CHAPTER 6

FINDINGS, RECOMMENDATIONS AND CONCLUDING REMARKS

6.1 FINDINGS OF THE STUDY

Findings from Morgan Stanley Credit Risk Assessment

The Morgan Stanley standards credit assessment shows that all five companies have to strategize better to at least meet the minimum standards. SKS and Bandhan are good in qualitative factors. Though the companies are good in some aspects of quantitative factors, it is found that all five have not met up the standards. As far as Spandana Sphoorty is concerned, it’s Gross Loan Portfolio and Operating Efficiency seems to be good. They ought to concentrate on other quantitative factors to improve the situation. Private NBFC-MFI’s EQUITAS, SKS and Bandhan are comparatively better than Public NBFC-MFI’s Spandana Sphoorty and SHARE. Both these MFIs’ has Portfolio at risk above 50 percent of their total portfolio. This is much alarming. SHARE has written off its loss to an extent of 11 percent which reflects an unusual situation. SKS, a prominent firm, a company which made the first IPO remained good upto 2010. Thereafter, its loan size was sliced to half, while Bandhan its competitor had tripled its portfolio during the same time period. The Gross Loan Portfolio is good for SHARE and Spandana Sphoorty. SKS and Spandana Sphoorty maintained loss reserves in four digit percentages. Operating income and profitability was negative for SKS, Spandana Sphoorty and SHARE which reflected adoption of their mistaken
strategy in expansion of portfolio. The operating efficiency of Bandhan, Spandana Sphoorty and EQUITAS seems to be good even during the crisis period. Invariably all institutions are good at their productivity. SKS and Bandhan are good at utilisation of their resources, whereby SKS uses contemporary sources of funds, but Bandhan uses traditional funds. The liquidity positions of private NBFC-MFIs were found to be better. The cumulative qualitative factor shows that Bandhan matches the MS Standard scores. Bandhan is good in its strategy, HR policy and new financial strategies, new source of fund raising etc. SKS is excellent in documentation and maintains transparency in declaration of all manuals which reflects the good governance as well it is extremely wedded with sophisticated and modern advanced technology. Both Bandhan & Spandana Sphoorty lags much behind in Information Technology. Transparency in operations is not adequately maintained by SHARE. Growth potential seems to be much brighter for Bandhan, EQUITAS and SKS. For SKS, disciplined strategy implementation and actions within the regulatory orbit will help to recapture the skipped out market. The cumulative Morgan Stanley score shows that EQUITAS performed better than all other MFIs. Moreover in another point of comparison between the Public and Private NBFC MFIs, it is found that the Private NBFC-MFIs’ SKS, Bandhan and Equitas performed better than Public NBFC-MFIs.

**Solvency position**

Considering the above, the solvency position is tested. The solvency position was negative for the most of MFIs all through the study period. Question rose as how the insolvent MFIs could generate good business. This made the researcher to relook into the model. Further Altman’s model 3 was implemented, which reflected similar results. Later Revised Version 4 of Altman Model for non-manufacturing Companies was executed
and it showed the real picture that SKS had better years with solvency position ie., 70 percentage of the study period. However in the later years, it is found to be insolvent. Bandhan was moderate as it was found to be solvent during 40 percentages of the study period. Spandana Sphoorty and SHARE are found to be Bankrupt for 70 percentage of the study period. EQUITAS had good turns throughout, had faced turbulence to an extent of 17% only, the least of all other companies.

**Multi Discriminating Analysis (MDA)**

Z Score model helped to classify MFIs into solvent and insolvent ones over a period of time. MDA facilitates to trace out the variables that discriminates solvency classification. The Liquidity and Loss Reserves are the best predictive discriminating variables between solvency and insolvent companies which the companies might have to seriously look into to avoid critical issues.

**Determinants of Return on Assets**

Multiple regression was executed to identify the significant factors leading to predict the Return on Assets. 96.5% of total variation in Return on Assets is explained by independent variables namely Portfolio at Risk, Capital Adequacy ratio, Deposit to Loan ratio, Write Off ratio, Debt-Equity ratio, Non-Interest Income, Cost per Borrower, Personnel Productivity ratio and Provisioning Operating Expenses ratio on a joint basis. Among the identified variables Write Off ratio, Debt-Equity ratio and Portfolio at Risk are the most statistically significant predictor variables in determining ROA.
**Survival analysis**

The survival analysis shows that the future of the MFIs. It is used to test the future growth of the MFIs. It describes a proportion of MFIs that may survive or die. It also reflects the same scenario as that of solvency position, that the Public NBFC-MFIs’ future is much dull. SHARE and Spandana Sphoorty are still closer to 1 which denotes that they are under the pressure of solvency risk. Whereas the private NBFC-MFIs SKS, Bandhan and EQUITAS the values are below 0.5 & 0.3 which means there are closer to zero i.e., Solvency Score. In spite of the issues faced by the MFIs’ they find the best means to improve in their future operations.

**Financial Sustainability Index**

This made the researcher to find out the financial sustainability index for the companies. As a part of that the variables had been identified using regression analysis, 4 variables were prominent and significant namely Capital Asset ratio, Yield, OELP and PaR >30 among the 7 variables. Four independent variables and dependent variable OSS were used to build the financial sustainability index. Standards and weight pertaining to each variable were used to find the index values. With base year as 2003-04, the cumulative score for 10 years is compared. It is found that SKS, Bandhan and EQUITAS were improving and Spandana and SHARE were too good in the initial years and not so well during the later years.

SHARE and Spandana Sphoorty are facing sustainability risk, whereas the SKS, Bandhan and Equitas are much stronger than the former, which insists the future of the latter three are much brighter than the earlier two Public NBFCs’. They are much self-reliant than the Public NBFC- MFIs.
Relationship between the performance indicators ie., Sustainability, Outreach, Operating Efficiency and Bad Debts:

Performance indicators used to test were Sustainability, Outreach, Operating Efficiency and Bad Debts. The sustainability is measured through Operating self-sufficiency and Return on Average Assets; Outreach through Gross Loan Portfolio; Operating Efficiency through Operating Expenses / Loan Portfolio & Productivity and bad debts through Portfolio at Risk.

- **Sustainability**

  The Operational Self Sufficiency and Return on Average Assets has significant relationship, thereby it is understood that triggering OSS will lead to better ROAA.

- **Operating efficiency and Bad Debts:**

  PaR has negative correlation with both operational efficiency and productivity, which means if operational efficiency and productivity increases, Portfolio at Risk will decrease which is a promising scenario.

- **Sustainability and Bad debts:**

  The OSS (Sustainability) well influenced by return on assets and the negative correlation with PaR highlights the truth; more control on PaR will ensure higher profitability.

- **Outreach, Operating Efficiency & Bad Debts:**

  Whereas the PaR increased, when the Gross Loan Portfolio increased and productivity declined.
**Paired Sample T test**

The OSS of Pre and Post AP Crisis ordinance bill reflect that there is a significant difference in performance between the two slots. OSS reflects better during the former years than the later years.

### 6.2 RECOMMENDATIONS

The quantitative factors score doesn’t look much promising. The scenario looks bleak for public NBFC MFIs than private NBFC MFIs. The PaR seems to be much alarming for public NBFC MFI’s, it is better to have high skilled field officers who could scrutinize the client history properly, so as to ensure the sanctioning of loans to good candidates and shall avoid ghost and fraudulent candidates.

Corporate governance of the MFI should be given more importance. The leadership had greater role to play in making the business models a successful one. Bandhan is one of the classic examples of its kind. The MFI got the in principle approval to run as a bank due to the accolades received by the CEO. The pioneer MFI, SKS a billion dollar company underwent huge crisis due to problems in its board.

The MFI industry experienced hyper growth. However the growth without compatible systems will not sustain for long. Extreme commercialization and spur expansion led to the coercive recovery practices which paved way to intense government interferences.

Sticking on to the reliable growth rate will help to have better monitoring and controlling system. The Andhra Pradesh based MFIs SKS, Spandana Sphoorty and SHARE is under loss. These types of firms should shadow the successful strategy adopted by Bandhan. Bandhan’s ADDO (Accounting, Documentation, Dissemination and Observance) method helped
to improve the collection efficiency and Operating Self Sufficiency. Proper and clear policy norms on operations, credit and collection should be put in place.

**Based on Solvency**

It seems there exist more inconsistency in the solvency of the Andhra Pradesh based MFIs. The growth model is much questionable. These MFIs projected themselves as firms serving the economically deprived citizen. Later course, they tasted the profit. Driven by the profit maximization objective, they changed the track, forgetting its vision and the concern for societal welfare. This change in attitude got transferred to the lowest cadre too which later led to government interference and strict regulation on its daily operations. Marrying the objective of the business and the business model is must before commencement of the operations. In addendum, high and due concentration on Liquidity and Loss Reserves will help the MFIs to remain solvent. The MFIs to have better solvency position shall have close watch over the above stated three variables which are best predictors for solvency of the companies.

**Based on Return on Average Assets (RoAA)**

Meeting up the fixed expenses alone for longer period may not be sufficient. Generating reasonable revenue is equally important to guarantee its long term solvency. Inorder to increase profit the MFIs shall provide much impetus on PaR, Debt Equity ratio & write off.

**Based on Survival Analysis**

Among the public NBFC MFI and Private NBFC MFI, private institutions perform better than public NBFC MFI. The AP based MFIs
survival shows that they are much risk prone in nature. The long term solvency is questionable. As stated earlier the model requires proper audit ensuring the compatibility of objective with the business model.

**Based on Financial Sustainability Index and financial performance:**

Long term sustainability depends on the ability of the firm to withstand on its own. Capital Asset ratio (CAR), Yield, OELP & PaR > 30 days are significant variables which reflects the sustainability of the MFIs. On a comparative basis private NBFC’s are performing better than the public NBFC MFI. They could withstand on their own funds than with the donors support which is appreciable. MFI’s reliance on donor support can be reduced by the public NBFC MFIs so as to ensure durable and healthy sustainability.

To increase the financial performance the MFI’s should pay attention on high Operating Self Sufficiency and low PaR. This will pave way to high Return on Average Assets.

**Based on Ordinance bill**

Preventive measure is better than Breakdown actions. Sudden passing of ordinance bill affects the industry in a huge way. No proper regulation existed earlier. Enactment of New Act and Ordinance Bill was a shock to the industry and made the system much handicap. It would be better if the systematic regulatory framework is set before allowing such new intermediation to penetrate and grow. However it is emphasized to have better regulatory framework which is the need of the hour.

The sudden enactment of ordinance bill in Andhra Pradesh, led to standstill of many NBFC MFIs. As part of proactive measure, the regulatory authorities should ensure that before the grant of license for new type of
intermediaries is done, prompt and proper legal and regulatory framework is drafted to guide their operations. This will facilitate the intermediaries to have clear and successful business model as well restricts them shifting to different models.

As a whole, more concentration should be given in predetermining the objectives and coupling it with the business model is much essential to ensure solvent and sustainable NBFC MFIs.

6.3 IMPLICATIONS

- Microfinance which created huge hype is losing its craze now. The government should come with stringent regulations before permitting any new type of financial service.

- Government should decide and restrict the forms of organizations that shall commence MF operations to avoid exploitation of common deprived public.

- The government can arrange for awareness programs for the MF clients to enhance the growth of MF.

- Analysts and decision makers generally give importance to the quantitative variables. However Qualitative factors pave major role in the continual growth and success of the MFIs in the current context. The study also supports this. Hence due importance should be given for qualitative factors too.

- Deploying technology similar to core banking solutions will be useful for the MFI to overcome credit risk difficulties.
• Providing the credit score information to the MFI’s, will facilitate the management in decision making and future planning. It will also help them to design activities to serve the deprived community without hurdles.

• ADDO system is found to be much effective. Making mandatory of such system especially for Public NBFC MFI too will overcome credit crisis and put things in place.

6.4 SUMMARY AND CONCLUDING REMARKS

The results show that the performance of the MFIs’ are not very convincing over the years. SKS, Bandhan and EQUITAS had been comparatively better than Spandana Sphoorty and SHARE. Multi discriminant Analysis also provides the same result. But in comparison with Morgan Stanley Standards, the credit score shows that all five companies underperformed in comparison with the standards. The Financial Sustainability Index shows that the SKS, Bandhan and EQUITAS proves to be improving than the base year, whereas Spandana Sphoorty and SHARE on the reversal side.

The Operating Self Sufficiency has been the crux of performance, which is found to be highly significant in improving the returns. It seems that there exists a difference in Operating Self Sufficiency (OSS) before and after the AP crisis ordinance bill. Hence, the researcher suggests them to take cautioned strategies and measured steps, stringent cost controlling techniques to improvise the situation.
6.5 SCOPE FOR FUTURE RESEARCH

The researcher has taken only NBFC- MFIs’. Further research could be done with other forms of MFIs like NGOs, Trust, Section 25 companies too. The Credit risk modeling could be performed as that is the pressing issue for MFIs.