ABSTRACT

Microfinance is one of the sustainable business models with a double bottom line of financial and social relevance in the turf of development. Microfinance was recognized as a development tool that enhanced income and the standard of living of the marginalized through a sustainable business model. Initially in India, many microfinance institutions were introduced to operate as social service organizations, but later they were transformed to non-banking finance companies to attract capital and business growth. Commercialization of microfinance institutions resulted in forcible recovery practices, and the inability to pay back the high interest rates resulted in a distress in the microfinance sector, which resulted in the intervention of a regulator (the Reserve Bank of India) that led to the issuing of NBFC-MFIs directions to protect customers and keep the social spirit of microfinance business.

The concept of social performance, financial performance in microfinance institutions, and the trend of commercialization resulted in understanding the effect of social performance on the sustainability of microfinance institutions. In this research work, the effect of social performance on the sustainability of microfinance institutions was analyzed by keeping in mind the following three objectives: a) to measure the social performance management of microfinance institutions, b) to assess the sustainability of microfinance institutions, and c) to establish whether there is a relationship between social performance and sustainability of microfinance institutions.

The independent variable of this study is the social performance of microfinance institutions i.e., targeting the poor and the excluded, adaptation of services, benefits to clients, and social responsibility. Dependent variables
of the study are financial performance of NBFC-MFIs-Portfolio growth, net profits, and financial ratios. Study population was non-banking finance company microfinance institutions that come under the jurisdiction of Bangalore and Chennai (Karnataka and Tamil Nadu) regional offices of Reserve Bank of India.

The effect of social performance on the sustainability of microfinance institutions was quantified using CERISE (Committee of Exchanges of Reflection and Information on Systems of Savings – Credit) and Social Performance Indicator (SPI) tool. Financial performance of the microfinance institutions were analyzed from 6 years audited financials of the microfinance institutions (Financial years 2009-2010 to 2014-2015), and various ratios were calculated from the audited financials and gathered information like portfolio at risk, written-off portfolio, and managed portfolio. The effect of social performance on the financial sustainability of microfinance institutions was analyzed using statistical tools such as regression analysis, correlation coefficients, and Student’s t-test. It is hypothesized that social performance management influences the sustainability of microfinance institutions.

RBI-NBFC-MFIs directions resulted in reductions in the portfolio yield, portfolio risk, personal expenses, administration and other expenses. Portfolio yield was 31.12% in the financial year 2010-2011, which reduced to 22.45% in the financial year 2013-2014. Portfolio risk was 2.11% in the financial year 2010-2011, which reduced to 0.24% in the financial year 2014-2015. Personal expense was 10.46% in the financial year 2010-2011, which reduced to 5.46% in the financial year 2014-2015. Administration and other expense was 2.95 in the year 2014-15. Even though there was reduction in the portfolio yield, after implementing RBI-NBFC-MFI directions all the NBFC-MFIs of the study were sustainable.
The study observed that targeting the poor and the excluded had positive and significant correlation with Return on Equity. Social performance criteria like geographic targeting, quality of services, and economic benefits had positive and significant correlation on the financial parameters like Return on Equity, operation self-sufficiency, and Return on Assets.

In the regression result of portfolio risk there is statistical evidence to say that two factors, namely, range of traditional services and clients’ participation are the influencing or determinant factors for portfolio risk ratio for the microfinance institutions. In essence, with respect to clients’ participation, a unit (1%) increase in clients’ participation would decrease the portfolio risk ratio on an average by 0.015%. It strengthens the logic that the success of microfinance repayments depends on the group strength and participation. Similarly, 1% increase in range of traditional services would increase the portfolio risk ratio on an average by 0.019%. It strengthens the logic that the major portfolio of MFIs lies in standard/generic loans than in customized loans, which results in a higher portfolio quality. In the regression result of return on equity, there is statistical evidence to say that the factor, namely, geographical targeting, is the influencing or determinant factor for Return on Equity for the microfinance institutions. In short, for 1% increase in geographic targeting, one would expect an average of 0.229% increase in Return on Equity. Along with the social performance objective of serving the areas where poor live, there are possibilities to increase Return on Equity.

The scores of social performance of NBFC-MFIs depict that NBFC-MFIs adopted social performance initiatives in the business operations and that there are areas for improvement. RBI NBFC-MFIs directions on the Interest Cap resulted in reductions in the portfolio yield, personal expenses, administration, and other expenses of the NBFC-MFIs, which helped the
borrowers of MFIs to access low-cost microcredit. The study concluded that the social performance of microfinance institutions has relationship with financial performance.