

MICROFINANCE DELINQUENCIES: ECONOMY

NEWS: Microfinance loan delinquencies jump 163% to Rs 43,000 crore in FY2025

WHAT'S IN THE NEWS?

India's microfinance sector witnessed a sharp rise in loan delinquencies to ₹43,075 crore in FY2025 due to overleveraging, poor credit checks, and income instability. Regulatory reforms, financial literacy, and ethical lending are essential to ensure sustainability and borrower protection.

Context: Rising Loan Delinquencies in Microfinance (FY2025)

- India's **microfinance sector reported a 163% surge** in loan delinquencies, reaching **₹43,075 crore** in FY2025.
- This sharp rise has raised concerns over **credit discipline, regulatory oversight, and borrower well-being**, especially in rural and semi-urban regions.

What is Microfinance?

- **Microfinance** provides **financial services** such as **microloans, savings, insurance, and remittances** to low-income individuals who are **excluded from formal banking**.
- Primarily offered by:
 - **NBFC-MFIs** (Non-Banking Financial Company - Microfinance Institutions)
 - **Small Finance Banks (SFBs)**
 - **Commercial Banks**
- **RBI Definition (2022):** A **collateral-free loan** given to a household with **annual income up to ₹3 lakh** is classified as a microfinance loan.

Key Trends in the Microfinance Sector (FY2025)

1. Decline in Overall Loan Portfolio

- **Gross loan portfolio fell by 13.9%** year-on-year:
 - From ₹4.42 lakh crore in March 2024 to **₹3.81 lakh crore in March 2025**.

2. Shift in Loan Ticket Sizes

- **High-ticket loans** (above ₹1 lakh): Increased by **38.5% YoY**.
- **Low-ticket loans** (below ₹30,000): Declined by **35.9% YoY**.
- Indicates **reduced focus on ultra-poor borrowers** and a shift toward **bigger, riskier borrowers**.

3. Reduction in Active Loan Accounts

- Number of **active microfinance loans** decreased from **16.1 crore to 14 crore**.

4. Borrower Consolidation

- Borrowers associated with **five or more lenders** dropped from **9.7% to 4.9%**, hinting at **reduced over-borrowing** but also **credit stress and cautious lending**.

Reasons Behind Rising Delinquencies

1. Overleveraging

- Many borrowers, especially in rural India, **take loans from multiple lenders**.
- Results in **unsustainable debt burdens** and inability to repay.

2. Weak Credit Appraisal Mechanisms

- Smaller MFIs and banks **relax credit standards** under pressure to meet targets.
- Leads to **loan approvals without adequate background checks**.

3. Income Instability

- Economic disruptions due to **COVID aftermath, rural inflation, crop failures**, and **seasonal unemployment** reduce borrowers' repayment capacity.

4. Inefficient Recovery Infrastructure

- **Post-COVID digital shift** and reduced **on-ground engagement** have weakened the recovery process.
- **Field agents and collection teams** are less active or understaffed in several regions.

5. Improper Loan Utilisation

- Loans meant for **productive income-generating activities** are often **diverted for consumption** needs like:
 - Weddings
 - Festivals
 - Medical emergencies

Government and Regulatory Initiatives

1. Pradhan Mantri MUDRA Yojana (PMMY, 2015)

- Enables **collateral-free loans up to ₹10 lakh** for micro and small enterprises.
- Loans disbursed through **MFIs, NBFCs, and banks**, refinanced by **MUDRA Ltd**.

2. Udyam Assist Platform (UAP)

- Supports informal micro-entrepreneurs (many of them MFI clients) to:
 - **Register as MSMEs**
 - **Access priority sector lending**, subsidies, and credit-linked schemes.

3. RBI's Credit Information Mandate

- Mandates **reporting of all microfinance loans to credit bureaus** (e.g., CRIF High Mark, CIBIL).
- Ensures **credit histories** are accessible to **prevent multiple borrowings**.

4. RBI's Revised Microfinance Regulatory Framework (2022)

- Applies uniformly to **banks, NBFCs, SFBs, and NBFC-MFIs**.
- Promotes **responsible lending**, limits interest rates, and enhances **borrower protection**.

Way Forward and Reform Measures

1. Strengthened Credit Assessment

- Develop robust **credit scoring tools** based on:
 - Repayment history
 - Household income profiles
 - Loan utilization behaviour

2. Leveraging Credit Bureau Data

- Use insights from **CRIF High Mark, Experian, CIBIL** to:
 - Detect early warning signals
 - Avoid repeated over-lending to the same households

3. Regulatory Oversight and Ethical Collections

- **RBI and state governments** must ensure:
 - **Fair recovery practices**
 - **No coercive or unethical loan collection**
 - **Proper grievance redressal mechanisms**

4. Financial Literacy

- **Train borrowers** in basic financial planning and debt management.

- **Raise awareness about:**
 - Rights and obligations under microfinance loans
 - Safe borrowing limits
 - Dangers of over-indebtedness

5. Digital Inclusivity

- Ensure **tech platforms used for lending and recovery** are accessible in regional languages and **suited for rural connectivity environments**.

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