Study on Interest Rates and Costs of Microfinance Institutions

2011

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LIST OF ABBREVIATIONS

APR	Annualised Percentage Rate
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CGAP	Consultative Group to Assist the Poor
CGT	Compulsory Group Training
CO	Credit Officer
COO	Chief Operating Officer
DFI	Development Financial Institution
EIR	Effective Interest Rate
GoAP	Government of Andhra Pradesh
GRT	Group Recognition Test
JLG	Joint Liability Group
M-CRIL	Micro Credit Rating International Limited
MFI	Microfinance Institution
MIX	Microfinance Information exchange
NBFC	Non Banking Finance Company
NGO	Non Governmental Organisation
NGO-MFI	Non Governmental Organisation turned Microfinance Institution
OER	Operational Expense Ratio
OER (A)	Operational Expense Ratio-Administrative
OER (P)	Operational Expense Ratio-Personnel
OMR	Optical Mark Recognition
PKSF	Palli Karma Sahayak Foundation
RBI	Reserve Bank of India
SBLP	Self Help Group bank linkage
SERP	Society for Elimination of Rural Poverty
SFMC	SIDBI Foundation for Micro Credit
SHG	Self Help Group
SIDBI	Small Industries Development Bank of India
WA-APR	Weighted Average Annualised Percentage Rate
XIRR	Irregular Internal Rate of Return
YoP	Yield on Portfolio

EXECUTIVE SUMMARY

Institutional credit is considered as a powerful tool for alleviating poverty. Microfinance in India has been through two channels of credit delivery to poor and low-income households – Self Help Group Bank Linkage Programme (SBLP) and the Microfinance institutions lending through groups as well as directly to individuals. Both these models which evolved and grew gradually during the 1990s. MFIs have been relatively faster in reaching out the under-served population even in the most difficult geographical regions of India. The MFI channel culminated in last decade in terms of its outreach, product diversity and technological innovation. However, as the sector scaled up, absence of a conducive regulatory framework along with few other political factors caused the Andhra Pradesh crisis in 2010. Due to the crisis the MFIs have suffered a huge loss in terms losing their loan portfolios. Moreover, as the Banks stopped lending to MFIs, they have not been not been able to disburse fresh loan to their clients. This has been also been a huge setback to the low income people across India that were being benefitted by the Microfinance services from the MFIs.

In the aftermath of the crisis, all stakeholders of industry have shown their commitment to introspect and re-strengthen the sector. Small Industries Development Bank of India (SIDBI) having played a key role in the development of microfinance in India commissioned this study for carrying out a detailed analysis of interest rates, costs and margins and product pricing of SIDBI assisted microfinance institutions. ACCESS Development Services carried out the study.

For the purpose of this study, 30 MFIs were visited. These MFIs were representative in terms of geographies, scale, operating models and legal forms. Primary data was collected at different levels including discussions with senior and middle management, branch staff, clients of the MFIs, as well as other relevant stakeholders of the sector. Different aspects of pricing, transaction costs, costs of funds, margins were studied.

Fifty one loan products were studied across these 30 MFIs to analyze the product pricing. APRs were calculated with different components of the loan pricing using the active loan samples collected from the field. In view of the ongoing revision of pricing across the industry, the price applicable as on December 31, 2010 was taken into account to make meaningful conclusions. As inclusion or exclusion of different components of the loan pricing i.e. fees, insurance and security deposit, among others result in different APRs; the APR calculations were calculated at the four different levels to enable the comparison at different levels so that the incremental effect of Fees, Insurance and Security deposit can be measured. As on December 2010, the microcredit products were available in the range of 18%-50% APRs (including only interest and processing fees). Comparative analysis of pricing was done across different tiers, models, legal forms of MFIs. The median weighted average APRs for Tier-I, II and III were found to be 27.75%, 30.07% and 26.51% respectively. These relatively higher APRs of the Tier-II MFIs can be attributed to higher transaction costs and higher financial costs incurred by these MFIs.

Median APR of For Profit MFIs was found to be almost 500 basis points higher than that of the Not for profit MFIs (Primarily NGOs). This was attributable to microfinance activities being one amongst the many other activities of the NGOs resulting in lower OERs to the Not for Profits (as the transaction costs are apportioned to different programme activities). The same holds true for the lower APRs of the MFIs with the SHG Model. Though the APRs of the SHG based MFIs (Primarily NGOs) were found to be significant lower than that of the MFIs with other models, these MFIs have relatively smaller outreach. The average outreach of the MFIs with Non SHG model was almost five times higher than that of the SHG based MFIs.

In terms of the geographical variations, other that the APR being higher in the north-eastern region, not much variation was found in the APRs that were prevalent in different geographical regions.

APRS were also studies in relation to yield on portfolio to give a more holistic picture. The revised pricing (as on April 2011) was also studied for 18 MFIs based on the descriptive information provided by them.

Over the years, the transaction cost was found to be showing a declining trend in Tier-I MFIs, however, Tier-II and Tier-III MFIs showed increasing trend in transaction cost. Among the different delivery models, Grameen model exhibited a regular decline in the OER. It was also found that the institutions following weekly repayment frequencies has the higher OER than that of the MFIs following fortnightly and monthly repayment frequencies. With the RBI guidelines issued and over emphasis of decreasing costs, there are chances that the institutions following weekly frequencies would change to fortnightly or monthly installment repayment system. This would have a direct impact on the costs of the institutions since field / credit officers visiting and travelling to the clients would be limited to ‘one’ and not ‘four-five’ per month. Some MFIs that invested in the technology and systems were able to significantly reduce their OERs over the years.

The weighted average cost of funds from different financial institutions (a sample of 80 financial institutions) was found to be in the rage of 8% to 15%. Larger MFIs and majority of the not for profit MFIs were found to have lower cost of funds as compared to the other for profit (primarily the Tier-II) MFIs. The Tier I institutions due to their widespread geographically diverse operations, superior systems and updated information, skills in negotiation, apart from larger quantum of loan requests are in a better position to bargain with the financial institutions and raise debts at a lower interest rates. There is also a perception among lenders that the larger institutions are not likely to fail; the smaller institutions with concentrated portfolio, raises the risk perception of lenders.

Margins show an increasing trend across all levels of MFIs over the years. However, the Tier II MFIs have much lower margins than the Tier I and Tier III categories due to their expansion cost to reach the economies of scale.

To study the above aspects in the global and regional context, benchmarking was done using the MIX data (2009) for institutions that have reported their data to MIX which included 22 of the 30 MFIs sampled MFIs of this study. In order to generate reasonable conclusions, a smaller sub-sample of Asian countries including Bangladesh, Cambodia, Indonesia and the Philippines were also chosen. Amongst global and Asian microfinance markets, Indian MFIs have developed a number of strong attributes and exemplary performance. APRs of Indian MFIs fall in a mid range (neither the lowest nor the highest) of the APRs when compared to eight other countries (for which APR were available). The median APRs (31.24%) including interest, fee and insurance of the studied Indian MFIs were well below the average median APRs of 9 other countries[1]. In absence of the APRs of south Asian MFIs, Yield on Portfolio was used for comparison. Though the sampled MFIs though have a relatively higher Yield on Portfolio than that of the median South Asian YoP, it is still lower than that of the global median figure and considerably lower than that of other comparable markets like Indonesia, Cambodia and Philippines. However, this comparison looks further encouraging in the light of the fact that the institutions operating in India have the highest weighted average costs of borrowings in the world. The financial institutions in India charge the highest rate of interest when compared with other Asian countries like Bangladesh, Cambodia and Indonesia. Even as operational costs of

[1] Using data available on MFTransparency’s website: www.mftransparency.org

Indian MFIs continue their gradual decline, they are offset by increasing financial costs. However, in global context it found that in case of Indian MFIs as also for South Asia and Bangladesh, the difference between the Yield and Financial expenses i.e. the margin above financial expenses is comparatively lower, which indicates the relative efficiency of the MFIs operating in these geographies. In terms of profitability, Indonesian and Indian MFIs were amongst the most profitable MFIs. However, when given a holistic view it was evident that the Indonesian MFI incurred higher cost and products were priced even higher to generate higher profits; In case of Philippines, the extremely high cost resulted in the low profitability; However, in case of Indian MFIs, the low cost and a moderate pricing resulted in a high profitability.

The risks facing the microfinance industry were also studied. MFIs that were studied face a variety of risks – some are internal to their business operations and a few are due to external factors. Amongst the top five risks factors were competition, political interference, lack of clarity on regulation of the sector, liquidity and high cost of funds. The major internal risks are credit risk due to over indebtedness of clients, credit risk borne by the clients though peer payment, etc which need to be measured and monitored.

On the technological front, it was found that the use of information and communication technology has the potential to make the microfinance processes more efficient by reducing costs in two ways – (1) lowering of operational costs by automating components of the credit process and (2) lowering and controlling risk and thereby risk cost by more effective monitoring and tracking. Almost all sampled MFIs had an automated MIS that enables them to track performance effectively. The MFIs have confirmed that investment in a good MIS application along with hi speed internet facility helps in the effective monitoring of the operations. However, concrete evidence of reduction in operating costs after setting off the investment and recurring costs of technological applications were still not available.

The MFI clients were interviewed in order to understand the transparency / disclosure of information provided by the MFIs to their clients and their level of awareness. The awareness of clients regarding the terms and conditions of the loans is directly proportional to the information shared by the MFIs. A comparative analysis has been carried out across different tiers, legal forms and models of MFIs.

The development activities conducted (through grants or from their profits or by charging from their clients) help in building capacities of the clients / members as well as increase the rapport and loyalty of the clients / members towards the respective institution. This has been observed during the interactions and discussions with clients / members of Bandhan, Equitas, Cashpor, among others; they feel a sense of ownership with the institution and would not go to any other institution for credit

The relevance and practicability of different recommendations by the Malegam committee were discussed with the MFIs and the data / information collected across MFIs was analyzed to understand the concurrence with the RBI guidelines. Some fundamental changes are needed in the way many of the MFIs operate right from client acquisition and relationship management, client education, lending and recovery practices and product development. Based on the overall analysis and discussion with the MFIs, MFI clients and other relevant stakeholders, some key recommendations have been made in the areas of cost reduction are investment in technology, need for a greater emphasis on client interface and responsible finance, rationalizing of salaries of CEOs of MFIs; risk management are changes in systems, policies and growth strategies to comply with the recent RBI guidelines, hidden risk due to repayment by peers, robust internal audit and control systems; management of client awareness and literacy by conducting financial literacy programmes, innovative methods for communicating to clients like pictorial aids, compulsory insurance, equity infusion and differential interest rates across geographies and scale need to be developed.

1. CONTEXT

Microfinance in India has been through two channels of credit delivery to poor and low-income households – Self Help Group Bank Linkage Programme (SBLP) and the Microfinance institutions lending through groups as well as directly to individuals. Both these models which evolved and grew gradually during the 1990s, registered a blistering pace of growth in outreach and portfolios in the next decade. However, the MFI segment has grown over 20 times in the last 5 years - from INR 8.97 billion loans outstanding in 2005, the MFIs reached the position of INR 183.44 billion loan outstanding in 2010. The SBLP program comparatively has grown at 30% year on year during the same period. In the last 5 years, the microfinance operations that were earlier concentrated in the southern and eastern states began to spread to other poorer regions with the large MFIs expanding their operations to these regions as well as with the emergence of local new-age institutions.

An as apex development finance institution, Small Industries Development Bank of India (SIDBI) has played a significant role in the development and growth of microfinance in India through the SIDBI Foundation for Micro Credit (SFMC). SFMC is the apex wholesaler for microfinance providing a complete range of financial and support services[2]enabling the growth of MFIs. These services have enabled the microfinance institutions, especially in their initial stage of development, to invest in systems and institution building, imbibe sound practices. Based on credit history created with SIDBI, the MFIs could access commercial funding; both debt and equity, which in turn fuelled the portfolio and outreach growth. The sector-building role played by SFMC has contributed to development of technical service providers for the MFIs, which enabled their growth.

However, the high rate of growth has raised some concerns. The interest rates were expected to decline significantly with increasing scale of operations and efficiencies and only a few MFIs have passed on the benefits by reducing interest rates charged to the borrowers. There have been concerns about lack of transparent pricing information on the interest fee and other fees charged to the client. The quality of governance of MFIs has also been matter of concern since the mission drift was discernable in some of the MFIs. In certain regions, aggressive competition among MFIs has resulted in excessive financing to clients, inadequate due diligence in client acquisition and financing, lowering of disciplinary standards and coercive recovery practices.

The sector has reached a stage at which the two channels seem to be competing with each other, doubting the efficacy/ ethics of the other model, creating polarization. The recent developments in Andhra Pradesh leading to a crisis in the whole sector are a result of lack of an integrated and coordinated response to manage these issues. Accusing the sector of exploiting the poor with high interest rates, and employing coercive methods with clients leading to their distress, the Government of Andhra Pradesh (AP) promulgated a sweeping ordinance that severely restricted the MFI operations in the state. Repayments of loans of both MFI and SHG channels were drastically affected in the state. Since a large part of the portfolio of most large MFIs is in AP, this affected the growth of the whole sector. Following the Ordinance in AP, the Reserve Bank of India set up a sub-committee of its Central Board of Directors to study issues and concerns in the microfinance sector. The sub-committee released its report in January 2011, recommending a separate

[2]SFMC provides loan funds, grant, equity, Liquidity Management Support (short-term loan scheme), loan syndication and institution and capacity building support to retailing MFIs.

category of NBFC-MFIs, along with stipulations on total microfinance loan to a borrower, interest rates and fees, loan sizes, income of client, margin and loan tenure, loan collection practices, among others.

This study was part of a larger project titled "Scaling up Sustainable and Responsible Microfinance Project" supported by World Bank and implemented by SIDBI through SIDBI Foundation for Microcredit (SFMC), a specialized department for carrying out micro finance activities. The project addresses the lack of access of the underserved segments of the population to financial services, an important constraint to improved productivity and incomes, and particularly in the aftermath of dual crises that have affected the microfinance sector in India; the global financial crisis which continues to affect MFIs and their clients, and more importantly the impact of the crisis in Andhra Pradesh, which has caused a precipitous drop in repayment in the affected region of the country, and may significantly undermine the outreach and sustainable of the sector throughout India. The study is a part of the component-'Strengthening Responsible Finance' which addresses many of the root causes of the AP crisis, and provides solutions for taking on the responsible finance agenda at such a critical time for the future of the microfinance sector. In particular, the Project strengthens the Responsible Finance agenda through creation of a Lenders' Forum, development of a common information platform similar to the Global Mix Market and formalizing of a system for monitoring of the microfinance Code of Conduct, among others.

The study was commissioned by SIDBI to ACCESS Development Services in February 2011, with the overall objective of *conducting a detailed analysis of interest rates, costs and margins of SIDBI assisted microfinance institutions. As part of the study, ACCESS was to comment on impact of caps on interest rates and margins and provide recommendations on further reducing costs of operations in these institutions.*

2. Methodology

The study was primarily based on primary data collected from 30 sample MFIs, pre selected in consultation with SFMC. Secondary data collected and utilized in the study is limited to the purpose of benchmarking the trends of the sample with regional and global data. The details are provided below:

Secondary Research

Review of secondary information available was undertaken to cover the following aspects:

- Global and regional benchmarking - For the benchmarking of the MFIs visited during the study against the global and south Asian markets, analysis was carried out using the MIX data for institutions that have reported their data to MIX.
- Studies and analytical reports relating to interest rates, yield, return on assets, margin and costs in microfinance, relevant to India, other Asian countries and globally, were reviewed to obtain an overview of the trends of these indicators for last three years. These reports include the Microfinance State of the Sector report, M-CRIL analytics reports, Sa-dhan reports on MFIs, CGAP papers, MIX bulletins and MIX market data and data from Microfinance Transparency.
- Reports/case studies on best practices on client education and literacy/communication practices were studied.
- Available research reports on interest rates of other sources of credit, banking data were also reviewed.

PRIMARY RESEARCH

ORGANIZATIONAL INFORMATION

The following documents and information were collected from each sample MFI, during visits to Head Office and Branch Offices:

- Last three year's audited financial statements and portfolio reports
- Staff structure and remuneration of field staff and CEO
- Client loan pass books and repayment schedules (for data on product pricing)
- Details of borrowings – source and terms and conditions of loans
- Shareholding pattern
- Grading/rating reports
- Outreach data for 3 years
- Details of loan products and other services (insurance)

SEMI-STRUCTURED INTERVIEWS

*(The tools and checklists used in the study has been attached as **Annexures 1 - 4**)*

Interviews were conducted with the following categories of respondents based on checklists.

- MFI Senior management (CEO, CFO, COO) – These semi structured interviews focused on strategic issues of drivers of costs, key risks faced, strategies of risk management, role of technology in reducing risks/transaction costs, cost of funds and fund raising, strategy for change in products/pricing (if any), implications of Malegam committee recommendations / RBI guidelines issued.
- MFI Staff (Operations manager, Branch/Area manager) – Interviews of operations staff were geared towards understanding the operating procedures, implications on costs, measures for avoiding multiple lending, perceived risks including competition, delinquency management, communication with clients, implications of operational level recommendations such as loan tenure and client income.
- MFI Clients – MFI clients were interviewed through a short questionnaire for data on other sources and costs of credit, incidence of peer repayments and awareness of clients regarding MFI's product details.
- Stakeholders - Interviews with other stakeholders and sector experts including technology service providers, banks/lenders, investors and financial experts were conducted to obtain their views on ways of cost reduction by MFIs and implications of RBI guidelines on the sector.

SAMPLING

Selection of MFIs: Purposive sampling method was used to select a representative sample of MFIs based on four criteria:

a) Size of operations/number of clients (Tier I, II and III)
b) Lending model (JLG, SHG, Grameen, Individual)
c) Legal Form of the institution (For Profit-NBFCs and Not For Profit-Society, Section 25, Trust)
d) Geographic coverage (Multi-region, North, South, East, West)

Sampling and Data Collection Plan

*(The schedule of visits to MFIs for data collection attached as **Annexure 5)***

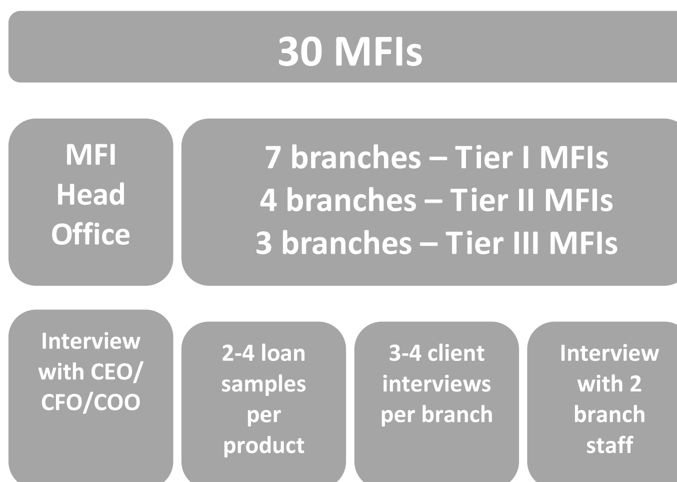


FIGURE 1: SAMPLING AND DATA COLLECTION PLAN

- 7-8 branches of Tier I MFIs and 3-4 branches of Tier II and III MFIs were selected through purposive random sampling to select branches from different geographic regions of the MFI.
- In case of MFIs with multi state operations, 50% of the branches were selected in the parent state of operations of the MFIs and the remaining 50% in their other operational states.
- Two loan samples of recent loans (less than 4 months old) for each loan product after the last interest rate reset by the MFI were selected for collection of loan documents for calculation of APR. This was done randomly from the list of clients who received loans in the last four months. Random selection of clients helped to negate any biasness to the samples.
- In each branch covered, 3-4 client interviews were conducted. These clients were again selected on a random basis from the list of members in that particular branch. This was done post discussions with the branch staff. If a selected client was unavailable then another client from the same group was selected based on availability.

APR Calculations

The following assumptions and considerations apply to the calculations of APRs in the study:

1. The products that account for at least 10% of the total outstanding loan portfolio of the MFI were studied.
2. The loan samples that reflect the loan pricing applicable until December 31, 2010 were used to calculate the APRs.
3. The Insurance amount used in the APR includes Service Tax.
4. Insurance charges and security deposit associated with the loan results in a cash outflow at the borrower level and affect the net outstanding balance. Therefore, the APRs were calculated at the following four levels to enable the comparison from multiple cash flow perspective:
    a. APR for Interest and Fees
    b. APR for Interest, Fees and Insurance charges
    c. APR for Interest, Fees, Insurance charges and Security deposit
    d. APR for Interest, Fees, and Security deposit (excluding Insurance)
5. To calculate the weighted average APRs of the products studied, outstanding loan portfolio of individual products was used to assign the weight to the average APRs of the loan samples for each product.

The process and methodology of APR calculations is outlined below:

1. **Collection of the descriptive information of the product**
   The products qualified for the APR calculation were first understood using the descriptive information provided by the Product Manager/ Senior Managers of the MFIs.
2. **Collection of loan samples from the field**
   Based on the descriptive information it was determined what all the features can affect the APRs and accordingly the samples were collected so that all the variations can be covered.
3. **Calculation techniques**
   For each of the loan sample cash flows was created using the exact dates and amount paid/received by the borrowers at the following four levels:
    a. Cash-flow for Interest and Fees
    b. Cash-flow for Interest, Fees and Insurance charges
    c. Cash-flow for Interest, Fees, Insurance charges and Security deposit
    d. Cash-flow for Interest, Fees, and Security deposit (excluding Insurance)

   The EIR was calculated for each of the cash flow using the XIRR. XIRR takes into account the exact dates at which the repayment installment were paid and thereby takes into account the correct number of days (between two consecutive installment) for which the outstanding balance remained with the client.

   The EIR (using XIRR) was just as an intermediate step to arrive at the APRs. The EIR includes the compounding effect and therefore it was converted into APR using the following formula.

   APR = [(1+EIR) ^ (1/365) -1]*365
4. **Verification of the calculations**
   The final APR calculations were sent to the MFIs for their review with a deadline to revert in case of any doubts. The queries of the MFIs who reverted with questions/clarifications were addressed. As communicated to the MFIs, the APR calculations of the MFIs who did not revert were considered final for further analysis

LIMITATIONS

1. Most of the MFIs visited had reduced the interest rates and processing fees following the AP Ordinance (October/November 2010) and very few loans had been sanctioned after such revision in pricing at the time of the study. Therefore, live loan samples of revised pricing were not available in all the branches visited by the team. In some instances, loans disbursed post the date of effect of pricing revisions have been as per the old terms and conditions and hence the APR calculated from such samples does not reflect the most recent product pricing.

2. There were substantial delays in scheduling of visits to MFIs due to State level *bandhs* (specifically in East and North East region) and non co-operation of a few MFIs for providing dates for visits. Many of the MFIs were busy due to financial year closing, financial audits and board meetings during the period from March to May.

3. The team could not collect all the required data because either the data is not tracked by MFIs or it was not provided to the team even after repeated reminders and follow-ups after conclusion of the visits (Spandana, Share, and Asmitha). Some MFIs did not agree to disclose certain data related to share valuations and premium offered, expected return on equity, salary of CEO etc.

4. Few sample institutions such as Uttarayan Financial Services, Annapurna Microfinance, among others are in the process of transitioning their microfinance portfolio from Society to NBFC and hence the Year 1 or Year 2 figures and ratios are either unavailable or skewed.

5. The sample size within each of sub-category analyzed in the study was not adequate to corroborate the findings. e.g. there are not many Not for Profit Institutions (seven Societies, three Trusts and one Section 25) in the study to confirm the findings of the study with respect to the entire population of such Institutions; similar the institutions selected in the western region are not adequate to conform the results for the region.

6. Some of the Tier III institutions are NGOs and carry out micro finance as one of their many activities. Staff and infrastructure are shared among different programmes. Segregation of operational costs for four such institutions based on scientific methods like activity based costing was not possible given the time available. The adjustments for financial costs for low cost lending resources mobilized by the MFIs however have been carried out.

7. Secondary Data on APR for MFIs across South/Southeast Asia is unavailable for comparison. The APRs are available only for Cambodia on the Microfinance Transparency's website. The comparable data for all the indicators of a large sample was available till 2009 only, in MIX market. It was found that 22 of the 30 MFIs visited during this study reported their data to MIX and the same sample set has been used for comparison. In order to generate reasonable conclusions, smaller subsample of Asian countries including Bangladesh, Cambodia, Indonesia and the Philippines were chosen. Within this data set, a few important indicators been chosen to try and understand the Indian landscape in the context of microfinance in Asia and the World. Nominal portfolio yield is a reasonable proxy indicator for interest rate pricing, and represents the approximate inclusive cost to the client**.** Operating expense ratio is the standard measure of efficiency and elaborates the cost side, especially when compared with other components of expenditure. The financial expenses / assets ratio is an approximate look at the cost of funds, which is a major element of interest rate pricing in most microfinance markets.

3. Description of Sample

A total of 30 SIDBI assisted institutions were selected on the basis of 4 criteria (scale of operations, geography of operations, legal forms and lending models) to ensure adequate representation of MFIs across all sub-categories within these criteria. The sub-categories and their definitions within each criterion group are mentioned in **Table 1**:

TABLE 1: DECRIPTION OF CRITERIA AND SUB-CATEGORIES USED FOR FOR SAMPLING AND ANALYSIS

Decription of Criteria and Sub-categories used for for Sampling and Analysis	
Scale	**Client outreach**
• Tier I	> 250,000
• Tier II	50,000 – 250,000
• Tier III	< 50,000
Geography	
• Multi-Region	Operations in more than 5 states of India
• North	Operation in the parent north state
• South	Operation in the parent south state
• East	Operation in the parent east / northeast state
• West	Operation in the parent west state
Legal Form	
• For Profit	All NBFCs
• Not for Profit	Societies, Trusts and Section 25
Model	
• SHG	Lending to groups of 15-20 members
• JLG	Lending to groups of 5 members
• Grameen	Lending to 5-8 groups of 5 (center) members each
• Individual	Lending to individual members

The list and basic details all sample MFIs is provided in **Annexure 6**.

The number of institutions, cumulative client outreach and cumulative loans outstanding under each of the groups and corresponding categories are depicted below:

Scale of Operations: *(Figures as on March 31st 2010)*

TABLE 2: SCALE OF OPERATIONS

Category	No. of MFIs		Cumulative Outreach		Cumulative Loan Outstanding	
	Nos	%	Nos(thousands)	%	INR million	%
Tier I	12	40	20,470	95	116,234	94
Tier II	9	30	876	4	4,698	4
Tier III	9	30	176	1	2,630	2

Total	30		21,523		123,563	

Tier I MFIs that constitute 40% of the sample in terms of number of MFIs cover 95% of the total number of clients and 94% of the cumulative outstanding portfolio of the entire sample MFIs. The client outreach of the Tier I institutions range from 80,000 to 56,00,000 clients and cumulatively they constitute 95% of the total client base in the sample.

Geography of Operations:

TABLE 3: GEOGRAPHY OF OPERATIONS

Categories	Number of MFIs	Percentage	Cumulative Client Outreach (in Thousands) (as on March 31, 2010)	Cumulative Loans Outstanding (Rs Million) (as on March 31, 2010)
Multi-region	9	30%	18,849	1,07,678
North	5	17%	754	4,309
South	7	23%	1,628	9,650
East	6	20%	124	1,850
West	3	10%	165	73
Total	**30**	**100%**	**21,523**	**123,563**

MFIs working in multi-regions/states form maximum (30%) proportion of the sampled MFIs and they constitute 88% of the client base. These institutions have operations in more than 5 states of India. The other categories have been divided as per their operations in one state in that particular region.

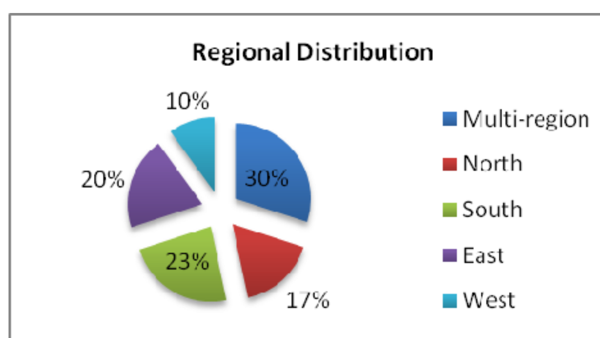


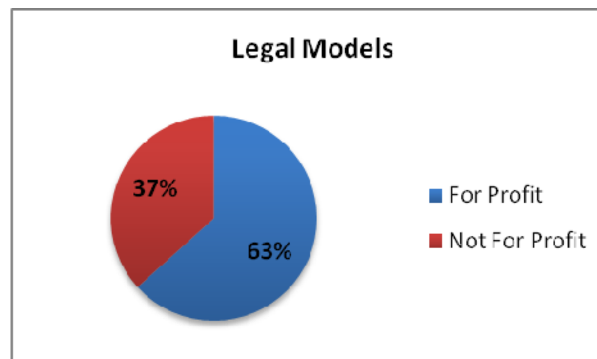
FIGURE 2: REGIONAL DISTRIBUTION OF SAMPLED MFIS

Legal Form of Institutions:

TABLE 4: LEGAL FORM OF INSTITUTIONS

Categories	Number of MFIs	Percentage	Cumulative Client Outreach (in Thousands) (as on March 31, 2010)	Cumulative Loans Outstanding (in Rs Million) (as on March 31, 2010)
For Profit	19	63%	19,719	113,658
Not For Profit	11	37%	1,803	9,905
Total	**30**	**100%**	**21,523**	**123,563**

For profit institutions comprise NBFCs, which is maximum percentage (64%) of the institutions sampled in the study. Seven Societies, one Section 25, Not for Profit and three Trusts have been clubbed under Not for Profit institutions for this study.



Lending Models followed by Institutions:

TABLE 5: LENDING MODEL FOLLOWED BY MFIS

Categories	Number of MFIs	Percentage	Cumulative Client Outreach (in Thousands) (as on March 31, 2010)	Cumulative Loans Outstanding (in Rs Million) (as on March 31, 2010)
SHG	9	30%	1,412	9,213
JLG	7	23%	1,432	10,118
Grameen	13	43%	18,516	104,192
Individual	1	3%	161	38
Total	**30**	**100%**	**21,523**	**123,563**

The predominant lending model is the Grameen model (mostly Tier I institutions), implemented by 43% of the institutions across the sample and constitute 86% of the cumulative client base. However, a few of the institutions followed a mix of JLG and Individual model and only one institution followed individual model entirely for which the findings have not been mentioned since it would not represent the model.

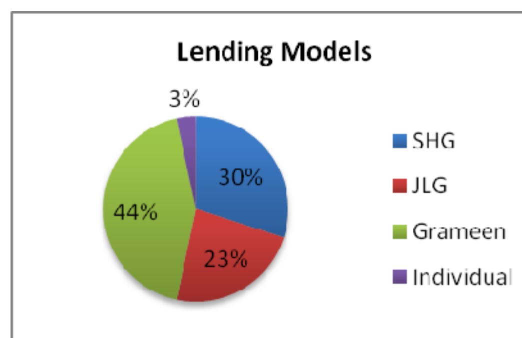
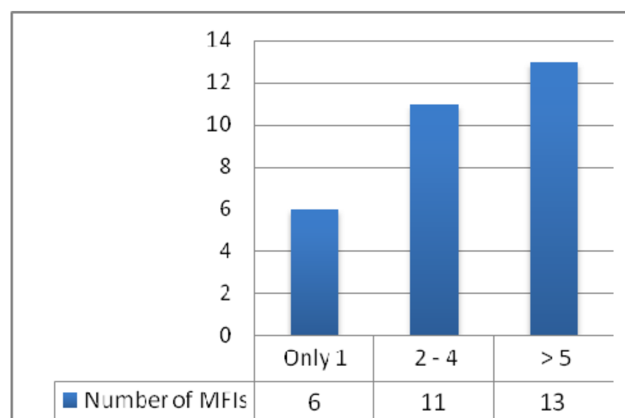


FIGURE 3: LENDING MODELS OF MFIS

Loan Products provided by Institutions:

Within the number of institutions visited, 43% of the MFIs had more than 5 loan products (BSFL had 25 products) and 37% of the MFIS had 2-4 loan products. However, the maximum concentration of their portfolio was in the IGA loan provided by the institutions. The remaining



products had 5-10% of their portfolio individually. Only 20% of the MFIs provided one loan product.

FIGURE 4: NUMBER OF PRODUCTS OF SAMPLED MFIS

INSURANCE SERVICES PROVIDED BY INSTITUTIONS:

Insurance is another service that is valued by the clients as well as provided by most of the sampled institutions. Only 10% of the institutions namely, NBJK, People's Forum and MAS Financial Services, did not provide any insurance services to their clients. Predominantly, the insurance services provided are credit linked – 77%; but four institutions (13%), viz., NEREFS, SKDRDP, RASS and RORES provide insurance services which are not linked to loans.

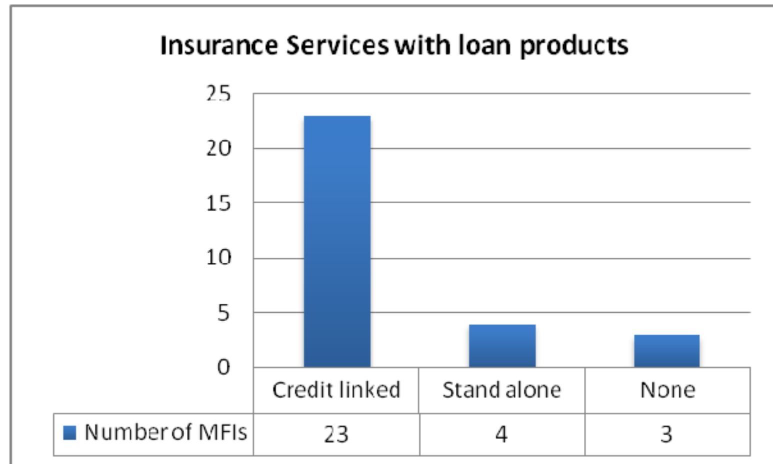


FIGURE 5: INSURANCE SERVICES WITH LOAN PRODUCTS

4. Pricing of Loans

What is APR?

The true price of a loan includes not only interest but other charges required by the lender as well as other techniques that influence the amount of money the client actually has and the amount of time the client has use of that money. Because of these multiple factors, as well as differences in interest calculation methods, comparing the pricing of different loan products can be very challenging. The Annual Percentage Rate (APR) is used to express the true price as a standard measure that allows for the comparison of credit charges among different loan products. The purpose of the APR is to convert the array of charges made for a loan into a simple, declining balance interest rate that would have an equivalent cost[3].

In simpler terms the APR can be obtained by multiplying the IIR (of the net cash flow of loan transactions) for the unit by the number of unit periods in the entire loan tenure. i.e.

APR = I * n

Where i = IRR of the net cash flow of the loan transactions for the unit period

And n = number of unit period (repayment frequency)

The IRR with compounding effect gives us the EIR (Effective Interest Rate) which is the European Union standard and is used in a large number of countries around the world; i.e.

$$EIR = (1+i)^{n} - 1$$

Calculation method for this Study

It is a common a phenomenon that the microfinance loans may have unequal repayment period for example if the MFI offers 15 days grace period on a monthly loan than first repayment period of such loan will be 45 days however rest of the installments may have only 30 days period. In case of weekly loan as sometimes the clients are required to propone or postpone some of the installments. In such cases since the n is not equal the IRR's may not be 100% accurate as it considers all the period to be equal. However, the organizations included in this study had a variety of products, it was important to take into account these variations accurately and still use a uniform method so that the rates of different products can be compared. For this purpose XIRR was used for calculations.

. XIRR takes into account the exact dates at which the repayment installment were paid and thereby takes into account the correct number of days (between two consecutive installment) for which the outstanding balance remained with the client. Since EIR can be directly calculated using XIRR, the EIR (using XIRR) was used as an intermediate step to arrive at the APRs. The EIR includes the compounding effect and therefore it was converted into APR using the following formula.

APR = [(1+EIR) ^ (1/365) -1]*365

[3] MicroFinance Transparency. (2010). *Formulas and Approaches Used to Calculate True Pricing.* Retrieved from http://www.mftransparency.org/pages/wp-content/uploads/2011/05/UnderstandingAPRCalculations-2011-05.pdf

APRs for Key Products

In the sample MFIs of the study, the microfinance products accounting for at least 10% of the total loan portfolio were included for the purpose of APR calculations. **Annexure 9** shows the number of products studied. For BSFL and SKDRDP five products were studied. Other MFIs were also found to have different products; however, these products had a very small portfolio or were in the pilot phase. It can be said that BSFL and SKSDRDP have maximum product diversity as they have not only developed different products but have also been successful in scaling them up.

A total of 51 products were studied across the 30 sample MFIs. The Average APRs of all the samples collected for each of the product is presented in **Annexure 7**.

Snapshot of the Dataset

- Number of MFIs in the sample: 30
- Total Number of Products: 51

- Median APR of the dataset
  - Interest+ Fee: 28.96%
  - Interest + Fee + Insurance: 30.57%
  - Interest + Fee + Insurance + Deposit: 32.33%
  - Interest + Fee +Deposit: 30.44%

- Costliest loan sample in the dataset
  - APR (Interest + Fee): 60.27%
  - APR (Interest + Fee + Insurance): 60.27%
  - APR (Interest + Fee + Insurance + Deposit): 60.27%
  - APR (Interest + Fee + Deposit): 60.27%

- Cheapest Loan sample in the data set
  - APR (Interest + Fee): 14.88%
  - APR (Interest + Fee + Insurance): 15.74%
  - APR (Interest + Fee + Insurance + Deposit): 15.74%
  - APR (Interest + Fee + Deposit): 14.88%

Number of Products Studied

TABLE 6: NUMBER OF PRODUCTS STUDIED

Number of Products	One	Two	Three	> Three	Total
Number of MFIs	17	9	2	2	30
Percentage	57%	30%	7%	7%	100%

The number of products studied under each MFI for the purpose of APR calculations is presented in **Annexure 9**.

APRs as per the latest Pricing Structures

Based on the efforts of SFMC, lenders' forum, recommendations of the Malegam committee and subsequently the RBI guidelines issued in May 2011, majority of the MFIs have revised the prices of their loan products. These revisions were affected prior to, during and post the visits of study teams to the MFIs. In order to include the most updated pricing data in the report, the sampled MFIs were requested to share the latest pricing structure of their loans. Out of the 30 MFIs, 18 MFIs responded with their latest pricing information, based on which the APRs for revised pricing have been calculated. Using the different combinations of the loan products such as loan term, repayment frequency, additional fees, insurance charges, the minimum and maximum possible APRs for the 31 products was calculated at the following three levels (presented in **Annexure 8):**

i. APR (Interest only)
ii. APR (Interest + Fee)
iii. APR (Interest + Fee + Insurance)

In consideration of the recommendations by the RBI, all these 18 MFIs have excluded cash/security deposit from their products. Therefore, the APRs including cash/security deposit are not applicable.

Note: These Post December-2010 APRs are based completely on the theoretical calculations as per the information shared by the MFIs and are not verified through collection of actual loan samples of clients.

WEIGHTED AVERAGE APR OF INSTITUTIONS ACROSS THE PORTFOLIO

APR always measures and refers to individual products and not directly at the institution. An MFI may have many loan products, each product resulting in a different APR. Hence quoting any figure as the APR of the institution will be technically incorrect.

However, for the purpose of comparison of the institutions, a representative figure is required. Using Average of the APRs of the products studied for each MFI would not be useful as different products invariably have different proportions in the total portfolio of the organization. Therefore weighted average APRs were calculated for each of the 30 MFIs. The outstanding portfolio of each product has been used to assign the weight in the average APRs of the respective products.

The graph below (**Figure 6**) gives a snapshot of the weighted average APRs (across portfolio of the studied product) of the 30 institutions at following three levels of calculations (based on the pricing applicable till December 31, 2010).

i. APR (Interest + Fee)
ii. APR (Interest + Fee + Insurance)
iii. APR (Interest + Fee + Insurance + Deposit)

The three bars are representing the WA-APRs for each MFI at different level, as mentioned above. Wherever any two bars in the **Figure 6** are equal for any MFI, it means that no differentiating component is offered by that particular MFI. However, wherever the length of any two bars (for any MFI) is different, the difference can be attributed to the incremental effect caused due to the differentiating component of pricing (Insurance or Security Deposit).

The weighted average APRs at all four levels are provided in **Annexure 9.**

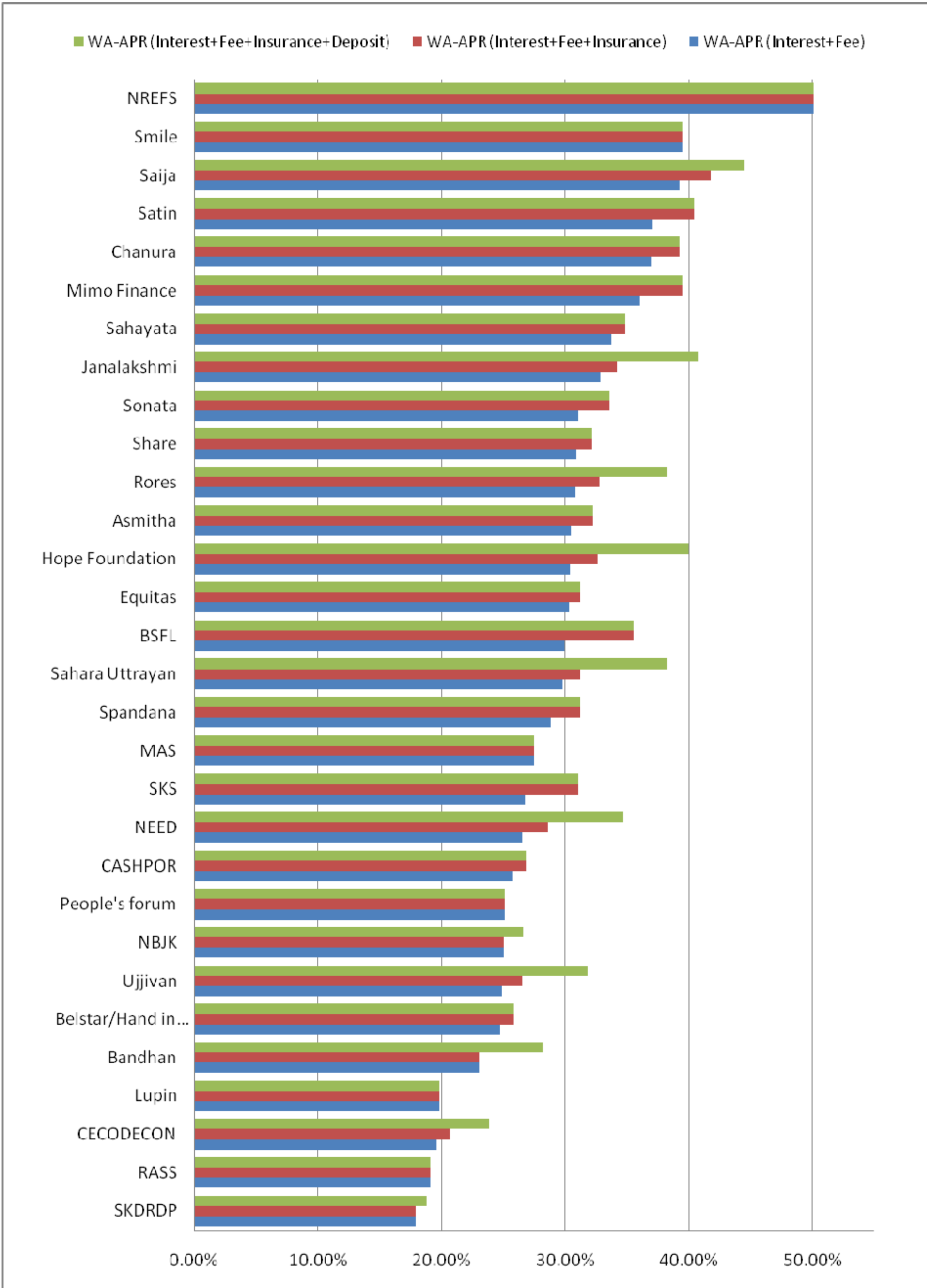


FIGURE 6: WEIGHTED AVERAGE APRS OF SAMPLED MFIS

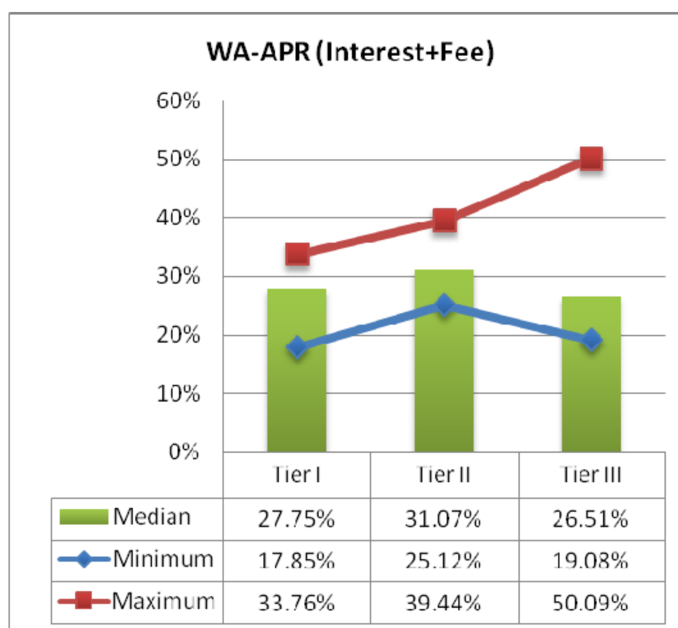
It can be observed in **Figure 6** that

i. Wherever security deposit is charged, there is a significant increase in the cost to the client (in terms of the APRs)
ii. The difference in the size of the WA-APR (Interest + Fee) and WA-APR (Interest + Fee + Insurance) represents incremental effect on APRs due to insurance charges. It can be seen that some MFIs such as CECOEDECON, Cashpor, Hand in Hand and Equitas offer a credit insurance at considerably lower prices, whereas BSFL, SKS, Spandana, Satin, Mimo Finance, are amongst the MFIs who offer more expensive credit insurance.

It is therefore clear that some of the MFIs have been charging the client with a considerably costlier insurance premium. While it is possible that the benefits associated with these costlier insurance products are proportionately higher; nevertheless being a mandatory (or deemed to be) component of the loan product, its adds to the effective cost borne by the client.

APRs across different Tiers

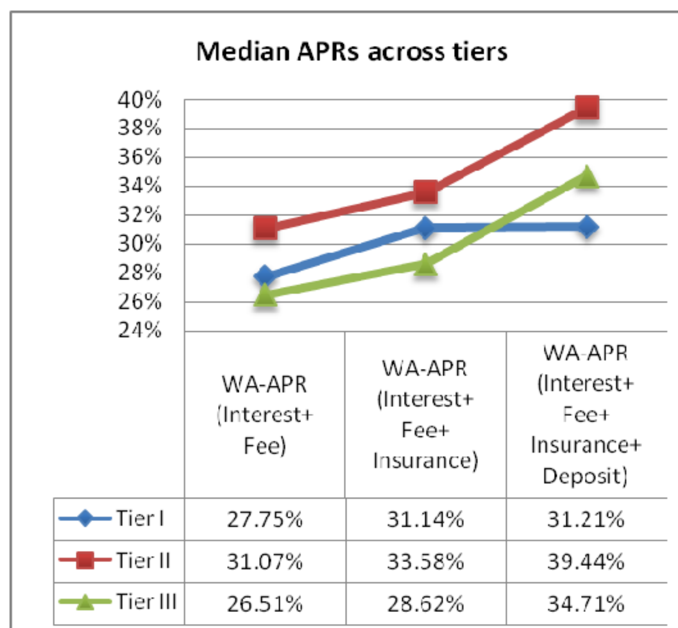
Figure 7 shows the variation in the APRs across different tiers of MFIs in terms of APR spread (difference between maximum and minimum APR) and maximum and median APRs. It is evident that Tier-I and Tier-III MFIs are very close to each other in terms of median APRs[4] (26.25% and 26.51% respectively). However, APRs of Tier II institutions were found to be higher (31.07%). Tier-I MFIs leverage the economy of scale and have relatively easier access to capital while Tier-III institutions (consisting the smaller, mostly the not for profit MFIs) have access to grants to both cover operating costs and as low cost on lending funds. The WA-APR varies from 17.85 to 33.76% in case of Tier-1. However, SKDRDP seems to be an outlier here with the lowest APR in the category. Without considering the APRs of SKDRDP the APR spread (Maximum – Minimum APR) of the category shrinks down from 15.91% to 10.71%.



	Tier I	Tier II	Tier III
Median	27.75%	31.07%	26.51%
Minimum	17.85%	25.12%	19.08%
Maximum	33.76%	39.44%	50.09%

FIGURE 7: WA-APR (INTEREST+FEE) ACROSS DIFFERENT TIERS OF MFIS

In case of Tier-III, the median APR is skewed toward the lower end of the APR spread. This is because of the unusually high APR of NEREFS (50.09%). NEREFS caters to the clientele in difficult geographies (Northeast and other hilly areas). The high costs of operating in tough geographies coupled with lack of infrastructure (bad roads, lack of power and poor banking services) explains the high APR of NEREFS. Without considering the APRs of NEREFS the APR spread of the category shrinks down from 31% to 20% with maximum APR being 39.2%.



	WA-APR (Interest+ Fee)	WA-APR (Interest+ Fee+ Insurance)	WA-APR (Interest+ Fee+ Insurance+ Deposit)
Tier I	27.75%	31.14%	31.21%
Tier II	31.07%	33.58%	39.44%
Tier III	26.51%	28.62%	34.71%

FIGURE 8: APRS ACROSS TIERS

[4] The **Mean WA-APR** refers to the average (sum of the values divided by the number of values) of sample WA-APRs under consideration whereas **Median WA-APR** can be described as the numerical value separating the higher half of a sample of WA-APR, from the lower half. The median of a finite list of numbers can be found by arranging all the observations from lowest value to highest value and picking the middle one. If there is an even number of observations, then there is no single middle value; the median is then usually defined to be the mean of the two middle values. Hence the Median WA-APRs have been considered for comparison across all categories.

With outliers being excluded, we can say that normally different tiers of these 30 MFI offers the microcredit credit in the following APR ranges (excluding insurance and security deposit):

i. Tier-I : (23%-34%)
ii. Tier-II : (25%-40%)
iii. Tier-III : (19%-39%)

The median APRs across different tiers, (at all three levels of APR calculations) can be seen in **Figure 8**. It is evident that while the APR increases as the different components of pricing (Insurance and security deposit) are included. However, in case of Tier I the incremental effect due to security deposit is negligible and therefore it can be concluded that most Tier I MFIs do not collect security deposit.

The variation in APR across tiers can be attributed to the following points:

- Tier-II Transaction cost is very high (around 500 basis points) as compared to Tier-I and Tier-III.
- Tier-II Financial Expense Ratio is higher (around 200 basis points) as compared to Tier-I and Tier-III.

APRs across different Legal Forms

Figure 9 shows the variation in the APRs among the "For profit" and "Not for Profit" MFIs. It is evident that the median APR of for profits is almost 500 basis points higher than the median APR of the Not for profits and the microfinance loan from For Profit MFIs is around 20% costlier than those from the Not for profits. The Not for Profit institutions do not charge fees on the loans provided to their clients whereas the For Profit institutions charge a fee of 1-2% of the loan amount.

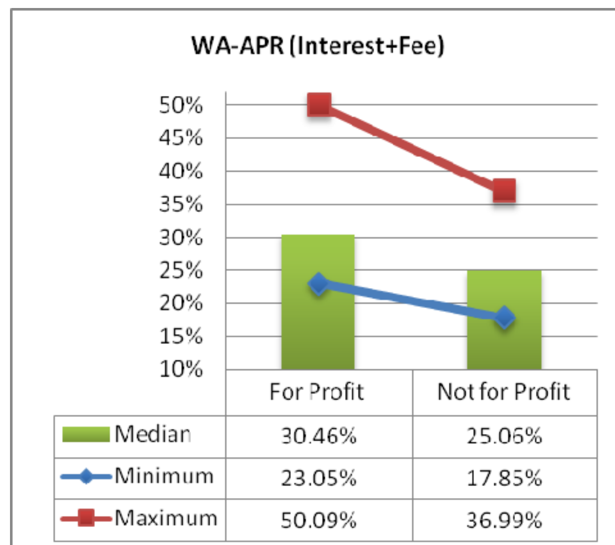


FIGURE 9: APRS ACROSS DIFFERENT TIERS OF MFIS

Though the Financial cost ratio is not varying across different legal forms, Not For Profit MFIs (primarily NGOs)have considerably lower OERs (Discussed in the Transaction Cost section of this report) as compared to For Profit MFIs which can be attributed to the variation in APR across legal forms. The low OERs were attributable to microfinance activities being one amongst the many other activities of the NGOs resulting in lower OERs to the Not for Profits (as the transaction costs are shared by different project activities)

APRs across different Lending Models

From **Figure 10**, it can be seen that the SHG methodology is a lending model to provide relatively cheaper credit to the client. The APRs across all three levels show a steep decline in APRs of SHG model as compared to JLG / Grameen methodology.

This decline can be explained by the relatively lesser cost of client acquisition in SHG model. Out of the 10 MFIs following SHG methodology 8 are Not For Profit MFIs. Majority of the SHGs these MFIs lend to are pre-formed (either for the SHG Bank Linkage Programme or formed under the some other core development

activity of the institution, for which grant support has been available). In such cases, the cost of client acquisition is lower.

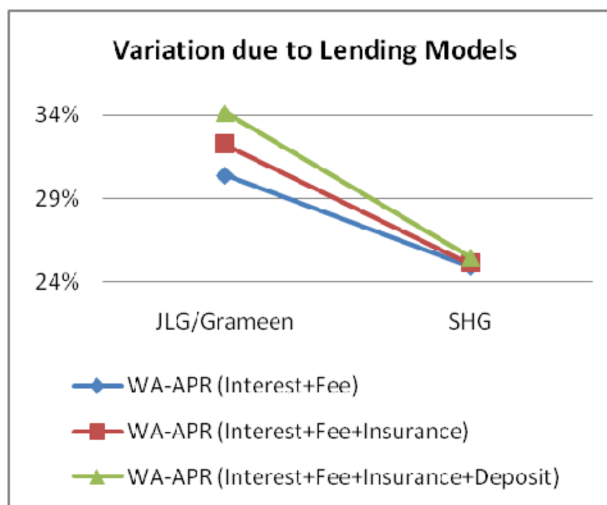


FIGURE 10: APRS ACROSS DIFFERENT LENDING MODELS OF MFIS

Also as discussed above, NGOs microcredit transactions share costs with other Programme activities and this result in lower OERs due to the total transaction costs being apportioned amongst different programmes. It was found that the Median OER (7.9%) of MFIs with SHG based models was significantly lower than the median OERs of the MFIs with JLG (16.8%) and Grameen (11.4%). These lower transaction costs are this difference in the OER explains the difference in the APRs of these delivery models.

Though the APRs of the SHG based MFIs were found to be significant lower than that through other models, these MFIs have relatively smaller outreach. The average outreach of the MFIs with Non SHG model was almost five times higher than that of the SHG based MFIs.

APRs across different Geographic regions

While analyzing the APRs in the geographic context it has to be understood that some MFI operate in a single state/region whereas some operates in multiple states/regions. Therefore while comparing the APRs across different geographic states/regions, such MFIs operating in multiple states/regions are to be included in more than one category of regions. Based on this assumption, the **Table 7** shows the categorization of the sampled MFIs for geographic comparison of APRs.

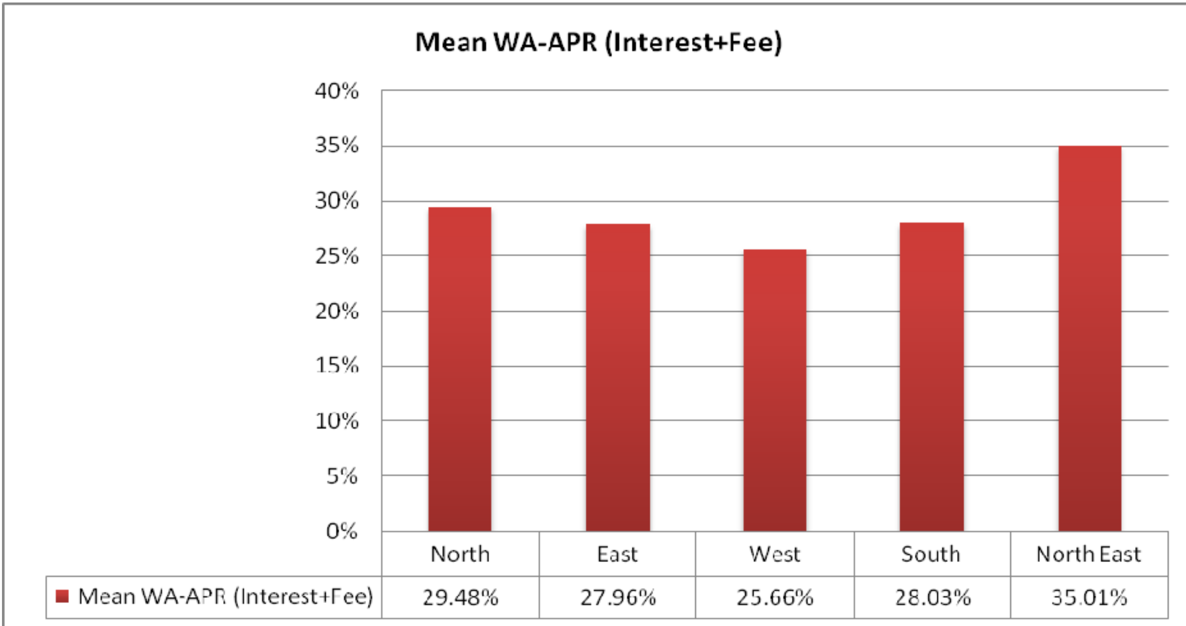
TABLE 7: GEOGRAPHIC PRESENSE OF MFIS

	Regions				
MFI	**North**	**East**	**West**	**South**	**North East**
Asmitha	*	*	*	Yes	
Bandhan	Yes	Yes	Yes		Yes
Hand in Hand				Yes	
BSFL	Yes	Yes	Yes	Yes	Yes
CASHPOR	Yes				
CECODECON			Yes		
Chanura					Yes
Equitas			Yes	Yes	
Hope Foundation				Yes	
Janalakshmi				Yes	
Lupin			Yes		
MAS			Yes		
Mimo Finance	Yes				
NBJK		Yes			
NEED	Yes				
NEREFS					Yes
People's forum		Yes			
RASS				Yes	
Rores				Yes	
Sahara Uttrayan		Yes			
Sahayata	Yes		Yes		
Saija		Yes			
Satin	Yes				
Share	*	*	*	Yes	
SKDRDP				Yes	
SKS	Yes	Yes	Yes	Yes	
Smile				Yes	
Sonata	Yes				
Spandana	*	*	*	Yes	
Ujjivan	Yes	Yes	Yes	Yes	

* Data unavailable

Since different geographic regions have an overlapping set of MFIs, the geographic comparison of APR is not the comparison among the MFIs but the comparison of different geographic submarkets based on the available microcredit products from different MFIs.

Figure 11 shows the geographic variation in APRs:



	North	East	West	South	North East
Mean WA-APR (Interest+Fee)	29.48%	27.96%	25.66%	28.03%	35.01%

FIGURE 11: REGIONWISE APRS

As seen in **Figure 11** above North East region has the highest APRs which is attributable to the high transaction costs for operating in that region.

APR VS YIELD ON PORTFOLIO

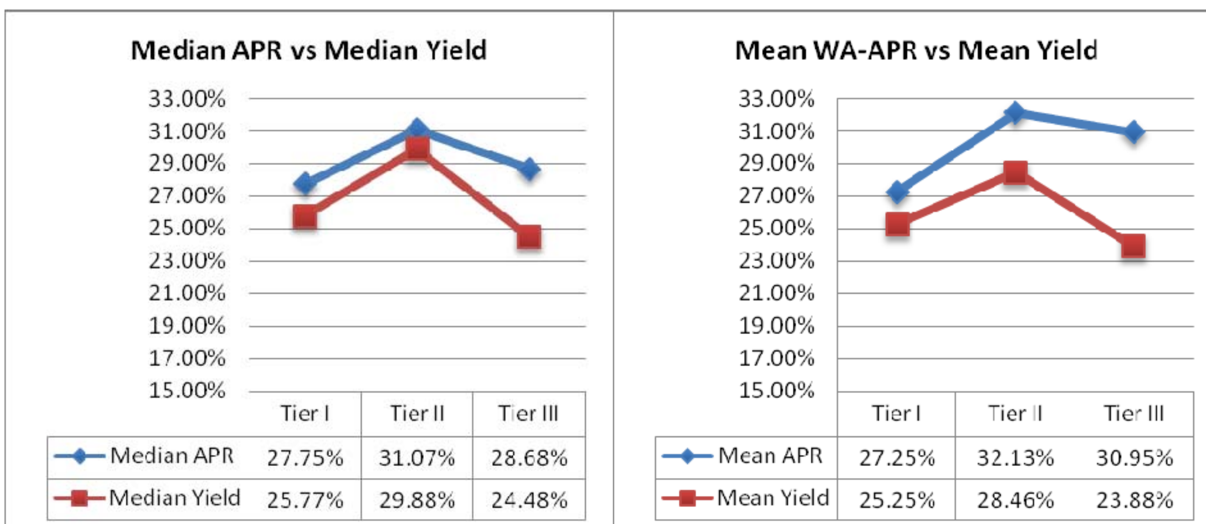


FIGURE 13: MEDIAN APRS VSMEDIAN YIELD

FIGURE 12: MEAN APR VS MEAN YIELD

Figures 12 and 13 show the variation in portfolio yield w.r.t. weighted average APR (Interest + Fee) across different tiers of MFIs. It is evident that though the portfolio yield follows the same trend as APR, it is lower than the APR. The same trend was indicated in both the Mean and Median Figures.

This signifies that the portfolio yield is not an effective proxy for pricing. It can be used to see a trend similar to pricing. However, the nominal figures of Portfolio yield cannot be used as the replacement of the exact APRs.

It also found that though the portfolio yield is always below the APR, the gap between portfolio yield and APR increases in Tier III MFIs due to the steeper decline in the portfolio yield compared to the APR. This increased gap indicates that

i. Some of the Tier III MFI may have late recovery of interest that is causing the steeper decline in the Portfolio yield.
ii. Most of the Tier III MFIs (mostly Not for Profits) are yet to develop a robust cash management system which can minimize the idle cash. Inefficient fund management reduces the turnover of funds resulting in lower portfolio yield.

BROAD BREAK-UP OF THE COMPONENTS OF THE INTEREST RATE

During the study, 51 products were studied in the 30 MFIs visited across the country. Using the pricing components of these 51 products average distribution of the product pricing has been calculated and presented below:

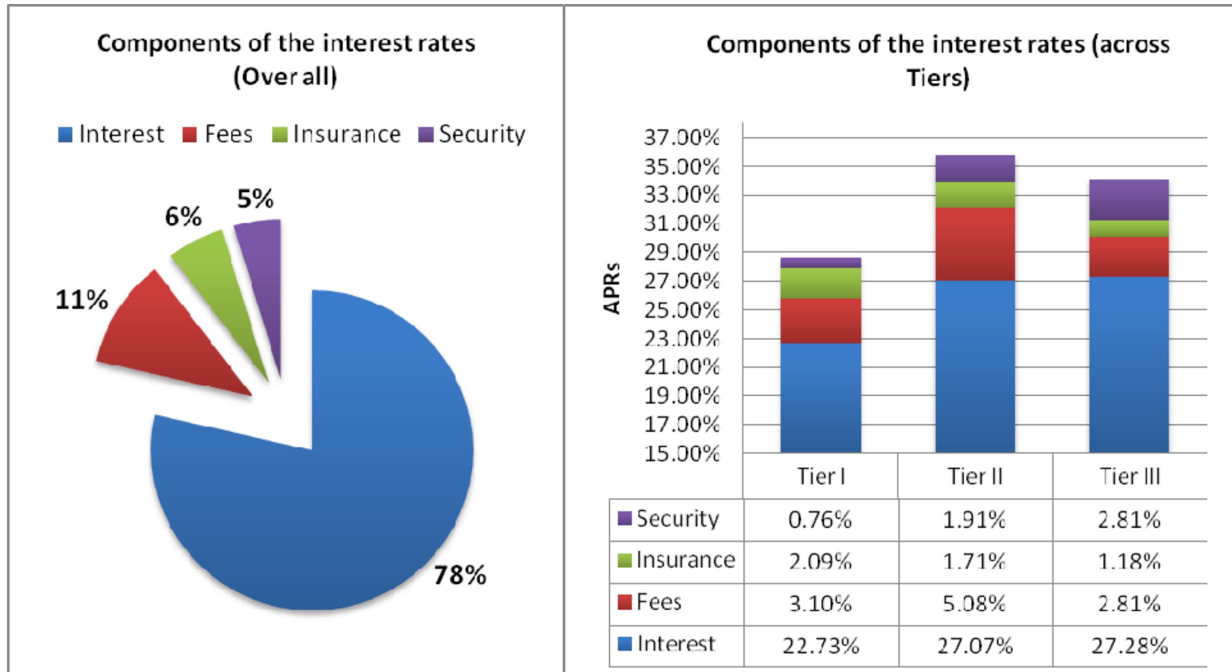


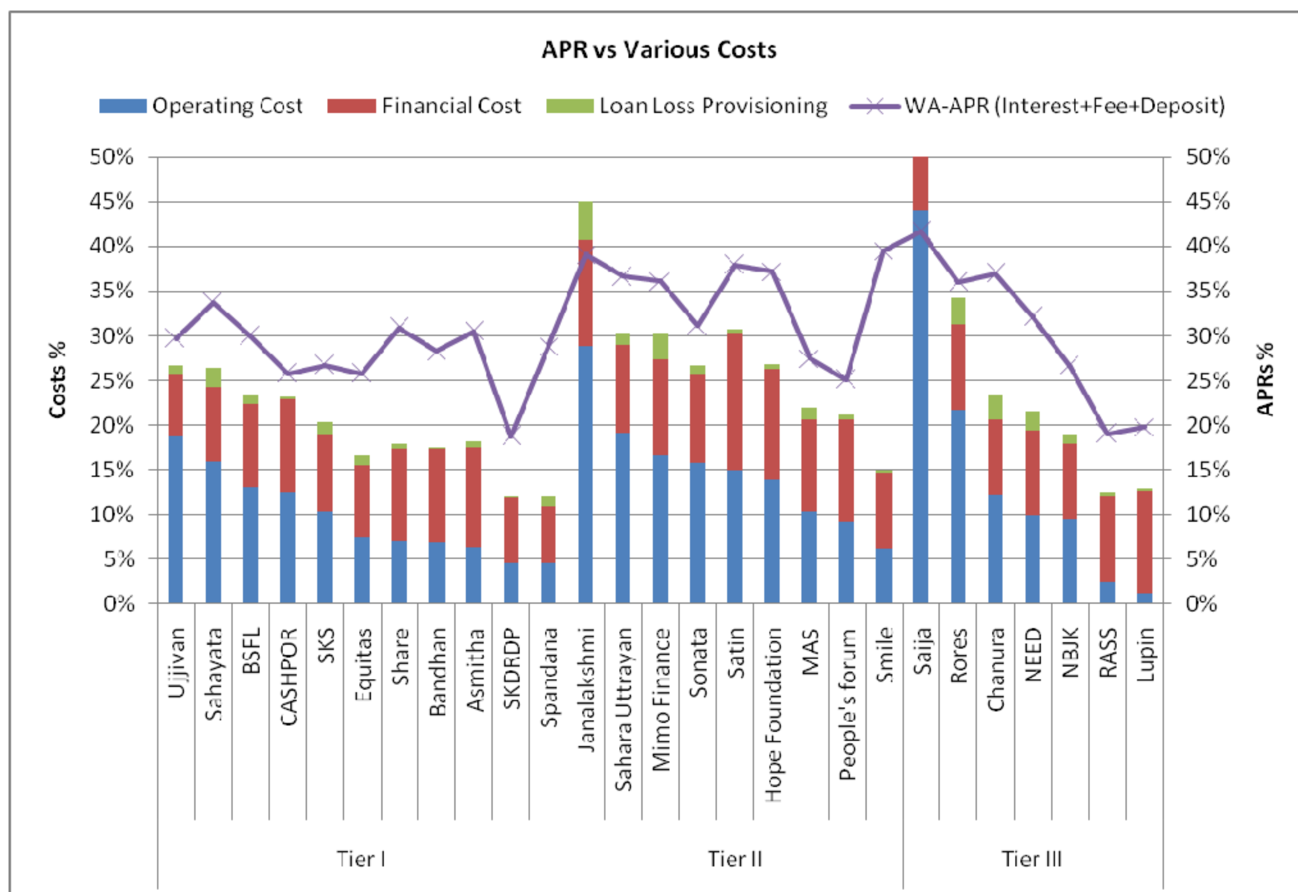
FIGURE 14: COMPONENTS OF THE INTEREST RATES (OVER ALL AND ACROSS TIERS)

Figure 14 shows the broad break-up of APRs in terms of the following four components:

i. Interest
ii. Fees
iii. Insurance Charges
iv. Security/Cash Deposit

This breakup is calculated using the average figures of the entire data set in the pie chart. The bar graph however also shows the distribution (incremental effect on APR) of different components across different Tiers of MFIs. It can be seen in the **Figure 14** that:

- In Tier-1 MFIs the average incremental effect of security deposit on APR is only 0.76% (76 basis points) which signifies that not many MFIs adopted the practice of collecting the security deposit.
- In Tier – II, the average incremental effect of fees on APR is relatively high (5.08%).



APR VIS-À-VIS VARIOUS COSTS

The above graph shows the different costs i.e. Financial Cost, Operational Cost and Loan Loss provisioning as the component of APRs for the sampled MFIs. It can be seen that the APRs[5] does not follow the trend of the total costs. This comparison was done to understand the pattern across MFIs.

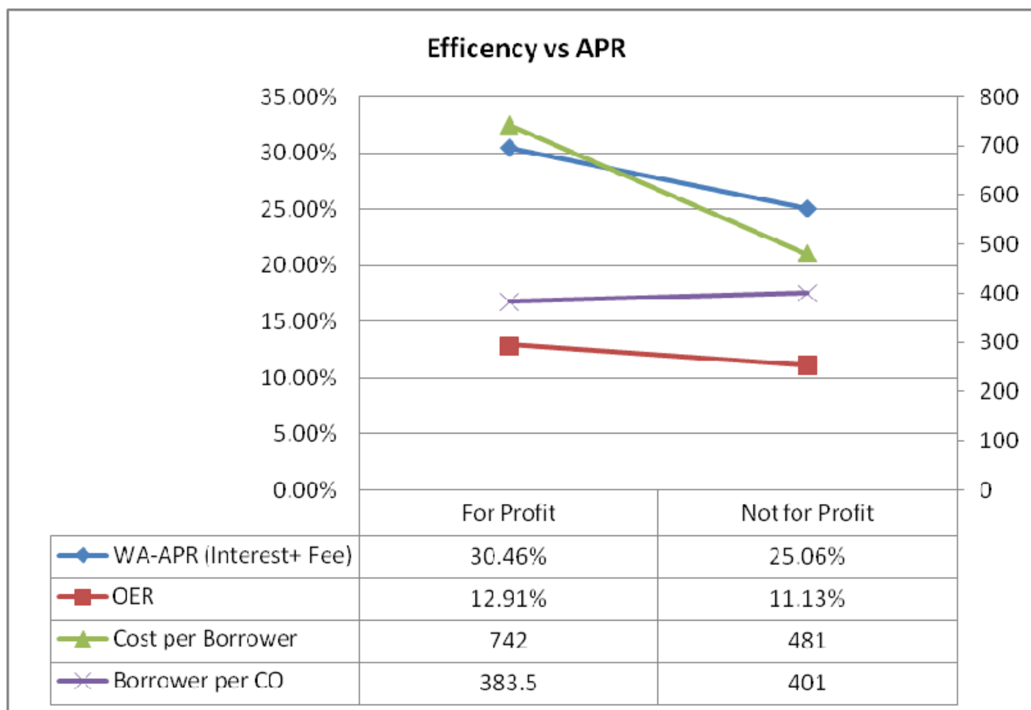
These MFIs are arranged tier wise in the reducing order of the total costs. The graph clearly shows that while the Tier-II MFIs had higher APRs, they also proportionally incurred higher costs. Tier-III MFIs had a significant variation in the APR and in the total costs as well. In Tier-I, though the APRs were relatively lower, majority of the MFIs incurred lower costs as well.

However, each of these two categories had few MFIs for which the gap between the APRs and the total costs was considerably high. Tier-I, II and III had 4, 2 and 2 MFIs for which the APR was is over 10% (1000 basis points) above the total costs. Two of the MFIs were also found to have operating with the negative margin. So while some of the MFIs maintained reasonable margins, some of the MFIs were in a position to reduce their interest rates.

[5] Since the security deposits (being interest free funds) reduces the cost of funds, for the purpose of this comparison, APR including the effect of security deposit i.e. WA-APRs (Interest + Fee + Security Deposit) were used.

It was found that the average Financial costs, Operating cost, and Loan loss provision for the entire sample were 9.32%, 12.29% and 1.11% resulting in a total cost (excluding margins) of 22.72%. This indicates that the RBI recommendation of 26% interest rate with 1% processing fee (equivalent to an APR of 28.07%) is a viable proposition for Indian MFIs.

EFFICIENCY INDICATORS VS APR



	For Profit	Not for Profit
WA-APR (Interest+ Fee)	30.46%	25.06%
OER	12.91%	11.13%
Cost per Borrower	742	481
Borrower per CO	383.5	401

FIGURE 15: EFFICIENCY VS APR

In order to understand the co-relation between efficiency and interest rate charged to the clients, analysis across three efficiency indicators (Operating Expense Ratio-OER, Cost per Borrower and Borrower per CO) with the Weighted APR across For Profit and Not for Profit institutions was done. **Figure 15** illustrates that as the costs increase, the APR of the institutions increases and as the number of borrowers per CO increase, the APR of the institutions decrease. The APR has a direct relationship with costs and inverse relationship with borrower per CO.

COMPARISON WITH GLOBAL AND REGIONAL BENCHMARKS

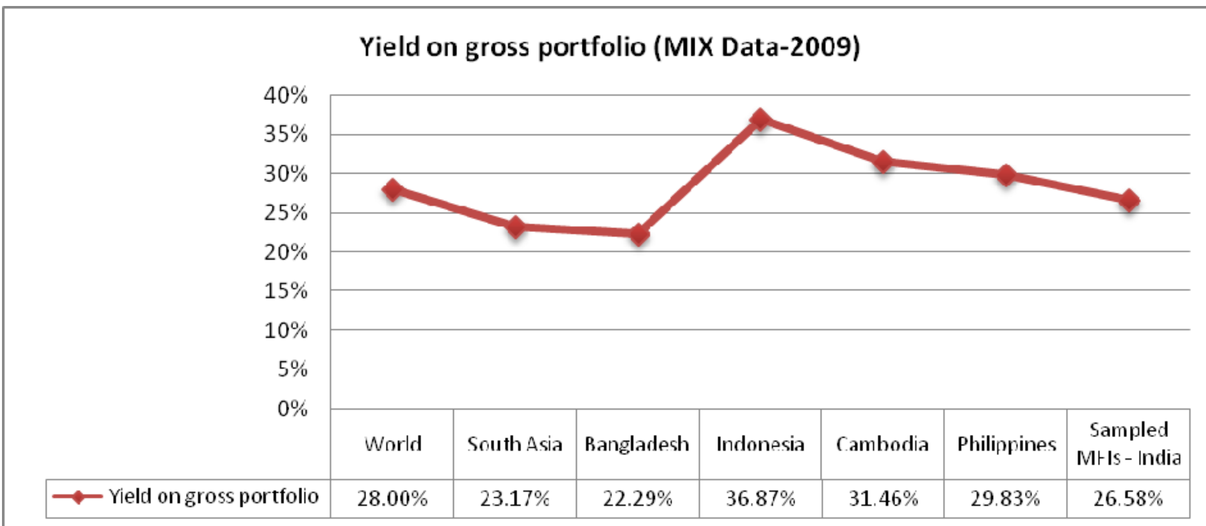


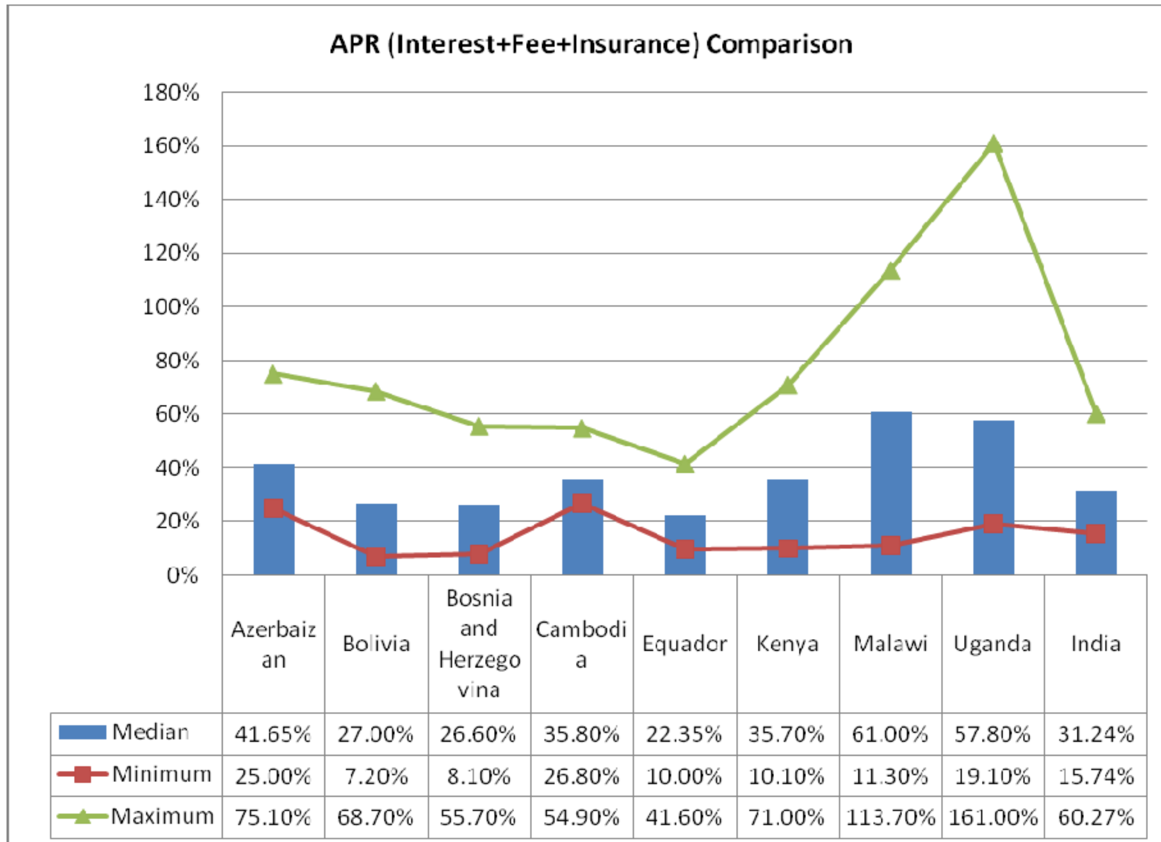
FIGURE 16: YIELD ON GROSS PORTFOLIO (MIX DATA-2009)

Since the comparable APRs are not available except for Cambodia in Asia, Nominal portfolio yield was used as a proxy for interest rate pricing as it represents the approximate inclusive cost to the client**. Yield on portfolio is usually lower than the APR, but it is still a useful indicator for comparison.**

Bangladesh and India have registered significant growth in micro finance portfolio in last 5 years. MIX data, on the trend in yield on portfolio over last 5 years indicate that, Bangladeshi institutions are reducing their yields while Indian institutions have raised them. MFIs in Bangladesh have a lower cost of capital due to access to subsidized loan funds from PKSF, whereas Indian institutions are much more susceptible to increasing cost of funds. However, as shown in **Figure 20**, the sampled MFIs though have a relatively higher YoP than that of the South Asia it is still lower than that of the global median figure and considerably lower than that of other comparable markets like Indonesia, Cambodia and Philippines.

APR COMPARISON ACROSS DIFFERENT COUNTRIES

Except India and Cambodia, APRs are not available for any other Asian countries. However, Microfinance Transparency has published the APRs for few other countries which have been used for comparison6 in **Figure 21**:



	Azerbaizan	Bolivia	Bosnia and Herzegovina	Cambodia	Equador	Kenya	Malawi	Uganda	India
Median	41.65%	27.00%	26.60%	35.80%	22.35%	35.70%	61.00%	57.80%	31.24%
Minimum	25.00%	7.20%	8.10%	26.80%	10.00%	10.10%	11.30%	19.10%	15.74%
Maximum	75.10%	68.70%	55.70%	54.90%	41.60%	71.00%	113.70%	161.00%	60.27%

FIGURE 17: APR COMPARISAN ACROSS COUNTRIES

It can be seen in **Figure 21** that while the Median APR (Interest + Fee + Insurance) of the 9 countries shown in the figure varies from 22.32% to 61.00%, the average median APR (Interest + Fee + Insurance) comes out to be 37.68%. The median APRs of the studied Indian MFIs are well below the average median APRs among the other countries. Only three countries (Bolivia, Equador, Bosnia and Herzegovina) show lower APRs than that of the India MFIs.

[6] Median figures of the entire data set for different countries (available at Microfinance Transparency's website) have been used for comparison.

Based on the above analysis, following are the major conclusions:

1. *There is a need to review the compulsory insurance products offered by some of the MFIs, (mostly the For Profit Tier I MFIs) who have been charging relatively high for the compulsory credit insurance. However, with the recent RBI guidelines issued regarding the insurance premium to be directly paid to the insurance provider, this cost of compulsory credit insurance is likely to reduce since the MFIs would not be allowed to charge any processing or administration charges for providing such an insurance product.*
2. *Higher transaction costs and higher financial cost for the Tier II institutions has resulted in relatively higher APRs in this category of institutions. Moreover, the Tier II institutions have very little margin due to their investments in expansion. These institutions are in their growth phase and have already invested in expansion. A little impetus provided in the form of grants for capacity building and equity or low costs funds for expansion, to these institutions can show results in reaching more number of clients and higher loans outstanding.*
3. *MFIs following the SHG model charge lower APRs; 80% of the MFIs following this model are not for profits. There is significant operational cost reduction due to monthly collection process, apportionment of costs amongst multiple programme activities as well as lower profit margins expected by these MFIs.*
4. *The APR reduces as the institution achieves scale. This has been observed for the Tier I institutions where the APR is lowest for the minimum and maximum APR across products. Tier I institutions have scope for offering lower APRs to clients.*
5. *APRs of Indian MFIs fall in a mid range (neither the lowest nor the highest) of the APRs when compared to eight other countries (for which APR were available). However, the APR of Indian MFIs was less than the average APRs of other countries.*

5. Transaction Costs

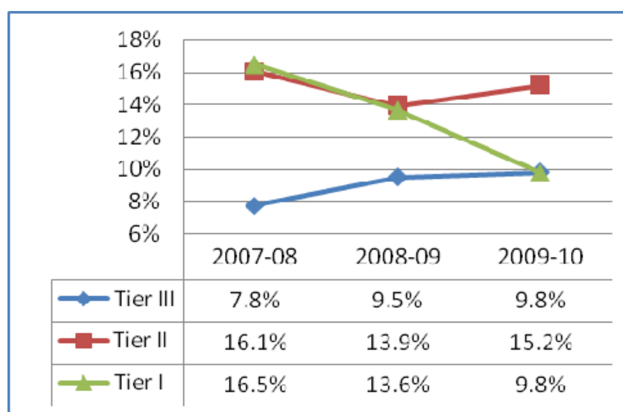
Microfinance is a human resource intensive service delivery model and transaction costs tend to be higher than other financial service providers since average loan sizes are small and services are usually delivered at doorstep. Transaction costs or operating costs in MFIs are typically driven by the lending model (Grameen/JLG/SHG/individual), average loan sizes, the processes of client acquisition and servicing practices of the institution. The two major sub components of Operating costs are Personnel or staff costs and administrative expenses (office rent, transport, utility charges, office supplies and depreciation of fixed assets).

Around 67% (20 out of the 30) of the sampled institutions follow either Grameen (13) or Joint Liability Group (7) as the core lending methodology and the remaining institutions follow SHG methodology. Grameen methodology characteristically has standard practices in member mobilization, group and center formation[7], in basic compulsory orientation training and recognition of groups, KYC completion, standard procedures of loan approval, sanction and disbursement. Repayment collections are done weekly at centre meetings. This standardization enables these MFIs to be more efficient.

The analysis presented below is based on the data of 28 MFIs. Hand in Hand (Chennai) and CECCODECON (Jaipur) are not included due to unavailability of disaggregated cost data for microfinance and other development activities.

OER in Tier I, Tier II and Tier III MFIs

Figure 23 shows sharp decline in Operating expense ratio for Tier I MFIs over the last three years in comparison to Tier II and Tier III MFIs. This infers the impact of outreach and high operational efficiency in reducing the OER for Tier I MFIs. Few Tier I MFIs such as Equitas, Sahayata and Ujjivan have initiated operations in the last three years and have achieved exponential growth in outreach and loan portfolio with higher operational efficiency.



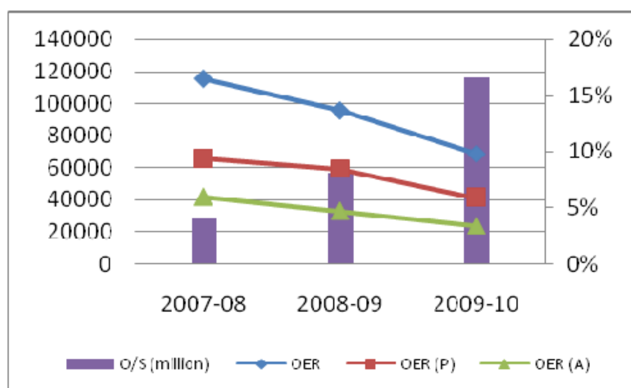
	2007-08	2008-09	2009-10
Tier III	7.8%	9.5%	9.8%
Tier II	16.1%	13.9%	15.2%
Tier I	16.5%	13.6%	9.8%

FIGURE 18: OPERATING EXPENSE RATIO ACROSS TIERS

Equitas and Sahayata have grown at 2700% and 2870% respectively in terms of client outreach over the last three years (March 2008 to March 2010). Moreover, they have invested in technology and systems to increase efficiencies which have in turn lead to the decrease in OER over the years. The OER of Equitas has reduced from 41.31% on 2008 to 7.58% in 2010; similarly, the OER of Sahayata has reduced from 107.5% in 2008 to 15.9% in 2010.

[7] Groups consist of 5 members and organizing 8-10 groups into a centre with respective group leaders and centre leaders

FIGURE 19: OPERATING EXPENSE RATIO IN TIER-I



Further break-up of OER into personnel and admin costs for Tier I MFIs shows similar declining trend for both the components of operating costs. Equitas and BSFL has sharp decline in personnel and admin expense from year 2007 to 2008. Other Tier I MFIs show a similar declining trend because of their gradual decline in OER components. The fast growing MFIs such as Sahayata, Equitas and Bandhan have managed to bring down their OER (A) significantly from the year 2007 to 2008. Overall, Tier I MFIs has shown good trend of declining OER in respect to their cumulative loan portfolio from Rs. 28,473 million in 2008 to Rs. 115,796 million in 2010.

Tier II MFIs are mostly comprised of MFIs in growth phase and are investing in and improving their operating systems to increase their outreach. This included Sonata, Janalakshmi, Mimoza Enterprise Finance Pvt. Ltd. and People's Forum. Most of the Tier II MFIs are in transition phase from not for profit to for profit entity and have consistent OER of 16.1% in 2008 to 15.2% in 2010 *(refer **Figure 25**)*. Further analysis of OER (Personnel) and OER (Admin) for tier II MFIs indicates increase in personnel expense from 6.7% to 8.2% in financial year 2009 to 2010. This increase in salary expense is due to recruitment of additional operation staff in the year 2009-10. Sonata and Satin Credit Care have most significant increase in personnel expenses from 2009 to 2010, while other tier II MFIs have shown consistent trend for operational expense. Overall, the increase in OER and specifically OER (P) for tier II MFIs is also reflected in the exponential increase in their portfolio from Rs. 2186 million to Rs. 4698 million.

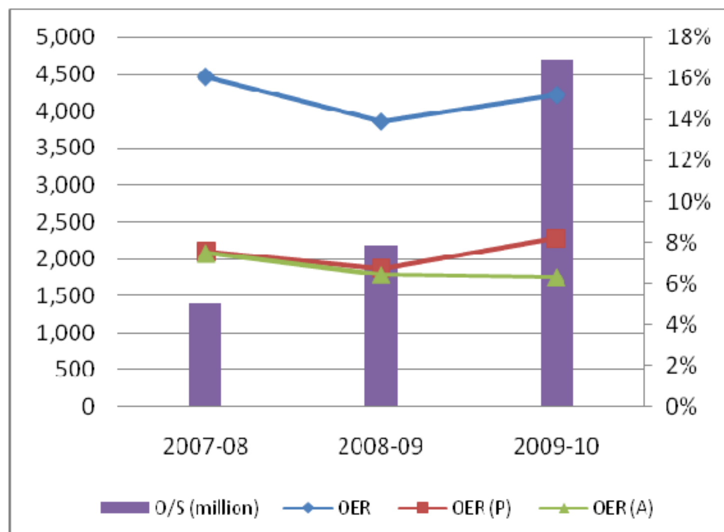


FIGURE 20: OPERATING EXPENSE RATIO IN TIER-II

Out of nine Tier III MFIs studied, seven are NGO-MFIs who have comparatively lower OER for all the three years due to subsidizing the operational costs of their microfinance activities through sharing of staff and infrastructure etc., among different programmes which are grant funded. It has been difficult to arrive at the accurate operational expenses for the microfinance activity in absence of segregated financial data/ clear accounting for expenses in the financial statements produced for micro finance operations. Some of these institutions separate financial statements for micro finance which are not consistent and hence reliable. Lupin Human Welfare &Research Foundation, RASS have the lowest OER of about 2% in this category due to

subsidization. Without including these two institutions (Lupin, RASS), the OER of the Tier III institutions is 18.38%.

The personnel expense ratio for Tier III MFIs shows increase from 3.4% to 5.5% due to expansion in Chanura Microfin, NEED and North East Region Financial Services Ltd., while the admin expense ratios have declined from 3.3% in 2008 to 2.9% in 2010. Rores functioning in Karnataka has witnessed a triple fold increase in operating expenses due to increase staff salaries.

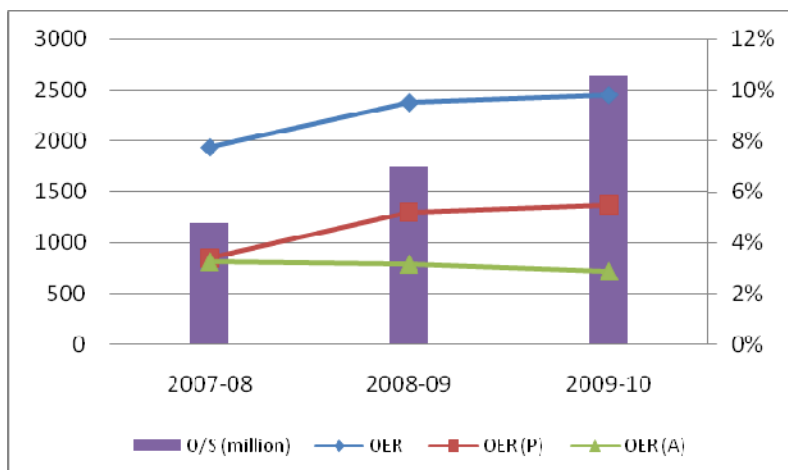
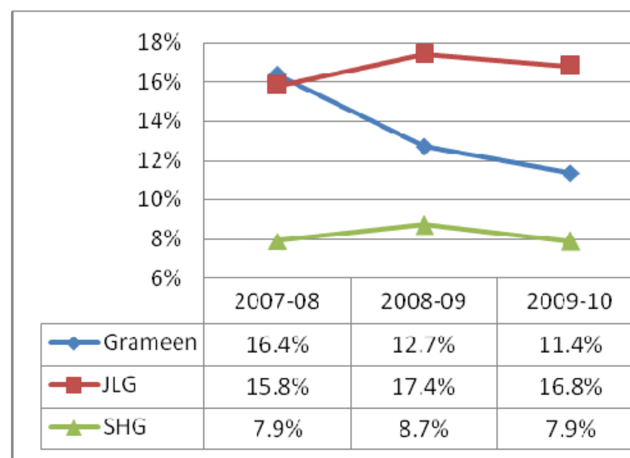


FIGURE 21: OPERATING EXPENSE RATIO IN TIER-III

There is a need to conduct a separate and detailed study on the costs of operations for the institutions catering to the clients in Northeast. The institutions need to be selected across all categories of institutions (tier wise, legal form wise and model wise). During the study, it was observed that the OER of the institutions (NEREFS and Chanura) operating in the northeast region are high due to the costs of providing credit services to their clients. The costs are high due to geographical spread (plains and hills), lack of infrastructure (bad roads, power deficiency and poor banking services) and associated costs like travelling, fuel for power generation. Hence, there is a need to have differential interest rate ceilings for institutions working in under-served and tough areas.

OER FOR DIFFERENT DELIVERY MODELS

The microfinance delivery model influences the operational expenses of MFIs. On the basis of analysis of 28 MFIs from the sample, SHG model has lowest costs of operations due to the operational characteristic of monthly meeting in half of the eight MFIs adopting this model, which reduces the costs of field staff visiting the group once in a month as compared to four times in Grameen or JLG model. This trend also conforms to the lowest pricing of loans of MFIs following SHG model. There is no significant variation in the OER for 7 MFIs following SHG model over the last three years. Apart from that, these MFIs (Lupin, NBJK and NEREFS) are also receiving grant / soft loans from SIDBI, NABARD and other funding agencies for the formation of SHGs and are involved in multiple activities with their microfinance clients. JLG model is followed by 7 MFIs in the sample and is comparatively high OER than Grameen and SHG model due to high operational cost. The OER ratios for these MFIs are also high since three MFIs in this category are in their expansion phase (Satin Credit Care Network Ltd,



	2007-08	2008-09	2009-10
Grameen	16.4%	12.7%	11.4%
JLG	15.8%	17.4%	16.8%
SHG	7.9%	8.7%	7.9%

FIGURE 22: OER ACROSS DIFFERENT DELIVERY MODELS

Janalakshmi Financial Services Pvt. Ltd & Saija Finance Pvt. Ltd.). The OER for the MFIs adopting Grameen model shows a sharp decline from 16.4% in 2008 to 11.4% in 2010. Grameen model is considered to be the most efficient model in microfinance and can achieve vast outreach in short span of time due to standardized systems and procedures. The 13 MFIs in the sample adopting Grameen model and mostly comprised of the entire Tier I MFIs. The decline in the OER for Grameen model can be deciphered as efficiency level achieved by some large MFIs like Bandhan, Equitas, Sahayata, among others.

OER ACROSS DIFFERENT LEGAL FORMS

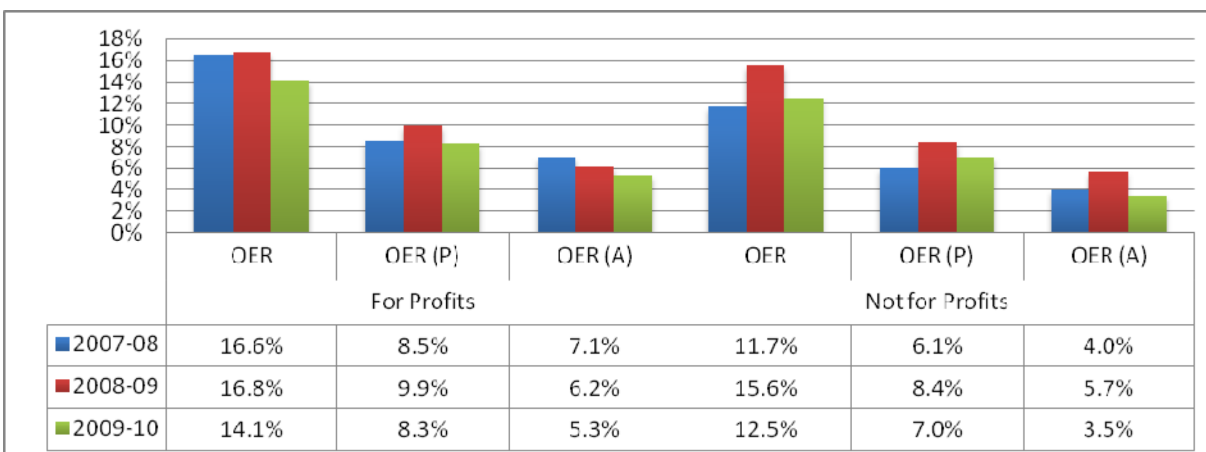


FIGURE 23: OER ACROSS DIFFERENT LEGAL FORMS

The OER of all institutions across legal forms shows the same trend in terms of reduction from Year 1 to Year 3. This is because of the scale achieved by the institutions during the last three years. **Figure 28** also shows that personnel expenses [OER (P)] in 2008-09 is more than the other two years due to the retention costs (in terms of higher salaries) to combat competition among MFIs.

OER ACROSS DIFFERENT REPAYMENT FREQUENCIES

The operating cost across different repayment frequencies (weekly, fortnightly and monthly) was compared based on the repayment frequencies offered by MFIs. **Figure 29** clearly shows that fortnightly repayment frequencies have the lowest operating costs. However, the lower costs of operations for institution offering fortnightly frequencies cannot be attributed to repayment frequency only because Equitas is an institution which has invested in technology (OMR based membership form, pre-printed payment stickers, real time collection and attendance monitoring, cash handling by external agency, among others) and operational systems

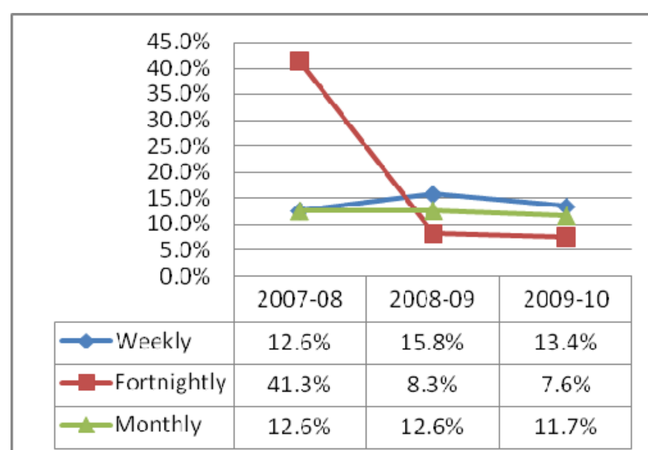
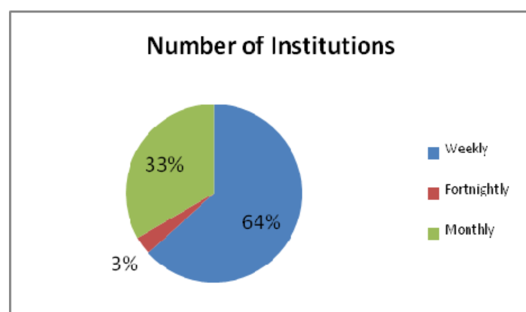


FIGURE 24: OER OF DIFFERENT REPAYMENT FREQUENCIES



(loan origination and loan collection done by separate staff, two-year loan, among others), which has an effect on the operational costs. The operating costs for institutions offering monthly repayment frequencies has been consistent over the years, whereas the institutions offering weekly repayment frequencies had a increase in Year 2 due to the expansion plans and investments in HR and branch costs during this year. The institutions (10) offering monthly repayments are a mix of all the categories including scale, models, legal form and operational area whereas the institutions (19) offering weekly repayment frequencies were primarily Tier I, Grameen and For Profit Institutions. Only one institution (Equitas) formed part of the institution offering fortnightly frequencies.

Further analysis of break-up of the OER into OER (P) and OER (A) shows the same trend across repayment frequencies.

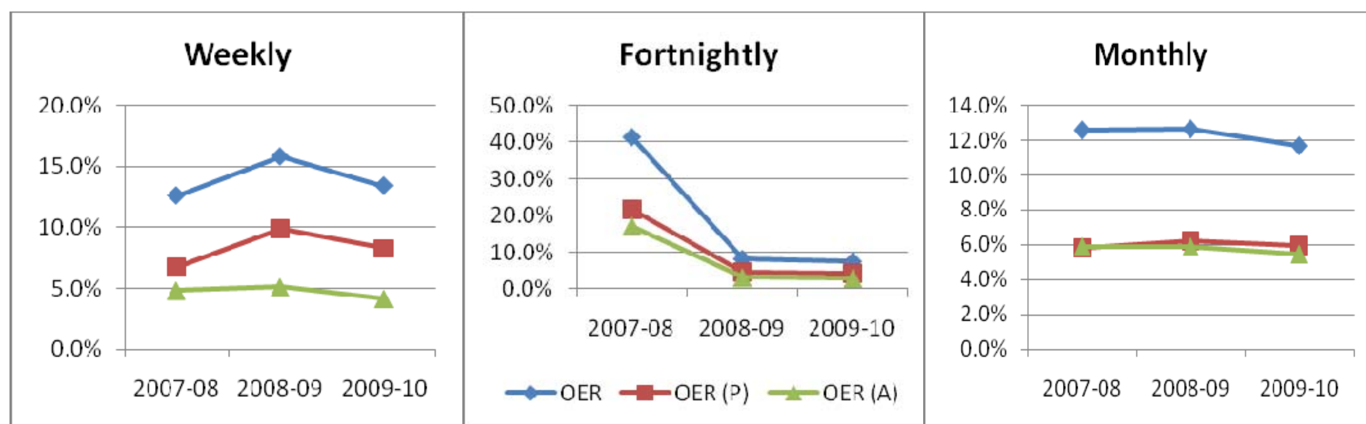


FIGURE 25: OERS FOR DIFFERENT REPAYMENT FREQUENCIES

The analysis across different repayment frequencies clearly shows that the institutions following weekly repayment frequencies has the maximum OER and institutions following fortnightly and monthly repayment frequencies have a lower OER. With the RBI guidelines issued and over emphasis of decreasing costs, there are chances that the institutions following weekly frequencies would change to fortnightly or monthly installment repayment system. This would have a direct impact on the costs of the institutions since field / credit officers visiting and travelling to the clients would be limited to 'one' and not 'four-five' per month. However, a balance need to be created between 'quality time' provided to the clients vis-à-vis 'costs incurred'.

6. Cost of Funds

Cost of funds is a significant component of the overall expenses of a financial institution. It drives the costs of providing credit services to the poor and subsequently the determination of pricing of loans for the clients. The funding pattern in Indian microfinance has been dominated by commercial debt (70% of total funds in 2010) over the past few years. Other sources of funds include portfolio securitisation (off balance sheet lending), savings (only one institution in sample), paid in equity and no cost sources such as grants and security deposits.

Based on discussions with the MFIs and few of the financial institutions, models of microfinance delivery and geographical area of operations had very less influence in their decision of lending since they were more concerned with the capacities, systems and processes of the institution. Hence the analysis across models of delivery and geographical area was not done for cost of funds for the MFIs.

The following section presents an analysis of the **financial expense ratio** of sample MFIs.

Cost of Funds across Legal Forms

The costs of funds for 'for profit' institutions in this study was more or less uniform across the last three years whereas the cost of funds for the 'non profit' institutions was lower in 2007-08 due to the availbility of revolving loan funds / cheaper source of credit during the period. Specific exampes include Revolving loan fund of Rs 10 million from SIDBI by NBJK and access to individual donations and low interest funds by Chanura Microfin and low cost funds mobilised by RASS. From 2008-09 onwards, financial expense ratio for non profit institutions rose higher since the availability of grants and low costs funds has been dwindling, and many MFIs were either commencing operations (Saija and Sahayata) or transitioning into for profit form, leading to higher risk perception of lenders and thereby higher priced onlending funds.

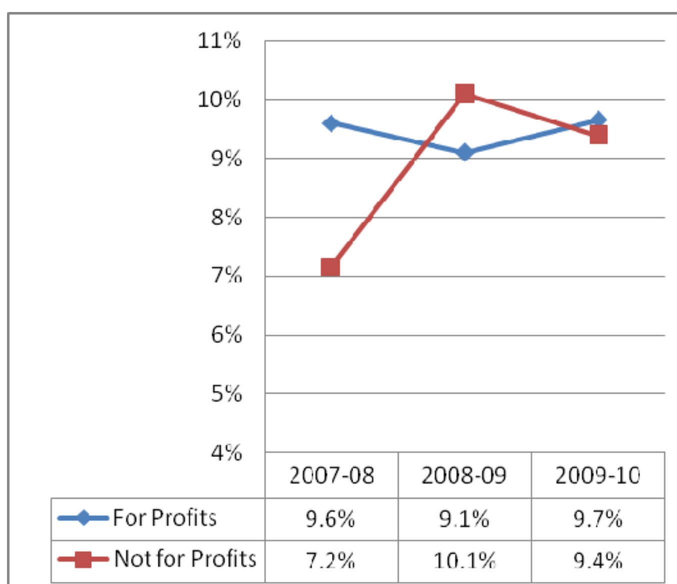


FIGURE 26: COST OF FUNDS BASED ON THE LEGAL FORM

Loans Outstanding versus Cost of funds across Not for Profits

The increase in loans outstanding from Year 1 to Year 2 is directly proportional to the costs of funds in Year 1 and Year 2 whereas the costs of funds reduce as the loans outstanding increases. This is due to the fact that as the MFI achieves scale, the MFIs have seasoned staff in place, and hence the institution is in a better position to bargain with the financial institutions for funds at a lower rate of interest.

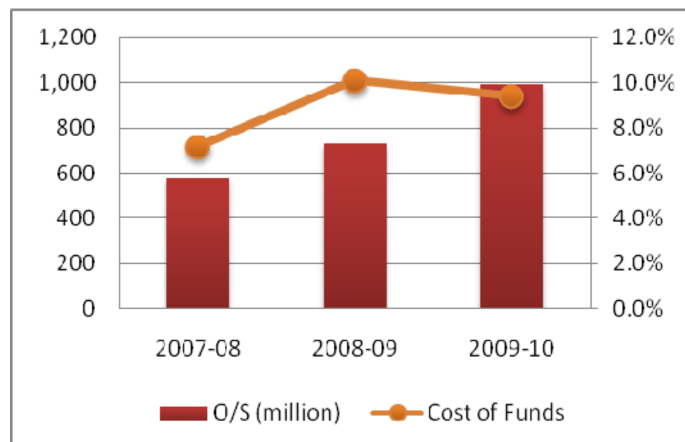
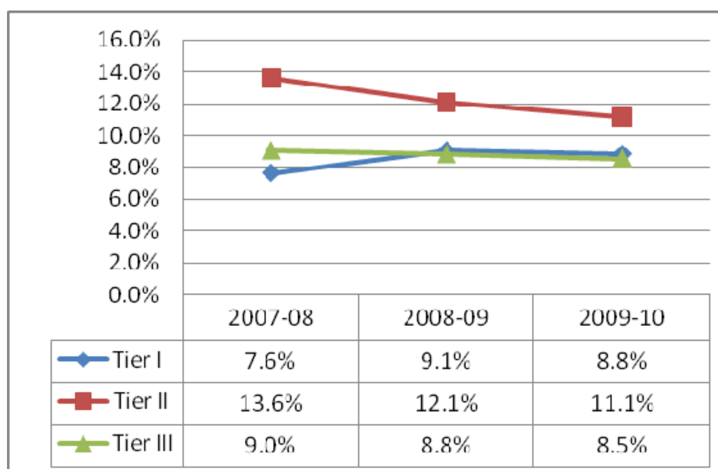


FIGURE 27: LOAN OUTSTANDING VS COST OF FUNDS ACROSS NOT FOR PROFITS

Cost of Funds across Tiers

Figure 33 shows the comparative trend of cost of funds of different Tiers of MFIs. As expected, sample Tier III MFIs, majority of which are non-profit institutions (seven out of nine are non-profit), have the lowest cost of funds, but the cost has steadily increased over the three years due to decrease in soft loans. Additionally, five out of nine Tier-III MFIs are based on SHG model, which attracts availability of loans at lower interest rates from banks and institutional lenders such as Rashtriya Mahila Kosh (RMK) (lending to Lupin and CECODECON @ 8%) and NABARD (lending to NEED @ 6.5%). Tier II MFIs are able to achieve a decline in their cost of funds from 13.6% in 2008 to 11.1% in 2010 with the infusion of equity in this period including in Janalakshmi, Mimoza Enterprise Finance Pvt. Ltd., Sonata, Satin Credit Care and People's Forum. Tier I MFIs in proportion to their portfolio received less equity to influence their cost of funds, significantly. However, the high premium mobilized on shares and the generation of funds and reserves from the operations helped to lower the overall cost. Increase in portfolio buy outs led to lower cost of capital for Tier I and Tier II MFIs in 2009 and 2010. The adjusted and unadjusted FCR across Tier III institutions are mentioned below:



	2007-08	2008-09	2009-10
Tier I	7.6%	9.1%	8.8%
Tier II	13.6%	12.1%	11.1%
Tier III	9.0%	8.8%	8.5%

FIGURE 28: COST OF FUNDS FOR DIFFERENT TIERS OF MFIS

	Unadjusted FCR	Adjusted FCR
2007-08	5.7%	9.0%
2008-09	7.8%	8.8%
2009-10	8.4%	8.5%

Weighted Average Interest Rates

TABLE 8: INTEREST RATE OF FINANCIAL INSTITUTIONS FOR MFIS

Type of Financial Institution	Number of institutions	Interest Rate (Range)
Nationalized Banks	37	9.5-14.5
Developmental Institutions	16	8.0-14.5
Private Banks	15	9.5-15.0
NBFCs	7	12.5-15.0
RRBs	5	9.0-13.5
Total	80	8.0-15.0

As part of the methodology of this study, the sanction letters / term sheets of the financial institutions were studied and it has been observed that a cumulative of 80 financial institutions have been supporting 25 microfinance institutions (5 institutions did not share the details). Based on the sanction letters / terms sheets provided by the microfinance institutions, the weighted interest rates were calculated across each financial and microfinance institution.

The various financial institutions providing funds have been categorized and the range of interest rates charged by these financial institutions is presented in **Table 8**.

The list of the banks under each of the category is mentioned in **Annexure 10. Table 8** clearly shows that the interest rates charged by the financial institutions are in the range of 8.0-15.0%, which has a direct impact on the interest rates charged by the microfinance institutions to their clients. Rashtriya Gramin Vikas Nidhi (RGVN), a development oriented financial institution which provides loans to microfinance institutions (Saija and Chanura Microfinance) at 15% interest rate. This rate is considerably high when compared to that of the other development oriented financial institutions. Few NBFCs like MAS Financial Services (to Cashpor and Satin), Reliance Capital (to Equitas, Mimoza, Uttarayan Financial Services, Sahayata, Satin, SMILE and Sonata), Tata Capital (Bandhan and Equitas), MV Microfinance Private Limited (to Sahayata, Satin and SMILE), among others are also involved in institutional lending and provide loans at more than 14% per annum; this is high as compared to the loans availed from other financial institutions.

The weighted average cost of funds for NEREFS is the highest and the operating costs in providing credit services to the clients is also high due to tough terrain and poor infrastructure in their operational area, and hence the interest charged to the clients is highest among the sample institutions studied. SKDRDP has the lowest costs of funds and the interest rates charged to the clients are the lowest. Similar trend is being observed in Lupin, Bandhan, Satin, Saija, SMILE, among others. This clearly shows that there is a direct and positive correlation between the cost of funds and the interest rates charged to the clients. Lower the weighted costs of funds across financial institutions, lower is the interest rates charged to the clients and vice versa.

In addition to the interest rates, the private banks charge a loan processing fees / upfront fees of 0.01 – 1.00% of the loan amount sanctioned. Developmental institutions like Maanveeya Holdings charge 1% of the sanction loan amount as the loan processing fees. Some nationalized banks like Corporation Bank, Bank of India, Punjab and Sind Bank, Allahabad Bank, among others also charge a loan processing fees ranging from 0.20 – 0.50% of the sanctioned loan amount.

The Tier I institutions due to their widespread geographically diverse operations, superior systems and updated information, skills in negotiation, apart from larger quantum of loan requests are in a better

position to bargain with the financial institutions and raise debts at a lower interest rate whereas the Tier II and Tier III institutions, due to low outreach and loans outstanding (as compared to Tier I institutions) apart from weaker systems are able to avail loans at a higher rate of interest. There is also a perception among lenders that the larger institutions are not likely to fail; the smaller institutions with concentrated portfolio, raises the risk perception of lenders.

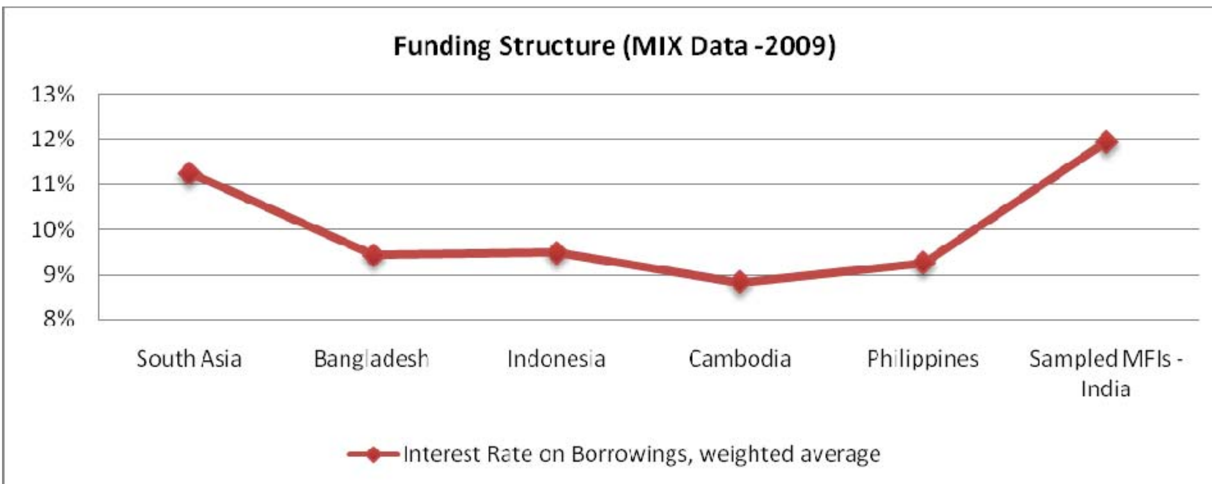


FIGURE 29: FUNDING COST (MIX DATA-2009)

It can be seen in **Figure 34** that the institutions operating in India have the highest weighted average costs of borrowings in the world. The financial institutions in India charge the highest rate of interest when compared with other Asian countries like Bangladesh, Cambodia and Indonesia.

There is a strong correlation between Yield on Portfolio and financial expenses. Even as operational costs continue their gradual decline, they are offset by increasing financial costs. However, it can be seen in **Figure 35** that while for the World and other Asian countries the YoP is following the same trend as financial expenses, in case of Indian MFIs as also for South Asia and Bangladesh, the difference is comparatively lower, which indicates the relative efficiency of the MFIs operating in these geographies.

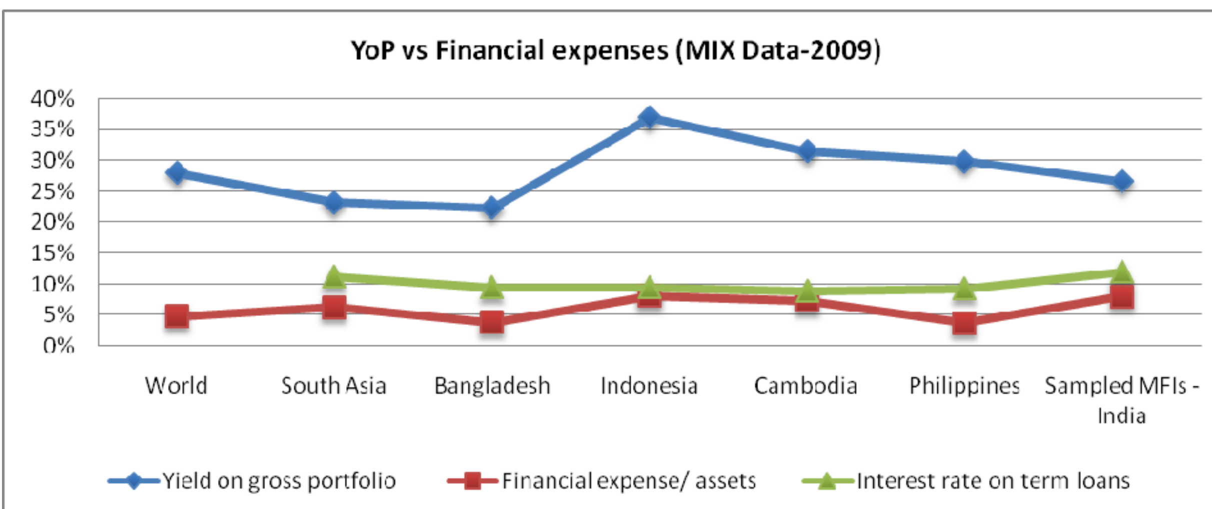


FIGURE 30:YIELD VS FINANCIAL EXPENSES

7. RISK COST MANAGEMENT

MFIs that were studied face a variety of risks –some are internal to their business operations and a few are due to external factors. Some of the larger players – SHARE, Spandana, Asmitha have not shared quality information on their strategies for risk management.

The MFIs rated the major risks they were facing. The top 5 risk factors and the number of responses are shown in **Table 9**.

External risk factors are considered as severe by MFIs. Competition from other MFIs is the major risk faced; in Andhra Pradesh, the competition is from the state programme of SERP and in other states, the MFIs compete with each other especially in semi urban and urban areas.

TABLE 9: RISKSBEING FACED BY THE MFIS

Risks	No of responses
Competition	13
Political	10
Regulatory	7
Liquidity/ Confidence of lenders	7
High cost of loans	5

INTERNAL RISKS

CREDIT RISK

The credit risk being a key risk inherent to the lending business has been addressed through a variety of measures.

1. Almost all MFIs claim to have a robust client acquisition mechanism and screening of clients.
2. Except in remote areas such as rural areas of Rajasthan or hilly regions of north east, in almost all other areas MFIs have experienced competition from other MFIs. The issue of multiple lending and thus over indebtedness of clients have been addressed by a few of the MFIs by ensuring that they open new branches only in areas where other MFIs are not operational. The others attempt to ensure that their clients are accessing not more than 3 MFI loans. Sharing information through credit bureaus is a risk mitigation measure to avoid multiple lending that has been initiated by MFI association.
3. The MFIs adopting company legal forms have robust technology based MIS to get almost real time data on defaults.
4. Only some of the MFIs have invested in internal audit and branch rating to manage risks.
5. 70% of the MFIs have insured the lives of the clients to cover the risk of default through death.
6. There are some good practices such as that of RASS, CECODECON, SKDRDP (mostly NGO-MFIs) who have invested heavily in client relationship for ensuring that credit risk is low.
7. The MFIs with company form have robust provisioning norms for eventual default risk and loan write offs with some of them adopting more stringent norms than prescribed by RBI. Out of 9 MFIs with not for profit legal form, 5 MFIs have inadequate/no loan loss provision or write off policy and practice.
8. Foreseeing client staff nexus/fraud as a key risk area, many of the MFIs have robust staff related policies such as frequent transfer of staff and non-posting of staff in their birth place/residence. However, these lead to higher operational costs since staff compensation/transfer costs are also higher.

CREDIT RISK BORNE BY CLIENTS THROUGH PEER PRESSURE

During field visits, the clients of 31% of MFIs mentioned that they repay on behalf of other defaulting members occasionally in order to keep their credit history with the MFI intact and/or due to the specific procedures of MFIs for such repayment. This risk transfer mechanism of MFIs, this mechanism is bound to fail when the frequency of defaults / default amounts increase or where multiple lending is rampant. This is a hidden beast which is not systematically measured by most of the MFIs and thus not addressed. Except Sonata, none of the others have even acknowledged this risk.

CASH TRANSIT RISK

Cash transit risk has been addressed by 48% of the MFIs having taken cash in transit insurance. Some MFIs such as CASHPOR have changed their processes to transfer this risk to the client groups where the group leaders deposit the cash at the branch. The MFIs in east and in north report higher level of risk due to frauds and law and order situation.

TECHNOLOGY AND RISK COSTS

Though MFIs under study have invested in technology for loan tracking as part of MIS, a few of them like Equitas have invested in adequate technology solutions to address risks comprehensively. Some of the MFIs such as Cashpor, Janalakshmi are investing in technology for back end operations. As of now, technology adoption of MFIs appears to be weak.

EXTERNAL RISKS

The external operating environment for the MFIs has changed drastically in the last year after the ordinance passed by Andhra Pradesh Government. The external risks are translating to severe operational risks for the MFIs. The MFIs operating in Andhra Pradesh are facing credit risk and liquidity risk. Liquidity risk has also been cited by MFIs in north and east India.

Following the microfinance crisis, MFIs are also finding it an uphill task to mobilize loans for on lending. Banks had been cautious in lending to MFIs and were awaiting the recommendations of RBI appointed committee. Liquidity risk is foreseen with the lenders hesitant to lend to the MFIs. A few of MFIs are also raising higher cost debt and are predicting further increase in cost of debt.

The MFIs are adopting the following risk management measures to cope with external risks:

- 60% (18 out of 30 MFIs have submitted their revised pricing information) of them have changed their pricing norms.
- A few of them like Equitas are having a relook at the business model.
- MFIs are investing in advocacy through industry associations as well as building in house capacity.
- With liquidity being tight and raising loan funds becoming an issue, some of the MFIs are consolidating their portfolio rather than spreading thin.
- MFIs are also considering improvements in information disclosures, transparency in operations, adoption of client protection principles, among others.

No amount of loan loss provisioning can help MFIs to tide over credit risk triggered by political action.

Perceived Risks and Risk management costs: Sonata Microfinance

In addition to the Operational risks including portfolio/credit risk, fraud and security, Sonata's management perceive external risks namely political risk and natural calamity as significant risks faced by their institutions in the current context. Sonata also recognizes that there is a possibility of peer repayment being a hidden risk, expected to be around 1%. The operational risks vary with products, with individual loans being more risky than group loans, and also with geography, with unreached and virgin areas being less risky than penetrated markets. As in most MFIs, Sonata has a policy of non-home posting for staff as a measure of risk management, and has an internal audit department that reports to the Board.

In order to manage external risks, Sonata actively participates in activities of the industry associations, and views the membership fees and costs of participation in the activities as the associated costs. In addition, Sonata takes up a leadership role in efforts towards managing external risks with the State through efforts for setting up the State Chapter for Microfinance Institutions Network (MFIN) to formally undertake local and regional policy advocacy and networking. Sonata also has an in-house team for local/regional networking and relationship management with government, politicians, religious leaders etc. as well as for reviewing any legal risks.

8. TECHNOLOGY AND COST REDUCTION

The use of information and communication technology has the potential to make the microfinance processes more efficient by reducing costs, mainly in two ways – (1) lowering of operational costs by automating components of the credit process and (2) lowering and controlling risk and thereby risk cost by more effective monitoring and tracking.

Sahayata has adopted a mobile based system to upload the data on repayments through an application called "True cell" which is installed in the mobile phone of all FCOs (Loan officers). After collecting the due repayments in the field, the FO can make the entry for each repayment collected from mobile and is information is synced in the servers of the Head office. If mobile network is not available on site, then FO can use the same application to enter the data in offline mode, which gets transferred to Head Office servers automatically when the FO in within network coverage area. This application not only helps in reducing costs but also helps to track and monitor delinquent loans. The duration of getting information and updating in the software reduces drastically which has a direct effect on the costs and risks. The branch and head office staff can take decisions and act as soon as the loans are delinquent thereby reducing chances of default. Cashpor is also in the process of adopting the similar application to improve the efficiency.

Almost all sampled MFIs, except for NBJK, Hope Foundation and Lupin Human Welfare & Research Foundation, have an automated MIS that enables them to track performance effectively. Many institutions like Sahayata, Equitas, Ujjivan, Sonata have online data updation, which ensures end of day reconciliation of data from branches to the Head office. The MFIs have confirmed that investment in a good MIS application along with hi speed internet facility has helped in the following ways:

- Monitor availability of funds in branches and Head office, thereby minimizing idle funds and leading to optimal use of funds
- Monitor disbursements, repayments and overdue, reducing risk of default, fraud etc.
- Decrease in number of HR required for MIS and monitoring in field

In addition to the basic MIS, some MFIs such as Equitas, Sahayata, Janalakshmi, Cashpor, BSFL, SKS, Spandana, Share, Asmitha, Ujjivan Financial Services, and MAS Financial Services have adopted technology solutions to further reduce delays in data transfer and resulting inefficiencies and risks and to digitize transactions on field.

Janalakshmi Financial Services (JFS) has made significant investments in maintaining and updating its technology infrastructure, systems applications and business solutions. Early on, JFS made an investment to define and document the processes of the core business life cycle. Beginning with the customer acquisition phase, loan disbursement, collection phase, and finally the closure phase, the mapping of processes identified the vital role of technology in driving business processes. JFL's technology infrastructure is defined by a three-tier framework. At the foundation lies the IT architecture comprising of the technology services and infrastructure. The architecture enables growth and ensures scalability of the business. Next, the core banking system (CBS) complemented by the Customer Relationship Management (CRM) application drives the business processes of JFS. Finally, delivery mechanisms such as the Smart Card seamlessly interface with CBS and CRM to cater to the increasing efficiency of the organization.

MFIs such as Sonata, SMILE and few others are in discussion with service providers for integration of mobile based and other technological applications for improving efficiency and reducing costs. SMILE has recently conducted a comprehensive IT review through a consulting agency to identify the best options.

However, concrete evidence of reduction in operating costs after setting off the investment and recurring costs of technological applications is still not available. In addition, the essence of the microfinance model that lies on high client interface may potentially get diluted through integration of technology, leading to possibilities of resurfacing of credit risks associated with default, lack of communication to clients etc.

Technological Innovations: Equitas Microfinance India Private Limited

Among other sampled institutions, Equitas is one institution which has undertaken several technological innovations. Equitas has a core banking solution called TEMENOS T24 in place. This product is an extension of T24 Banking software, developed specifically for Microfinance and Community Banking sector.

Some of the technical innovations undertaken by Equitas are as follows:

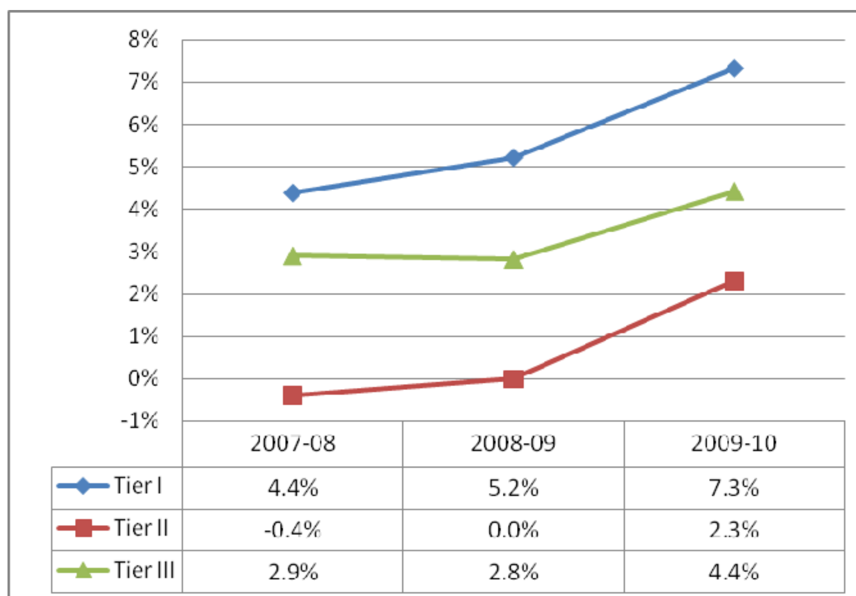
6. *Automated Form processing – 80% of the information in the membership form is Optical Mark Recognition (OMR) based and can be entered into the system just by scanning; remaining 20% of the information is entered by staff.*
7. *Real time collection and attendance monitoring at the head office and steps taken thereof (immediately). A central server obtains SMS-based information on the proceeds of every collection meeting within fifteen minutes of its completion. An internet-based application helps Branch & Area Managers detect any irregularity in their collections immediately; and facilitates quick resolution of such an irregularity.*
8. *Pre-printed payment stickers – pre-payment printed stickers are sent by the head office to the branch offices one day prior to the collection day and all un-stuck stickers need to be returned within three days. This is a surrogate to the printed receipts and a risk coping mechanism. This system has reduced the need for manually writing the receipts thus saving costs and time in maintaining records.*
9. *Cash handling by an external agency which collects all the cash from branch offices in the evening and provides cash in the morning for disbursements, based on the requirements of each branch. Though this may be marginally costlier than staff handling cash, the incidence of frauds are reduced and the cash management is superior.*

The investment in technology and systems has enabled Equitas to scale up efficiently and the organisation is operational self-sufficient within 2 years.

8. MARGIN

Net Margin indicates whether an institution is covering its costs and revenue out of its operations. The net margin is all sources of revenue less the cost of funds and operating expenses. Net margin provides a broader picture than net interest margin, which measures all interest earned and collected from loans and investments less the cost of funds for the total fund deployed in the operations.

Figure 36 shows the analysis of margin calculated as - net revenue generated by the MFI to the total average gross loan portfolio. The analysis of margins for 27 MFI[8] in different tiers of MFIs clearly shows that tier I MFIs are able to generate sufficient revenue with their economy of scale and providing basket of financial services efficiently to their clients. The average margin continuously increased from 4.4% in 2007-08 to 7.3% in 2010 due to exponential growth in the portfolio size from Rs. 28,473 million in 2008 to Rs. 115,796 million in 2010. The Tier II MFIs have much lower margins than the Tier I and Tier III categories due to their expansion cost to reach the economy of scale and shows positive trend only in last year. The positive trend of Tier I and Tier II MFIs can also be attributed to equity investment at substantial premium as cheaper sources of funding. No dividend has been declared so far by these institutions.

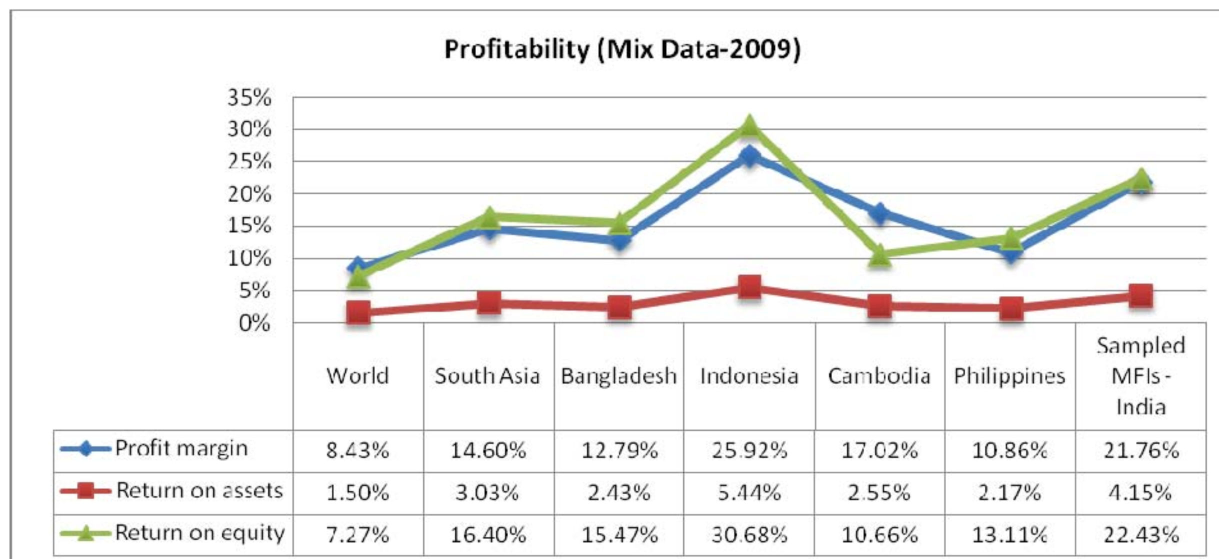


	2007-08	2008-09	2009-10
Tier I	4.4%	5.2%	7.3%
Tier II	-0.4%	0.0%	2.3%
Tier III	2.9%	2.8%	4.4%

FIGURE 31: MARGIN ACROSS DIFFERENT TIERS OF MFIS

[8] Few MFIs like Ujjivan Financial Services Limited and Equitas Microfinance Limited are not included for 2007-08 and Sahayata Microfinance Pvt Limited for 2008-09 since they had high negative value due to their start up cost.

PROFITABILITY



	World	South Asia	Bangladesh	Indonesia	Cambodia	Philippines	Sampled MFIs - India
Profit margin	8.43%	14.60%	12.79%	25.92%	17.02%	10.86%	21.76%
Return on assets	1.50%	3.03%	2.43%	5.44%	2.55%	2.17%	4.15%
Return on equity	7.27%	16.40%	15.47%	30.68%	10.66%	13.11%	22.43%

FIGURE 32: PROFITABILITY DATA (MIX DATA-2009)

Figure 37 shows that the Indonesian and Indian MFIs are amongst the most profitable MFIs. However, this has to be seen holistically. From **Figure 38** shown below it is evident that the Indonesian MFI incurred higher cost and products were priced even higher to generate higher profits. In case of Philippines, the extremely high cost resulted in the low profitability. However, in case of Indian MFIs, the low cost and a moderate pricing has resulted in a high profitability. There is a significant scope of transferring the benefits to the clients in terms of reduction in interest rates especially by tier 1 MFIs. If the cost of funds, which has seen an increasing trend in the past in India, can be brought down, the cost to the client can be reduced across the industry without affecting its sustainability.

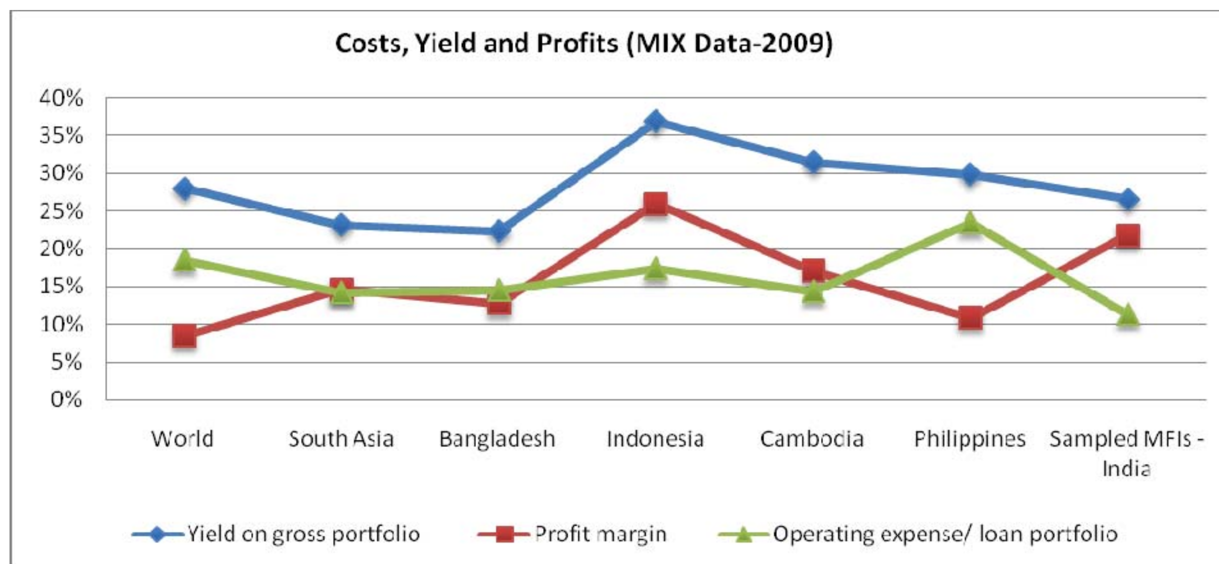


FIGURE 33: COST, YIELD AND PROFITS (MIX DATA-2009)

INFLATION ADJUSTED RETURNS

Inflation adjustments has been carried out for return on assets and return on equity for the year ending 2010, to understand whether the MFI produces enough surplus in real terms and is able to keep its assets intact in real terms. For equity investor, the net return should be positive and equal to or more than what they would earn from the next best investment[9]. Financial investments in the long run are not based on year to year fluctuations of inflation; but whether over a period, the real returns are positive and acceptable.

Number of Institutions	Inflation adjusted return on equity		Inflation adjusted return on assets	
	Positive	Negative	Positive	Negative
Total	26	2	8	20
Across Tiers				
Tier 1	11	0	6	5
Tier 2	8	1	1	8
Tier 3	7	1	1	6
Across Legal Forms				
Profit	17	2	7	12
Not for profit	9	0	1	8

The above table shows that around 71% of MFIs posted negative Return on Assets in real terms and 7 % of MFIs gave negative Return on Equity. The position would be more critical in 2010-11 in view of the inflation rate increasing to 9.6%. With interest rates already high, the scope for pricing loans to neutralize the inflation is very limited. **Figure 39** provides details of the ROA and ROE across Tiers and Legal Forms:

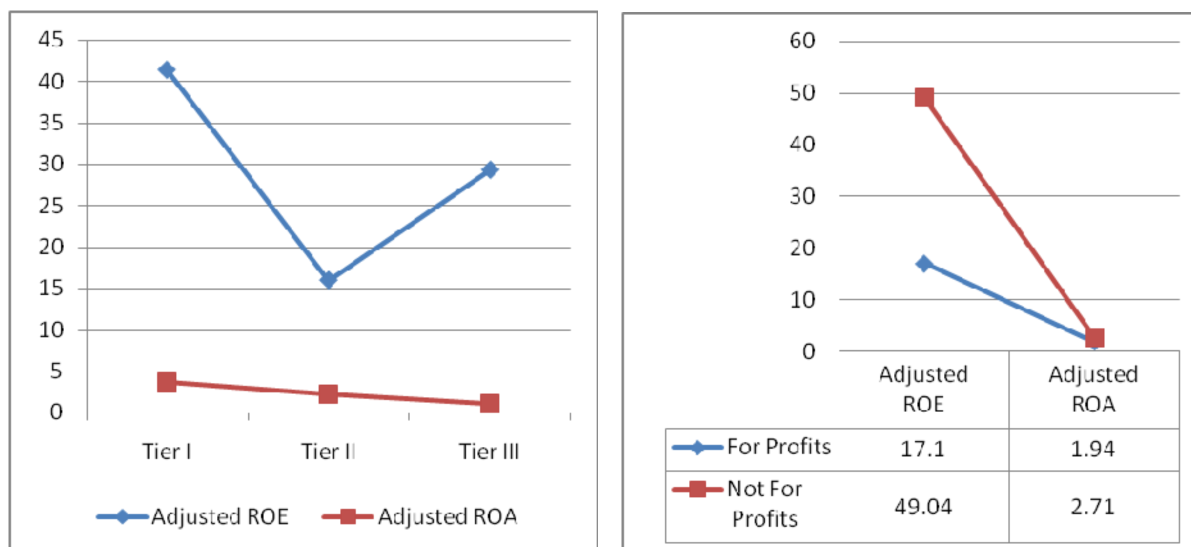


FIGURE 34: ADJUSTED ROA VS ADJUSTED ROE

[9]But practically the comparison of acceptable rates of return can be made on unadjusted rates - compare a return on equity of 13% with return of 10 on fixed deposits - with or without adjustments, investment in equity is better. If rate of inflation is 15%, both investments give a negative return in real terms, still the equity investment is better.

KEY FINANCIAL RATIOS ACROSS TIERS

Figure 40 shows the Operational Expense Ratio, Financial Cost Ratio, Loan Loss Provision Ratio when compared with Yield across tiers. We can observe that the Tier III institutions have the lowest difference between the Yield[10] and the three ratios (combined). This can be attributed to the OER of two institutions (Chanura Microfin and NEREFS) operating the North east which was part of the Tier III. The Tier I institutions have the maximum difference between the Yield and three ratios (combined) due to more client outreach and high loans outstanding.

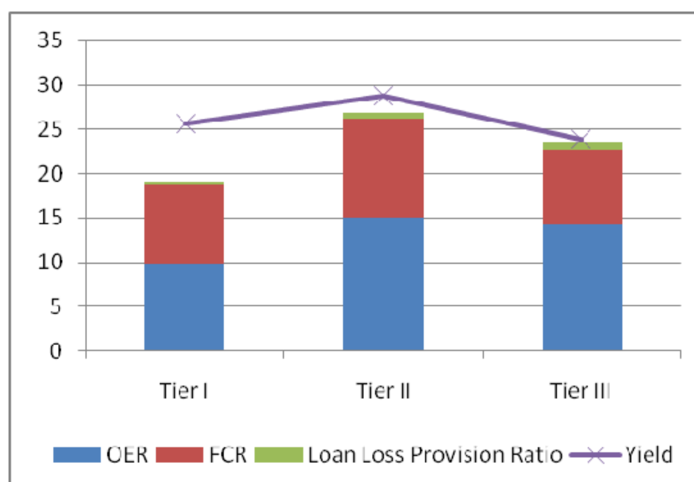


FIGURE 35: OER VS FCR VS LOAN LOSS EXP VS YIELD

The Tier II institutions have very little difference due to their investments in expansion. These institutions are in their growth phase and have already invested in expansion. A little impetus provided to these institutions can show results in reaching more number of clients and higher loans outstanding.

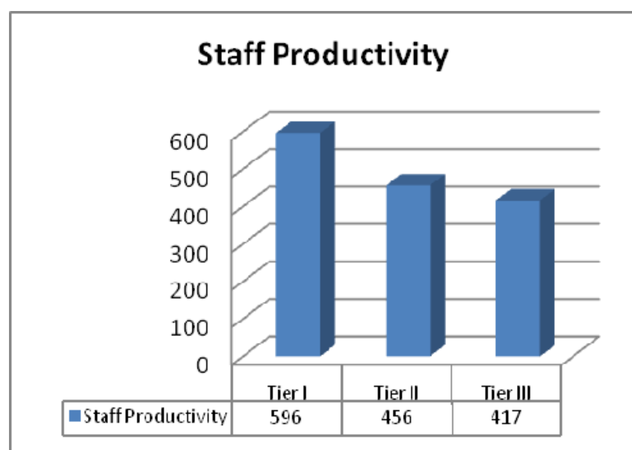


FIGURE 36: STAFF PRODUCTIVITY - TIERWISE

The staff productivity has been calculated by dividing the total number of borrowers with the total number of field staff (credit officers). This comparison across Tiers clearly shows that Tier I institutions have the most productive staff since most of these institutions follow Grameen model which has standard systems and processes which help in replication and expansion at a faster pace. The Tier II and Tier III institutions have almost similar staff productivity because the Tier II institutions have invested on hiring more staff for expansion which in turn has a negative effect on the staff productivity.

The maximum staff productivity has been shown by Equitas due to their operational model. The client acquisition and loan origination is done by separate staff whereas the loan repayment collection is done by different staff. This reduces the chances of favoritism for providing loans and increase efficiency of the staff.

[10] Yield need not be compared with APR since APR is of products and Yield is of the entire institution. A detailed comparison between Yield and APR has been mentioned in the APR section above.

COMPARISON OF INDIVIDUAL AND GROUP LENDING MODELS

A comparison was done across individual and group lending models. The group lending models included institutions forming Self Help Groups, Joint Liability Groups and Grameen groups. **Figure 42** clearly depicts that the difference in WA-APR (Interest + Fee) and a combination of three ratios (OER, FCR and Loan Loss Provisioning) is similar across both the models. However, the staff productivity is significantly varying across these two models of lending (individual – 95 and group – 512 borrowers per field officer). The results are based on 29 institutions in group lending model and one institution in individual lending model- MAS Financial Services (MAS).

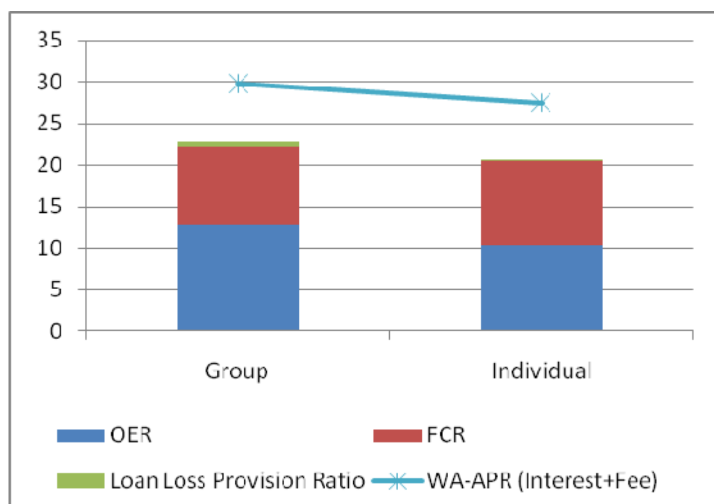


FIGURE 37: INDIVIDUAL VS GROUP LENDING MODELS

MAS Financial Services as an institution is different from other MFIs due to the following reasons:

1. *Caters to non-poor clientele, one category above the poor clientele as served by the microfinance institutions.*
2. *High loan size in the range of Rs50,000-10,00,000*
3. *Operational area is primarily urban and few pockets of semi-urban*
4. *Lending against collateral (Post Dated Cheques and Property, in some cases).*

DEVELOPMENT ACTIVITIES BY THE MFIS

The margins generated by the institutions are not only utilised for expansion and increasing client outreach but also to provide various activities to their clients.

Some institutions like Equitas and Bandhan earmark 5% of their surplus to undertake developmental activities like eye camps, skill-building programs, health awareness programs, among others for their clients. In addition, Equitas provide Rs2,000 per month per branch and salary of one CSR representative (per 10 branches) for conducting health camps for their clients.

Institutions like Cashpor and Ujjivan provide scholarships / grants to students / staff from the surplus generated and conduct several development programs like women and childcare, community health leaders training program, among others with the help of grants from funding institutions.

Ujjivan also forms village development committees which consist of their staff and mature members. This committee decides on the community development programs / projects to be undertaken in a particular village, in consultation with the entire village. Once the program / project is finalised, the costs of the same is provided by Ujjivan. Ujjvan earmarks Rs25,000 per branch towards this support and activities like education materials, water containers, toys to children; carpets & chairs to Aganwadi Schools; building pulleys in the community well; among others.

Ad hoc relief activities are also undertaken by few institutions for their clients from the surplus generated (Asmitha, Chanura Microfin, Mimoza, Uttarayan Financial Services, SHARE, Spandana) and grants from funding agencies (NEED, Hand in Hand, SKDRDP, NBJK, Mimoza, People's Forum, Hope Foundation, RASS, Ujjivan Financial Services).Institutions like SKS, Bandhan, Uttarayan Financial Services, Janalakshmi Financial Services, People's Forum, SMILE, who have transitioned their microfinance portfolio from a Not for Profit institution to For Profit institution conduct the developmental activities through this institutional form as procuring grants is easier.

Institutions like CECODECON (0.33% of the loan amount), Bandhan (1% of the loan amount), BSFL (specified fees for a particular activity) and others charge some amount from their clients to provide capacity building and additional services to their clients.

The development activities conducted (through grants or from their profits or by charging from their clients) help in building capacities of the clients / members as well as increase the rapport and loyalty of the clients / members towards the respective institution. This has been observed during the interactions and discussions with clients / members of Bandhan, Cashpor, Equitas, Ujjivan, among others; they feel a sense of ownership with the institution and would not go to any other institution for credit.

9. Transparency/Disclosure of information provided and Awareness of clients

The MFI clients were interviewed in order to understand the transparency / disclosure of information provided by the MFIs to their clients and their level of awareness. The details from analysis of information provided and level of client awareness are provided in **Table 10**.

TABLE 10: INFORMATION DISCLOSURE AND AWARENESS OF CLIENTS

Name of MFI	Number of clients interviewed	Transparency of information provided (%)	Awareness of Clients (%)
Asmitha	10	100	73.00
Bandhan	29	90	78.26
Basix	27	90	72.07
Cashpor	26	100	86.17
Cecodecon	6	90	74.00
Chanura	10	100	70.25
Equitas	29	100	84.64
HIH	27	90	78.00
Hope Foundation	16	70	86.12
Janalakshmi	8	100	58.33
Lupin	11	100	82.71
MAS	14	70	92.50
Mimo	16	80	83.75
NBJK	12	80	79.98
Need	12	90	70.79
NEREFS	29	100	83.90
Peoples Forum	11	100	92.68
RASS	13	100	96.15
RORES	12	50	53.32
Sahayata	31	90	86.31
Saija	12	100	83.32
Satin	16	100	82.14
Share	34	90	68.75
SKDRDP	26	90	95.20
SKS	24	100	86.35
Smile	16	70	75.69
Sonata	18	90	70.79
Spandana	16	80	68.44
Ujjivan	28	100	87.66
Uttrayan	11	100	84.44

Average	550	90	79.52

The transparency / disclosure of loan information to the clients and the awareness level of clients were measured across the following parameters:

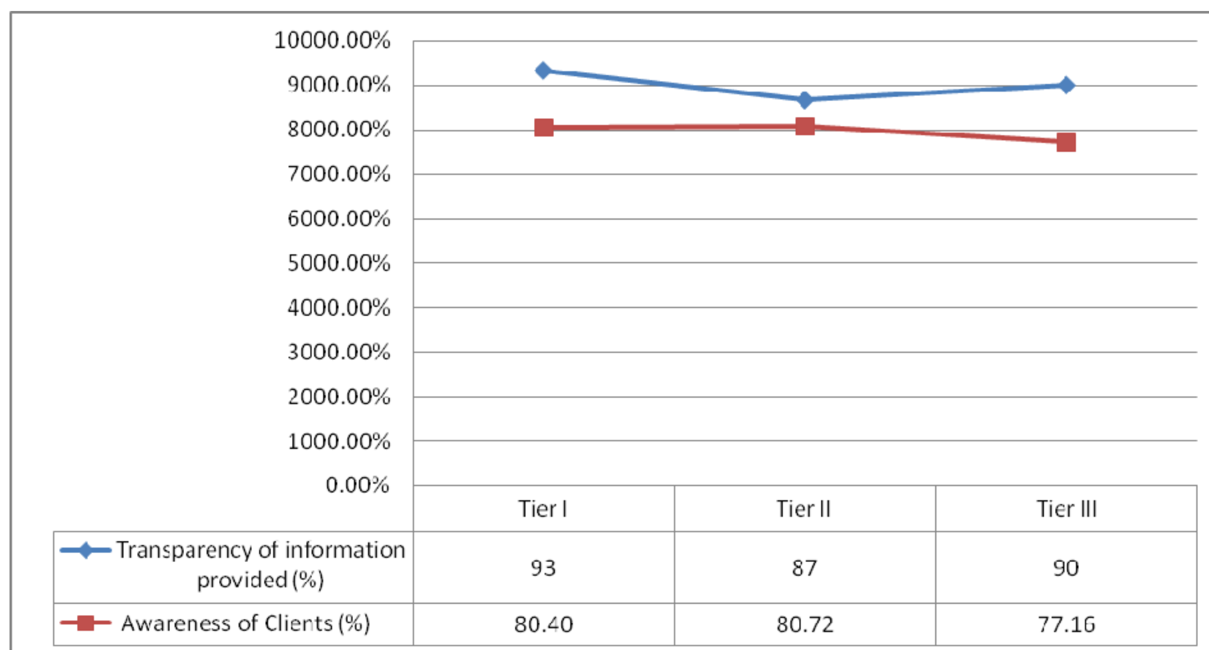
1. Purpose of the loan
2. Date of the loan availed
3. Amount of the loan
4. Tenure of the loan
5. Pricing information of the loan
   a. Interest rate,
   b. Loan processing fees,
   c. Insurance charges,
   d. Security amount.
6. Repayment amount and frequency
7. Pre-payment terms and conditions

The percentages of transparency / disclosure of loan information across MFIs were calculated based on the information shared by the MFI to the clients (on the above parameters) while providing the loans and the percentages of awareness level of clients were calculated based on the clients who were aware of the information shared by the MFI. For example, Ujjivan shares 100% of the loan information whereas only 87.66% of the total clients interviewed (28) were aware of the loan information shared.

Table 10 clearly shows that the awareness of clients regarding the terms and conditions of the loans is directly proportional to the information shared by the MFIs. However, there are some variations like Janalakshmi, Share, Sonata and Spandana where the awareness of the clients of MFIs is not proportional and the clients of these MFIs were unaware of the terms and conditions of the loan commensurate to the information shared by these MFIs.

RASS discloses all information of the loan in their passbooks and their clients were aware regarding the same as they have the maximum awareness levels regarding the terms and conditions of the loan. The minimum information of the loans was disclosed by RORES and their clients were least aware of even the minimum information disclosed.

TRANSPARENCY BY MFIs AND AWARENESS OF CLIENTS ACROSS TIERS



	Tier I	Tier II	Tier III
Transparency of information provided (%)	93	87	90
Awareness of Clients (%)	80.40	80.72	77.16

FIGURE 38: INFORMATION DISCLOSURE AND AWARENESS OF CLIENTS (TIER WISE)

The difference in awareness of the clients vis-a-vis the information disclosed / shared with the clients is low in the case of Tier II MFIs whereas the difference is high in Tier I and Tier III MFIs; this clearly shows that the Tier I and Tier III MFIs disclose the parameters of the terms and conditions of the loan only during the disbursement / mention in their passbooks without communicating the details to them and hence the awareness levels of the clients is correspondingly low.

TRANSPARENCY BY MFIs AND AWARENESS OF CLIENTS ACROSS MODELS

The information disclosed by MFIs working in Grameen model is the highest followed by SHG and JLG. However, the awareness levels of clients are lowest in JLG model followed by SHG and Grameen. This difference is due to the purpose and objective of formation of the groups, i.e., Grameen and JLG is formed to avail loans from the MFIs with an affinity towards its members whereas in the case of SHGs, the members not only come together to avail loans from the MFIs but also save among themselves; moreover their systems followed help to re-call and hence are more aware regarding the terms and conditions of the loans they avail from the MFIs.

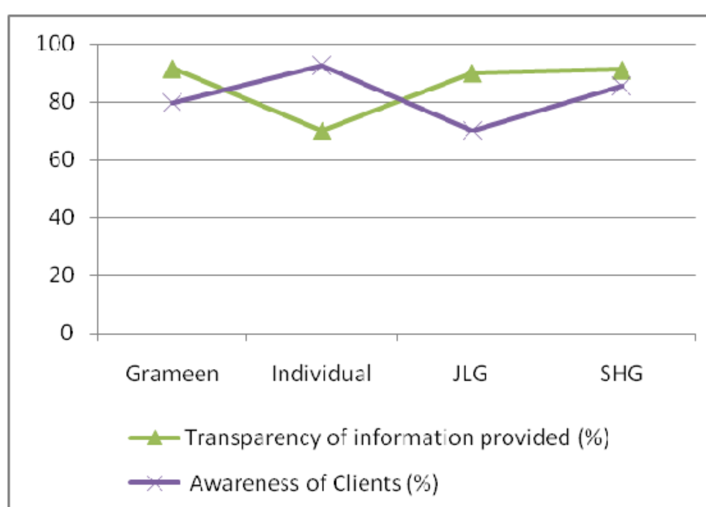


FIGURE 39: INFORMATION DISCLOSURE AND AWARENESS OF CLIENTS (MODEL WISE)

In **Figure 44**, client availing loans from MFI following the individual model has the highest awareness levels. This is a biased figure since MAS Financial Services was the only institution following absolute individual model and thereby is not a representative sample.

TRANSPARENCY BY MFIS AND AWARENESS OF CLIENTS ACROSS LEGAL FORMS

The For Profit institutions are more transparent than the Not for Profit institutions whereas the awareness of their clients are similar. This is due to fact that For Profit institutions are mandated by the apex bank and other networks / associations to be transparent.

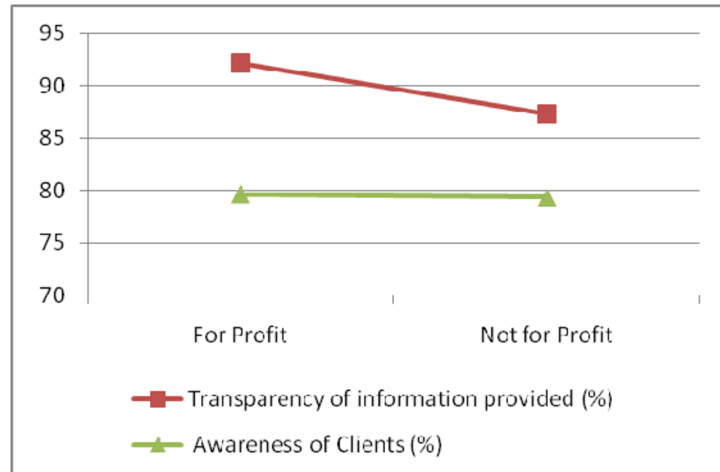


FIGURE 40: INFORMATION DISCLOSURE AND AWARENESS OF CLIENTS (LEGAL FORM WISE)

10. RECENT RBI GUIDELINES FOR NBFC-MFIS AND DRAFT MICRO FINANCE INSTITUTIONS REGULATION AND DEVELOPMENT BILL

After the commencement of the study there have been two important policy developments – in May 2011 the Reserve Bank of India decided to accept the broad framework of the recommendations of the Malegam Committee for the microfinance industry with some modifications in its Monetary Policy for 2011-2012 (the detailed guidelines are yet to be issued) and the second development - in July 2011 the draft Microfinance (Development and Regulation) Bill was circulated for public opinion by Government of India.

The study focused on some of the Malegam committee recommendations. The field study had nearly been completed when the two important policy developments took place and hence how these policy developments would affect the sector and the MFIs is largely inferred from the study results.

RBI while accepting the broad framework of regulations recommended by the Malegam Committee has indicated that bank loans to all MFIs, including NBFCs working as MFIs on or after April 1, 2011, will be eligible for classification as priority sector loans only if the prescribed percentage of their total assets are in the nature of "qualifying assets" and they adhere to the "pricing of interest" guidelines to be issued; that a "qualifying asset'' is required to satisfy the criteria of

- loan disbursed by an MFI to a borrower with a rural household annual income not exceeding Rs60,000 or urban and semi-urban household income not exceeding Rs1,20,000;
- loan amount not to exceed Rs35,000 in the first cycle and Rs50,000 in subsequent cycles;
- total indebtedness of the borrower not to exceed Rs50,000;
- tenure of loan not to be less than 24 months for loan amount in excess of Rs15,000 without prepayment penalty;
- loan to be extended without collateral;
- aggregate amount of loan, given for income generation, not to be less than 75 per cent of the total loans given by the MFIs; and
- loan to be repayable by weekly, fortnightly or monthly installments at the choice of the borrower;
- that banks should ensure a margin cap of 12 per cent and
- interest rate cap of 26 per cent for their lending to be eligible to be classified as priority sector loans;

In the following paragraphs, the readiness of the MFIs and the effect of the above stipulations on the MFIs are discussed.

INTEREST RATE CAP

In 2010, the cost of funds is low for Tier I institutions and has the lowest operating cost. So, for Tier I institutions, it may not be difficult to adhere to the interest rate cap suggested by RBI. For Tier II institutions, both operations cost and cost of funds is higher than Tier I institutions, so they might face little difficulty in adhering to the interest rate cap. Tier III institutions would be most affected and adhering to the interest rate cap, would be a tough task since it has the highest cost of operations. A few of the institutions are already within the interest cap limits prescribed by RBI. However, several of them like Asmitha, Share, SKS, Sahayata, Sonata, Mimoza, Satin, Janalakshmi, Hand in Hand, Chanura, NEREFS and RORES would need to reduce their interest rates and other charges.

On the basis of the yield on portfolio data of financial year 2010 -11, the For Profit institutions can adhere to the interest cap due to the highest yield. In fact, some of them are well positioned to offer further reduction in interest rates to clients. As far as Not For Profit institutions are concerned, they can easily adhere to the RBI guidelines since the costs of funds are low and operation cost are in comparable with the For Profit institutions. As far as the Not for Profit institutions are concerned they will need to make few adjustments to the interest rates in order to remain profitable if the cost of funds and transaction costs increase.

The cost of operations is higher in institutions following the JLG model followed by Grameen and SHG model that has the least cost of operations. This is because the institutions following the SHG model have received grants for SHG promotion which reduces the cost of initial client acquisition. Moreover, the SHG lending usually involves monthly meetings and monthly repayments thus reducing the operational cost further. Institutions that are following SHG model can adhere to the interest cap but institutions following the JLG model may find it difficult and they have to invest in credit process/product reengineering.

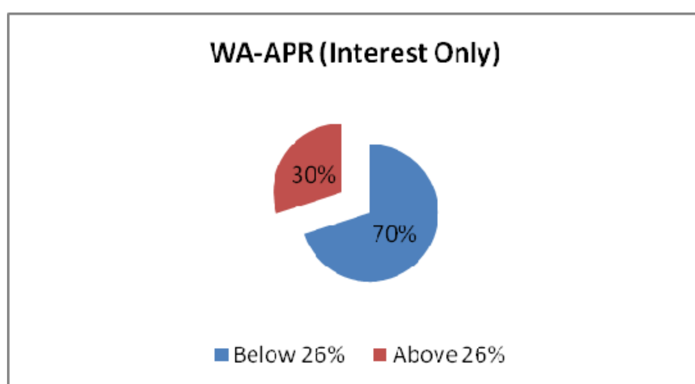


FIGURE 41: MFIS BELOW AND ABOVE 26% APR

Based on the loan samples collected from the MFIs till December 2010, 21 of the MFIs were below the 26% interest rate stipulated by the RBI guidelines and 9 MFIs were above 26%. The Weighted Average APR of the interest rates charged by MFIs across products of an institution was used for this analysis. Details of the institutions along with their respective interest rates are mentioned in **Annexure 12**.

The above observations can be corroborated with the discussions held with each of the MFIs regarding their terms and conditions of the loan products offered. Most of the institutions have either reduced their interest rate post the crisis and RBI guidelines issued. Please see the section on APR for further details.

A reduction in interest rates for the Tier II and Tier III institutions would affect profitability and their ability to raise equity for expansion. These institutions will need equity infusion from reliable domestic sources such as SIDBI.

HH income of Rs60,000 in rural areas and Rs120,000 in urban areas

The maximum client household income of Rs60,000 in rural areas and Rs120,000 in urban areas is within limits for most of institutions including Chanura Microfinance, NBJK, Saija Microfinance, Uttarayan Financial Services, Bandhan, among others, based on the meetings and interactions with clients. However, household income is difficult to be measured and tracked on an ongoing basis. MFIs will need to find out reliable ways to track / verify the same and get a certification from the clients. Moreover, now on, the institutions might focus more in the urban areas since the household income in urban areas is easier to measure as compared to the household income in rural areas and also higher density of clients leading to operational efficiencies. In any case, the need for verification and regulatory compliance would increase the cost of operations. For this clause, absolute compliance by MFIs is difficult.

Maintaining 75% of loans for income generation

This guideline is followed by all the institutions visited since most of institutions focus on loans for Income Generating Activity, which will ensure smooth repayment of their loans. Moreover, loan utilization checks are also conducted by many of the MFIs to track the loan usage. A rigorous check is possible in case of capital Investments; however loans for working capital for trading and petty business in which many of the clients of MFI are engaged is difficult to be checked and certified. Very strict utilization checks at household level will again increase cost of operations for MFIs. While certification by household and superficial checking by MFI is possible, absolute compliance is not possible.

Within Twenty four months in excess of amount of Rs15,000

At present, the first loans provided to the clients by the institutions range from Rs500 to Rs10,100 for a period of one year. Only the second or subsequent loan sizes are more than or equal to Rs15,000. However, the tenure of these loans is for one year. Except for Equitas, all other institutions have largely one-year loan. SKDRDP have longer loan tenures will need to fine-tune their lending procedures and MIS to ensure credit risks are minimized. There is a high risk perception among MFIs for offering loans longer than a year which has to be overcome by investment in appropriate credit processes. Though this is essentially a customer protection measure to ensure that the product suits client cash flows, in the longer term this will ensure better risk management at MFIs since client drop out/defaults will be reduced due to appropriate loan terms. Moreover, the institutions might reduce their loan sizes in order to cope with this clause. Reduction in loan size would ensure that the repayment period is within 12 months. This can lead to client dissatisfaction and drop out which can increase operational costs.

Total indebtedness of clients and awareness of MFIs about other loan sources of clients

Presently, only a few of the MFIs have adopted policies and systems to ensure that clients are not over indebted. Remote and sparsely populated areas with inadequate infrastructure have utmost a single MFI which is operational. Urban, semi urban and easy to reach rural areas with adequate law and order situation have several MFIs. The institutions that are working in a limited geography/client base are more aware of other loans availed by their clients. However, quantification of these loans to ascertain total indebtedness of the clients from institutional sources needs a concerted action by the sector.

The MFIs will need to prepare themselves for sharing information to credit information bureau. This will need additional systems (scientific verification of Know Your Customer norms, computerization of data to supply information to credit information bureau) in a few MFIs. The charges levied by the credit information bureau will add to cost of operations but the cost and burden on staff for verification of indebtedness will be reduced. Overall risk cost will also be reduced since this process will enable MFIs to identify quality customers.

Loans without collateral

The MFIs will face no problems in complying with this aspect since all the MFIs are providing loans to their clients without any collateral. The only collateral utilized is the social collateral among the members of the groups by most of the MFIs. Security deposits are collected by only few of the MFIs who are not for profits. Thus NBFC MFIs will be largely in a position to comply with this requirement.

DATA COLLECTED IN CONJUNCTION WITH THE RBI GUIDELINES ISSUED

The data / information collected during the study has been utilized to understand the concurrence with the RBI guidelines and the analysis across MFI Tiers, Legal forms and Models is presented below:

TABLE 11: MFI DATA IN RBI STRUCTURE (TIER WISE)

	Tier I	Tier II	Tier III
No. of borrowers	18,53,469	97,368	22,078
Average Loan size	5,680	5,466	14,894
Outstanding Loan Portfolio	10,52,69,58,902	53,21,93,214	32,88,38,406
Interest Rate (as per RBI guidelines)	26%	26%	26%
Costing of the Loan	20.61%	28.14%	24.63%
Operating Costs - Operating Expense Ratio	9.77%	15.00%	18.38%*
Cost of Capital (debt) - Financial Expense Ratio	8.84%	11.14%	9.11%
Loan Loss Provisioning Ratio	2.00%	2.00%	2.00%
Profit / Margin	5.39%	-2.14%	-3.49%

*Institutions like CECODECON, Lupin and RASS has not been included in the average OER of Tier III institutions since most of the costs are been borne by their parent institutions.

The Tier II and III institutions show a negative margin due to high operating costs and high costs of funds. The reasons are mentioned below:

- Operating costs of Tier II and many of the Tier III MFIs are high since these MFIs are in the growth phase (Sonata, Mimo, Janalakshmi, People's Forum, Uttarayan Financial Services, among others) and have invested in the expansion.
- The operating costs of Tier III MFIs is high since we have two MFIs (Chanura Microfinance and NEREFS) in this Tier who are working in the Northeast where the costs are high due to geographical spread (plains and hills), lack of infrastructure (bad roads, lack of power and poor banking services) and other associated costs like travelling, fuel for power generation.
- Costs of Funds of Tier II MFIs are high since these MFIs are in the process of transition from Society/Trust/Section 25 to NBFC (Uttarayan Financial Services, People's Forum, SMILE) and some have commenced their operations in the last 1-2 years (Janalakshmi, Saija, Satin) and yet to achieve scale.
- Cost of funds for Tier III MFIs are less as compared to Tier II MFIs since these MFIs have availed grants and low cost funds, for expansion (Chanura, NBJK, RASS).However, the costs have been adjusted against the market rate of interest.

The analysis across tiers of institutions, financial institutions may invest (through equity and debt) in Tier II institutions and few of Tier III institutions who are in the growth phase and are in the process of transition and hence high OER. These institutions can grow at a rapid pace if proper and adequate support is provided in terms of funds for onlending and grants for expansion.

TABLE 12: MFI DATA IN RBI STRUCTURE (LEGAL FORM WISE)

	For Profit	Not for Profit
No. of borrowers	10,37,862	1,91,300
Average Loan size	5,768	5,499
Outstanding Loan Portfolio	5,98,68,26,816	1,05,19,20,510
Interest Rate (as per RBI guidelines)	26%	26%
Costing of the Loan	25.78%	20.80%
Operating Costs - Operating Expense Ratio	14.12%	14.89%
Cost of Capital (debt) - Financial Expense Ratio	9.66%	9.65%
Loan Loss Provisioning Ratio	2.00%	2.00%
Profit / Margin	0.22%	-0.54%

The For Profit institutions have a marginal high profit margin when compared with the Not For Profit institutions (excluding institutions like Lupin, SKDRDP, RASS). The reasons are as follows:

- Operating costs of For Profit institutions are high since most of the MFIs (Sonata, Mimo, Janalakshmi, Uttarayan Financial Services, among others) in this category are in the growth phase and hence invested in expansion. Moreover, NEREFS, being an NBFC is also included in this category and their costs of operations are high due to operations in the Northeast which is a tough area.
- Operating costs of Not for Profit institutions is also high when the exceptional institutions like Lupin, RASS, SKDRDP have been excluded (which have low OER due to the costs been subsidized by grants).

TABLE 13: MFI DATA IN RBI STRUCURE (MODEL WISE)

	Grameen	SHG	JLG/Individual
No. of borrowers	14,24,347	1,90,083	1,99,250
Average Loan size	5,627	6,595	6,430
Outstanding Loan Portfolio	8,01,47,97,223	1,25,36,80,882	1,28,11,08,002
Interest Rate (as per RBI guidelines)	26%	26%	26%
Costing of the Loan	22.56%	18.89%	31.43%
Operating Costs - Operating Expense Ratio	11.36%	7.65%	19.38%
Cost of Capital (debt) - Financial Expense Ratio	9.20%	9.24%	10.05%
Loan Loss Provisioning Ratio	2.00%	2.00%	2.00%
Profit / Margin	3.44%	7.11%	-5.43%

The institutions following the SHG model has the highest margin due to the operating costs being the lowest and vice versa for the institutions following the JLG / Individual model. The reasons for the same are as follows:

- The operating costs of institutions following the SHG model is low since the SHG promotion expenses are borne by grants. Grants have a direct effect in reducing the OER since the SHG promotion costs like expenses of field officers, capacity building and training costs of the staff and members, group management costs, among others are borne by these grants in the initial years. However, assigning these costs and then calculating the OER would be difficult since many a times the amount of grants availed by an institution cannot be directly attributed to

group development costs. Example, grants for health programme are mobilized by the NGO and the staff involved in health programme also carry out group promotion. Half of the institutions following the SHG model have a monthly collection system which further reduces costs.

- The operating costs of institutions following the Grameen model are lower than institutions following the JLG/Individual model due to economies of scale. These are institutions which are in the Tier I and hence have the maximum outreach and loans outstanding.
- Operating costs of institutions following the JLG / Individual model is high since these institutions are in the transition phase (Janalakshmi) or have commenced their operations in the last two years (Saija).

However, there are practical difficulties in measurement and maintenance of profit margins as these tend to fluctuate over time with changes in cost of funds and changes in the number and maturity of MFI branches.

The analysis across different lending models clearly shows that Grameen model potentially has a higher margin and need to be supported due to the unique feature of standardization which propels growth and expansion. However, SHG model has its own significance in terms of women's empowerment by building leadership qualities and increasing decision making power in the household, among others.

Assumptions

- All figures have been taken as average across the sample and as per the audited statement of accounts of FY 2009-10.
- As a prudent measure, Loan Loss Provisioning Ratio has been taken as 2% across all categories. Moreover, some of the MFIs do not make such provisions.

Microfinance Institutions Development and Regulation Bill

As per the draft bill, RBI is proposed to be given wide powers to regulate the sector by prescribing a number of guidelines on various operational aspects of MFIs including margin cap and prudential norms. While there are reservations expressed about the power given to the regulator resulting in micro managing the sector, the micro finance development council can play a very crucial role in tempering the micro management. Thus SIDBI and other industry representatives have a crucial role to play in ensuring orderly growth of the MFIs.

Moreover, the present RBI guidelines issued for NBFCs will be now made applicable for other legal forms as well with suitable modifications. Thus the non NBFC MFIs also have to prepare themselves for similar regulation.

The bill has specifically recognized that further development and geographical spread of the microfinance sector requires operations of the MFIs are not equated with money lending. Many of the present external risks faced by the MFIs have been due to a lack of comprehensive regulation and also multiplicity of acts/authorities in regulating MFIs. However, a comprehensive regulation of the sector by RBI will reduce

the influence of the state Government through some of the state acts. This should enable the MFIs, who perceive political interference as a high risk, to operate in a more enabling legal environment.

The Bill has broadened the scope of services provided by microfinance sector as it defines microfinance to include microcredit, savings products, remittances, pensions, insurance and others. The conditions under which savings products may be offered have not been delineated. Currently, only MFIs that are incorporated as cooperatives or local area banks can offer such products. It is, hence, important that operational guidelines for savings products be provided, with sufficient safeguards. Systematic studies will need to be carried out in understanding the costs involved in mobilizing low ticket savings and designing appropriate products. Due diligence norms need to be evolved for deposit taking MFIs. SIDBI can help the MFIs to develop the skills and systems to mobilize savings; policy advocacy measures will be needed to promote deposit insurance coverage for the deposits mobilized by MFIs.

The micro finance development council (MDC) can help build a more comprehensive database concerning various aspects of micro finance. Analytically rigorous policy-oriented research will need to be encouraged. The costs and benefits of administering and complying with the provisions of the microfinance Bill and of delivering microfinance services need to be analyzed and results incorporated in regulatory and operational practices. SIDBI can play a sector building role be enabling such policy studies to be carried out periodically. SIDBI being a member of MDCs can advice on policies and measures relating to use of technology, establishing of credit bureaus and financial literacy and financial education of microfinance members.

Since RBI can direct MFIs to become members of credit bureaus, the MFIs to need to prepare themselves for joining the credit information bureaus for which SIDBI can play a facilitating role.

11. RECOMMENDATIONS

Based on the study, following are the recommendations:

1. Cost reduction

1.1 Technology: The pool of knowledge, on available technologies for front and back end technologies for microfinance operations is limited. Moreover, the impact of investing on such technological applications on reduction in costs and increase in efficiency has not been well established. Experience of Equitas shows that technology can help scale up and achieve efficiencies of scale very quickly; SIDBI can consider undertaking a separate study on technology-based solutions available and adopted by MFIs, the costs vis-a-vis benefits to MFIs. Based on the study a technology fund may be set up enabling Tier II and Tier III institutions to scale up operations effectively. The nature of funding can be soft loans or pure grants.

1.2 Client interface: With the recent RBI regulations on interest cap, there is a risk of excessive emphasis on reduction of transaction costs leading to dilution of the rigor of client acquisition, client training, centre meetings and relationship building, which form the fundamental pillars of microfinance service delivery. Though after the recent crisis there is greater emphasis on relationship building and Responsible Finance, MFIs will need technical assistance to undertake an assessment of their processes and arrive at a balance between cost reduction and client servicing. SIDBI and other development financing institutions can part finance the costs of such technical assistance especially for Tier II and Tier III institutions.

1.3 Salary norms: Since salaries constitute the major operating cost of the micro finance operations, MFIs need to adhere to salary norms for CEO and senior officials since these are skewed and there is increasing discomfort of the high salary levels. However, there are also good practices - Equitas CEO draws 40 times the salary of the field officer and downsized his pay packet to adhere to these norms set in the mainstream industry. Similar norms need to be developed through consensus building for adoption in the MF sector. Initiatives can be taken by industry associations as well as by lenders including SIDBI.

2. Risk management

2.1 Systems and Processes: In view of the recent RBI guidelines on stipulation on loans outstanding with borrowers, most MFIs will need to change their systems and processes as well as growth strategy in order to comply, since this issue will now manifest as dual risk of non-compliance as well as portfolio risk due to multiple lending and over indebtedness of clients. Adopting responsible finance principles and client centric business growth would only help MFIs face the external risks. Multipronged risk management strategy has to be followed by the MFIs. The consortium of lenders and adoption of a common governance policy across all MFIs can play a significant role in assessing the compliance of MFIs to the guideline through portfolio audits and compliance assessments.

2.2 Reporting to the Credit Bureaus: RBI guidelines issued have made mandatory for all MFIs to submit data to the credit information bureaus. Currently, two Credit Information Bureaus (CIBs), Equifax and High Mark are operational and have gathered data from few Tier I institutions. However, to make the CIBs comprehensive, the integration of Tier III and some of Tier II institutions in the current CIBs would be

important and this would be a major challenge. There is a need to provide technical support in the form of handholding and capacity building to these institutions. The Lenders Forum and other DFIs can provide support to such institutions in the form of grants to build their systems and subsidy to access Credit Information Reports from the CIBs. Technical Service Providers and other Capacity Building Institutions would help in providing such handholding and capacity building support to such institutions.

2.3 Portfolio risk of hidden defaults: The portfolio risk of hidden default due to peer repayments should be recognized as a risk that needs to be measured and monitored through data collection and reporting as part of risk management of MFIs. Portfolio audits should cover these aspects.

2.4 Audit and Control systems: Internal audit and branch rating systems are in practice in Tier I and Tier II MFIs. However, most Tier III institutions and some Tier II institutions still do not have robust internal audit and control systems. Such organizations will continue to require support from development institutions to set up and operationalize these processes. Technical assistance from service providers will have to be subsidized by development financial institutions.

3. Client awareness and Literacy

3.1 Financial Literacy: Only three institutions (CECODECON, Sahayata and Ujjivan) have undertaken some generic client literacy (generic financial literacy for clients apart from their products and services) initiatives. While these initiatives have been undertaken through grants from funding agencies, there is a need to undertake more such activities for their clients. The institutions are more focused towards providing credit services to their clients. It is not practical for MFIs to undertake these activities within the present stipulations on interest rates and fees. These initiatives either need to be taken up with Government or through donor support. One time in depth training on financial literacy through external agencies need to be arranged by MFIs and the staff can provide any incremental training regarding ongoing developments. SIDBI being part of Micro finance development council can influence the RBI to set up dedicated funding for such initiatives.

3.2 Transparency and Awareness of clients: The institutions visited were transparent with respect to providing information to their clients on their pricing details by mentioning it in the passbooks, educating them during Compulsory Group Training (CGT) and Group Recognition Test (GRT), among others. However, there is a need to undertake more innovative methods of communicating this information such as pictorial aids etc., in order to improve retention level of clients.

3.3 Compulsory Insurance: While compulsory insurance provides cushion for MFIs against risk of default in case of death of clients, clients require more comprehensive insurance on voluntary basis. The best practices in providing voluntary insurance services by MFIs need to be studied and scaled up with across other MFIs. Need based policy advocacy with IRDA/RBI will be necessary to enable NBFC MFIs to distribute these products.

3.4 Profitability and equity infusion: With interest rate cap, the profitability of MFIs will not be as robust as in the past which will affect their ability to attract equity. The consortium of lenders and other financial institutions has to play an enabling role in ensuring domestic equity funds are available especially to the Tier II and Tier III MFIs by augmenting its equity funds.

4. **Differential Interest Rates:**

The findings of the study clearly show that a uniform interest rate cap of 26% may not hold good for all institutions across India. There is a need to devise differential rate of interest for remote areas like Northeast and other hilly region, sparsely populated areas as western Rajasthan where the sparse population, infrastructure (roads, power, banking services) and geography (hills and plains) makes service delivery expensive. The study clearly depicts that the costs (costs of funds and operating) of providing credit services in such areas is more and hence the interest rates charged to clients is also high, which is necessary for sustainable growth of such institutions. Hence, we suggest that there is a need to have differential rate of interest for such institutions.

5. **Viability Gap Funding:**

The start-ups will need to be supported till they achieve viable level of operations. Interest rate cap is likely to lengthen the period for achieving operational self-sufficiency. Viability gap funding may be provided by DFIs based on business plans and milestones to be achieved.

Annexure 1: List of Documents Required

1. A brief note on the history and organogram / organizational structure of the organization.
2. Annual Reports for the last three years.
3. Financial Statements (with schedules) for the last three years, if unavailable in the Annual report
4. Rating / Grading or Assessment reports (Credit and Social), if any.
5. Any other reports available including Impact Assessment, Market Research, among others.
6. Details of the products and services offered (loans, savings and insurance) as on March 31, 2010 and December 31, 2010 and modifications, if any.
7. Distribution of loans outstanding across loan products and services offered by the MFI

Name of the loan product	Loans outstanding (31 March 2010)	% of share in total portfolio	Loans outstanding (31 Dec 2010)	% of share in total portfolio

8. Last 3 years' Portfolio reports (monthly/quarterly)
9. Operational manual for the microfinance operations of the organization.
10. Microfinance operational information of the organization for last three years (number of groups, number of members, number of active borrowers, number of field staff, number of villages/districts covered, loans outstanding, portfolio at risk, among others) according to the following table:

Key Indicators	2007-08	2008-09	2009-2010	Dec 31, 2010
Number of Groups				
Total number of Clients				
Total number of Active Clients (loanee)				

Total Savings mobilized (of SHGs) (Rs. in Lakhs)				
Share Capital (Rs. In Lakhs)				
Average Savings mobilized per member per month				
Average Savings per SHG (in Rupees)				
Total Loan outstanding (Rs. In Lakhs)				
Average Loan Outstanding (in Rupees)				
Total External Loan outstanding (Rs. in Lakhs)				
Rate of Interest charged (by the NGO/MFI)				
Rate of Interest (other MFI, FI)				
Repayment Rate (Internal)				
Repayment Rate (External)				
No of Villages				
No of Districts				
No of States				
No. of Branches				
No. of Field offices				
No. of Field staff / credit officers				
Portfolio at Risk (> 30 days, >60 Days)				

11. Number, quantum / amount and product wise loan disbursed by the organization as on March 31, 2010 and December 31, 2010 according to the following table:

Loan Products	Number of Loans	Amount / Quantum of Loans
Total		

12. Copies of agreement / contract / term sheets with financial institutions for loans and grants.

13. Details of all loans / grants received by the organization from financial institutions (FIs) and others (date of receiving of loan, cumulative amount of loan received, repayment terms and period of loan, principal outstanding as on March 31 2010 and December 31 2010 and interest rate charged) according to the following table:

Amount of Loans received

Name of FI	Receipt Date	Amount (in Rupees)	Period (in years)	Interest rate	Repayment terms	Outstanding	
						as on March 31, 2010	as on Dec 31, 2010

Amount of Grants received

Name of FI	Receipt Date	Purpose of grant	Amount (in Rupees)	Purpose, if any

14. Salaries and other perks including ESOPS

	Salary	Other perks	ESOPS
CEO			
Middle level manager			
Branch manager			

Field officer			

15. Insurance details:

Parameters	2007-08	2008-09	2009-10	As on Dec 2010
Insurance Premium Collected from the field				
Actual Insurance Premium paid to the Provider				
Number of Insured persons				
Number of Claims processed				
Amount of Claims processed				
Number of Claims Settled				
Amount of Claims Settled				

Annexure 2(A): Interview Checklist with MFI staff (Senior and Operation)

Name of MFI : ____

Form : (For profit company/section 25 co/society/Trust /other (specify)

Name of the persons interviewed : ____

Designations : ____

Years of experience of the MFI : ____

1. Terms and conditions of the credit products (as per the checklist of APR)

Costs and Margin

2. Details and clarifications on break-up and trends of costs (based on 3 years financial statements)
3. Details and clarifications on break-up and trends of income
4. Trends of income versus trends in costs – (analyze before hand and then discuss – do they move in the same direction or in different directions – if the latter, then obtain detailed information on the reasons)
5. Broad Processes followed in a branch in client acquisition, client education, loan origination, appraisal, disbursement and recovery (Also the views of the MFI on whether any part of their process considered unique and if so what are the cost implications)
6. Aspects of transaction costs for providing services to the members / clients – which processes are driving costs? How can they be reduced?
7. What are the various costs of loan funds in addition to interest? How do these costs compare among different kinds of lenders – SIDBI, private banks, public banks, other institutions. What is the trend?
8. What are the different risks (perceived and actual) to provide services to the members / clients and the costs associated with it?
9. How does risk/risk cost vary with (1) products, (2) region, (3) any other parameters?
10. How are the margins targeted? For each product? For the institution as a whole?

Interest rates and charges

11. Has the MFI changed the interest rate of the major product/s in the last 3 years? Details of when and how much?
12. What were the reasons based on which this change was made?
13. Has the MFI changed the other charges (processing fees, insurance charges, pre-payment fees etc.) for the major product/s in the last 3 years?
14. What were the reasons for these changes?
15. What will be the effect on MFI if the Malegam committee recommendations on interest rate and other charges are accepted by RBI?
16. What about loan size cap and purpose restriction? How will this affect interest rates?
17. Who are the competitors to the MFI? What are their charges – interest and others?
18. What are the rates charged by mainstream banks for similar loans? Is it cost effective for the clients to borrow from banks/co operatives?

Equity costs

19. What is the shareholding pattern?
20. What is the share premium fixed in different rounds of raising equity?
21. How does the MFI ensure adequate return on shares (and premium)? What is adequate return?
22. If Malegam committee recommendations, are accepted by RBI whether the MFI will be able to attract equity and whether it will be able to provide adequate returns on equity?
23. How can the MFI retain the equity investments in the business?

Technology

24. What kind of technological interventions have been done in operations?
25. What is the level of scale (number of clients/number of branches) at which these interventions have been carried out?
26. Have these interventions led to reduction in cost of operations in these branches? If yes, in what ways (which costs) and by how much?
27. What are the investment costs for the technological application?

28. Is the management looking to scale it up to other branches? What is the time frame? What are the considerations driving this decision?
29. What is the MIS application used by the organization?
30. How has the application impacted operations and monitoring?
31. Has it led to reduced costs (risk costs, costs of supervision)?

Developmental activities

32. Does the MFI undertake developmental activities for its clients?

Directly or through another sister establishment?

33. How are the costs of these activities covered – from separate grants, income from MF operations, both?

Annexure 2(B): Interview Checklist with MFI staff (Field / Operations)

1. Broad Processes followed in a branch in client acquisition, client education, loan origination, appraisal, disbursement and recovery
2. How can efficiency be improved and costs be reduced?
3. Product details
4. Who are the competitors to the MFI? What are their charges – interest and others? How does the MFI compare with others?
5. What are the different risks (perceived and actual) to provide services to the members / clients and the costs associated with it?
6. How is the loan default risk managed by the branch?
7. What are the materials and processes used by staff for communication to clients on products, interest rates and other costs?
8. Social and community related activities conducted by the organization (check materials and report, is available)
9. Training and CB activities conducted by the institution (check materials)
10. The Malegam committee has said that loans of Rs15,000 and above should carry a term of two years – what are the implications of this to the MFI?

Annexure 3: Client Questionnaire

MFI name :______________________________

Branch name :______________________________

District name :______________________________

Village Name :______________________________

Date of visit :______________________________

Interviewer Name :______________________________

1. Client details

Name	Client of MFI since	Gender	Caste – SC/ST/Minority/ OBC/others	Education	Occupation/Sources of income for family
					1) 2) 3)

2. Details of the **current loans** outstanding with MFI **(as ascertained from client record/passbook)(Mark √)**

Score	Loan product/ purpose	Date	Loan amount disbursed by MFI to the client	Term of loan	Interest rate	Loan processin g fee	Insurance Charges/ fee/ premium	Security deposit	Repaymen t schedule	Any other charges
Yes										

No										
NA										

*NA=not applicable

3. Information shared by MFIs to the client on the loans and procedures on a scale of 1 to 10 on the 10 parameters in question 2 above. (Count "YES" and "NA" for scoring) **Score ___________**

4. Awareness level of the clients on the current outstanding loan from the MFI. **(in discussion with the clients and in comparison with the client record/passbook)**

Score	Loan product/ purpose	Date/ month	Loan amount disbursed by MFI to the client	Term of loan	Interest rate	Loan processin g fee	Insurance	Security deposit	Repaymen t schedule	Late payment/ prepayme nt charges
Response of the client										
Aware										
Unaware										

5. Awareness of the clients on the loans and procedures on a scale of 1 to 10 on the 10 parameters in question 4 above. (count Aware and Unaware for scoring) **Score ___________**

6. Details of the other loans (availed in last 12 months) from other sources for the household (MFI, Banks, Finance Cos., Commission Agents, Traders, Relatives, Moneylenders etc.):**(as ascertained from the household record)**

Source of loan	Loan product/ purpose	Date/month	Loan amount	Term of loan	Interest rate	Loan processing fee	Collateral/deposit

7. Cost and Time taken for availing the loans (MFI, Banks, Finance Cos., Commission Agents, Traders, Relatives, Money lenders etc.): **(Maintain the same order as question 6)**

Source of loan	Average time between loan application and loan disbursement	Number of visits to be made by client to get the loan	Direct expense to avail that loan (Photocopy, photographs, revenue stamps, travel cost, among others)	Indirect expense for availing loan (Bribes, commission, loss of wages, among others)

8. Participation in social and community related activities organized by the institution

Activity	Does member know about the social activity? (Y/N)	Does member attended these activity (Y/N)	Payment/charges to avail the benefits (Y/N/DK)	Whether this activity done by MFI or sister organization or in collaboration with a social institution?	Whether only MFI clients can avail these services? (Y/N)

9. Managing default members in the SHG/centers/JLG

Have you ever paid for the default member in your group? (Y/N)	How many times?	Did you need to borrow money for that? (Y/N)	In how many days the money has been repaid back to you?

Annexure 4: Tool for Financial Analysis

Name of MFI	
Address and other contact details	
Age of MF operations	
Legal status	

Financial Products offered by the MFI to clients		31-Mar-08	31-Mar-09	31-Mar-10
a) savings				
Number of products				
b) loans				
Number of products				
c) insurance				
Number of products				
d)remittance				
e) pension				
f) other				

Other services provided				
a)				
b)				
c)				

Growth in the last three years

Basic details		31-Mar-08	31-Mar-09	31-Mar-10	Annualized +/- in percentage
Number of clients	Number				
Number of active borrowers	Number				
Number of active loan accounts	Number				
Number of active savers	Number				
women clients to total clients	percentage				
client drop out	percentage				
Number of branches	Number				
Out of which in rural areas	number				
Number of total staff	Number				
Number of credit officers	number				
Total staff					
Staff turnover	percentage				
Loan outstanding	amount				
Savings outstanding	amount				
Total assets	amount				
Average savings outstanding per client	amount				
Average Loans outstanding per client	amount				
Specify how clients are defined					
Check how the MFI define active borrower					
GNI per capita					

Average outstanding loans to GNI per capita	amount		0%	0%	
Non financial					
Number of clients in Enterprise promotion courses	Number				
% of clients in enterprise promotion courses	percentage				
Number of clients in client education courses	Number				
Percentage of clients in client education courses	percentage				
Number of clients covered in women empowerment initiatives	Number				
Percentage of clients covered in women empowerment initiatives	percentage				

	Unadjusted Financial statements				**Adjustments (+ or -)**			**Adjusted financial statements**		
	Income Statement	**31-Mar-08**	**31-Mar-09**	**31-Mar-10**	**31-Mar-08**	**31-Mar-09**	**31-Mar-10**	**31-Mar-08**	**31-Mar-09**	**31-Mar-10**
	Operating Income									
1	Interest on loan portfolio									
2	Fees and commission on loan portfolio									
3	Income from other finance -related services									
4	Income from investment									
5	Other Income									
6	**Total Operating Income**									
	Financial Expenses									
7	Interest & fee expenses on borrowings									

8	Interest on deposits										
9	other financial expense										
10	**Total financial expense**										
11	**Gross financial margin**										
	Loan Loss Expenses										
12	Loan loss provision expenses										
13	Loan written off										
14	Value of loans recovered										
15	**Total loan loss expense**										
16	**Net financial margin**										
	Operating Expenses										
17	Personnel expenses										
18	Administrative expenses										
19	Depreciation										
20	Other administrative expenses										
21	Other Operating Expenses										
22	**Total Operating expenses**										
23	**Net Operating Profit/ (Loss)**										
	Pro. For Capital Reserves										
	Net Profit										
25	Non operational revenue										
26	Non operational expenses										
27	**Net Income (before taxes)**										
28	Taxes										
29	**Net Income after taxes**										
30	Cash Donation										
31	Donations for loan capital										

32	Donations for operating expenses										
33	**Total Consolidated Profit /(Loss)**										

Unadjusted balance sheet							Adjusted Balance Sheet		
Assets		**31-Mar-08**	**31-Mar-09**	**31-Mar-10**		**Assets**	**31-Mar-08**	**31-Mar-09**	**31-Mar-10**
	Cash and Due from Banks					Cash and Due from Banks	0.00	0.00	0.00
	Fixed deposits in banks					Fixed deposits in banks	0.00	0.00	0.00
	Short term investment in market instruments					Short term investment in market instruments	0.00	0.00	0.00
	Total loan portfolio					Total loan portfolio	0.00	0.00	0.00
	(Loan loss reserve)					(Loan loss reserve)	0.00	0.00	0.00
	Other Reserves					**adjustments to loan loss provision**	0.00	0.00	0.00
	Other short term assets					Other short term assets	0.00	0.00	0.00
	Long term investments					Long term investments	0.00	0.00	0.00
	Net fixed assets					Net fixed assets	0.00	0.00	0.00
						adjustments to depreciation			
	Total Assets					**Total assets**	**0.00**	**0.00**	**0.00**
Liabilities						**Liabilities**			
	Savings Accounts :forced					Savings Accounts :forced	0.00	0.00	0.00
	Savings Accounts :voluntary					Savings Accounts :voluntary	0.00	0.00	0.00

	Time deposits			
	Loans: Commercial Banks			
	Loans:			
	Loans: subsidized			
	Other short term liabilities			
	other long term liabilities			
	Total liabilities			
Equity				
	Paid in equity from shareholders			
	Donated equity -prior year cumulative			
	Donated equity -current year			
	Prior years retained earnings with donation / losses			
	Current years retained earnings/ losses			
	Other capital accounts/reserves			
	Net Profit			
	Total Equity			

Time deposits	0.00	0.00	0.00
Loans: Commercial Banks	0.00	0.00	0.00
Loans:	0.00	0.00	0.00
Loans: subsidized	0.00	0.00	0.00
Other short term liabilities	0.00	0.00	0.00
other long term liabilities	0.00	0.00	0.00
Total liabilities	**0.00**	**0.00**	**0.00**
Equity			
Paid in equity from shareholders	0.00	0.00	0.00
Donated equity -prior year cumulative	0.00	0.00	0.00
Donated equity -current year	0.00	0.00	0.00
Prior years retained earnings with donation / losses	0.00	0.00	0.00
Current years retained earnings/ losses	0.00	0.00	0.00
Other capital accounts/reserves	0.00	0.00	0.00
Net profit	0.00	0.00	0.00
Total Equity	**0.00**	**0.00**	**0.00**
Subsidies in cost of funds, operating expenses etc.,			

	Total liabilities and equity			

Total liabilities and equity	0.00	0.00	0.00

Average loan portfolio			
Average gross loan portfolio	-	-	-
(at least quarterly averages preferable, if not, take average of year end balances)			
Average assets			
Average assets (avg of year end balances)	0	0	0
Average equity			
Average equity (avg of year end balances)	-	-	-
Average debt	0	-	-

Ratio analysis		31-Mar-08	31-Mar-09	31-Mar-10
Profitability / Sustainability				
Adjusted Return on Assets (AROA)	(Net Operating Income, less Taxes)/ Average Assets			
Adjusted Return on Equity (AROE)	(Net Operating Income, less Taxes)/ Average Equity			
Operational Self-Sufficiency (OSS)	Financial Revenue (Total)/ (Financial Expense + Loan Loss Provision Expense + Operating Expense)			

Efficiency / Productivity / Risk				
Operating Expense /average Loan Portfolio	Operating Expense / Period Average Gross Loan Portfolio			
Adjusted Cost per Borrower (rupees)	Operating Expense/ Average Number of Active Borrowers			
Borrowers per credit officer	Number of Active Borrowers / Number of credit officer			
Portfolio At Risk> 30 days	Portfolio at Risk > 30 days/ Gross Loan Portfolio			
(to be obtained from portfolio report)				
Revenues				
yield on portfolio	Financial income from portfolio/average loan portfolio			
total Yield	Financial Revenue/ Average Loan portfolio			
Adjusted Profit Margin	Net Operating Income/ Financial Revenue (Total)			
Margin	net operating income/average gross loan portfolio			
Expenses				
Adjusted Total Expense Ratio	(Financial Expense + Loan Loss Provision Expense + Operating Expense) / Average gross loan portfolio			
Adjusted Financial Expense Ratio	Financial Expense/ Average gross loan portfolio			
Adjusted Loan Loss Provision Expense Ratio	Loan Loss Provision Expense/ Average gross loan portfolio			
Adjusted Operating Expense Ratio	Operating Expense/ Average gross loan portfolio			
adjusted salaries ratio	salaries to average gross loan portfolio			
adjusted administrative expenses ratio	administrative expenses to average gross loan portfolio			

Financial Management				
Gross Loan Portfolio / Total Assets	Gross Loan Portfolio/ Total Assets			
Debt equity	average debt / average equity			
Other key indicators				
Salary and compensation package in MFI				**31-Mar-10**
salary of Manager				
salary of Field staff				
Ratio of Salary and perks of CEO to field staff				

Annexure 5: Schedule of Visits to MFIs for Data collection

Sl. No.	Name of the MFI	Dates of Visit (Parent State)	Dates of Visit (Other States)
	East Zone		
1	Nav Bharti Jagriti Kendra	Mar 11-13, 2011	
2	Sajja Finance Pvt. Ltd.	Mar 8-10, 2011	
3	North East Region Financial Services Ltd.,	Mar 31-Apr 5, 2011	
4	Chanura Microfin	Mar 28-30, 2011	
5	Bandhan Financial Services	Mar 14-17, 2011	Apr 2, 2011
6	Sahara Uttarayan	Mar 10-12, 2011	
7	People's Forum	Mar 7-9, 2011	
8	Asmitha Microfin Ltd	May 2, 2011	May 20-21, 2011
	North Zone		
1	Cashpor Micro Credit	Mar 28-30, 2011	May 9-10, 2011
2	Sonata Finance Pvt. Ltd.	Mar 10-12, 2011	Apr 30, 2011
3	NEED	Mar 18-20, 2011	
4	Mimoza Enterprise Finance Pvt. Ltd.	May 9-11, 2011	
5	Satin Credit Care Network Ltd.	May 12-13, 2011	May 18, 2011
	South Zone		
1	Equitas Microfinance Ltd.	Mar 3-5, 2011	May 3-5, 2011
2	Bharatiya Samrudhi Finance Ltd.	Mar 10-12, 2011	May 4, 2011
3	SKDRDP	Mar 19-21, 2011	
4	Share Microfin Ltd.	May 2, 2011	May 19-20, 2011
5	SKS Microfinance Ltd.	Mar 30-31, 2011	Apr 25-26, 2011; May 19, 2011
6	Spandana Sphoorty Financial Ltd.	Mar 22-24, 2011	Apr 26-27, 2011;

			May 19, 2011
7	Rashtriya Seva Samiti	Mar 25-28, 2011	
8	Janalakshmi Financial Services Pvt. Ltd.	Apr 11-13, 2011	
9	RORES MED Trust	Apr 14-15, 2011	
10	Ujjivan Financial Services Pvt. Ltd	Apr 7-9, 2011	Apr 22, 2011
11	Hope Foundation	Apr 18-20, 2011	
12	Hand in Hand	Mar 16-18, 2011	
13	SMILE	Apr 28-30, 2011	
	West Zone		
1	CECODECON	Mar 1-2, 2011	
2	Lupin Human Welfare & Research Foundation	Apr 6-7, 2011	
3	Sahayata Microfinance Pvt. Ltd.	Mar 21-23, 2011	May 3-5, 2011
4	MAS Financial Services Ltd.	May 2-4, 2011	

Annexure 6: Basic Details of Sample MFIs

S. No.	Name of the MFI	Tier	Model	Legal form	Operational Area	Client Outreach	Loans Outstanding
						2009-10	2009-10
1	Nav Bharti Jagriti Kendra	Tier III	SHG	Not for Profit	East	9,908	5,74,47,377
2	Saija Finance Pvt. Ltd.	Tier III	JLG	For Profit	East	7,960	4,57,29,000
3	North East Region Financial Services Ltd.	Tier III	SHG	For Profit	East	43,130	1,43,76,75,000
4	Chanura Microfin	Tier III	JLG	Not for Profit	East	5,125	2,72,63,490
5	Bandhan Financial Services	Tier I	Grameen	For Profit	Multi Region	25,24,935	11,96,56,45,597
6	Sahara Uttarayan	Tier II	Grameen	For Profit	East	11,988	6,24,65,788
7	People's Forum	Tier II	SHG	For Profit	East	46,865	22,02,80,000
8	Asmitha Microfin Ltd	Tier I	Grameen	For Profit	Multi Region	13,40,288	10,82,89,18,639
9	Cashpor Micro Credit	Tier I	Grameen	Not for Profit	North	4,17,039	1,96,89,33,227
10	Sonata Finance Pvt. Ltd.	Tier II	Grameen	For Profit	North	85,897	49,89,96,233
11	NEED	Tier III	JLG	Not for Profit	North	32,718	20,13,60,981
12	Mimoza Enterprise Finance Pvt. Ltd.	Tier II	Grameen	For Profit	North	52,345	36,71,62,254
13	Satin Credit Care Network Ltd.	Tier II	JLG	For Profit	North	1,66,102	1,27,30,88,686
14	Equitas Microfinance Ltd.	Tier I	Grameen	For Profit	Multi Region	8,88,600	4,78,55,47,820
15	Bharatiya Samrudhi Finance Ltd.	Tier I	JLG	For Profit	Multi Region	11,14,468	7,74,87,08,000
16	SKDRDP	Tier I	SHG	Not for Profit	South	11,21,690	6,14,86,88,114
17	Share Microfin Ltd.	Tier I	Grameen	For Profit	Multi Region	28,10,000	16,93,54,04,333
18	SKS Microfinance Ltd.	Tier I	Grameen	For Profit	Multi Region	57,95,028	29,36,72,04,521
19	Spandana Sphoorty Financial Ltd.	Tier I	Grameen	For Profit	Multi Region	36,70,000	21,30,08,27,762
20	Rashtriya Seva Samiti	Tier III	SHG	Not for Profit	South	47,265	67,51,26,686
21	Janalakshmi Financial Services Pvt. Ltd.	Tier II	JLG	For Profit	South	79,808	67,04,58,804

22	RORES MED Trust	Tier III	JLG	Not for Profit	South	26,238	15,19,15,717
23	Ujjivan Financial Services Pvt. Ltd	Tier I	Grameen	For Profit	Multi Region	5,66,929	3,70,77,37,907
24	Hope Foundation	Tier II	SHG	Not for Profit	South	57,445	20,23,60,000
25	Hand in Hand	Tier I	SHG	Not for Profit	South	82,118	43,78,42,256
26	SMILE	Tier II	Grameen	For Profit	South	2,14,280	1,36,45,87,822
27	CECODECON	Tier III	SHG	Not for Profit	West	5,323	6,84,45,000
28	Lupin Human Welfare & Research Foundation	Tier III	SHG	Not for Profit	West	4,276	3,41,89,000
29	Sahayata Microfinance Pvt. Ltd.	Tier I	Grameen	For Profit	Multi Region	1,39,179	1,03,89,32,000
30	MAS Financial Services Ltd.	Tier II	Individual	For Profit	West	1,61,580	3,88,47,340

Annexure 7: Average APRs for Key Products (as per the pricing structure applicable till December 31, 2010)

S. No.	MFI	Product	APR (Interest + Fee)	APR (Interest + Fee + Insurance)	APR (Interest + Fee + Insurance +Deposit)	APR (Interest + Fee + Deposit)
1	Asmitha	General Loan	30.46%	32.24%	32.24%	30.46%
2	Asmitha	Special Loan	29.68%	31.45%	31.45%	29.68%
3	Bandhan	Suchana Loan	23.05%	23.05%	28.24%	28.24%
4	BASIX	Samruddhi - Agri Allied Loan	30.50%	36.36%	36.36%	30.50%
5	BASIX	Samruddhi - Agri Allied - Non Dairy	29.12%	35.04%	35.04%	29.12%
6	BASIX	Samruddhi - Crop Loan	27.49%	32.60%	32.60%	28.38%
7	BASIX	Samruddhi - Livelihood Support to women JLG Loan	31.29%	39.03%	39.03%	31.29%
8	BASIX	Samruddhi - Microenterprise (NFS) Loan	29.87%	35.29%	35.29%	29.87%
9	CASHPOR	IGL	25.77%	26.81%	26.81%	25.77%
10	Hand in Hand	Education Loans	15.00%	16.09%	16.09%	15.00%
11	Hand in Hand	Grameen Loan	24.98%	26.08%	26.08%	24.98%
12	Hand in Hand	Sanitation Loan	15.54%	17.22%	17.22%	15.54%
13	Sahayata	Fresh Loan	34.60%	35.83%	35.83%	34.60%
14	Sahayata	Mid Term Loan	32.28%	33.05%	33.05%	32.28%
15	Sahayata	Re-Loan	31.01%	31.52%	31.52%	31.01%
16	Share	General Loan	30.87%	32.19%	32.19%	30.87%
17	SKDRDP	First Loan	18.02%	18.02%	20.39%	20.39%
18	SKDRDP	Housing Loan	17.82%	17.82%	18.82%	18.82%
19	SKDRDP	Infrastructure Loan	17.71%	17.71%	18.25%	18.25%
20	SKDRDP	Livelihood Loan	17.23%	17.23%	17.79%	17.79%
21	SKDRDP	Revolving Loan	17.99%	17.99%	18.88%	18.88%

22	SKS	Income Generation Loan	26.71%	31.08%	31.08%	26.71%
23	SKS	Mid Term Loan	26.71%	31.08%	31.08%	26.71%
24	Spandana	Abhilasha Loan	28.79%	31.19%	31.19%	28.79%
25	Ujjivan	Business Loan	24.45%	26.08%	31.31%	29.52%
26	Ujjivan	Family Loan	26.22%	27.93%	33.52%	30.36%
27	Equitas	MF Loan-I	25.81%	26.64%	26.64%	25.81%
28	Equitas	MF Loan-II	25.62%	26.48%	26.48%	25.62%
29	Hope Foundation	Group Loan	30.35%	32.60%	39.94%	37.16%
30	Janalakshmi	Small Group Loan	32.80%	34.19%	40.72%	39.03%
31	MAS	MSME Loan	27.45%	27.45%	27.45%	27.45%
32	Mimo Finance	JLG Loan	36.46%	39.91%	39.91%	36.46%
33	Mimo Finance	Meso Loan	30.21%	33.39%	33.39%	30.21%
34	People's Forum	SHG Loan	25.12%	25.12%	25.12%	25.12%
35	Sahara Uttarayan	Small Loan	29.81%	31.18%	38.28%	36.59%
36	Satin	JLG Loan	37.91%	41.47%	41.47%	37.91%
37	Smile	Micro Credit	39.44%	39.44%	39.44%	39.44%
38	Sonata	General Loan	31.07%	33.58%	33.58%	31.07%
39	Sonata	Individual Loan	32.97%	34.09%	34.09%	32.97%
40	CECOEDECON	SHG Loan	19.60%	20.67%	23.85%	22.53%
41	Chanura	SSS Loan	36.99%	39.20%	39.20%	36.99%
42	Lupin	Microfinance Loan	19.79%	19.79%	19.79%	19.79%
43	NBJK	JLG Loan	23.39%	23.39%	28.04%	28.04%
44	NBJK	SHG Loan	25.86%	25.86%	25.86%	25.86%
45	NEED	JLG Loan	26.51%	28.62%	34.71%	32.12%
46	NEREFS	Microfinance Loan	50.09%	50.09%	50.09%	50.09%
47	RASS	SHG Loan	19.08%	19.08%	19.08%	19.05%
48	Rores	Individual Loan - Weekly	28.07%	29.62%	33.22%	31.46%
49	Rores	Group Loan	31.16%	33.10%	38.83%	36.52%
50	Saija	Saija Mahila RIN	38.08%	40.60%	40.60%	38.08%

51	Saija	Saija Karibari Rin	42.52%	45.31%	55.71%	52.26%
		Average	**28.19%**	**29.99%**	**31.48%**	**29.61%**

Annexure 8: APRs as per the latest pricing structure

Note: *these APRs are based completely on the theoretical calculations as per the information shared by the MFIs and are not verified in the field.*

S. No.	MFI	Product	APR (Interest)		APR (Interest + Fee)		APR (Interest + Fee + Insurance)		APR (Interest + Fee+ Insurance+ Deposit)		APR (Interest + Fee + Deposit)	
			Min	Max	Min	Max	Min	Max	Min	Max	Min	Max
1	Asmitha	General Loan	19.60%	24.55%	19.60%	29.97%	20.40%	31.12%	NA	NA	NA	NA
2	Asmitha	Special Loan	22.35%	24.91%	26.28%	64.90%	26.55%	82.32%	NA	NA	NA	NA
3	BASIX	Samruddhi - Agri Allied Loan	24.00%	24.00%	26.71%	27.96%	28.18%	31.57%	NA	NA	NA	NA
4	BASIX	Samruddhi - Agri Allied - Non Dairy	24.00%	24.00%	26.71%	27.96%	28.18%	31.57%	NA	NA	NA	NA
5	BASIX	Samruddhi - Crop Loan	24.00%	24.00%	25.80%	27.39%	28.57%	32.54%	NA	NA	NA	NA
6	BASIX	Samruddhi - Livelihood Support to women JLG Loan	24.00%	24.00%	27.07%	27.96%	29.09%	31.57%	NA	NA	NA	NA
7	BASIX	Samruddhi - Microenterprise (NFS) Loan	24.00%	24.00%	26.71%	27.96%	28.18%	31.57%	NA	NA	NA	NA
8	CASHPOR	IGL	23.94%	23.94%	26.08%	26.08%	27.17%	27.17%	NA	NA	NA	NA
9	Sahayata	MidTerm Loan	26.00%	26.00%	28.24%	28.24%	Details not available		NA	NA	NA	NA
10	Sahayata	Re-Loan	26.00%	26.00%	27.56%	28.24%	Details not available		NA	NA	NA	NA
11	Share	General Loan	26.00%	26.00%	27.56%	27.56%	Details not available		NA	NA	NA	NA
12	Spandana	Abhilasha Loan	19.78%	24.63%	19.78%	26.86%	21.97%	29.11%	NA	NA	NA	NA
13	Spandana	Pragathi Loan	24.00%	26.00%	24.00%	31.05%	29.03%	36.18%	NA	NA	NA	NA
14	Ujjivan	Business Loan	26.00%	26.00%	27.46%	28.32%	28.05%	33.06%	NA	NA	NA	NA
15	Ujjivan	Family Loan	26.00%	26.00%	28.05%	28.32%	28.88%	33.06%	NA	NA	NA	NA
16	Equitas	MF Loan-I	25.00%	25.00%	26.15%	26.17%	26.73%	26.77%	NA	NA	NA	NA
17	Equitas	MF Loan-II	25.00%	25.00%	26.15%	26.17%	26.73%	26.77%	NA	NA	NA	NA
18	Hope Foundation	Group Loan	22.71%	22.71%	24.77%	24.77%	Details not available		NA	NA	NA	NA

19	Janalakshmi	Small Group Loan	26.00%	26.00%	27.16%	28.05%	27.30%	29.09%	NA	NA	NA	NA
20	Mimo Finance	JLG Loan	26.00%	26.00%	28.12%	28.12%	28.68%	28.68%	NA	NA	NA	NA
21	Mimo Finance	Meso Loan	24.91%	24.91%	28.44%	33.00%	30.13%	34.55%	NA	NA	NA	NA
22	Sahara Uttarayan	Small Loan	20.44%	23.67%	21.44%	25.98%	22.05%	27.39%	NA	NA	NA	NA
23	Satin	JLG Loan	25.84%	27.98%	28.37%	30.53%	31.83%	34.02%	NA	NA	NA	NA
24	Sonata	General Loan	25.90%	26.00%	26.78%	27.94%	27.94%	30.10%	NA	NA	NA	NA
25	Sonata	Individual Loan	25.96%	26.00%	26.59%	26.95%	27.50%	27.78%	NA	NA	NA	NA
26	Lupin	Microfinance Loan	20.50%	20.50%	21.15%	26.44%	NA	NA	NA	NA	NA	NA
27	Saija	Saija Mahila RIN	26.00%	26.00%	28.21%	28.41%	29.70%	30.85%	NA	NA	NA	NA
28	Saija	Saija Karibari Rin	26.00%	26.00%	28.21%	28.41%	29.70%	30.85%				
29	Bandhan	Suchana Loan	Under Revision									
30	Chanura	SSS Loan	No Change									
31	NEED	JLG Loan	No Change									

Annexure 9: Weighted Average APR across the portfolio

S. No	MFI	Tier	Legal Form	Model	Number of Products Studied	WA-APR (Interest+ Fee)	WA-APR (Interest+ Fee+ Insurance)	WA-APR (Interest+ Fee+ Insurance+ Deposit)	WA-APR (Interest+ Fee+ Deposit
1	Asmitha	Tier I	NBFC	Grameen	2	30.46%	32.24%	32.24%	30.46%
2	Bandhan	Tier I	NBFC	Grameen	1	23.05%	23.05%	28.24%	28.24%
3	BSFL	Tier I	NBFC	JLG	5	29.91%	35.55%	35.55%	29.96%
4	Belstar/Hand in Hand	Tier I	Society	SHG	3	24.73%	25.83%	25.83%	24.73%
5	CASHPOR	Tier I	Section 25	Grameen	1	25.77%	26.81%	26.81%	25.77%
6	CECODECON	Tier III	Society	SHG	1	19.60%	20.67%	23.85%	22.53%
7	Chanura	Tier III	Society	JLG	1	36.99%	39.20%	39.20%	36.99%
8	Equitas	Tier I	NBFC	Grameen	2	25.79%	26.62%	26.62%	25.79%
9	Hope Foundation	Tier II	Trust	SHG	1	30.35%	32.60%	39.94%	37.16%
10	Janalakshmi	Tier II	NBFC	JLG	1	32.80%	34.19%	40.72%	39.03%
11	Lupin	Tier III	Society	SHG	1	19.79%	19.79%	19.79%	19.79%
12	MAS	Tier II	NBFC	Individual	1	27.45%	27.45%	27.45%	27.45%
13	Mimo Finance	Tier II	NBFC	Grameen	1	36.07%	39.50%	39.50%	36.07%
14	NBJK	Tier III	Society	SHG	2	25.06%	25.06%	26.56%	26.56%
15	NEED	Tier III	Society	JLG	2	26.51%	28.62%	34.71%	32.12%
16	NEREFS	Tier III	NBFC	SHG	1	50.09%	50.09%	50.09%	50.09%
17	People's forum	Tier II	NBFC	SHG	1	25.12%	25.12%	25.12%	25.12%

18	RASS	Tier III	Society	SHG	1	19.08%	19.08%	19.08%	19.05%
19	Rores	Tier III	Trust	SHG	2	30.84%	32.74%	38.26%	36.00%
20	Sahara Uttrayan	Tier II	NBFC	ASA	1	29.81%	31.18%	38.28%	36.59%
21	Sahayata	Tier I	NBFC	Grameen	3	33.76%	34.82%	34.82%	33.76%
22	Saija	Tier III	NBFC	JLG	2	39.20%	41.79%	44.42%	41.66%
23	Satin	Tier II	NBFC	JLG	1	37.91%	41.47%	41.47%	37.91%
24	Share	Tier I	NBFC	Grameen	1	30.87%	32.19%	32.19%	30.87%
25	SKDRDP	Tier I	Trust	SHG	5	17.85%	17.85%	18.79%	18.79%
26	SKS	Tier I	NBFC	Grameen	2	26.71%	31.08%	31.08%	26.71%
27	Smile	Tier II	NBFC	JLG	1	39.44%	39.44%	39.44%	39.44%
28	Sonata	Tier II	NBFC	Grameen	2	31.07%	33.58%	33.58%	31.07%
29	Spandana	Tier I	NBFC	Grameen	1	28.79%	31.19%	31.19%	28.79%
30	Ujjivan	Tier I	NBFC	Grameen	2	24.84%	26.49%	31.80%	29.71%

Annexure 10: Banks under each category of funding sources

Nationalized Banks		Developmental Institutions	Private Banks	NBFCs
Allahabad Bank	Jammu and Kashmir Bank	Ananya	Bank of Bahrain and Kuwait	Aditya Birla
Andhra Bank	Karnataka Bank	Basix	Barclays Bank	HLF Pvt. Ltd.,
Axis Bank	Karur Vysya Bank	Bellweather Fund	BNP Paribas	Mahindra Finance
Bank of Baroda	Lakshmi Vilas Bank	FWWB (I)	Catholic Syrian Bank	MAS Financial Services
Bank of India	Oriental Bank of Commerce	IFMR Capital	Citi Bank	MV Microfinance Pvt. Ltd.,
Bank of Maharashtra	Punjab National Bank	Kerala Financial Corporation	Development Credit Bank	Reliance Capital
Bank of Rajasthan	Punjab and Sind Bank	KFSC / NCD	Deutsche Bank	Tata Capital
Canara Bank	State Bank of Hyderabad	Manveeya	Federal Bank	
Central Bank of India	State Bank of India	NABARD	HSBC	
Centurion Bank of Punjab	State Bank of Patiala	National Housing Bank	ICICI Bank	
City Union Bank Limited	State Bank of Tranvancore	Opportunity International	Kotak Mahindra Bank	
Corporation Bank	State Bank of Mauritius	Rabo India	Royal Bank of Scotland	
Dena Bank	South Indian Bank	Rashtriya Gramin Vikas Nidhi	Standard Chartered Bank	**RRBs**
Dhanalakshmi Bank	Syndicate Bank	Rashtriya Mahila Kosh	Societe Generale	Aravrat Gramin Bank
HDFC Bank	Union Bank of India	SIDBI	Yes Bank	Karnataka Vikas Gramin Bank
IDBI Bank	United Bank of India	Uttaranchal Government		Mewar Anchalik Gramin Bank
Indian bank	Vijaya Bank			Pragathi Grameen Bank
Indus Ind Bank				South Malabar Gramin Bank
ING Vysya Bank				
Indian Overseas Bank				

Annexure 11: Benchmarking of Studied MFIs with that of the Global, South Asian and other comparable markets

**Data source: MIX Data -2009*

	World	South Asia	Bangladesh	Indonesia	Cambodia	Philippines	Sampled MFIs-India
Costs							
Administrative expense/ assets	6.05%	4.13%	2.78%	5.85%	5.12%	7.84%	3.67%
Operating expense/ loan portfolio	18.45%	14.19%	14.55%	17.43%	14.40%	23.40%	11.32%
Personnel expense/ loan portfolio	10.15%	8.63%	10.94%	11.77%	9.43%	12.27%	6.42%
Funding							
Interest Rate on Term Loans, weighted average	NA	11.25%	9.43%	9.48%	8.83%	9.25%	11.94%
Financial expense/ assets	4.80%	6.25%	3.77%	8.06%	7.30%	3.73%	7.99%
Debt to equity ratio	2.85	5.55	6.64	4.22	3.37	4.53	5.31
Profitability							
Profit margin	8.43%	14.60%	12.79%	25.92%	17.02%	10.86%	21.76%
Return on assets	1.50%	3.03%	2.43%	5.44%	2.55%	2.17%	4.15%
Return on equity	7.27%	16.40%	15.47%	30.68%	10.66%	13.11%	22.43%
Pricing							
Yield on gross portfolio (nominal)	28.00%	23.17%	22.29%	36.87%	31.46%	29.83%	26.58%

Efficiency							
Average loan balance per borrower	530	145	116	505	568	276	146
Average loan balance per borrower / GNI per capita	0.2799	0.15655	0.2066	0.22715	0.727	0.16035	0.14175
Borrowers per loan officer	235	301	240	252	165	238	453
Gross loan portfolio to total assets	76.47%	76.85%	76.93%	76.80%	83.45%	67.85%	81.12%
Loan loss rate	0.38%	0.01%	0.00%	0.56%	0.27%	0.38%	0.41%

Annexure 12: Details of WA-APR (Interest Only) across Microfinance Institutions below and above 26%

Microfinance Institutions	WA-APR (Interest Only) below 26%	Microfinance Institutions	WA-APR (Interest Only) above 26%
Hand in Hand	16.93%	Sahayata	28.83%
SKDRDP	17.11%	Sonata	28.84%
CECODECON	17.48%	Janalakshmi	29.05%
RASS	17.73%	Rores	29.10%
Lupin	18.83%	Mimo Finance	29.42%
Bandhan	20.81%	Saija	32.65%
Ujjivan	22.24%	Satin	33.18%
People's forum	22.37%	Chanura	34.81%
NBJK	23.60%	NEREFS	48.37%
BSFL	23.66%		
NEED	23.75%		
Hope Foundation	23.79%		
Smile	24.51%		
Share	24.56%		
SKS	24.56%		
Spandana	24.56%		
MAS	24.59%		
Asmitha	24.60%		
Sahara Uttrayan	25.55%		
CASHPOR	25.77%		
Equitas	25.79%		