Strategic Approach for Reviving Indian MFIs

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The Andhra Pradesh (AP) Microfinance crisis has attracted the attention of researchers, academicians and policy makers for analyzing the reasons for its failure and also for suggesting suitable policy measures for its revival. The rapid expansion of lending in search of abnormal returns, loose regulation and unprecedented reactions of burdened customers, and the possible contagion to the financial sector has brought the RBI's intervention. This paper believes that short-term customer protection measures would not ameliorate the situation. Microfinance Industry, with its linkages to other constituents in the financial services sector, requires integrated, multi-dimensional, strategic initiatives for long-term sustainable growth and avoidance of future systemic shocks. Better governance for trust, market diversification to avoid concentration risk, collaborative competition to harness the value chain, and market nurturing for sustainability are suggested at strategic level. Streamlining operations with IT integration, improving productivity of manpower, and effective credit appraisal are suggestions at operational level.

Section I
Introduction

The current scenario in the Indian Microfinance industry is a culmination of two major issues – underestimation of risks associated with lending to the lower income groups of society and the public response to a misconceived shift in the objective of Microfinance business. The industry had a stupendous growth due to its ability to attract various sources of capital. The industry came to a screeching halt in 2010 as the state government of Andhra Pradesh (AP) introduced

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regulations, reacting to the suicides of the debt burdened clients of the Microfinance Institutions (MFIs). Potential long-term consequences of the AP crisis and the impact of the emerging regulatory framework of Reserve Bank of India (RBI) on MFIs have become a hot topic of research. The expert viewpoints indicate that many MFIs with huge exposures to AP region or otherwise are on the brink of financial ruin and there are questions on their sustainability in the long-run (Ghiyazuddin and Gupta, 2012). If measures are not taken immediately, it may lead to bankruptcy of many MFIs (Sriram, 2012).

Social Inclusion, the unquestionable merit of the model of Microfinance, warrants support from the regulatory authorities of Money, Banking, Financial Services, and Capital Markets. The sought after goal of Financial Inclusion would remain a distant dream, if left to the existing channels of the financial services industry. The regulatory framework is expected to create an enabling environment for the industry players to pursue objectives of philanthropy and profit making. There is an imminent need for players of the industry to win back the trust of the clients and to deploy successful strategies, drawn from the applicable theories of strategy on business management.

This paper examines the characteristics of the Microfinance Industry from the perspective of corporate and business strategy to give a direction for its renewed operations in India, and also to prevent it from slipping into the jaws of bankruptcy. The rest of the paper is presented as follows: Section II would establish the need for the study, Section III would deliberate on some of the theories on corporate strategy relevant to MFIs, Section IV would suggest possible strategies which the MFIs could adopt, and Section V would present the concluding remarks.

Section II
Need for the Study

There is adequate literature on the microfinance industry, in the form of case studies, white papers, policy reviews, and research articles on the themes of Successful Models, Performance Analysis, Risks and Returns, Regulatory Framework etc., when compared to the themes on analysis of the Industry Structure, Competitive, and Business Strategies, of the players in the microfinance industry. The erstwhile, splintered, multi-format MFIs are today referred to as Microfinance Industry, owing to their accumulated experience on various business models, markets, products, consumer behaviour, risks, and rewards. Microfinance as a phenomenon has a social development tag attached to it, so they cannot be compared to any other Institution in the financial services sector, which are essentially for profit entities. Hence, MFIs cannot adopt the strategies adopted by entities which operate with the objective of shareholder wealth maximization. However, if the essence of the celebrated models of business strategy, is understood as optimal and effective deployment of scarce resources to the achievement of organizational objectives, then the paper argues that they are relevant for MFIs also. As mentioned in the opening lines of this section MFIs are referred to as entities belonging to Microfinance Industry, and hence, require more than just short-term, adhoc approach for revival. Strategic analysis of any business opens up multiple perspectives to a problem, thereby assisting the formulation of a more appropriate action oriented policy.

Section III
Review of Theories on Corporate Strategy

Approaches, Process and Tools: Corporate Strategy is a word used in the context of a firm, rather than at the level of an industry. "The reasons why firms succeed or fail is perhaps the central question in strategy" (Porter, 1991). The recorded history of business strategy in the management literature dates back to 1960s with major works of, Ansoff (1965), Chandler (1969), and Andrews (1971). The adoption of these theoretical frameworks by renowned Business Consulting Firms has made them acceptable in the industry (Abplanalp and Lombriser, 2005). There are various approaches to the strategic management process. Process Orientation (Chandler, 1969) – bringing together actions and resources to achieve the basic long-term goal – Capability Orientation (Porter, 1985) – positioning the competitive advantage of the firm through a strategic course of action, after a thorough analysis of the external environment – Evolving Orientation (Mintzberg & Waters, 1985) – a strategy emerging out of the compelling forces of the external environment, without adequate rational planning – Resource Orientation (Eisenhardt and Martin, 2000) – leveraging on firm's valuable, rare, inimitable, and non-substitutable resources to create successful competitive advantages to sustain dynamic external environment.

Strategic Management Process follows a logical sequence of steps, like Strategic Analysis, Strategy Formulation, Strategy Implementation, and Review of Strategy, as discussed repeatedly in the literature. There are some minor departures as shown in the works of Goodstein, Nolan and Pfeiffer (1993), Abplanalp and Lombriser (2005), etc. The process commences with a crucial step, Strategic Analysis, of analyzing the internal and external environment in which the organizations are operating. Initially the analysis of environment at the macroeconomic and industry levels is taken up followed by internal analysis at the firm level, to position a strategy. Literature on Strategy has indicated various time-tested strategic tools of external environment analysis, like the Porter's Five Forces, PEST analysis. At the firm level Value Chain Analysis, and Core Competency models are in vogue. SWOT Analysis, is a comprehensive framework, which encompasses both the external and internal analysis. Though most of these tools were intended to be used in relatively stable environments, their suitability for a dynamic environment is still unchallenged, owing to their fundamental nature.

Stability, Growth, and Retrenchment, broadly, are the three distinct generic strategies adopted by firms, in practice, most often, a combination of the first two is found during a favourable business environment and the first and third during unfavorable business conditions. The most celebrated three generic strategies of Porter are of course the Cost Leadership, Differentiation and Focus, wherein the firm can choose one after having understood its competitive advantage and its fitment to the external environment in which it is operating (Pretorius, 2008).

Impact of Business Environment on Strategy: The theories and tools of strategy referred above were built for stable environments, in terms of, market structures, regulations, patterns of demand and supply, entry and exit of firms. Stable environments do not change significantly, and are relatively predictable. Reality in business environment is more dynamic than stable, ever since the proliferation of globalization and information technology. The business environment is changing faster than before (Achrol, 1991; Hamel and Prahalad, 1994; Conner, 1998, as cited in Roger B Mason, 2007). The analysis of external environment is a crucial step in the process of strategy formulation and if the environment turns out to be dynamic, a single approach to strategy formulation would not suffice. The various dimensions of dynamicity in external environments are defined in the literature on strategy as velocity, complexity, and turbulence. Velocity is "the speed or rate at which new opportunities emerge" (Davis *et al.*, 2009). Complexity is "a measure of heterogeneity or diversity in environmental, sub-factors such as customers, suppliers, socio-politics and technology (Teopaco, 1993; Lane and Maxfield, 1996; Chae and Hill, 1997; Chakravarthy, 1997, as cited in Roger B Mason, 2007). Turbulence is defined as dynamism in the environment, involving rapid unexpected change in the environment sub-dimensions (Conner, 1998; Vorhies, 1998, as cited in Roger B Mason, 2007). In summary the complexity approach to studying the impact of environment on strategy believes that the external environment with the firm is a Complex Adaptive System (Black and Farias, 1997; Tedesco, 1998; Peters, 1999, as cited in Roger B Mason, 2007). The winning strategy for firms in a complex and turbulent environment is "adaptive innovation" (Roger B Mason, 2007), wherein the firm continuously innovates, to create a chaos in the environment through its new products essentially to thwart competition.

Turnaround Strategies: When firms faced with crisis are awaiting revival or turnaround, they require certain complimentary strategies apart from the generic strategies to renew their operations and retrace the growth path (Pretorius, 2008). Pretorius, defines turnaround as rescue of a firm, whose decline has threatened its existence, through re-orientation of position, strategy, structure, control systems and power distributions. Turnaround is often defined using metaphors owing to the complexity of its determinants (Bollen *et al.*, 2005; Kale and Arditi, 1998; Pretorius and Hotzhauzen, 2008; Probst and Raisch, 2005; as cited in Pretorius, 2008). The Resource Munificence Theory (Castrogiovanni, 1991) refers to the scarcity or abundance of critical resources available to the firm when it is facing the distress.

Finance is not the only scarcity to which this theory refers to. Environment Munificence Theory, as envisaged (Dess and Beard, 1984; Francis and Desai, 2005; Arogyaswamy *et al.*, 1995), talk about the environment's ability to hold or accommodate an organization at the time of distress. Robbins and Pearce (1992) discuss that Causality Theory, which classifies the causes of business failure to operational (internal) or (external) strategic factors. If the firm's competitive advantage or the demand for the basic product is eroded requiring the repositioning of the product or service, then it is a case for revival due to strategic problems, else the causes are operational. In Slatter (1984), the situation for revival is classified into three categories: hopeless cases, short-term survivors, and sustained recovery possibilities. Pretorius (2008) presents a matrix of Munificence and Causality theories in two separate sets, one defining the pre-condition requiring turnaround and the other suggesting a suitable strategy. Micheal Harker (1996), opines market intelligence is the life blood of the planning process and a crucial input for the turnaround strategy. The study by Schendel *et. al.* (1976), classifies the recovery strategies into two groups: as Efficiency Oriented (those improving efficiency), and Entrepreneurial Oriented (those requiring strategic repositioning). Bibeault (1982), Pearce and Robbins (1993) and Arogyaswamy *et. al.* (1995) viewed the turnaround process in two stages: stemming the decline and implementing recovery strategies. They further opine that the degree of success of strategies would depend on the level of distress, firm size, and resource availability for spearheading the turnaround. The Structure-Conduct-Performance paradigm of Scherer (1980) propounds that the conduct of the firm depends on the structure, in terms of size, and industry environment, which in turn affects its performance. In summary, the research studies give a direction that the generic strategies applicable for the stable business environments need to be complimented to put in place with combination of strategies to effectively steer the firm out of distress.

Section IV
Need for Strategic Approach

The Microfinance Industry in India and specifically in Andhra Pradesh is characterized by players who operate with differences in their organizational formats, business objectives, and expectations of owners. Most of the theories propounded in the realm of business management literature presume that the corporate form of organization with shareholder's wealth maximization principle. A straight jacket application of them would be inappropriate in the context of MFIs, because the MFIs are primarily motivated by societal development.

(a) Pre-Formulation Scenario Analysis

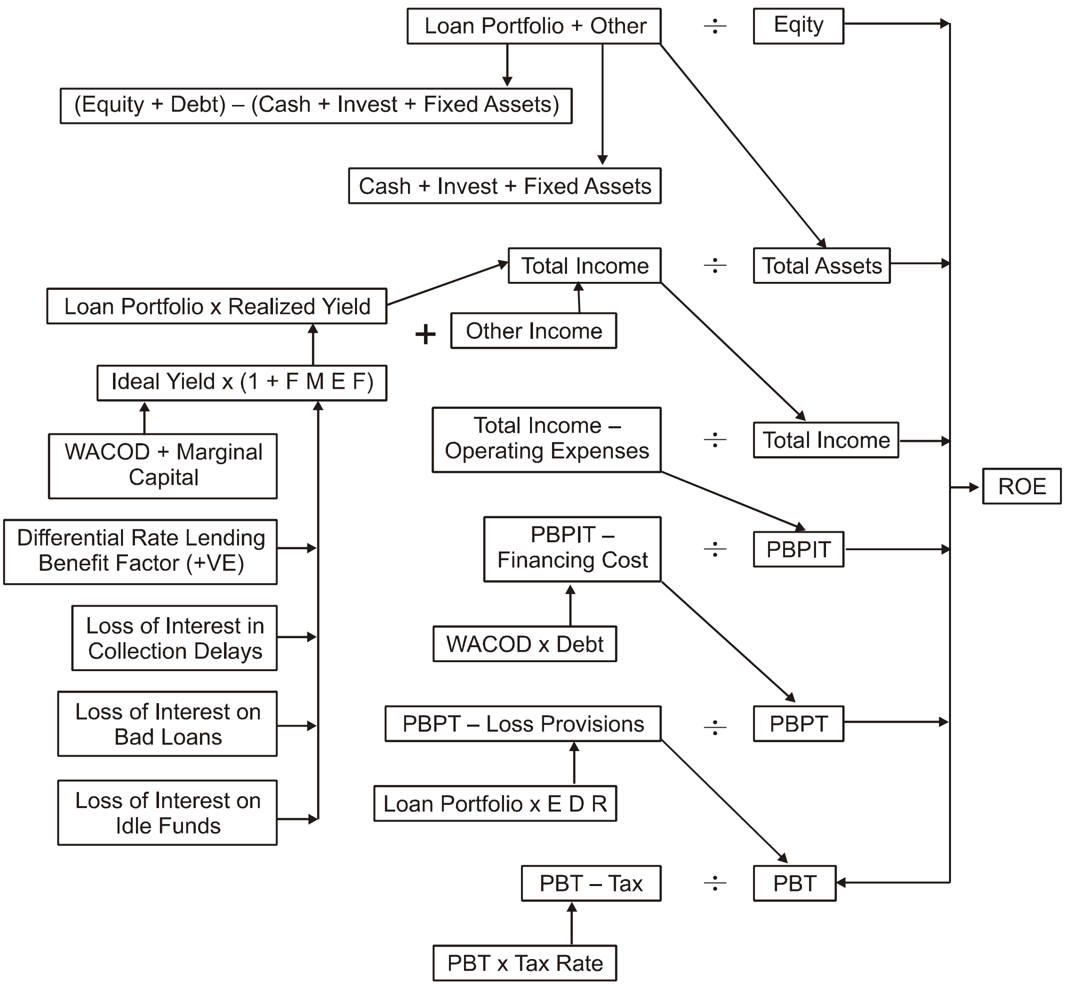
The market of MFIs on the supply side is characterized by players operating in different formats *viz.*, the Non-Government Organizations (NGO-MFIs), Non-Banking Finance Companies (NBFC-MFIs), Cooperative Banks. NGO-MFIs with knowledge of the customer and the desired proximity to influence their financial discipline; the NBFC-MFIs or Corporate-MFIs with access to huge low cost capital, IT enabled business processes; the Cooperative Banks, the oldest format of MFI, with the authority to accept saving deposits. Microfinance Industry harboured competition among unequals, without any major threat of entry, and each player aggressively lent, increasing their loan portfolio, to capture as much market share as possible, undermining the basic tenets of credit appraisal. Loans without collaterals, poor earning capacities of the borrowers, and moral hazards related to adverse selection of clients by the loan disbursement officers, were some of the significant risks which the MFIs were taking, without any planning and systems to manage such risks. Over and above the sellers of Microfinance got the buyer's power wrong, in the sense, their unexpected acts of suicide and ability to muster political support for a stifling ordinance of AP in 2010. The mono product nature, without significant differentiation, did not give adequate room to build a portfolio of products, which could have been handy, at these troubled times of cash crunch, to generate alternative sources of revenues. Liquidity and Trust are the two most important limbs of the financial services industry, and today the MFI is crippled on both counts. The industry shows the ordinance of Andhra Pradesh as the proximal cause of the current distress, but the root cause is multiple lending to not so credit worthy borrowers. Still there is a ray of hope, strongly embedded in the products and services which they can offer.

MFIs should pursue the generic strategies of stability and focus, until clarity emerges in the regulatory environment. As there has been a significant fall in the annual growth rates of borrowers and portfolios as is evident from (Box 1). They have to focus on managing risk of declining growth rates of borrowers and portfolio. MFIs should adopt the process approach – to align their entire business processes towards an enlarged goal of providing life cycle financial solutions to the low-income strata of the society. MFIs are facing a situation of financial resource constraint coupled with uncertainty about the capability of environment to help it sustain. While it is difficult to suggest similar functional strategies, at the firm level, to all the MFI players, it is, winning back trust from both customers and fund providers to revive their operations, is the need of the hour. In the medium- and long-term the players should focus on efficiency oriented strategies to reduce their cost of borrowing and operations, to pass it on to the borrowers at lower interest rate. MFIs need to take a nurturing approach to strategy which essentially means, that they should be able to nurture the fund providers – to enjoy a continuous source of finance – and, at the same time, nurture the lives, livelihoods, and financial discipline of their clients, to wed both social upliftment and wealth maximization objectives. There is more to be done at the regulatory and industry level also to avoid any systemic crisis (Rane and Thomas, 2011). Protecting tax payer's money and avoiding systemic crisis are the predicaments of the government regulators. It is a tight rope walk to come out with a policy without pronouncing closure for the troubled financial institutions.

(b) Understanding Drivers for MFI Success

The Diagram 1 on the Drivers of MFI's Success – measured as Return on Equity – highlights how various operational key indicators, *viz.*, Financial Leverage (Total Assets to Equity), Asset Utilization (Total Income to Total Assets), Operating Expense Burden [Profits Before Provisions Interest and Tax (PBPIT) to Total Income], Financial Expense Burden (Profits Before Provisions and Tax (PBPT) to PBPIT), Loan Loss Provision (Profits Before Tax (PBT) to PBPT), Tax Burden (Profits After Tax (PAT) to PBT), are related to ROE. Asset Utilization depends on how well the firm deploys its funds into loan portfolio, IT and other infrastructure. Total Income depends on Realized Yield, on the loan portfolio after making adjustments to the Ideal Yield through the Fund Management Efficiency Factor (FMEF), and Other Fee based Income. The Ideal Yield is the sum of Margin Cap (Levied by RBI) and

Digram 1



the Weighted Average Cost of Debt (WACOD), which might be affected negatively due to Loss of Interest due to collection delays, bad loans, idle funds and positively due to Differential Rate Lending (if it is possible). PBPT is influenced by the financial expenses of the MFI, which again is a function of the average cost and quantum of debt funds. PBT is the amount left after the mandatory Loan Loss Provisions, which are based on Expected Delinquency Rates (EDR), and not the Ideal Delinquency Rates as suggested by the RBI.

(c) Strategic Measures

This paper presents indicative measures, to turnaround the current situation of MFIs in India, to be adopted at two levels, *viz.,* Strategic and Operational. While the suggestions at the strategic level require change in the format of organization; strengthening governance issues; forging strategic alliances for effective market reach and delivery; and enhancing product portfolio. The operational strategies focus on improving efficiencies of systems and processes in the functional domains. Creating a congenial business environment is beyond the scope of a firm, but concerted action at the industry level, would ensure positive pressure for the promulgation of a favourable regulatory environment. The strategies proposed are more applicable for the NBFC-MFIs and NGO-MFIs, which are the most hit during the recent Andhra Pradesh crisis. The Cooperative Banks are relatively less hit, and in the true sense they are not typical MFIs.

Strengthening Governance: The increasing preference for the NBFC-MFI format (Table 1) is a good trend to follow. Registering as an NBFC would enhance RBI monitoring but also would give the credibility to raise funds, which is crucial for any lending institution. This format brings in more business as is evident in Box 2 shows that NBFC-MFIs have a major share of borrower accounts and outstanding portfolio as compared to NGO-MFIs. Good Governance requires that the MFIs develop an accountability matrix that redefines accountability structure of the organization in the context of internal and external environment (Dixon *et.al,* 2006).

Market Diversification to Avoid Concentration Risk: The overall MFI penetration and, MFI and Self Help Group (SHG) combined penetration, are in the Southern Region of India (Johnson, 2008). Demand and acceptance might have been the reasons for this level of geographic concentration, which, generally, is not a sound strategy for any financial institution. MFIs have begun to look at other states in India to expand their activities, and now as a matter of strategy should consciously make efforts to diversify geographically (Box 3). The concentration of MFIs is in the low income market segment, and there is a need to diversify into other market segments, like the rural artisans, petty traders, self-employed, rural and semi-urban SMEs.

Leveraging on Core Competencies: Careful examination of the heterogeneity of the MFI players, depicts that it is difficult for a single organization to possess all the competencies, like capability to raise low cost funds, time tested operating procedures, IT applications, and knowledge of customer to dominate its value chain. Forging strategic alliances with other MFIs after a critical evaluation is a measure to be explored in the short-turn to effectively harness (Narayan *et.al.*, 2013) the synergies. Bancassurance and Corporate Agency Models of the Insurance Industry can be the style to emulate. NGOs can be the right candidates to get the target market reach and Cooperative Banks can help in sharing the savings deposit services.

Nurturing Clients for Long-Term Captive Markets: MFIs primarily lend to the not so financially strong population distinguishing it from other financial institutions. Unless the economic environment – in which the population inhabits – provides them livelihood opportunities, it is difficult to up sell financial products or services to them. Long-Term Market Nurture Strategy (Narayan *et.al.*, 2013) taking up of initiatives to build competencies in the people to scale up the livelihood ladder, like some of the non-credit offerings (Box 4) of large 10 MFIs may be attempted by others.

(d) Operational Measures

Innovating Products for Competitive Advantage: MFIs, criticized for the mono-product format, need to revamp their product mix, adding and innovating various other products, to cater to the life cycle needs of the target segment. The portfolio should comprise of judicious mix of collateral and non-collateral based loans, as well as consumption and non-consumption loans. MFIs may explore possibilities to vend various financial services for a fee based income to enhance their revenue streams. MFIs should also try alternatives similar to EXIM Bank's Buyer's Credit, where the products of social entrepreneurship, or rural India, can be sold along with finance, like the consumer durable and auto loans of the banking industry. Some of the large MFIs are successful with working capital lending for SME traders in groceries.

Improving Process Efficiency for Cost Effectiveness: Cost Effectiveness is an all time effective strategy pursued by businesses. Turbulent environments squeeze operating margins of firms, requiring serious thought on cost efficiency. The RBI's circular also talks about the cap on margins[1] of MFIs (10 per cent for large MFIs, 12 per cent for small MFIs). Leveraging on IT in all possible processes in the pre-sanction appraisal, post-sanction monitoring, and default recovery can reduce administrative costs. Similarly the manpower requirements are to be re-assessed

1. The amount which can be added to the average financing cost of the MFI with another 1 per cent loan processing fee that can be charged to a customer for his loan. This is Annual Percentage Yield that can be expected by an MFI on its loan portfolio.

and rationalized (Box 5), they need to be retrained on both soft and computing skills to improve their attitude towards service and productivity. Economies of scale occur at higher portfolio sizes and larger loans, and customer retention is a key for this. Progressive rebates on interest rates, for larger loan sizes may be explored to retain customers and arrest multiple lending. It may be noted that the regulation on margins takes away the flexibility to pursue cost reduction strategy, over a period of time in the long-run. Table 2 and 3 shows the increase in average costs per borrower and operating expense ratio (per cent) especially post AP crisis.

Appropriate Finance Mix lower the Cost of Funds: The finance mix defines the maximum expected yield on the loan portfolio of an MFI, especially after the margin caps on the anvil. Till 2010 MFIs raised debt at an average of 10-12 per cent, but after the increased risk perception of MFI lending, the rates have risen to 14 to 18 per cent (*M-CRIL Microfinance Review*, 2012). With an increasing operating costs (Box 6 and Table 4) and imminent write-offs of bad loans, retained earnings cannot be a source of funds. Similarly the sentiment against MFI, cannot infuse fresh equity funds. With negligible grants and no legal access to the clients' savings deposits makes debt the only route through which MFI can raise their funds. Hence to reduce the cost of borrowings, they should improve their credit worthiness through better recovery rates and display improved credit appraisal mechanisms. To resolve immediate cashflow problems, Private Equity and Venture Capital Funds may be approached by convincing them about their markets for Microfinance outside AP, long-term higher returns bargaining for a moratorium period of atleast 5 years. The sub-prime crisis cast doubts on securitizing as a phenomenon, even on collateral based loans. MFIs should not depend on this process, since the loans that are securitized are not collateral based, and are offered to lower income group. The receivables being securitized are relatively much riskier, though initially they showed almost zero per cent delinquency. Some of the large NBFC-MFIs have also experimented with Optionally Convertible Cumulative Preference Shares, and Compulsorily Convertible Bonds. These are good solvency management instruments, especially when burdened with short-term illiquidity, coupled with good business prospects in the long-term.

Medium Debt Maturity to Avoid Default Risk on their Liabilities: MFIs can borrow debts (Table 5) for longer term (3 to 5 years) from the markets and financial institutions, and lend them in assets with average maturity of less than one year. Unless there is an unfortunate timing of large scale defaults in the maturing year of debt, it is unlikely that they would default. With the capacity to lend at higher rates of interest, they can also create adequate reserves.

Asset Allocation and Yield: Allocation of assets (Table 6) is a crucial aspect of any investment strategy, more so for a financial institution. The larger the percentage of deployment into loans and advances, there are larger possibilities to generate the required rates of return (Table 7). Idle funds and sub-optimal investments should be avoided. Table 6 shows the MFI allocation over the last 3 years. While a reasonably fair amount of fund is deployed into loans, the cash and short-term holdings are large in the recent years, owing to the defaults, and liquidity problems of the MFIs. As a matter of strategy the MFIs should target minimum deployment of 85 per cent of their borrowings, to loan funds each year, since they do not have the typical CRR and SLR requirements like a bank.

Credit Quality, Delinquency and Yield: There is no substitute to a sound credit appraisal mechanism in any financial institution, deriving its chief revenue through lending. Box 7 highlights certain indicators on this count. In the immediate preceding years to the crisis, the ideal minimum time of 6 months, for the formation of a group for lending, was not followed scrupulously, leading to hurried lending (*M-CRIL Microfinance Review*, 2012). Customer retention, investing reasonable time in group formation, networking, and solidarity building are key to fight delinquency. Higher delinquency rates influence achievement of the ideal rates of yield on the loan portfolios. Over the years the MFIs are off the ideal yield on loan portfolios by 7-8 per cent, due to the loan loss provisions, delayed collections and delinquency (*M-CRIL Microfinance Review*, 2012). The Bangladesh's Grameen Model of lending creating the necessary peer pressure for repayment can be a good strategy to emulate.

Section V
Conclusion

Summing it all, at the strategic level, diversification strategies of markets, market segments, and products would enhance loan portfolio and other fee based income. Diversification requires recapitalization with low cost of funds, which is possible with the appropriate organizational structure of NBFC-MFI. Strategic Mergers and Alliances, with other MFI players will build competencies of networking with the target customer segment to generate loyal and large consumer base. Taking up the responsibility to nurture long-term demand through social capacity building and livelihood generating initiatives are crucial to regain the misplaced trust in MFIs in Andhra Pradesh and prevent it from being contagious to other states. At the operational level, Continuous Product Innovation will remove the mono-product tag to MFI, process efficiencies driven by IT infrastructure, rationalized and well trained manpower, will bring down the operating costs. Low cost debt weighted finance mix would reduce the cost of borrowing, and longer term debt maturities would ease the default risk tension of the MFI. Investing time and money in building strong networks and trustworthy climate among the target customer segment would enhance the credit quality. The near zero per cent default risk cannot be substituted with any other strategy. Like the capital intensive industries, financial corporations also succeed on profitable asset allocation strategies. Of course, finance is the only asset of this industry, and hence keeping it sensibly invested all the time, without being idle is the key for effective asset utilization strategy. All is not bad for the Microfinance Industry in India, since the AP crisis has not shown any contagion on delinquencies in other states. The speed at which the central government is responding with regulatory measures is going to create an encouraging external environment for the revival of this great engine of financial and social inclusion.

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Box 1

Annual Growth Rates of Borrowers and Portfolios

Aspect	*2007-08*	*2008-09*	*2009-2010*	*2010-11*	*2011-12*
Borrowers	66	59	43	7	-27.3
Portfolio	132	125	76	7	-18.3

Note: The rural and urban divide of the client profile is 57.6 per cent and 42.4 per cent in 2012.

Source: *M-CRIL Microfinance Review*, 2012.

Table 1

Number of NGOs and NBFCs Covered by M-CRIL Review

Type of MFI	*2000*	*2003*	*2005*	*2007*	*2009*	*2011*	*2012*
NGOs	42	71	58	34	26	20	12
NBFCs	2	7	10	15	23	33	41

Source: M-CRIL Microfinance Review, 2012.

Box 2

Format-wise Share of MFI Business

- NBFCs share of all borrower accounts as on March 2012 - 85 per cent
- NBFCs share of outstanding portfolio as on March 2012 - 83.4 per cent
- NGOs share of all borrower accounts as on March 2012 - 12.1 per cent
- NGOs share of outstanding portfolio as on March 2012 - 14.2 per cent

Source: M-CRIL Microfinance Review, 2012.

Box 3

MFI's Geographic Spread of Markets

- 39.3 per cent of the MFIs in India have significant presence in South India, 26.8 per cent in the East and North East, 10.7 per cent in the West, 12.5 per cent in North and 10.7 per cent across India.
- Out of 25.85 million active borrower accounts reported by 56 MFIs in the M-CRIL analysis, Karnataka Andhra and Tamil Nadu have 4 million, 3.75 million and 3.4 million active borrowers, accounting for a little over 50 per cent of the total.
- Coverage of eligible population by MF loans in the north and west is less than 40 per cent.

Source: M-CRIL Microfinance Review, 2012.

Box 4

Non-Credit Offerings of MFIs

- Financial services, poverty reduction, employment generation, business growth, gender equality, development of start ups, children schooling, health Improvement, water and sanitation, housing, adult education, youth opportunities are the development initiatives reported by MFIs.
- Health services, enterprise services, women's empowerment services and education services, are the non-financial services offered by the MFIs.

Source: M-CRIL Microfinance Review, 2012.

Box 5

Human Resource & Productivity

Staff per Institution

- Large - 10 MFIs - 5550; Others - 736
- NBFCs - 1781; NGOs - 1226; Sec. 25 Co - 1406; Coop - 108
- MIX Benchmark for East Asia - 324; South Asia - 890

Accounts per Staff Member

- Large - 10 MFIs - 264; All MFIs - 223; NBFC - 232; NGOs - 164; Sec.25 Co - 327; Coop - 311;

Portfolio Serviced per Staff Member in Lakhs of INR

- Large -10 MFIs - 18.5; All MFIs - 16.5; NFCs - 16.8; NGOs - 14.2; Sec.25 Co - 23; Coop - 15.3

96.3 per cent of Clients are Women but around 52.5 per cent of MFIs employ < 5 per cent Women Loan Officers

Source: M-CRIL Microfinance Review, 2012.

Table 2

Average Cost per Borrower in INR

Category	*2000*	*2003*	*2005*	*2007*	*2010*	*2011*	*2012*
MFIs + AP	600	570	590	520	520	716	1084
MFIs	600	570	590	520	520	716	861

Source: M-CRIL Microfinance Review, 2012.

Table 3

Operating Expense Ratio in Percentage

Category	*2003*	*2007*	*2008-09*	*2009-10*	*2010-11*	*2011-12*
MFIs	20.5	15.9	11.9	8.8	10.3	12

Source: M-CRIL Microfinance Review, 2012.

Box 6

Cost of Operations of MFI

- Cost per borrower Rs.1084 ($21)of Indian MFIs is < the global average of 85$
- Operating Expense Ratio depends on average loan size; It is 25.6 per cent for < Rs. 4000 loan size, and 7.8 per cent for > Rs.10,000 loan size.
- Salaries the largest component of operating cost, followed administrative expenses. Salary allocation ranges from 40 per cent (NGOs) to 60 per cent (NBFCs).
- Economies of scale in MFI depends on Portfolio Size. OER ranges from 27.6 per cent to 10.2 per cent for portfolio size of < 25 Crores to >=500 Crores, respectively.

Source: *M-CRIL Microfinance Review*, 2012.

Table 4

Yield and Operating Expense Ratio of MFIs

Category	*2002*	*2004*	*2006*	*2008-09*	*2009-10*	*2010-11*	*2011-12*
Yield	19.9	25.2	24.8	27	28	27.2	21.6
OER	18.8	15.6	15.9	11.5	8.6	10.3	11.7

Source: M-CRIL Microfinance Review, 2012.

Table 5

Finance Mix of MFIs

Category	*2003*	*2005*	*2007*	*2010*	*2012*
Institutional Debt	34	63	75	70	67.5
Client Savings	25	10	8	1.3	0.2
Other Liabilities	8	7.8	7	7.5	8
Grants	30	5	3	0.4	0.4
Paid in Equity	7	10	6	10	23.7
Retained Earnings	-4	0.2	0.2	6.6	-0.8

Source: M-CRIL Microfinance Review, 2012.

Table 6

Asset Allocation of MFIs

Category	*2010*	*2011*	*2012*
Net Portfolio	68.9	80.6	75.1
Fixed Assets	1.2	1.2	1
Cash	10.3	13.5	17.6
ST Investments	16.6	0.02	0.19
LT Investments	0.1	1	1
Advances	0.4	0.5	0.2
Other Current Assets	2.5	3.2	4.9

Source: M-CRIL Microfinance Review, 2012.

Table 7

Trend in ROE Weighted Average

Category	*2010*	*2012*
India	18.8	-26.4
India without AP	18.8	7.4
L-10	26.7	-13.1

Source: M-CRIL Microfinance Review, 2012.

Box 7

Credit Quality of MFIs

Portfolio at Risk for > 30 days - PAR-30

- NGOs - 12.1 per cent; Co-op 11.2 per cent; NBFC - 29.2 per cent; L-10 - 29.5 per cent
- The ratio is < 2 per cent when the data on AP is excluded from the above national averages.
- Portfolio size influences the PAR -30. It ranges from 7.5 to 19.7 per cent for the portfolio sizes of < Rs.50 crores and > Rs.500 crores.
- Client Satisfaction influences Client Retention; Client Retention and Portfolio quality are inversely related. The average client retention rate of Indian MFI is 64 per cent.

Multiple Lending in AP

- MFIs loan was just 80 per cent of the eligible borrowers, the SHG loans were 250 per cent of the same.

Over Indebtedness in AP

- Rs.4500 p.m. loan repayment, per family, for Rs.8500 p.m. family income, around 55 per cent
- National Average loan repayment per family per month Rs.930

Loan Loss Write-offs as a Percentage of Portfolio

Categories	*2010-09*	*2010-11*	*2011-12*
All MFIs	0.5	4	20
AP MFIs	0.8	6.6	34.4

Loan Loss Reserve Ratios and PAR30

Category	*NGOs*	*Co-op*	*NBFC*	*L-10*
PAR30	12.1%	11.2%	29.2%	29.5%
LLR	1.3%	3.4%	3.6%	3.4%

Source: M-CRIL Microfinance Review, 2012.

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