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MUDRA Bank on a roll

The new agency can make a difference to small finance banks

The Micro Units Development and Refinance Agency Bank or MUDRA Bank, which was launched on April 8 this year, appears to have made an impressive start. Last week, Finance Minister Arun Jaitley said that it had already advanced over ₹24,000 crore to over 3.7 million micro enterprises and he expected advances to cross ₹1.2 lakh crore by the end of the current financial year, with over 12.5 million borrowers. By the yardsticks of even the most efficient organisations, this is a phenomenal achievement; by the standards of India's public institutions, even the well-run ones, this seems to be a creditable record, matching the pace at which bank accounts were opened under the Prime Minister's Jan Dhan Yojana. Over time, evaluation studies of both programmes will provide a better understanding of both how such rapid scaling up was achieved and what kind of impact it has had. Meanwhile, it is useful to look at the opportunities and challenges faced by this organisation as it deals with its mandate of universalising access to credit among micro enterprises.

MUDRA Bank is currently set up as a subsidiary of the Small Industries Development Bank of India (Sidbi), which itself was hived off from the then Industrial Development Bank of India (IDBI) to deal with its small business portfolio. The model that IDBI and Sidbi primarily followed was a refinancing model; state-level institutions, like state finance corporations, extended loans to these enterprises and these were then refinanced by the apex institutions. Over time, the state-level architecture withered and, at present, is virtually defunct. This effectively shut down the main channel of funding for the national institutions; the little that they could do through direct lending and refinancing banks kept them afloat. Along the way, IDBI morphed into a universal bank, while Sidbi remains but, some might say, a pale shadow of its former self.

This is not to deny in any way the importance of a refinancing institution. In many situations, it is an essential component of a robust financial framework. It provides liquidity and can help shape lending policies and risk management practices. The question is really about the strength of the delivery network. Here, MUDRA Bank will have a significant potential advantage over the Sidbi model. Its refinancing activities are not going to be restricted to a specific set of institutions. It has the mandate to use the entire range of financial service providers currently servicing the micro segment. Some of this is being done by banks, but non-banking financial companies (NBFCs) and microfinance institutions (MFIs) are active players in this field and they, particularly the latter, stand to gain access to significantly more resources to lend onward to the target segment. In fact, MUDRA Bank may well play a critical role in the viability and success of the newly licensed small finance banks, which are mandated to lend the bulk of their funds to priority sector borrowers, a large proportion of which will qualify as micro enterprises. So, a much more viable architecture is emerging. Of course, with such large amounts of money being talked about, great care has to be taken with risk assessment and management. Going forward, this should become a significant institutional capability in MUDRA Bank.