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FIN-TECH LEVERAGE IN MICROFINANCE INSTITUTIONS: A STUDY ON INDUSTRY LEVEL OPERATIONAL EFFICIENCY AND FINANCIAL PERFORMANCE

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ABSTRACT

Microfinance is a decisive financial service as it provides access of capital and other supportive services to the financially underserved. The microfinance is a well-regulated industry defends the exploitation of unorganized money lenders. Micro Finance Institutions (MFI) served the additional clients on average with growth rate of 6% yearly. Adoption of advancements in Financial Technologies helped the MFIs to introduce Innovations in their operations. During the study period these innovations resulted in improved operating efficiency and earnings reasonably a good return on Investments. Micro financing Industry has huge untapped market in the lending sector and can flourish when the services extend to the all low-income clients. Maximizing the client base for Micro financing Industry is highly desirable for inclusive growth of Economy.

KEYWORDS: *Microfinance, Digital Innovations, Operating Efficiency, Financial Performance*

1. INTRODUCTION:

The microfinance sector in India consists of various categories of microfinance institutions (MFI) includes NBFC MFIs, Banks, Small Finance Banks (SFBs), NBFCs and Non-profit MFIs. Credit portfolio of all MFIs as of 31 March 2020 is Rs 236427 Crores.

Sustainability and growth of Industry depends on adequacy of returns and getting hold of considerable size. High Growth rate of Micro finance is extremely significant for inclusive growth of Indian Economy. Digital innovations in the financial services are resulting in more convenience, cost effective and security to the consumers. These innovations are continuously adopted in every Industry and MFIs are also part of this integration. Digital Innovations such as Mobile Banking, Biometric based Point of Sale systems, Digital Field Automation Systems and Open Application Program Interfaces (APIs) in the Microfinance are driving the industry towards fundamental changes. These changes include redesigning of Product line and operational models, change in governance structures, creating and use of new channels of Product delivery.

Recent development in the Product innovations of MFIs are resulting mainly on decreased transaction cost per service, enhancing customer base, improving customer loyalty, rapid and effective information reporting on customer's Business transaction.

2. OBJECTIVES OF THE STUDY

This study focuses on viability and growth of Micro Financing Institutions in India. It consists of the following objectives

1) To study the recent developments in the products and growth of MFI Industry.

2) To study the operational efficiency of the Industry and
3) To analyze the financial performance of the Industry.

3. DATA SOURCES, PERIOD OF THE STUDY AND RESEARCH METHODOLOGY:

Secondary data from the publications of Sa-Dhan (Association of MFIs) **[1],** MFIN India (NBFC-MFIs Association) **[2]** ,NABARD **[3]** , RBI **[4]** and Individual MFIs **[5].** Operational and Financial data during the period of 2013 to 2020 is used in the study. Data is analyzed and results are worked out with simple statistical methods.

4. RESULTS OF THE STUDY

Recent developments in the products and growth of MFI Industry

Digital innovations in the financial services are resulting in more convenience, cost effective and security to the consumers. For many years Indian MFIs have been substance with a plain vanilla loan product due to the regulations and lack of competition between the institutions. In the competitive environment many of product and process innovations entered in the microfinance services.

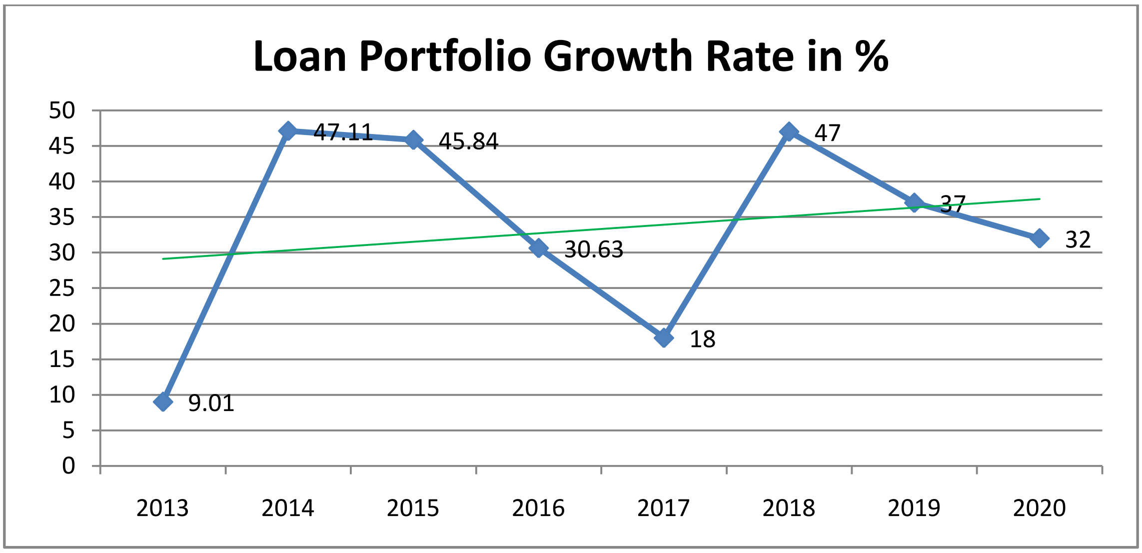
Growth of MFIs:

In 2013 total client reach was 2.8 crores and increased to 4.2 crores as of March 2020. During the period 2013-2020 MFIs served the additional clients on average with growth rate of 6% yearly. During this period growth rate in terms of CAGR (Compounded Annual Growth Rate) in is just 6%.

The average loan served per customer was Rs 8112 and it is increased to Rs 14700 during the period 2013- 2018. But this average loan is very low as compared to the Micro credit limit to the individual clients.

Amount of Loan Portfolios of MFIs are Rs 25699 Crores in the year 2012-2013 and increased to Rs94391 Crores in 2019-20. Growth rate achieved during these 8 years period is 17.66% in terms Compounded Annual Growth Rate (CAGR). Year wise growth is very impressive with exception of 2017-18. During this year demonetization effect can be attributed for the low growth as compared to succeeding year. Yearly growth in the Loan portfolios is presented in the Figure 1.

Figure 1: Growth of Micro Finance Institutions Gross Loan Portfolio



Data source: Sa-Dhan Bharat Microfinance Reports (BMR)

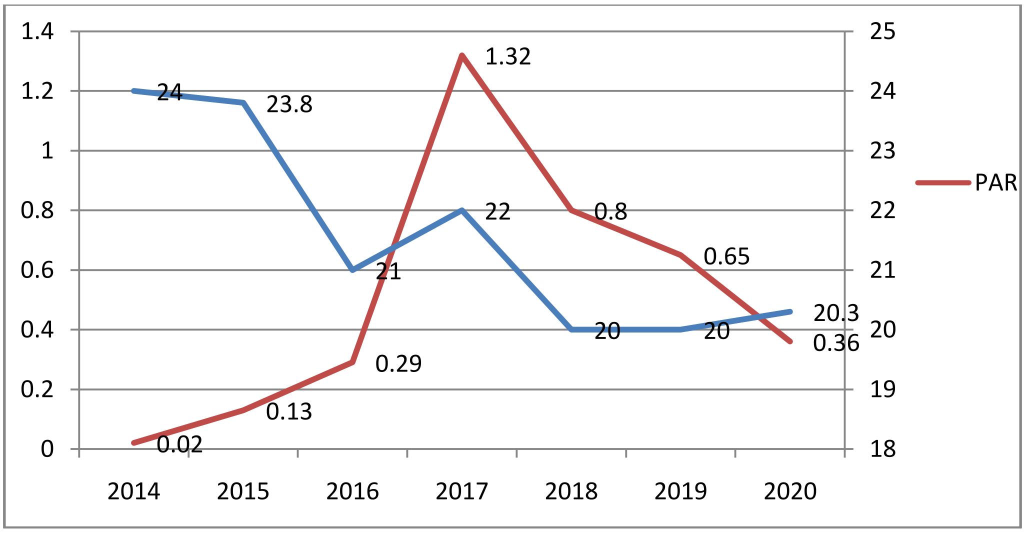
Operational efficiency of the Industry

Staff Productivity in MFIs is measured with Active Borrowers per Credit Officer (ABCO). ABCO measures the number of active borrowers served by a Credit Officer. MFIs which have systems and processes in place can handle a greater number of clients as these automated systems facilitates minimal time for credit officers to be spent at the client level. ABCO results in the number which is significant measure of productivity of staff as it determines the quantity and quality of time spent by the credit officer with a borrower, affecting the service quality. With very low ratio of ABCO, better service is possible, but it involves a higher cost to MFIs. Similarly, a very high ABCO ratio would affect the service quality.

During the study this ABCO is continuously decreasing indicates that Credit Officers are more concerned about quality of service rather than quantity of clients served. Despite automated systems used for client service in almost in every MFI, Lower ABCO should reflects decreased PAR value and increased higher growth in size of Loan Portfolio.

Lending business is generally marked with the inherent risk of default in repayment. Maintaining a healthy loan portfolio with low default risk ensures the achievement of the objectives of an MFI. Portfolio at Risk (PAR) indicates the proportion of outstanding amount of all loan accounts having past due or arrears to the total loan portfolio. In general, PAR 30, that is, the amount of loan portfolio remaining unpaid 30 days and beyond crossing the due date, would be used as a measure to assess the portfolio quality. Higher the PAR value indicates that higher the probability of Non-Performing Assets (NPA). During the study period Par value ranges from 0.02 to 1.32. It is clearly indicating very healthy Loan portfolios of MFIs.

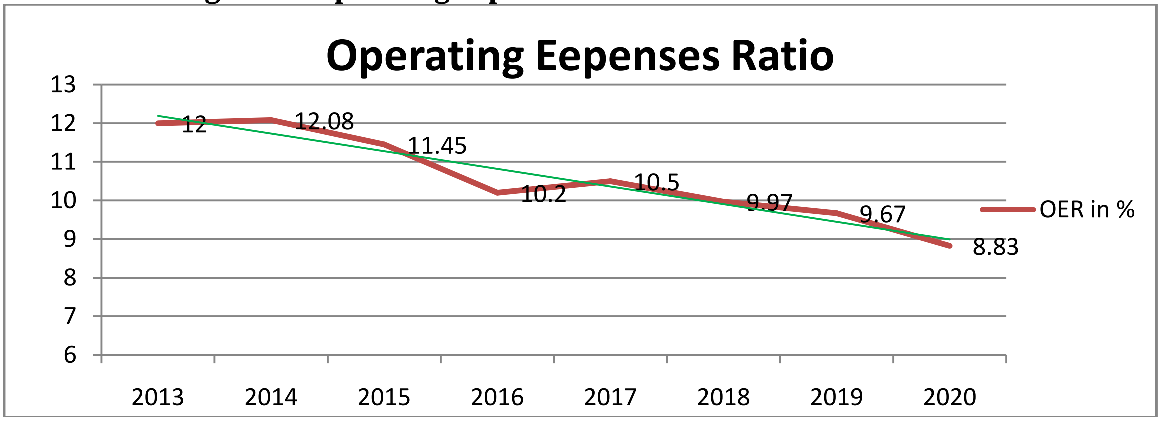
Figure 2: Yield Trend of MFIs and PAR



Data source: Sa-Dhan Bharat Microfinance Reports (BMR) There is negative correlation between Loan portfolio Growth rate and PAR Values. Correlation between these is -0.72 indicating that higher the growth rate does not lead to the risk of default. Efficient management of loan portfolio is clearly observed as decreasing PAR value with the increased Portfolio growth. Study point out the higher PAR values are influencing the yield on Portfolio but increased size of portfolio and rate of interest charged may cause this decreasing yield rate.

Operating Expense Ratio is another measure used to evaluate the operational Efficiency of MFIs. It is the Ratio of administrative and salary expenses to average loan portfolio.

Figure 3: Operating expenses of Micro Finance Institutions



Data source: Sa-Dhan Bharat Microfinance Reports (BMR)

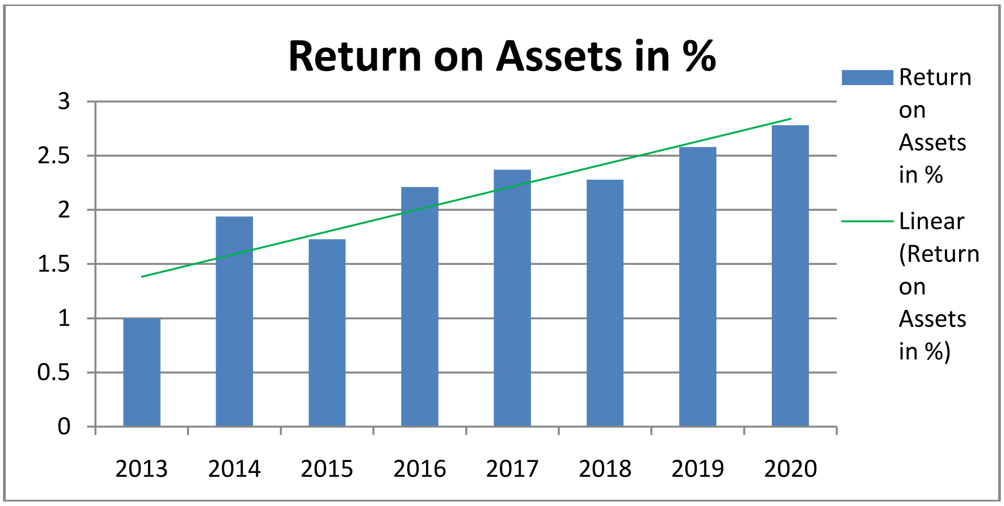
Downward trend in the Operating expenses ratio in the figure 3 during the study period indicating that the efficient handling of operations. Though average number of clients handled by credit officers is decreased continuously, the reason for decreased average operating expense ratios can be attributed with the increased Loan Portfolio size and use of online tracking systems.

Financial Performance of Micro Financing Institutions

MFIs requires large amount of financing for increasing the client base. External financing for the MFIs is possible only when it shows immense potential in profitability, measured by the Return on Assets (ROA) and Return on Equity (ROE). Investors analyze the Potentiality of Industry in terms of profitability which is measured by the Return On Assets(ROA) and Return on Equity(ROE).

Evaluating the MFIs Financial performance provides greater insights to understand their profitability and financial position.

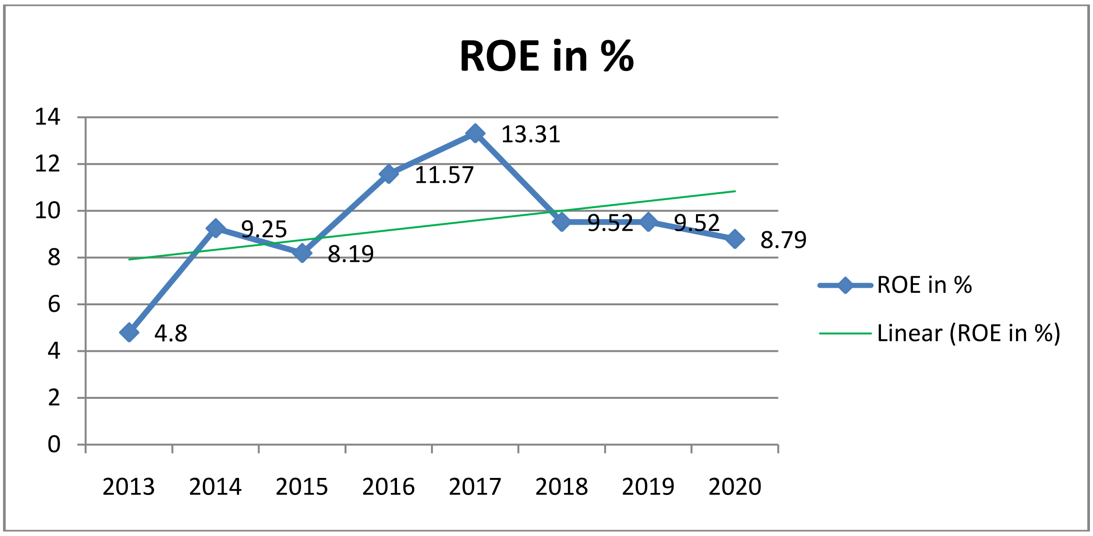
Figure 4: Return on Assets of Micro Finance Institutions.



Data source: Sa-Dhan Bharat Microfinance Reports (BMR)

Return on Assets (ROA) is most commonly used benchmark for measuring the profitability. It is a ratio of Net Profit after Tax and Total Assets. It indicates how efficiently assets are used to produce the profits. During the study period ROA is increase from 1% to 2.78 %. Figure 4 clearly indicating the upward trend in the growth of ROA which is an indicator of the efficient operations management of the MFIs.

Figure 5: Return on Equity of Micro Finance Institutions.



Data source: Sa-Dhan Bharat Microfinance Reports (BMR)

Return on Equity (ROE) is a key ratio which measures the amount of profit that is available to shareholders' equity. This earnings performance ratio is widely used by the investors and shareholders in their investment decisions. Figure 5 indicates that during study period increased trend in ROE from 4.78 % to 8.79% indicates that is profitability of industry is improving. Unquestionably it can be attributed to the advantage of adapted Digital innovations in the operations management as per the preferences of the clients.

During the study period increasing in the profitability has made the Micro Financing Industry is attractive for the investors to infuse more capital.

5. CONCLUSION

Low growth rate in the reach of clients and very minimal average loan per borrower is clearly point out necessitate the scale up operations of the MFIs. Though regulatory restrictions limiting the freedom of MFIs, usage of Digital innovations bringing dramatic changes in their operations management and making this industry captivating to its stakeholders. Apart from the microcredit services needed by financially underserved other allied financial services such as Micro insurance, Micro pensions and transfer services, as well as remittances providing the huge opportunity for the sustainability and growth of MFIs.

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