2015). Through these lending policies, there are more possibilities for improving access to all underserved populations.

The research also suggests that all the old regulations that are present in the microfinance sector are concentrated on sector expansion but the new regulations have identified the necessity for prudential regulations to mitigate all the systemic risks and make sure that there is sector stability (Czura et al., 2022). From the qualitative study also certain findings mainly include the drawbacks of the old regulations. These old regulations are consisting of inappropriate regulations for digital innovation whereas all the new regulations introduced for the microfinance sector address the role that is played by the technology for all the digital services of finance. These new regulations also include certain guidelines for the protection of data and also for cybersecurity there are some guidelines present (Czura et al., 2022).

4.1 Data Analysis

MAXQDA is one of the effective tools which can be utilized for performing research and analysis. Mainly for the Qualitative data analysis, this MAXQDA is designed and this research mainly involves conducting interviews so that this tool is more valuable for the data analysis (Gutiérrez-Nieto & Serrano-Cinca). Once the data is gathered through this process a clear analysis is performed by the application of proper testing process. All the textual data is also analyzed in this Qualitative research including all the legislative records and policy documents. Content analysis is chosen for recognizing all the trends, themes, and shifts present in regulatory frameworks. This particular approach mainly assists in tracing the evolution of the regulations and recognizing the main drivers behind the regulatory transformations (Gutiérrez-Nieto & Serrano-Cinca). All the underlying motivations are also explored through this approach.

Content Analysis is the most suitable analysis method for performing analysis of the data. Through this content analysis, the implications that are present due to the new regulations are known (Godfroid et al., 2022). By using this content analysis in this research study all the textual data is well analyzed. For the regulators and policymakers, effective insights are provided. A transparent method of research is provided through this content analysis, therefore, a lot of credibility is ensured for all the research findings that are present in this study. Validations are made easier by using this content analysis and also all the findings are enriched (Godfroid et al., 2022).

4.2 Results

Through performing a research study there are key results obtained. This research has revealed the particular changes in regulations between the older and new frameworks. For instance, it highlighted certain changes in the requirements of licensing, measures of consumer protection, requirements of collateral, and interest rate caps (Radhakrishnan, 2015). This research has also assessed the implications that are present due to the regulatory changes on different stakeholders. This mainly included the analysis of the impacts on microfinance institutions, costs of regulatory compliance, finance access, and complete microfinance sector stability.

This research has also provided valuable insights for all microfinance practitioners, policymakers, and regulators. They can be able to inform the policy decisions in the future, and necessary adjustments in practices of the industry to improve the microfinance sector's efficiency levels and effectiveness (Zamore et al., 2019). Through the research analysis performed certain gaps and challenges present in the regulatory framework are also revealed. These gaps are mainly found in the older regulations. The main areas in which the old regulations have lacked are also clearly addressed. From the results that are obtained from the research, it is very evident that there are lot many variations present in the older and new regulations in the microfinance sector. Therefore all the new regulations that are introduced are focused on huge growth and technological advancements (Zamore et al., 2019).

5. Conclusion

From this conclusion, it is clear that by new regulations the microfinance industry in India has experienced significant growth and become a significant part of the country's financial ecosystem. While addressing the dynamic nature of microfinance operations the outdated regulations governing the microfinance industry have posed challenges. For addressing these challenges the old and new regulations in the microfinance industry are compared in this study (Czura et al., 2022). There are various key findings emerged through the analysis of old and new regulations. In the microfinance industry, greater emphasis on consumer protection, fair practices, and transparency has been placed by the new regulations. For mitigating over-indebtedness many measures have been introduced and protect the microfinance borrower's interests.

The stability of the sector is ensured, regulatory arbitrage is eliminated, and risk management is focused on the new regulations. The enhancement in financial inclusion rates has been identified as one of the significant positive impacts of new regulations. The role of digital innovation and the technology in microfinance sector are recognized by the new regulations. The barriers and challenges that are associated with the transition from old to new regulations have been highlighted by the research findings (Iqbal et al., 2019). For ensuring compliance with new regulations microfinance and other regulated entities requires to invest in staff training. Confusion may be created and the successful implementation may hinder the implementation inconsistencies in new regulations.

In conclusion, it is identified that the new regulations in the microfinance industry in India have created positive changes. The evolving requirements of the target market, consumer protection, and financial inclusion promotion have been strengthened by the new regulations. However, while implementing and enforcing new regulations there is a possibility to experience a few challenges. So that to ensure the microfinance industry's sustainability there is a necessity to promote continuous monitoring, regulatory reforms, and coordination among stakeholders (Singh & Kapoor, 2019). To foster a thriving microfinance industry that promotes financial inclusion the regulatory framework is refined further by the policymakers and this can be possible by recognizing the strengths and weaknesses of both old and new regulations.

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