**Lifting the urban poor out of poverty: Assessing the role of Non-Banking Financial Institutions in India[[1]](#footnote-1)**

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Four Indian urban-focused non-banking financial companies show interesting evidence of success, particularly in terms of their outreach and financial sustainability.

**Key points**

A comparative assessment of four (Swadhaar, Janalakshmi, Ujjivan and Equitas) urban-focused Indian Non-Banking Financial Companies provides evidence of their success in becoming financially sustainable as well as expanding their outreach.

Assessed over a period of six years, the NBFCs show evidence of their success in contributing towards outreach and sustainability, however it was found that Swadhaar and Janalakshmi needed to focus further on impact.

Some common factors across all four institutions that contributed to their success in serving the urban poor were found to be commercialization (or financial systems approach), strategic positioning, organizational leadership and reaching out and offering services beyond credit.

The World Bank (2012) estimates that 1.4 billion people were living on less than US$1.25 a day in developing countries in 2005. It is now widely accepted that poverty is a multidimensional phenomenon. Hulme (2003) and others have discussed various characteristics and processes that form an integral part of poverty analysis with focus on social exclusion and vulnerability. Classifying the urban poor as “poor” under the current determinants of poverty consisting of income, expenditure and calorie consumption is even more challenging. The money metric measures have their merits, but fail to rightfully classify the urban poor for several reasons (Thoebecke, 2005) including the fact that generalized price indices can be misleading (Mitlin, 2004; Mitlin and Satterthwaite 2012).

Amongst the various strategies developed internationally for poverty reduction, a very popular tool that has emerged is microfinance (Hulme 2000). All-Party Parliamentary Group (2011) refers to microfinance as a broad term that can include a large number of varied financial products, including micro-credit, micro-savings and micro-insurance. However, most Microfinance Institutions (MFIs) have increasingly focused on microcredit, which is often used synonymously with microfinance. Empirical studies on the impact of microfinance as an effective tool for poverty reduction suggest mixed results from various parts of the world. While some find it effective, others question the extent to which the provision of capital alone can help the poor.

Like the discourse on poverty, microfinance industry in India too has a rural bias (Copestake, 2010; Basu et al, 2005). Urban microfinance is a comparatively recent phenomenon. According to the Michael and Susan Dell Foundation (2006), this late attention to urban microfinance in India can be attributed to the general belief held by potential investors and entrepreneurs that the existing models in the rural areas, especially the group lending model, cannot work in diverse and transient urban communities.

Until the infamous Andhra Pradesh crisis in 2010 (see Priyadarshee and Ghalib, 2012 for details), the microfinance sector in India has witnessed a rapid growth over the last few decades. State governments, NGOs and financial institutions are the main players in the sector. Within the financial institutions, there are Banks (State Banks, Regional Rural Banks, Small Industries Development Bank of India, National Bank for Agriculture and Rural Development, and Co-operatives), Non-Banking Financial Companies (NBFCs), and Microfinance Institutions (MFIs). The latest addition now is that of “NBFC-MFIs” which are based on a hybrid institutional model supposedly catering to the low income segment as opposed to a regular NBFC.

After this brief introduction, the following section explores poverty within an urban context, followed by a discussion on the role that microfinance plays in combatting it. This is followed by a detailed discussion on the role that four Non-Banking Financial Companies have played in providing microfinance services in urban India. This also includes a detailed comparative analysis that delves into the three elements that comprise the triangle of microfinance: outreach, sustainability and impact. Prior to drawing conclusions, the penultimate section discusses the observations, trends and lessons learnt which cover the strategic positioning of the NBFCs along with their organizational leadership and what measures they take to reach out to the population in terms of providing services beyond credit.

**POVERTY IN AN URBAN CONTEXT**

The Global Monitoring Report (World Bank 2013) highlights a number of urbanization matters. The number of people living in urban settlements has risen from about 1.5 billion in 1990 to 3.6 billion in 2011. Ravillion (2001) writes about the urbanization of poverty suggesting that the poor urbanize faster than non-poor, more so in the case of India. The Census of India (2011) suggests that about 31% of the population is urban. However, the issue of classification gets tricky when it comes to distinguishing the urban from the rural areas as countries use different classifications for urban areas based on varied determinants such as population, geographical spread or the sheer proximity to resources. The World Bank (2013) reiterates this and states that there is no consistent and universally accepted standard for this purpose.

It is estimated that 76.4 million people in the urban areas live below the poverty line in India (Government of India 2012). The rate of decline in rural poverty has been higher than in the urban areas with 8.0 percentage points decline in rural poverty from 41.8% in 2004-2005 to 33.8% in 2009-2010, while 4.8 percentage points decline was witnessed in the urban areas from 25.7% to 20.9% during the same period. Comparing the Gini ratio, it also reports that inequality in rural areas has declined between the year 1977-78 to 2009-2010, which, however, seems to have steadily arisen in urban areas between the corresponding period.

The anti-poverty programs in India have largely focused on rural areas with only little attention given to the urban poor. Judy and Schuler (2004) and Meng et al. (2005) suggest that poverty analysis traditionally has focused on the rural areas. Sridharan et al. (2008), from their extensive review of literature, highlight the fact that during the past 40 years, studies on urban poverty in India are relatively few and highlight the issues faced by the urban poor. Loughhead et al (2001), in a report prepared for DFID, suggest that urban poverty reduction in India needs considerable efforts by national, state and local governments; international organizations, civil society and the private sector.

While there is substantial discourse on the conceptualization, framework, measurement, approaches to poverty and poverty reduction, the predominant trend in measuring poverty continues to be the traditional money-metric measures that surfaced during the 1990s. Despite having its own merits, using this measure as a determinant of the scale of poverty is problematic for various reasons. This is particularly so in the context of urban poverty. Firstly, the urban poor are largely wage earners that make both income and consumption levels fluctuate frequently shifting them in and out of poverty. Secondly, a basket or bundle of goods assumed for the well-being of an individual is different across countries (Thorbecke, 2005) and may then be underestimated for some countries (Tacoli & Satterthwaite, 2003). This assumption is equally valid for the urban and rural poor of a developing country including India, where their needs as well as the means to fulfil them are different. Thirdly, in an urban poverty-stricken area (often a slum/settlement), there may be households with income or consumption that is slightly more or less than the benchmark of US$1.25 a day. However, characteristics such as inadequate income, an inadequate, unstable or risky asset base, inadequate shelter, poor provision of public infrastructure, insufficient provision of basic services, insufficient protection of poorer groups’ rights through the operation of the law, voicelessness and powerlessness (Satterthwaite 2002), commoditization, environmental hazard, and social fragmentation (Baharoglu et al 2003; Baker and Schuler 2004; Chamhuri et al 2012) put everyone residing in the slum in the same category. Finally, the urban poor tend to both earn more and also spend more as the goods are likely to be more expensive in the urban areas (Mitlin 2004).

Contextualization of the urban poor helps understand the multidimensional nature of poverty. Literature on poverty now encompasses aspects such as deprivation, vulnerability, social exclusion (Hickey and Toit, 2007), powerlessness and marginalization (Hulme, 2003) which are part of the experience of poverty. Acknowledging horizontal inequalities (Stewart 2009) helps design programs with positive discrimination for social and religious minority groups that tend to be at the bottom of the pyramid even in the urban context. For instance, the urban poverty ration at national level is highest for Muslims at 33.9% as per the planning commission, GOI (2012).

The complex phenomenon of urban poverty makes it imperative that it is addressed at micro and macro levels, starting from local to global. Units and levels of intervention can be at various levels starting from households to communities, local and state governments, national policy makers, international donor agencies, NGOs, and private stakeholders. Strategies include the creation of safety nets, policy interventions, provision of services and infrastructure, community mobilization, livelihood interventions, creation of access to finances, social protection, networking with International communities, proper channeling and mobilization of aid amongst others (Appadurai 2002; Barrientos et al. 2010, Barrientos & Hulme 2009; Beall and Kanji 1999, Hjorth 2003; Mitlin 2003; Rakodi 1995; Satterthwaite 1998; Sahley and Pratt 2003).

Considering that access to finance, livelihood interventions and asset creation are all related to economic aspects, one popular tool that has been associated with poverty alleviation is microfinance, which seems to have gained significant attention in the past few years. Ledgerwood et al (2013) highlight the fact that the industry has grown exponentially in terms of outreach, service providers, products, models and clients.

# MICROFINANCE AND POVERTY REDUCTION

*"58% of the poor who borrowed from Grameen are now out of poverty. There are over 100 million people now involved with microcredit schemes. At the rate we're heading, we'll halve total poverty by 2015. We'll create a poverty museum in 2030.” – (Professor Muhammad Yunus, speaking to Time Magazine in 2006)*

According to Beatriz and Jonathan (2010), microcredit initially focused on getting loans to the poor to augment their savings. The push to “microfinance” came with the recognition that households can benefit from access to financial services and not just credit for microenterprises. As a result, the attention diverted towards the “less poor”, and the development of commercially viable financial products and services. Microfinance includes insurance, transactional services, and importantly, savings (Barr, 2005). Microfinance can also be described as “the provision of a broad range of financial services to poor, low income households and micro-enterprises usually lacking access to formal financial institutions” (CIDA, 2002).

Barr (2005) suggests that as an instrument of financial development, microfinance helps in reducing poverty. Beck et al (2007) in a research using panel data found that financial development helped the poor by impacting their incomes. According to the study, 60% of the impact of financial development on the poorest quintile works through aggregate growth, while about 40% through reductions in income inequality.

Given below is a pictorial representation of the relationship between microfinance and poverty reduction.



Figure 1. Relationship between microfinance and poverty reduction (Ganji, n.d). (Color figure can be viewed in the online issue, which is available at wileyonlinelibrary.com).

Khandker (2005) employed panel data from Bangladesh to study the impact of microfinance on poverty and found that the access to microfinance contributes to poverty reduction. It also had a special impact on female participants, with overall poverty reduction at the village level by 1% each year in the programme areas. In another study, Pitt and Khandker (1998, 2006) revealed that Grameen Bank of Bangladesh was able to reach 50% of its villages covering more than 2 million borrowers of which 94% were women. Positive impact on the economic and social well-being of participants was observed along with an overall income growth and poverty reduction at the village level.

Matin and Hulme’s (2003) examination of Bangladesh Rural Advancement Committee’s Income Generation for Vulnerable Group Development Programme suggests that its outreach has been impressive and it has been able to reduce poverty. The study concludes that IGVGD is capable of reaching the chronic poor with the dual protective and promotional approaches to livelihoods.

Benda’s (2012) study of the impact of Rotating Savings and Credit Associations (RoSCAs) on the well-being and pro-poor community development in rural northern Rwanda suggests that the money pooled in by the group was used for fulfilling their basic needs and building of assets. The gains of RoSCA were not just economic but also social, as it buildt social capital within the community.

Hossain (2012) studied the social impact of BRAC microfinance operations on 208 clients in relation to non-income poverty (also termed as social poverty). He has reported a positive but varying degree of social impact of the microfinance programs on clients. However, a significant impact was observed on potable water and sanitary condition of the respondents.

Zeller and Meyer (2002) discuss the Indian scenario, policy and programmes, and suggests that microfinance is a win-win proposition. He argues that microfinance can contribute towards poverty alleviation and food security through financial services like savings and investment, reduced cost of self-insurance and contribution to consumption smoothing. Imai et al (2010) use national household data from India to estimate the poverty reducing effects of MFI loans, and has found that loans for productive purposes were more important for poverty reduction in the rural areas, whereas simple access to MFIs in the urban areas has larger average poverty-reducing effect. In another study, Chen and Snodgrass (2001) studied the operation of Self Employed Women’s Association Bank in India, and found that the use of credit provided by the bank led to a rise in household and per capita income.

Brook et al. (2008) report the findings of a study of six villages where the Self Help Group (SHG) program was run by two NGOs. They found that over a period of three years, the poor moved above the poverty level with an increase in their household savings by 647%. The study also found that the poor and the very poor were actively involved in the group activity as opposed to their wealthy counterparts.

While the empirical evidence so far seems optimistic with a positive impact of microfinance on poverty reduction, there are other sets of evidences that say otherwise. Coleman (1999) used data from a quasi-experiment conducted in Northeast Thailand in 1995–1996 to test the borrowers’ welfare in a group lending model. The results indicate that programme loans have had little impact after controlling for self-selection and endogenous programme placement. In another of Coleman’s (2006) work, the outreach and impact of two microfinance programmes in Thailand has been explored. Findings suggest the likelihood of the wealthy participating significantly more than the poor, and the power dynamics making the wealthy take leadership positions compared with the poor who are likely to be left out.

Similarly, Weiss & Montgomery, (2005) conducted a study on the impact of MFI on poverty reduction by comparing the poverty impact studies from Asia and Latin America. They concluded that the evidence that microfinance was reaching the core poor in either of these regions was very limited. Navarajas et al. (2000) examined the social worth of five microfinance organizations in Bolivia by analyzing the depth of their outreach. They found that the poor being served by the MFIs were near the poverty line and better off compared with the poorest. The urban poor borrowed more often, though the rural poor were most likely the poorest. This section has provided a lot of evidence on the efficacy of microfinance in removing urban poverty.

# MICROFINANCE IN INDIA AND THE ANDHRA CRISIS

Poverty reduction oriented microfinance can be traced back to the 1970s, when Professor Muhammad Yunus of the Grameen bank decided to lend his personal money to the poor women in Bangladesh. In India, the microfinance movement started in the rural hinterlands with the nationalization of banks in 1969. The banking industry was directed by the Reserve Bank of India to channelize 40% of their lending activities towards the priority sector which largely included the agriculture and related activities, women and other weaker sections of the society.

The first microfinance model in India, called the Self Help Group (SHG) model, came into existence in the 1980s whose beneficiaries were women. Since then the microfinance industry has grown manifold, moving away from state-sponsored to private entities entering the microfinance market. M-CRIL (2012) reports a growth rate of 62% per annum in terms of numbers of unique clients and 88% per annum in terms of portfolio over the five years 2005-2010. With around 32 million borrower accounts in October 2010, India has the largest MFI sector in the world.

In the year 2010, the microfinance industry witnessed a severe crisis when the Government of Andhra Pradesh, a state in Southern India, promulgated an ordinance to stop the microfinance operations by nightfall and directed all microfinance operations to be suspended till all the MFIs got themselves registered with the District Registration Authority. This measure was the result of a series of suicides that were attributed to coercive recovery practices and high interest rates that MFI’s charged. While the other school of thought believed that the Ordinance was a political gimmick as the MFIs were competing with the State lead SHG programs.

Although the Ordinance was issued and implemented in only one State, its impact was widespread and resulted in the overall decline of microfinance sector in India. According to M-CRIL (2012), CRILEX – the MFI Growth Index for India, which rose from 100 in March 2003 to 8,005 in March 2011, fell for the first time to 6,290 in March 2012.

# NON-BANKING FINANCIAL COMPANIES AND URBAN MICROFINANCE IN INDIA

CRISIL (2009) reports that there are over 3,000 MFIs, NGOs, and NGO-MFIs in India, of which about 400 are involved in lending programs. A majority of these organizations are in the rural areas, while their number is far less in the urban areas. This section explores the services, products and operations of four NBFCs that serve the urban poor in India. This has been done by analyzing cross-sectional data of the four institutions viz. Ujjivan Financial Services Pvt. Ltd (UFSPL), Equitas Micro Finance Private Limited (EMFPL), Janalakshmi Financial Service (JFS) and Swadhaar FinServe (SF). These institutions have been selected based on the following criteria:

1. Their specialty in providing microfinance services at the urban level,
2. Their scale and outreach in the urban microfinance
3. Their recognition as leading MFIs in India by various credible agencies and networks such as MFIN, MIX, and Sa-Dhan. The CRISIL’s (2014) report recognizes them as “India’s 25 leading MFIs”.

Table 1 below shows a summary of their mission and vision:

|  |  |  |
| --- | --- | --- |
| **Institution** | **Stands for** | **Vision & Mission** |
| **Ujjivan Financial Services Private Limited** | Better Life | Provide full range of financial services to the economically active poor to build better lives. |
| **Swadhaar FinServe** | Self-Support | To be the preferred provider of micro financial services. |
| **Janalakshmi Financial Services** | People's Wealth | To emerge as a full scale financial services provider for the Indian sub-prime sector. |
| **Equitas Holdings Private Limited** | Transparency | To improve the quality of life, by increasing total household asset value of those who are not effectively serviced by the formal financial sector, by providing transparent and trustworthy access by developing cutting edge technology, and forming partnerships and alliances. |

**Table 1: Vision and Mission of four NBFCs**

Table 2 below provides an overview of operational and financial performance of the four NBFCs that form the basis of this study. For each of the four organizations, the table lists products, services and partnered products that each agency offers, the number of states that they operate in, the total number of branches, the Gross Loan Portfolio (GLP), and the number of borrowers.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Particulars** | **Ujjivan Financial Services Private Limited** | **Swadhaar FinServe** | **Janalakshmi Financial Services** | **Equitas Holdings Private Limited** |
| **Company Type** | NBFC | NBFC | NBFC | NBFC |
| **Established since** | Dec-04 | Mar-05 | Jun-06 | Jun-07 |
| **Products and Services offered** | 1. Group loan 2. Individual loan 3. Insurance | 1. Group loan 2. Individual loan 3. Credit linked life insurance | 1. Group loan 2. Individual loan 3. Education loan 4. Housing loan 5. Enterprise financial services | Group Loan |
| **Partnered Products** |  |  | 1. Insurance 2. Micro pension 3. National pension scheme 4. Prepaid cards 5. Savings | 1. Insurance 2. Housing loan |
| **No of States it operates in** | 24 | 4 | 16 | 7 |
| **Total number of branches** | 423 | 42 | 154 | 361 |
| **Gross Loan Portfolio (USD in millions), 2013** | 269.28 | 33.9 | 341.81 | 250.25 |
| **No of active borrowers, 2013** | 1,297,131 | 156,529 | 1,412,738 | 1,821,087 |

**Table 2: Operational and financial performance of four NBFCs**

The table above shows that all the four NBFC have started their operations within ten years. This shows that they are young organizations and have been established in the recent past. However, within a short span of time, they have been able to generate lot of interest in the microfinance market which is evident from their loan portfolios and the number of active borrowers. It can also been seen that though Equitas Holdings was established most recently and works only in seven states, it has the largest number of active borrowers. This is despite the fact that its portfolio of offered products is limited to only three. This indicates that outreach of a NBFC is not related to the number of states it serves in or the number of products offered by it. It is the reach to the needy and quality of products that matters the most.

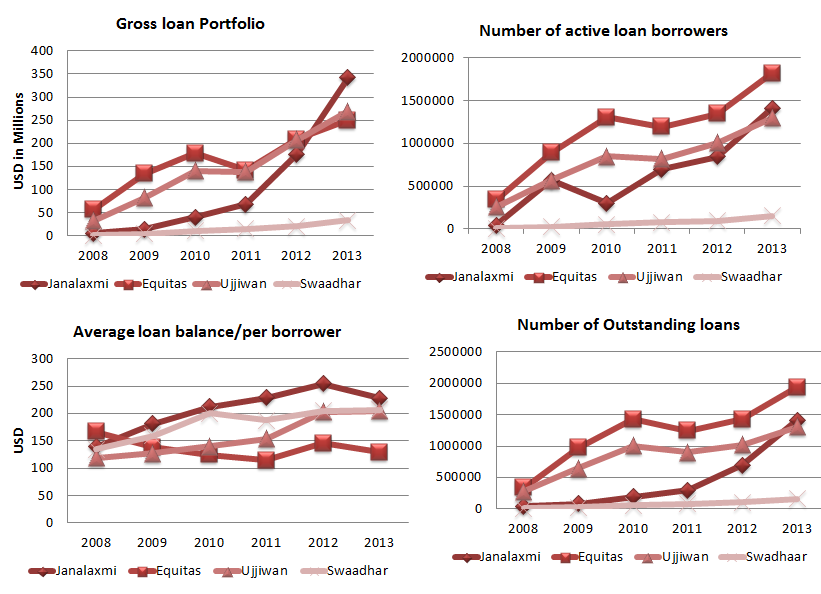
# COMPARATIVE ANALYSIS AND DISCUSSION

The debates and different viewpoints regarding the impact of microfinance on poverty have been covered in sections 2 and 3. It will be appropriate to briefly dilate upon some of the measures to judge the impact of microfinance on poverty. Ghalib (2013) suggests that it is *depth* of the outreach (poverty levels of the beneficiaries as opposed to numbers) that is more important to measure the impact of microfinance on the poorest, while Otero (1999) recognizes financial sustainability as important in considering the ‘institutional’ importance of MFIs. Zeller and Meyer (2002) developed a conceptual framework called *the triangle of Microfinance* to study the performance of MFIs. This triangle contains a small circle that characterises all infrastructure innovations that can be implemented to improve *financial sustainability* (examples include improved financial management systems and policies, the introduction of ICT and management information systems for accurate reporting to aid in decision making, etc.), the *impact* (such as designing and implementing cost-effective complimentary services for the borrowers), and *outreach* (such as designing and implementing strategies and policies that attract and target the right type of clients, carrying out a detailed needs analysis based on empirical research to identify deserving individuals and households).

Based on this framework, the following sections analyse these four organizations by employing six years (2008-13) data obtained from the Microfinance Information Exchange.

## OUTREACH

Data on outreach includes the following information for the four NBFCs: number of active borrowers, number of outstanding loans, gross loan portfolio in USD, and average loan balance per borrower.



**Figure 2: Outreach of the four NBFCs**

Figure 2 shows that all the four organizations have seen a consistent growth in their Gross Loan Portfolio (GLP) till FY2010-11, the year the microfinance crisis ocurred. While Equitas and Ujjivan experienced a drop in the GLP in FY2010-11, Janalakshmi and Swadhaar continued to witness growth in FY2011. GLP for all the four institution grew in subsequent years. It can be inferred from this that the organizations with smaller portfolio and scale of operations were cushioned from the immediate impact of the crisis, while the bigger ones got hit.

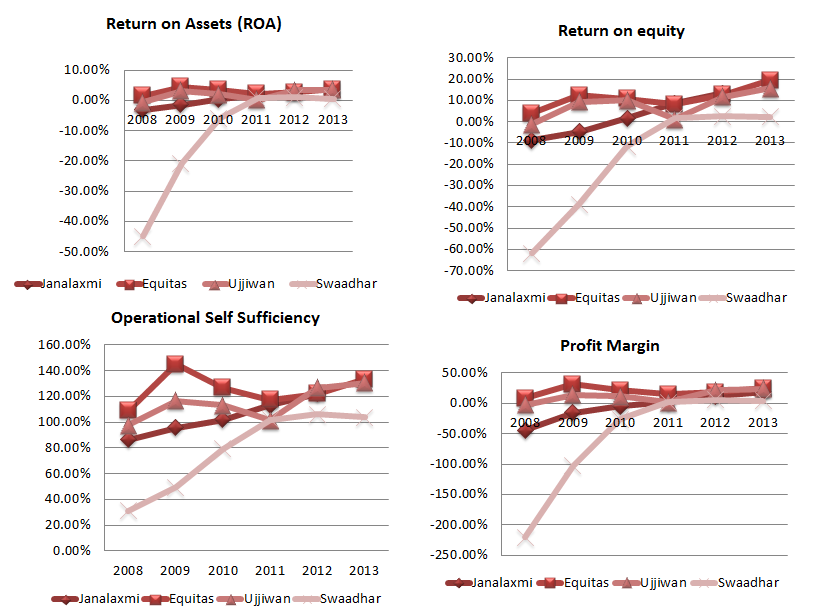
The Number of Active Borrowers (NAB) shows a similar trend between Ujjivan and Equitas; both of them saw a consistent rise in NAB until FY2010-11, when it declined. It rose again in the subsequent year. The fluctuation in Janalakshmi’s NAB has been intriguing as it decreased in the FY2009-10 before the crisis. However, it increased by 231% the next year. Swadhaar is the only agency amongst all four that has seen a consistent but slow and gradual increase in NAB till 2013.

In terms of Number of Outstanding Loans (NOL), the trend between Equitas and Ujjivan is repeated; the only time there is a dip in NOL is during the crisis period. In the remaining years, they has been a consistent increase. Janalakshmi and Swadhaar yet again see a consistent growth in NOL over the five years.

In order to measure depth of the outreach, average loan balance per borrower has also been measured. The year-on-year movement of average loan balance per borrower comes up with some interesting results. Ujjivan is the only organization among the four that has a growing average loan balance per borrower over the six-year period, while the others show a mixed trend during this period.

## SUSTAINABILITY

## The second element of the triangle is sustainability, which encompasses an institution's financial stability and its potential to grow. The financial indicators related to sustainability are Return on Assets (ROA), Return on Equity (ROE) and Operational Self-Sufficiency (OSS) (CGAP 2009; Meyer and Zeller 2002). Figure 3 below is a graphical representation of the changes in ROA, ROE and OSS of these organizations over a period of six year ranging from 2008 to 2013.



**Figure 3: Sustainability of the four NBFCs**

It is evident from the Figure above that Janalakshmi has consistently enjoyed increasing returns both on equity and assets over the six years period. Janalakshmi rather demonstrates an impressive leap in its ROE from 1.60% in 2010 to 8.54% in 2011and continued to grow in subsequent years. Swadhaar too has shown an increasing return on equity and asset except for the year 2011 when there was a drop in both the figures with subsequent rise in the next year. A very interesting phenomenon that is emerging from the data is that both Equitas and Ujjivan, which are bigger MFIs in terms of their scale and volume and being the second and third most profitable MFIs outside Andhra in the FY2012-2013 (Equitas 2012), show decrease in the percentage of both ROE and ROA from the pre-crisis period. However, there was an increase of returns on equity and assets in the FY2012 for both, though Ujjivan has seen a drastic rise. It can be implied from this that large organizations are likely to make smaller returns though this may still be sustainable for them. With respect to OSS, Equitas and Ujjivan are the leaders with OSS as high as 133.34% and 130.64% respectively and profit margin of 25.00% and 23.45% respectively.

**Factors leading to outreach and sustainability**

Ivatury (2006) finds that providing financial services to the poor is costly as the size of transactions is often small, the population may often be scattered and their credit history may not be available. To effectively deal with high transaction cost, all the four NBFC covered in this study bear a similar approach to sustainability: reduction in operational cost and technologicalenhancement. Ivatury (2006) suggests that MFIs with operational cost of 12-15% of assets are considered efficient.While currently all the four institutions are within the range of 12-15% of Operational Cost (OC), Equitas is the only institution which has stayed below 15% throughout the six years. Ujjiwan has seen consistent decline in OC. But the most striking performance has been by Swadhaar where operational cost was brought down from 36.37% in 2009 to 10.11% in 2013. Investment in technology is a strategy that all the four organizations have adopted in varied proportion. They use core banking solutions and have a central back-end team which makes the turnaround time for processing both loans and disbursements.

## IMPACT

The third and final component of the triangle of microfinance is *impact*. The ability of microfinance to create an impact has been widely debated in the academic literature. Its impact on poverty can be measured by using Randomized Control Trials (RCTs) (Banerjee et al 2013; Karlan et al 2010). Srinivasan (2012) suggests that as effective as RCTs are, it needs to be recognized that the capacities of MFI do not allow them to work with customers that are not under the influence of MFIs in anyway. It is pertinent to add that the urban poverty comprises dimensions of human development as discussed in sections 2 and 3 of this paper.

Out of the four organizations, Ujjivan has a well-documented and systematic quantitative impact assessment process. Its assessment focuses on economic growth and quality of life indicators like gender empowerment, access to resources, and education etc. The impact assessment report by Ujjivan (2012-2013) suggests that during the period of 2010 -2013, out of 3000 customers, 87% defined their current state of well-being as “Positive” compared with 60% three years ago. Between 2010 to 2013, the average monthly income of all respondents increased by over 51%, while the number of self-employed women rose from 48% in 2010 to 61% in 2013, and their monthly income rose by an average of 85% over the three-year period. 40% families had enrolled their children in private schools compared with 28% three years ago.

To measure the impact of their microfinance operations, Equitas follows an ‘assets building’ approach. They do this by making a systematic estimation of the value of a customer's household effects at a time when he or she enters a system and this process is repeated with an interval of every two years to take a stock of increase or decrease in the asset base. As per the respondents, close to 50% increase in the asset base has been observed so far. Swadhaar and Janalakshami focus on qualitative data for impact assessment. They collect live stories of customers to see how and in what way access to credit has impacted their lives.

It is important to note that both the qualitative and quantitative measures have their own merit. In case of live story coverage, there is risk of selection bias if the sample is not randomly chosen and only those customers who have done well are selected. Similarly, quantitative assessment may not give a larger picture of a customer’s life and may only touch aspects that can only be measured in terms of numbers, for instance increase in income.

This may also suggest that systematic assessment, retrospection and reflection on impact could be a higher priority for organization who has achieved larger scale while the smaller ones focus more on growth and sustainability.

The impact assessment studies have their flaws. A report compiled by the All-Party Parliamentary Group on Microfinance (2011) recommends that ‘more investment is needed in the research base to develop evidence about what microfinance interventions work the best to reduce poverty’. Zeller and Meyer (2002) suggest that all MFIs try to contribute to the three objectives of outreach, financial sustainability, and impact howsoever they prefer one over the other. “Some may produce large impacts but achieve limited outreach. Others may have smaller impacts but are highly sustainable.”(Zeller and Meyer, 2002). The analysis of four organizations along the three objectives shows that they have by and large been successful in achieving outreach and sustainability, though Swadhaar and Janalakshmi may need to invest further to create better impact.

**OBSERVATIONS, TRENDS AND LESSONS**

**Commercialization or Financial Systems Approach**

The legal structure of all the four organizations is a *Non-Banking Financial Company*. Their peculiarity is that they follow a commercial approach to business while synchronizing their activities with the social mission. “What has promoted the growth of NBFCs is their localized presence, a higher level of customer orientation than banks and lower documentation requirements albeit at higher interest rates for borrowers. Conversely, depositors earn substantially higher rates of interest as compared to the traditional savings instruments of banks. In this way, NBFCs are able to attract a large volume of deposits from the general public” (Sa-Dhan, 2006, p. 25). While there has been a debate about the ‘mission drift’ when the MFIs grow in size and follow the financial system approach, there is a fairly large segment of academicians and field practitioners, who believe otherwise. A number of researchers have held varied opinions about whether commercialization is good or bad for microfinance. Some argue that competition will lead to improvements in products and systems resulting in increased options for the borrowers, while others state that it tends to cause a ‘mission drift’ amongst MFIs (see for instance Christen 2000 and Ryhine 2001). Hence, there is reason to believe that in the context of urban poverty, the NBFC structure of these organizations can be an element that favours them.

**Strategic Positioning**

Events in the microfinance sector in Andhra Pradesh came to be known as a ‘crisis’ because of the scale. Andhra Pradesh is a state in Southern India which has the highest concentration of both MFIs and borrowers (Almost 1/3rd of the total outreach) and that is why it had a momentous impact on the entire microfinance industry across the country and even abroad. These four organisations of this study have followed a smart strategy to launch and continue operations outside Andhra Pradesh they chose to work in states that were less served and hence had higher chances of growth. In a similar fashion, while most MFIs are concentrated in rural areas these MFIs focused on urban poverty which was again a neglected area and hence a market with great potential. Strategic positioning in terms of selection of geography, choice of models, mode of operation and choice of technology seems to be the differentiator giving these organisations an edge over the other.

**Organizational Leadership**

The leadership spearheading these four organizations brings professionalism, years of experience and access to extensive networks. All the founding leaders i.e Ms Veena Mankar of Swadhaar, Mr. Samit Ghosh of Ujjivan, Mr. Chandra of Janalakshmi and Mr. Vasudevan of Equitas Holdings Private Ltd., have over a decade of experience of working in the financial sector. Their knowledge of the financial sector, technical know-how, use of sophisticated technology including core banking systems and high degree of professionalism in operations may be some attributes of the financial sector that these leaders have been able to replicate in the field of microfinance. Organizational leaders determine the roadmap for success, drive key initiatives within the organization and take the risk needed.

**Reaching out Beyond Credit**

Trends in the *modus operandi* of MFIs vary throughout the globe. Some places need commercially-driven microfinance models such as in Latin America and some need development-oriented models more specifically in relation to poverty reduction. While some institutions use a minimalist approach and stick to credit alone, others opt for engaging their customers beyond credit.

In sections 2 and 3, we have explored the complex and multidimensional nature of urban poverty. The four institutions studied have also strategically engaged their target segment in interventions beyond credit, encompassing a number of development activities. All have a sister concern that implements these development projects as exhibited in Table 3 below.

|  |  |  |  |
| --- | --- | --- | --- |
| **NBFC** | **Development partner** | **Legal structure** | **Areas of intervention** |
| **Ujjivan Financial Services Private Limited** | Parinaam Foundation | Not for profit Section 25 company | 1) Ultra poor program 2) Education 3) Financial literacy 4) Livelihood and community development |
| **Equitas Holdings Private Limited** | Equitas Microfinance Private Ltd | Non-Banking Financial Institution | Credit and other financial products |
| Equitas Development initiative Trust | Charitable trust | 1) Vocational training 2) Health care 3) Rehabilitation of pavement dwellers |
| Equitas Dhanya Kosha | Private limited Section 25 company | Food security |
| **Janalakshmi Financial Services** | Janalakshmi Social Services | Not for profit Section 25 company | 1) Incubation of social business models 2) Education, skills and livelihood 3) Community mobilization |
| Janaadhar constructions pvt. ltd | Private Ltd company | Construction of low-cost and affordable housing |
| **Swadhaar FinServe** | Swadhaar FinAccess | Not for profit Section 25 company | Financial literacy and inclusion |

**Table 3: Development partners, legal structure and areas of intervention of the four NBFCs**

The clear demarcation of both the type of involvement financial and non-financial dimensions through setting up different agencies is a strategy that comes with several benefits. While a for-profit company is likely to have direct financial benefits, not-for-profits can accept donations and charities; they are exempt from tax and have a lesser possibility of regulatory interference (Sa-Dhan, 2006, p. 14).

Equitas’s unique concept of a chain of grocery store called as *Equitas Dhanya Kosha* is designed to address the food security needs of the urban poor. These stores are like any super market though their benefit is threefold: the households are provided an interest-free monthly rolling credit of Rs 1,000 which is loaded on a card and can be availed in times of difficulty; secondly, the goods are sold on prices cheaper than the MRP which means savings; and thirdly, about 8% of the savings against MRP is given back to every customer on a monthly basis. This also means that a substantial part of the customer’s income never changed hands outside the relationship with this financial institution.

Contributing to the overall well-being of the customer segment is also an investment towards the longevity of engagement with the customers. While the social development programs benefit the customers directly, interactions with customers and adding value in more than one sphere of their lives is likely to influence their loyalty towards the financial institution and may also instill stickiness. For instance, financial literacy has the potential to build financial capabilities leading to household financial management which in turn may result into better portfolio quality for the financial institution.

# CHALLENGES FACED

The last area where some convergence is seen is the challenges that the industry in its entirety is facing. While there may be a number of such aspects, two of these have been highlighted below:

1. Regulatory and political environment has been perceived both as a challenge and an enabler when favorable for the sector. Matin and Hulme (2003) suggest that current regulations for MFIs in some countries can pose a challenge to their growth for several reasons; one such reason being not being able to hold savings. Given the post Andhra crisis environment, subsequent evolution of the microfinance bill, and the regulatory guidelines for MFIs, there are several constraints imposed on the working of MFIs.
2. Another industry-wide challenge is the retention of human resources, as attrition in the sector is quite high. Given the sensitivity and sensibility needed to serve the urban low income communities, it is essential that the staff is in line with the vision and mission of the organization. All four MFIs which participated in this study invest heavily in extensive training and capacity building of the staff. However, opportunities available in big cities make it difficult to retain a trained and qualified staff.

# CONCLUDING REMARKS

Microfinance as a tool for poverty alleviation has been acknowledged in recent times (Hulme 2000; Otero 1999). However, its benefit and use have generally been limited to the rural poor in India. In this paper, we first contextualize urban poverty, followed by an extensive review of the existing literature. Zeller and Meyer (2002) suggest that there are three overarching policy objectives that the MFIs try to attain. These are outreach, financial stability and impact, which they call the *‘triangle of microfinance’*. Performance of MFIs has been established by applying this framework of analysis.

Due to the limited attention to urban poverty in India, fewer MFIs and NBFCs have chosen to work in this segment. Using the triangle of microfinance, we analyse the performance and operations of four NBFCs in India and explore the manner in which they engage with and address urban poverty. The comparative analysis of the outreach, sustainability and impact over a period of six years shows that they have been successful in contributing towards these three objectives for the 2008-2013 period in the areas of outreach and sustainability. However, Swadhaar and Janalakshmi need to invest further in creating better impact.

Amongst other trends, it was observed that both the larger organizations, namely Equitas and Ujjivan, have seen growth in terms of outreach through the pre-crisis period, while fall in outreach was noticed in the year of the crisis with outreach growing again in subsequent years. Apparently, though not Andhra-based, these organizations were still impacted by the crisis. On the other hand, the smaller ones (Swadhaar and Janalakshmi) remained cushioned from the crisis.

Another observation is that the larger organizations saw a decline in returns on equity and assets, considered a yardstick to measure sustainability and profitability, over a period of three consecutive years until the year of the Andhra crisis. Given that the larger organizations continue to grow in terms of outreach, yet accrue smaller returns, it could be their deliberate choice to position themselves between sustainability and profitability. The smaller organizations, on the other hand, enjoy better ROE and ROA.

As for the impact assessment programs, it appears that the larger organizations tend to conduct systematic quantitative impact assessment studies, while the smaller ones tend to opt for the life stories of their customers which are generally qualitative in nature. From the analyses, it can be inferred that while the smaller organization prioritize sustainability and profitability, the larger ones seems to have a greater focus on impact. Other common factors observed that make these organizations successful in serving the urban poor are commercialization or financial systems approach, strategic positioning, organizational leadership, and reaching out beyond credit.

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