P. Chidambaram inaugurates the 2012 Summit

Reconstructing the Sector: Brick by Brick

The Microfinance India Summit opened with Hon’ble Finance Minister, P. Chidambaram delivering the inaugural address and declaring the important task of microfinance programmes in the overall financial inclusion strategy. “In fact”, expounded P. Chidambaram, “the financial inclusion architecture will remain incomplete unless we take microfinance into the financial services delivery system.”

The Hon’ble Union Finance Minister went on to empathize the important complimentary role of microfinance institutions with the Government of India’s SHG bank linkage programme. He remarked that the government alone cannot ensure financial inclusion of the poor and needs the microfinance industry as part of the greater strategy of financial inclusion in India.

Chidambaram motivated microfinance institutions to expand their product portfolio to meet the needs of the poor and to consciously focus on unserved and underserved regions. Further he encouraged the sector towards greater responsible finance, transparency, and governance.

Special addresses by M.V. Nair, Chairman, Task force on Financial Inclusion, CII; Stuart Milne, Chief Executive Officer, HSBC India; and Lise Grande, UN Resident Coordinator and UNDP Resident Representative in India empathized the importance of building on the positives of the sector, keeping clients at the center, and continuously innovating to provide appropriate products and services.

Dr. Puha, author of “State of the Sector Report 2012”, presented the findings of the report, showing a mild recovery. He concluded by saying, “As long as the ultimate focus of microfinance initiatives are towards the poor and their livelihood improvement, microfinance will survive, sustain and grow. The only relevant expectation that it should strive to meet is that of the vulnerable customers.”

As the day unfolded the tone and remarks from sector experts and key stakeholders were positive - while the sector has plenty of work ahead, steps have been taken to clearly define the rules of the game, put clients at the center and set reasonable expectations on outcomes and performance.

The inaugural day ended with the Microfinance India Awards 2012, presented to three distinguished institutions and one exceptional individual: Cashpor Micro Credit, Utkarsh Micro Finance Pvt. Ltd., MicroSave, and R.N. Malla, CMD, IDBI Bank.

“The objective of microfinance is clear: to promote financial services to those who haven’t received it.”

-Jairam Ramesh, Union Minister of Rural Development

See page 7 for excerpts of his speech. Click here to listen to his full address.
Understanding client preference – key to survival and growth
by Nisha Singh

Financial organisations are successful because they are client-centric, not in spite of it. This is as true on Wall Street as it is in the villages of India. Recent work such as financial diaries and other demand side studies have highlighted the fact that the poor are not a homogenous group and have extremely complex financial lives and needs. While the past decade and half in microfinance was focused on growth by sticking to simple one size fits all credit products, the recent crisis as well as impact studies are beginning to show that if MFIs want to stay in the business of microfinance, they need to adopt a client-centric approach. This starts with creating a better understanding of the clients needs, but it is not a one-time activity, so MFIs need to adapt their processes and operations to build the business around understanding and responding to the preference of the clients. Models such as KGFS and Janalaxmi are showing a lot of promise but this is the beginning of a long journey on creating robust institutions where being client centric is a part of the DNA of the institutions and is reflected in ever aspect of the institutions functioning.

Alexia Latortue, Deputy Chief Executive Officer, CGAP, who was moderating the session titled “What Do the Poor Need?: Aligning Products and Services”, mentioned that as the industry grows and moves forward in this direction, there is a need for creating better tools and methods to both collect data on client preference and effectively use the data that institutions are already collecting into the product development and delivery processes.

Consumer lenders in various countries have made serious investments into setting up methods for collection and analyzing data that allows them to offer highly customized products to their clients as and when they need it. There is an opportunity to explore similar collective investments in data analytics within the microfinance industry. While expensive, such an investment would allow more institutions to focus building client responsive products and services, which is key to long-term survival and growth.
Winners of the Microfinance India Awards 2012

Cashpor Micro Credit, Microfinance India Organisation of the Year Award (Large)

Utkarsh Micro Finance Pvt. Ltd., Microfinance India Organisation of the Year Award (Small/Medium)

MicroSave, Microfinance India Contribution to the Sector Award (Enabling Institution)

Mr. Rajendra Mohan Malla, Microfinance India Contribution to the Sector Award (Individual)

Left to right: Stuart Milne (HSBC), Brij Mohan (ACCESS), Govind Singh (Utkarsh), Mani Shankar Aiyar (Member of Parliament, Rajya Sabha), R.M. Malla (IDBI), David Gibbons (CMC), Vipin Sharma (ACCESS), Mukul Jaiswal (CMC), Kartin Agarwal (CMC), Ajay Shekher Mohura (CMC), and Dinesh Verma (CMC).
Rebuilding the foundation – with trust

by Nisha Singh

One of the major challenges facing the microfinance sector in India in the aftermath of the impasse in Andhra Pradesh, was the trust deficit between the MFIs and the investor community. Over the last two years various stakeholders have tried to come together and help rebuild this trust. As a development bank, SIDBI has been a key player in this journey. During the session “Financial Streams Dry Up!: Mitigating the Funding Drought” P.K. Saha, Chief General Manager, Small Industries Development Bank of India (SIDBI), talked about some of the key steps that SIDBI has taken that will allow the sector to continue on a path of steady recovery and future growth. These include debt restructuring for MFIs, a microfinance equity fund for small and medium MFIs, as well as increased focus on corporate governance and transparency.

The crisis revealed the true “rules of the game” and that only those institutions that were intent on playing fair would survive. Saha remarked that the current funding drought is driven by the increased risk perception amongst the investor community. By promoting greater transparency and better corporate governance at the institutional level, this perception can be altered to create an environment of trust that will allow for the sector to continue to grow.

Perspective

As a participant of the Microfinance India Summit over the last nine years, what value does the Summit bring to the sector?

It brings people together from different types of institutions, and it is particularly valuable for field staff who are "on the front line". The Summit helps them to see that they are part of a large and important movement; it would be better if there were more of them at the Summit and they had more chance to share their experiences and to be recognized. The “State of the Sector Report”, which is a by-product of the Summit, has become the internationally preferred source for information about Indian microfinance.

In reflecting on the past decade, how have you seen the sector change?

MFIs have grown, massively; they have then been humbled, deservedly; and meanwhile the SHG movement, India’s and indeed the world’s largest microfinance programme, has continued to grow, albeit more slowly, and has more or less maintained its position, in spite of political interference and official neglect.

What aspirations do you have for the future of microfinance in India?

Let’s hope that microfinance will cease to be dominated by institutions and programmes whose focus is to increase poor people’s debts rather than to help them save, that cooperative institutions will play a more important role, that the role of foreign money and foreigners will be reduced, that financial inclusion and microfinance will converge, that existing commercial banks will reach down to unbanked people directly rather than financing MFIs to do it, and that all the players will realize that microfinance on its own, even when it does include savings as well as indebtedness, is only a part, and a fairly small part, of the total process of escaping from poverty. India remains the world leader in poverty, by a very wide margin, and microfinance alone is not going to fix that.
On social performance:

Interview with Girija Srinivasan, author of the “Social Performance Report 2012”

What is a key first step in social performance (SP)?

An MFI is in the business of serving the clients’ needs and should therefore be able to collect and use the information about clients’ needs and preferences. Proper training of staff is an integral part of understanding and responding to client needs more effectively. It is critical that there is better training of staff, both at the field level and at the middle management level. The field staff who interact with clients on a day to day basis need to realise that the most important aspect of their job is to understand what the clients need, document that and feed it back into the institution so that the products and services can be tailored appropriately. Investments also need to be made in training the mid-level staff to underscore the importance of client centricity, so that this can truly become part of the organisation’s processes and systems and overall functioning.

What are the major challenges and hurdles faced in SP?

The question of how do we do it while still being financially sustainable is critical and needs to be addressed. The MFIs today are under a lot of pressure from both regulators and investors. They need to invest in creating better systems and also collecting data to show their impact and social commitments. But all of this comes at a cost and with increasingly thinner margins, this is squeezing the MFIs and could push them out of the market.

Over the past decade as microfinance has grown, MFIs have tested a lot of different software systems to collect and manage data better. Some of these have worked better than others but majority of them still do not provide support for collecting and reporting client related non-financial data. This in turn creates issues because while the institution maybe collecting client information, if they are not able to systematically analyse it, it is of little value to them and the cost of collecting this data is even higher in such situations. There is a need to help MFIs get better at both collecting and using the data, so that the costs can be brought down and also the institution is able to leverage the information that it already has to improve efficiency.

What are the critical issues?

While it is important to highlight and create awareness about the social impact, it is also essential to look at social performance within the framework of organisational performance. Social indicators need to be mainstreamed into current ratings and assessment processes so that when institutions receive feedback, it is comprehensive and covers all aspects of organisational performance.

Donors and investors that are a committed to supporting the growth of the microfinance industry need to support not only assessment and reporting, but also provide support for institutional capacity building. This will allow the institutions to build their own capacity to collect, use and report their outreach and impact better. Having the capacity to use the client level data to make decision and changes to products, will also ensure that the quality of the data improves.

What have you observed in regard to impact?

As the microfinance industry has grown and matured, there has been a growing debate around impact and outreach, specifically around what changes in the lives of clients can be attributed to MFIs. “Social Performance Report 2012” has a chapter that attempts to summarize the key issues that are being discussed.

While the debates will continue till there is more evidence about actual impacts, from an MFI perspective, there is a need to focus on tracking and documenting the changes in the lives of their clients. They might not be able to directly take credit for all of it, if they do see positive changes, at least some parts of it can be attributed to their work. However, if they don’t track it then they have no way of knowing what is happening in the lives of the clients.
Q&A

A look at current conditions in microfinance with Vijay Mahajan, Founder & Chairman of BASIX and President of Microfinance Institutions Network (MFIN)
(The following are excerpts of the interview)

We are at an interesting point in the history of microfinance where the model is being challenged in terms of its impact on poverty, its losing credibility, in terms of drifting from its mission and increasingly coming under formal regulations. What can be done to restore its credibility?

In the first place, microfinance originated not as a general form of finance but as a part of an innovative means to impact poverty. Practitioners got seduced to believe that their karma was financial indicators and these terms became their standard. On the other hand the impact of poverty took a back side. The sector needs to return to a balance. I’m not talking about a pendulum swing to the other side, but a balance in financial performance and poverty impact.

Last December the Reserve Bank of India brought out a regulatory framework for NBFC-MFIs then later modifications in August. What was your reaction to these changes?

The broad direction of the regulations I am absolutely fine with. The government acknowledged that a 26 percent interest rate was acceptable, which was a big deal from previous 10 and 12 percent rates. The regulations have gone in the right direction. It sounds like ten microfinance conducts; under normal circumstances I would not like it, but the industry called it on itself. The August modifications addressed margin caps and interest rates. It also provided a lifeline to institutions operating in AP.

The impasse in AP among the state government, federal government, and MFIs persists; what do you anticipate to happen in the coming months?

The high court has finished its hearing and the final judgment should come out soon. The ruling should not apply to NBFCs and will make it legal for them to start operating again. However, the ruling and opposition party are in agreement on no repayment; on the ground not much will change. It is unusual to have the government and opposition aligned, but in this case it is a matter of electoral votes.

MFIs are looking at consolidating to reach scale and cover costs. How will this impact the sector?

I’m totally fine with small MFIs in the same geographical region consolidating operations. The concept of all India institutions is unyielding. We are too large a country. For good on site supervision this is difficult; there are logistical problems. When you club state and regional areas you are tightly executed, but when it is all India it is expensive to supervise and you invite all kinds of behavior.

What measures may help in a greater flow of funds for the sector?

Passage of time and regaining confidence; banks need to see that under the new regulatory regime and political economy there is still reasonable growth to come. The demand at the bottom of the pyramid remains, which is the same logic that got us started working together in the first place. Over time this will return, as it is difficult for banks to serve the bottom of the pyramid.

At last year’s Summit MFIN joined with Sa-Dhan in launching a unified code of conduct. What impact has this had on the sector?

Very little. In order for this to have impact, enforcement mechanisms need to be in place and encourage practice. In a microscopic way the roll out of the credit bureaus has encouraged enforcement. The regulation to lend for more than two MFIs was unenforceable, but now every MFI is supposed to check if there are two lenders. It is a clear violation if they are the third lender. Micro catch-ability has increased and the catchers have themselves improved - in this way the enforcement is improving.

Looking ahead, what aspirations do you have for the sector in the coming years?

The foundation of microfinance addresses poverty squarely; this should always be in an operationally sustainable manner. The sector needs to start expanding their products: 90% of the sector provides 52-week loans. The cash flow for agriculture and animal husbandry does not support this. Before the poor were desperate for loans and would take anything. Microfinance needs to go beyond credit to help poor people save and to provide insurance, etc. Microfinance is not about filling a gap in financial services, but filling a gap in poverty impact - impacting people, not pleasing shareholders.
Microfinance 2.0, time to rebuild

Two days of deliberations, conversations with old and new acquaintances, reflections on the past and strategies for the future were brought to a close with the Union Minister of Rural Development’s valedictory address. As a strong critic of microfinance, Union Minister of Rural Development, Jairam Ramesh’s acknowledgement of the role of microfinance in delivering last mile services to those without was a positive reinforcement to the sector.

Jairam Ramesh gave credit to the sector despite it promising more than it could deliver. “There is a role for both microfinance models, Ramesh declared, “but we must rebuild.” The Union Minister went on to say, “The objective of microfinance is clear: to promote financial services to those who haven’t received it.” He remarked that the sector needs to be more modest, but articulated that it does have a role in bringing communities and people into the financial sector.

Mr. Y.C. Nanda, former Chairman of NABARD and Chairman of ACCESS-ASSIST, remarked during his speech that legitimacy is being restored to the sector. However, he stated, “Both the SHG bank linkage programme as well as the MFI model need restructuring brick by brick. The MFI supported a body blow to what happen in Andhra and the consequences thereof will take some time before they fully recover.”

Dr. Arvind Mayaram, Secretary, Department of Economic Affairs also gave an address at the valedictory and aptly spoke on the way forward for microfinance in a rapidly changing environment. He stated that the sector must understand why microfinance has addressed critical issues and how it can continue to meet the needs of the poor in a country where 35 percent of the population live below the poverty line.

“There is a need for new models of assessing risk for the poor and looking at new ways of financing [microfinance] through capital markets...to create resources that are cheaper so that on-lending can be much more competitive in nature,” remarked Arvind Mayaram.

While recovery has been slow, legitimacy has been restored to the sector and microfinance 2.0 is underway.