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High bad debts under Mudra a myth, says govt

An internal note of the government on Mudra loans has said that loans given under the scheme through MFIs have high rates of recovery

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The government has sought to allay fears that loans extended under the Mudra scheme, particularly those given through microfinance institutions (MFIs), would add to bad debts in the lending system.

There were apprehensions that these unsecured loans carried high risks. Mudra loans are given to the vulnerable sections of society to carry out their small businesses, as they do not have access to the formal banking system.

Playing down such concerns, an internal note of the government on Mudra loans has said loans given under the scheme through MFIs have high rates of recovery.

“The traditional strength of MFIs in high rates of recovery continued with Mudra as well,” it says. Their overdues were well below one per cent as on March 31, 2016.

Mudra provides loans through MFIs and banking system to “own account businesses” run, particularly by Scheduled Castes, Scheduled Tribes, women and other backward classes.

Loans sanctioned under the Mudra scheme stood at Rs 1,37,449 crore and disbursements at Rs 1,32,954 crore to 34.8 million individuals in the first year of its operations - 2015-16.

Almost one-third of these loans — Rs 45,904 crore — were lent by MFIs, including those working in non-banking financial companies (NBFCs) space, the note adds.

The note, however, does not talk about the recovery rate of loans extended through the banking system (two-thirds of the total credit disbursed under the scheme).

PERFORMANCE OF MUDRA IN 2015-16

	Loans	Number of accounts	Disbursement of loans (₹ crore)
Shishu	Up to ₹50,000	32,401,046	**62,027.69**
Kishore	₹50,000-5 lakh	2,069,461	**41,073.28**
Tarun	₹5 lakh-10 lakh	4,10,417	**29,853.76**
Total		34,880,924	**1,32,954.73**

Source: Mudra

When the scheme was launched in 2015, apprehensions were expressed in certain quarters that a huge chunk of loans might not be recovered due to high risk businesses of these small borrowers. In fact, a union leader had remarked that a majority of these loans might go bad and add to the non-performing assets (NPAs) of lenders.

The note, however, says that a credit guarantee mechanism set up under Mudra helps reduce the risk underlining such loans that are unsecured in nature. The government has set up Credit Guarantee Fund for Mudra Units to reduce the credit risk to banks and MFIs.

The guarantee is provided on a portfolio basis to a maximum of 50 per cent of the default amount.

The note also says the Mudra scheme has enabled MFIs to reduce the interest rate they charge to the eventual borrower by four per cent. This might have also helped recover dues.

Also, MFIs have an incentive to improve appraisal processes since access to the credit guarantee and refinance is contingent upon achieving these benchmarks, the note adds.

Even after such benchmarks are met and initial access is obtained, risk-based pricing of guarantees ensures that lenders continue to have a sharp focus on diligence and recovery, the note says, adding that Mudra has opened up the possibilities for purchase of cleaned-up portfolio of MFIs by banks. This provides space for loan trading and intermediation through financial markets.

Under Mudra, loans are provided in three categories — up to Rs 50,000 under 'Shishu', above Rs 50,000 and up to Rs 5 lakh under 'Kishore', and above Rs 5 lakh up to Rs 10 lakh under 'Tarun'.

The note says clear patterns have emerged in the lending behaviour of MFIs and banks. MFIs are better placed in providing smaller loans with shorter tenures. They reach most women, Scheduled Castes, Scheduled Tribes, other backward classes and minorities in terms of extending Mudra loans than banks. Banks, on the other hand, perform better in reaching bigger borrowers.

It is no surprise that the average size of loans extended by MFIs under the scheme is Rs 19,992 (Shishu), while for banks the average of the loan is Rs 78,500 (Kishore).

The relationship is symbiotic as new customers start shifting away from traditional money lenders to MFIs and then graduate to becoming bank customers, the note says.

The Pradhan Mantri Mudra Yojana was launched in 2015 to cater to vulnerable sections of society who run small businesses. Later, Mudra was converted into a bank as a wholly-owned subsidiary of the Small Industries Development Bank of India.

According to a survey by the National Sample Survey Office in 2013, there were 57.7 million small business units, mostly individual proprietorships, which run small manufacturing, trading or services activities. Most of these ‘own account enterprises’ are owned by people belonging to scheduled castes, scheduled tribes or other backward classes. Only four per cent of such units get institutional finance.