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The Challenge Of Micro Finance: Balancing Financial Sustainability And Social Responsibility

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ABSTRACT

The progress made by micro finance in India in the last decade has been significant. It has been successful in supporting equitable growth at the bottom of the pyramid (BoP). Reserve Bank of India defines micro finance as "provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi-urban or urban areas for enabling them to raise their income levels and improve their living standards". The mission of Micro Finance Institutions (MFIs) all over the world has been to lift billions of people out of poverty through financial inclusion. This social mission requires MFIs to be financially sustainable. It is essential that players in this sector are not only able to cover their costs but also generate profits. Thus the question arises, should micro finance be profitable? If it is profitable can it be socially responsible. Herein lies the challenge of reconciling financial profitability with social responsibility. The study answers this question by analyzing the financial and social impact of the Indian Micro Finance Sector and a select MFI in India and concludes that financial and social returns can be complementary and mutually beneficial.

KEY WORDS: Micro Finance Institutions, Financial Sustainability, Social Responsibility, Social Performance Management

1. INTRODUCTION

Micro Finance or Micro Credit was envisaged as a tool for reducing poverty by financially empowering the poorest member of the society. From the time it was introduced in the 1980's the Micro Finance Sector has been focusing on Financial Inclusion, Social Performance Management and Economic Profitability. Micro Credit which was seen as a miraculous tool for poverty alleviation in the early 2000's was followed by a crisis period in the early 2010's which damaged the sectors reputation caused by over indebtedness of beneficiaries and greed for excessive profits by unscrupulous Micro Finance Institutions (MFIs) in countries of Southern India, Pakistan, Morocco and Nicaragua. It was concluded that this crisis was the result of excessive search for profit, uncontrolled growth of MFIs and lack of regulation. Then came the phase of reforms to empower and professionalize the sector to establish responsible, ethical and inclusive microfinance.

THE CHALLENGE

Micro Finance is a sector that holds social responsibility as its rationale. For this sector maintaining a balance between profitability and social responsibility remains a challenge. Many a time the dilemma has been should microfinance be profitable. If it is profitable can it be socially responsible. Profitability in micro finance is acceptable provided it serves the social mission of scaling up financial services for those at the Bottom of the Pyramid (BoP). It should be remembered that profitability is not the end but a means to the end of social responsibility. In

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other words MFIs have to be financially sustainable to be socially responsible. Again the challenge is how social performance can be measured. While it is easy to measure profitability through widely accepted yardsticks of measurement, the measurement of social performance is a challenge.

MICRO FINANCE IN INDIA

The microfinance sector in India has made great strides during the last decade by adopting a wide variety of innovations in improving access to financial services to the poor. The sector is estimated to have a total outreach of more than 42 million clients through the MFI channel, which indeed is an encouraging trend. India has been at the forefront of the Microfinance revolution in the world enabling financial and credit inclusion for millions of bottom-of-pyramid consumers thus supporting them with their livelihoods. Even a crisis couple of years back could not hold the industry back and it reformed itself and emerged stronger..

2. OBJECTIVE OF THE STUDY

The objective of the study is to examine if micro finance can be both profitable and socially responsible. In other words can it balance financial sustainability with social responsibility.

3. METHODOLOGY

The study concentrates on the financial and social performance of a select micro finance institution Madura Micro Finance. The MFIs financial and social performance has been examined to draw conclusion. To judge financial performance accepted financial performance indicators like revenues, profit after tax, operating efficiency ratio, ROA and ROE have been used. To judge social performance CERISE – SP14 a social audit tool to evaluate assess and benchmark performance has been used.

The Social Performance Task Force (SPTF) a nonprofit member organization working in close co-operation with stakeholders of inclusive finance has developed and promoted standards and good practices for Social Performance Management in an effort to make financial services safer and beneficial. In 2012 SPTF released the Universal Standards for Social Performance Management (known as Universal Standards). These standards are a set of core business practices adopted in 2012 which provide guidance to MFIs on how to balance financial and social performance, in other words earning profits without losing track of their social mission. This is achieved by ensuring that policies, procedures, internal controls and training are all built to achieve their social mission. The CERISE – SP14 social audit tool allows MFIs to measure themselves against six dimensions of the Universal standards It assesses the extent to which social mission is integrated into strategy and operations.

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Source: https://sptf.info/

- Dimension1 – Define and monitor social goals
- Dimension 2 – Commitment to social goals
- Dimension 3 – Design products that meet clients' needs
- Dimension 4 – Treat clients responsibly
- Dimension 5 – Treat employees responsibly
- Dimension 6 – Balance social and financial performance

INDIAN SCENARIO

There has been a phenomenal growth in the Indian Microfinance Sector over the past 18 years. There has been a quantum jump in the number of institutions providing micro finance services. . 29 States, 5 Union Territories and 591 districts are currently serviced by micro finance institutions in India A branch network of 14,026 and 1, 10,914 employees with an outstanding loan portfolio of Rs.68,789 crores have reached out to over 35 million clients according to 200 MFIs that have reported. Table 1 indicates that the average loan outstanding per borrower has increased from 11,425 to 14,700 per borrower and 93% of loans were used for income generation purposes. Loan outstanding has grown by 47% over the previous year and outreach increased by 19% It is encouraging to note that women constitute 96% of total clients. It thus indicates that the MFI sector in India has been constantly working towards their social responsibility mission.

The financial indicators have however shown a decline in the last 2 years. The main reasons are the effect of demonetization which was an unanticipated event and the strain faced by the banking sector on accounts of stressed assets and other adverse events which slowed down the flow of credit to the deprived sections of society. It should however be applauded that the Capital Adequacy Ratio has remained much above the desirable level of 15%. This has been the result of robust risk management practices adopted by the MFIs

The Government of India and the Reserve Bank of India have provided the necessary legitimacy and impetus to the sector by creating a conducive policy and regulatory framework for Micro finance Institutions (MFIs) to operate in the country. MFIs in general comply with the regulations, take care of client protection issues and adhere to the Industry Code of Conduct. The Micro Finance industry in India has thus proved that social responsibility need not be sacrificed for financial sustainability. The sector has emerged victorious in the task of balancing profitability and social responsibility.

PERFORMANCE OF MFIS IN INDIA

OUTREACH INDICATORS	**2018**	**2017**	**2016**
Client Outreach(lakhs)	351	295	399
Women Clients	96	96	97
Gross Outstanding Portfolio(in crores)	68789	46842	63853
Average loan per Borrower (Rs)	14,700	12751	11425
Financial Indicators			
Operating Expense Ratio	9.97%	10.50%	10.22%
Finance Cost Ratio	13.03%	14.8%	13.83%
Yield	18.56%	22%	21%
Net interest margin	9.55%	8.08%	10.0%

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Operational Self Sufficiency	110	114	113
ROA	1.63%	2.4%	2.2%
ROE	7.48%	13.31%	19.31%
Leverage	2.8	2.9	3.2
NPA	1.48%	0.69%	0.15%
CAR	22.1%	21.13%	19.39%

Source: Bharat Micro Finance Report 2018

TABLE NO 1

MADURA MICRO-FINANCE LIMITED

Madura is a leading NBFC-MFI which provides unsecured microfinance loans in rural and semi-urban areas to women self-help groups. More than 11.7 lakh members from 25,000 villages across 6 states of India have received micro credit from them. One of the pioneers in the social and financial inclusive movement in rural India with a mission to deliver productive and low cost capital. They have been working at a data driven, technology-enabled operational efficiency approach which enhances skills and productivity in the communities that they serve. From table 2 it can be inferred that Madura Micro Finances' financial and social performance has been commendable. The outreach indicators of social responsibility and financial indicators of profitability are very satisfying with an upward trend. The results indicate profitability (means) has been matched with social responsibility (end)

PERFORMANCE OF MADURA MICRO FINANCE

OUTREACH INDICATORS	2017	2018	2019
Gross Loan Portfolio (Rs million)	8226	11,842	19,569
Active Borrowers	5,15,104	6,88546	9,56,712
Branches	217	282	356
Financial Indicators			
Revenues (Rs.million)	1,795	2,331	3,746
Profit after tax (Rs million)	302	398	805
Net NPAs	Nil	Nil	Nil
Operating Efficiency (OPEX/GLP)	6.69%	6.19%	5.04%
Return on Assets	3.8%	4.1%	4.2%
Return on Net Worth	21.4%	19.9%	25.1%

Source: Company Annual Reports and authors compilation

TABLE NO 2

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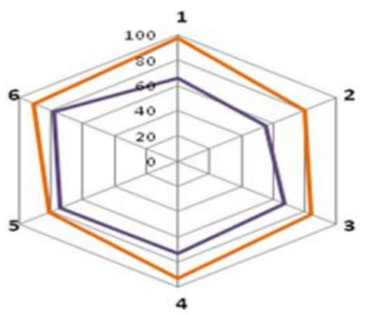
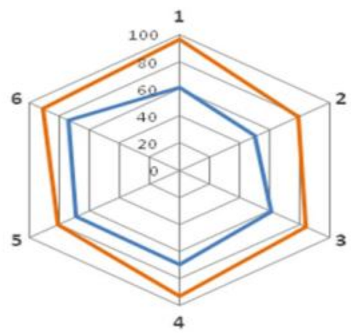
SOCIAL PERFORMANCE ASSESSMENT OF MADURA MICRO FINANCE

Global vs Madura's average score



Asia vs Madura's average score



_____ Global
_____ Asia
_____ Madura

Source: Company Annual Report 2019

The above Social performance assessment done by BNP Paribas using CERISE SPI4 tool indicates Madura's social performance is better than industry average both globally and in Asia (across 272 MFIs globally)

The dimensions of assessment included delivering high-quality and appropriate services, responding to the needs of clients, their families, and communities, and ensuring responsibility toward its employees, its clients, the community it serves, and the environment. It is thus concluded that Madura has been committed to translating their mission of social impact into practice.

The performance of Indian Micro Finance Sector and Madura Micro Finance testifies that financial profitability can be reconciled with positive social impact. Madura Micro Finances' initiatives have proved that financial and social return can be complementary and mutually beneficial.

4. CONCLUSION

The question of profitability lies at the very heart of the business model of MFIs. To be profitable and assist their clients MFIs must be able to find the right balance between financial return and social return. This is even more so important given the nature of micro borrowers who are excluded by the regular financial service providers.

The above study has however indicated that MFIs with good financial results show good social performance as well. Hence Financial Sustainability and Social Responsibility are not contradictory, rather they are complementary.

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