How Efficiency and Performance influence Outreach of SKS Microfinance India?

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Abstract— Developing countries are generally characterized by dualistic economy; a disparity between rich and poor. To overcome the problem micro financing institutions are promoted by Government to support poor people. The idea is to make available loans at cheaper rates to needy and financially weak population. Microfinance is a huge worldwide industry; moving from a non-profit to a "commercial" model has allowed the industry to grow and serve more people. The industry manages to attract capital in the field by attracting private investors resulting which the institutions can achieve scale and have greater impact. But sometimes the objective of achieving outreach is hampered due to financial unsustainability, inefficiency and non-performance. Financial unsustainably is one of the most serious problems of MFI's in Asian Region which causes high range of operational inefficiencies. Most microfinance institutions are still small and vulnerable to constraint on their resources. It is essential for a micro financing company to be financially self-sufficient by reaching economies of scale which will help these firms to improve outreach performance. The variables i.e. efficiency, performance and outreach are the parameters to judge the health of micro financing industry. This paper has studied the functioning and performance of SKS Microfinance-one of the largest micro financing provider of India in respect of efficiency, performance and outreach level from 2003 to 2020. This paper tries to study the working pattern of SKS microfinance and also the impact of efficiency and performance on the outreach of SKS Microfinance. SKS Microfinance is considered in the study due to its huge scale of operation and also it can be considered as a case study by other start up and developing micro financing firms.

Index Terms— *Financial Sustainability, Outreach, Efficiency, Microfinance, Performance*.

INTRODUCTION

Microfinance is defined as provision of thrift, credit and financial services and products of very small amount to the poor in rural, semi-urban or urban areas for enabling them to raise their income levels and improving their living standards. (Arunachalam, 2011). The objective of providing credit by Microfinance institutions (MFIs) is to help poor who have no access to commercial banks and which in turn reduce poverty. Lending money to below poverty line is a costly affair increasing the operational cost of MFI's. MFI's are required either to be financially sustainable or to depend on Western donors and NGOs for financial support. MFI's charge low interest rates to achieve outreach and increase profitability. There is a substantial shift from subsidizing MFI to financial sustainability. Financial sustainability is requited to face competition, commercialization, technological changes and financial liberalization and government policies. These developments have induced microfinance institutions to bring changes in services and activities. It is required to understand the extent of impact on outreach due to financial sustainability goals. As lending money to the poor – especially the very poor and/or the rural poor – can be very costly, the outreach and sustainability is difficult to attain. The compatibility versus the trade-off between sustainability and outreach has always remained a debatable issue.

SKS Microfinance which is one of the leading micro financing institution in India was started in 1998 as nonprofit SKS Society. It was funded by individual and institutional donations and focused on markets within its home state of Andhra Pradesh. In 2005 SKS decided to pursue an aggressive growth plan and transformed into non-banking financial company named SKS Microfinance and regulated by the Reserve bank of India. Since transformation, SKS has been successful in creating a for-profit model of microfinance using commercial funds that is scalable. Delivering services at the doorsteps of its members and following clear-cut processes, SKS has been able to ensure a repayment rate of over 99 % on its loans. SKS Microfinance is India's largest and one of the world's fastest-growing microfinance organizations. It claims that its mission is to empower the poor by providing them collateral-free loans for income generation. In a first of its kind, a group of four venture capitalists led by Sequoia Capital India has become the promoter of SKS Microfinance Ltd, as the country's largest microfinance institution (MFI) prepares to make an initial public offering (IPO). SKS uses the group lending model where poor women guarantee each other's loans. Borrowers undergo financial literacy training and must pass a test before they are allowed to take out loans. Weekly meetings with borrowers follow a highly disciplined approach. Re-payment rates on our collateral-free loans are more than 99% because of this systematic process. SKS also offers micro-insurance to the poor as well as financing for other goods and services that can help them combat poverty.

As the model of SKS Microfinance is quite successful in India, the present study aims to analyze the data of the company in the areas of outreach, efficiency and financial sustainability. For this purpose data ranging from 2003 to 2020 has been collected and analysis and interpretation are drawn on relationship and impact of financial sustainability and efficiency on outreach of SKS microfinance. The remainder of the paper is organized as follows. Section 2 discusses the literature on micro financing industry, funding sources and relationship between outreach, financial sustainability and efficiency. In section 3 we set out the research methodology and explain the variables of efficiency, outreach and financial sustainability in detail. Section 4 continues with a description of the data set, after which the estimation results are presented in section 5. In section 6 we summarize the main findings and provide conclusions we derive from the analysis.

I. LITERATURE REVIEW

Micro finance is an important tool for improving the standard of living of poor. World Bank statistics reveals that there is almost 3 billion of world population living under $25 per day and among them, around 1 billion living under $1 per day. MFIs received a substantial share of investments from government and development partners. As per the report of "Consultative Group to Assist the Poor", 2008, there was a potential annual increase of 55 percent in outstanding portfolios of development finance institutions to microfinance institutions. Government and international organizations have been cooperating to fight poverty in different parts of the world. In recent years, microfinance has been recognized as an effective tool to alleviate poverty (Mahjabeen,2008; Daley-Harris, 2002; Lalitha, 2008; Evansluong, 2010).

Microfinance institutions (MFIs) focus on providing credit to the poor who have no access to commercial banks. This leads to increase in cost and financial unsustainability. However in many cases MFIs succeed in lending to domestic small companies and poor agents by maintaining sustainability. Western donors and NGOs provide financial support by offering them loans against below-market interest rates (Hermes et.al. 2011). Recently, there seems to be a shift from subsidizing MFIs institutions to a focus on financial sustainability and efficiency of these institutions due to increased competition among MFIs, the commercialization of microfinance, technological changes and financial liberalization and regulation policies of the government (Rhyne and Otero, 2006).

In India microfinance services has been provided through SHG bank linkage model and the major service providers are banks which includes commercial banks, Regional Rural banks, cooperatives banks and local area banks (Bhattacharjee & Staschen, 2004). As per the report of World Bank, 2000 (cited by Agarwal & Sinha, 2010) funds have been granted by various agencies and banks at subsidized credit which leads to creation of Non-Performing Assets. It is evident that MFI are facing challenges to maintain financial sustainability in lines of social welfare. The concept of social performance has seemed to overshadow the

state of financial health of MFIs. Ability to earn sufficient margins to cover operational cost is the crucial factors of financial sustainability (Agarwal and Sen, 2009).

In India, a review of the studies done on microfinance sector has revealed that fewer studies are focused on financial health of MFIs. Meyer (2002) indicated, "Measuring Financial sustainability requires that MFIs maintain good financial accounts and follow recognized accounting practices that provide full transparency for income, expenses, loan recovery and potential losses". As per Varman (2008) the efficient functioning of these MFIs is important for persistent financial access of the poor segment of the society. Mordruch (1999) as cited by Crabb (2008) studies 22 MFIs in India (5 star rated-MIX) and their financial performance is compared on 22 ratios. The research emphasized the need for empirical work on MFI's sustainability. As per Bogan et.al. (2007), 48% of South Asian micro financing institutions are financially sustainable, 68% are operationally sustainable and 32% are unsustainable but there portfolio at risk is 6%.

Outreach and financial sustainability are complimentary as number of clients increase economies of scale and hence reduce cost (Christen et al 1995; Rhyne and Otero 1994). On the other hand Hulme and Mosely (1996) argued that there is an inverse relationship between outreach and financial sustainability. Kereta (2007) argued that it is difficult to measure financial sustainability of MFIs as almost all MFIs are subsidized and supported by grants and donations. Zeller & Meyer (2002) stated that the financial unsustainability in MFI arises due to low repayment rate or non-materialization of funds promised by donors or government.

MFIs sustainability can be achieved only through huge demand for credit, saving and insurance services but the user should be able to pay full cost of services availed. The key to financial sustainability is controlling cost and bad debt, increasing volumes and offerings varied financial services options. It can be done by raising equity capital. The studies reflect negative impact of loans at subsidized interest rates on repayment culture of borrower which in turn impact on financial sustainability (Mahajan and Nagasri,1999). Financial viability of MFIs also depends on generating own funds apart from grants and soft loans. This can be done by taking deposits and raising capital from market. As well as private equity and venture capital also plays an important role in sustainable development (Bogan et.al. (2007). Masood & Ahmad (2010) depicted that firm performance can be judged using the concept of economic efficiency. Economic efficiency has two components (i) technical efficiency (ii) allocative efficiency. Technical efficiency refers to the ability and willingness of any firm to maximize output with a given set of inputs while allocative efficiency refers to the ability and willingness of a firm to use these inputs optimally given the input prices.

MFI's having more than 10,000 active borrowers are found to be sustainable. South Asian MFI's are inefficient and can be improved through managerial skills, technology and training (Gow, 2006). Organizations must use the most advanced methods of internal income-generation so as to achieve financial sustainability; this will enables them to make autonomous decisions that truly reflect local, rather than international priorities. The reasons of financial unsustainability are inadequate financial infrastructure, unfavorable policy environment, lack of investment in agricultural, rural development & infrastructure, as well as lack of social intermediation (ADB report, 2000). It has been revealed that reveals that there are various social performance assessment outreach indicators and institutionalized rating process but assessment of financial performance has yet to gain grounds (World Bank Report, 2000)

Qayyum and Ahmed (2006) analyzed the performance of MFIs in South Asia through Outreach, Institutional Characteristics, Financial Structure, Overall financial performance, efficiency Indicator, productivity indicator, and risk and liquidity indicator. Studies reveal that interest rates play a major role in profitability of SHG. A study conducted by M-CRIL in 5 RRBs estimates that the cost covering ROI for linkage banking for RRBs lies between 20% to 22% (Sinha et.al, 2003). Banks are making a profit with their SHG portfolio, notwithstanding the lower ROI, but mainly due to non-occurrence of NPA (Seibel, 2002). MFIs explore new funding opportunities by securitizing microfinance loan portfolios. At the same time private institutional investors such as pension providers, insurance companies and trust discover microfinance as an attractive supplement for their portfolio. (Dieckmann ,2007)

II. OBJECTIVES OF THE STUDY

i. To examine the efficiency, performance and outreach indicators of SKS Microfinance.
ii. To study the impact of efficiency and performance indicators on outreach indicators of SKS Microfinance.

III. RESEARCH METHODOLOGY

The study is about the impact of performance and efficiency on outreach of SKS microfinance limited. Data of performance, efficiency and outreach variables are collected through MFI's ratios of past 16 years i.e. 2003 to 2020. The data is secondary in nature and derived from the website of SKS microfinance. Correlation and regression has been applied to study the impact of performance and efficiency variables on outreach of SKS Microfinance.

Variables to study Performance, Efficiency and Outreach of MFI's:
- Average loan balance per borrower
- Operating expenses/loan portfolio
- Performance Variable: Return on assets
- Average outstanding balance / GNI per capita
- Average salary/ GNI per capita
- Performance Variable: Return on equity

IV. RESULTS AND DISCUSSION

To study the efficiency, performance and outreach of SKS Microfinance limited two ratios under each category are considered to analyze the results. The first set of ratio for efficiency, performance and outreach and its analysis are as under.

First set of ratio:

1. Outreach Variable: Average loan balance per borrower
2. Efficiency Variable: Operating expenses/loan portfolio
3. Performance Variable: Return on assets

Second set of ratio:

1. Outreach Variable: Average outstanding balance / GNI per capita
2. Efficiency Variable: Average salary/ GNI per capita
3. Performance Variable: Return on equity

TABEL 1

Descriptive statistics of outreach, performance and efficiency ratios (1st set of ratio)

	Mean	Standard Deviation	N
ALB	14.3567	4.46015	17
OELP	13.1489	2.60795	17
ROA	-3.3322	16.05438	17

The above table represents the mean values and standard deviation values of outreach, efficiency and performance ratios i.e. Average loan balance per borrower, operating expenses/loan portfolio and return on assets respectively.

The mean value of Average loan balance per borrower is 14.3567 and the standard deviation is 4.46015, while the Operating expenses to loan portfolio have a mean value of 13.1489 and standard deviation is 2.60795. The performance variable i.e. Return of assets are highly fluctuating with mean value -3.3322 and standard deviation is 16.05438.

TABEL 2: Correlation table of outreach, efficiency and performance ratios (1st set of ratio)

	ALB	OELP	ROA
Pearson Correlation ALB	1.000	.137	.731
	.137	1.000	-.389
OELP	.731	-.389	1.000
ROA			
Sig. (1-tailed) ALB	.	.363	.013
	.363	.	.151
OELP	.013	.151	.
ROA			
N	17	17	17

The above table represents the correlation between outreach and efficiency variables and outreach and performance variables. To study the relationship, Pearson correlation technique has been used which indicates that both the variables of performance and efficiency are positively correlated to outreach variable. The correlation of efficiency and outreach is .137 which indicates a positive but a weak relationship. However the performance and outreach are showing strong positive association by having correlation value of .731.

TABEL 3: Model Summary of outreach, efficiency and performance ratio (1st set of ratio)

R	R Squ.	Adjt. R Squ.	Std. Err.	Change Statistics				
				R Squ.	F	Df 1	Df 2	Sig.
.86 2	.74 4	.658	2.6 0	.74	8.7	2	6	.01 7

a. Predictors: (Constant), ROA,OELP

TABEL 4: Anova Table of outreach, efficiency and performance ratio (1st set of ratio)

Model	Sum of Squares	Df	Mean Square	F	Sig n
Regression Residual Total	118.358 40.785 159.144	2 6 8	59.179 6.798	8.706	0.1 7

a. Predictors: (Constant), ROA,OELP
b. Dependent: ALB

The R value which is .862 indicates that there is a strong impact of performance and efficiency on outreach variables. However R square (.744) and Adjusted R (.658) square indicates that there is strong impact of performance and efficiency variables on outreach. The F value is 8.706 which indicate that the results are significant at .017 which is less than .05.

TABEL 5
Descriptive statistics of outreach, performance and efficiency ratios (2nd set of ratio)

	Mean	Standard Deviation	N
AOB	12.7200	3.5015	17
RS	2.6911	.64447	17
ROE	-4.1700	42.186	17

The above table represents the mean values and standard deviation values of outreach, efficiency and performance ratios i.e. Average outstanding balance / GNI per capita, Average salary/ GNI per capita and return on equity respectively.

The mean value of Average outstanding balance to GNI per capital is 12.7200 and the standard deviation is 3.50151, while the average salary / GNI per capital have a mean value of 2.6911 and standard deviation is .64447. The performance variable i.e. Return of equity are highly fluctuating with mean value -4.1700 and standard deviation is 42.18626.

TABEL 6: Correlation table of outreach, efficiency and performance ratios (2nd set of ratio)

	AOB	RS	ROE
Pearson Correlation AOB	1.000 .769 .721	.769 1.000 .247	.721 .247 1.000
RS			
ROE			
Sig. (1-tailed) AOB	. .008 .014	.008 . .261	.014 .261 .
RS			
ROE			
N	17	17	17

The above table represents the correlation between outreach and efficiency variables and outreach and performance variables. To study the relationship, Pearson correlation technique has been used which indicates that both the variables of performance and efficiency are positively correlated to outreach variable. The correlation of efficiency and outreach is .769 which indicates

a strong positive relationship. However the performance and outreach are also showing strong positive association by having correlation value of .721.

TABEL 7: Model Summary of outreach, efficiency and performance ratio (2nd set of ratio)

R	R Squ.	Adjt. R Squ.	Std. Err.	Change Statistics				
				R Squ.	F	Df 1	Df 2	Sig.
.94 4	.89 2	.856	1.3 3	.89 2	24. 7	2	6	.00 1

a. Predictors: (Constant), ROE,RS

TABEL 8: Anova Table of outreach, efficiency and performance ratio (2nd set of ratio)

Model	Sum of Squares	Df	Mean Square	F	Sig n
Regression Residual Total	87.470 10.615 98.085	2 6 8	59.179 6.798	8.706	0.1 7

a. Predictors: (Constant), ROE, AS
b.Dependent: AOB

The R value which is .944 indicates that there is a strong impact of performance and efficiency on outreach variables. However if R square (.892) and Adjusted R square (.856) is observed it reflects a strong impact of performance and efficiency variables on outreach. The F value is 24.7 which indicate that the results are significant at .001 which is less than .05.

CONCLUSION

Micro financing is a movement that envisions "a world in which many poor and near-poor households have permanent access to an appropriate range of high quality financial services, including not just credit but also savings, insurance and fund transfers". The microfinance sector in India has developed a successful and sustainable business model which has been able to overcome challenges traditionally faced by the financial services sector in servicing the low income population by catering to its specific needs, capacities and leveraging pre-existing community support networks.

The concept has grown over the past two decades. Over the years, major commercial banks and multinational corporations have decided to sponsor it. However, this type of financing has a darker side too. Most of studies are qualitative which tell that more than 90 per cent of the people who receive micro credit are poor and most of them succeed in businesses started with these loans. But the suicides committed by Indian farmers after being harassed by the microfinance institutions (MFIs) for their inability to repay the debt have raised serious moral and ethical issues against the institutions. The aggressive debt-collection tactics of these MFIs have left us wondering if the government has been playing ignorant to the modus operandi of MFIs. Moreover, the interest rates charged by micro financing institutions are usurious.

Today, it's a need for MFIs to pay attention to their performance and efficiency. For them the critical concern should be to achieve financial sustainability and in turn achieving outreach level. But unfortunately, we've seen a major mission drift in micro finance, from being a social agency first, to being primarily a lending agency that wants to maximize its profit. Thus, there is a great need to set out rules limiting interest rates and stipulating legal consequences for the MFIs who badger/ harass borrowers for payments.

The study will help micro financing institutions to understand the matrix of financial sustainability, outreach and efficiency and also they can follow the successful model of SKS microfinance. The MFI's can develop their portfolios accordingly and achieving sustainability and outreach. Government and other private lenders and NGO's of micro financing institutions can also frame the policies of money lending and also understand the importance of financial sustainability of micro financing institutions.

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