FOCUS ON:

INDIAN MICROFINANCE

Looking Beyond the AP Act and its Devastating Impact on the Poor

In December 2010 the Government of Andhra Pradesh passed a law (the "AP Act") which effectively shut down private sector microfinance in the State. The AP Government stated that its goal was to protect the poor. Now, 15 months later, the impact of the AP Act is clear: rather than protecting the poor in AP, it has had the opposite effect and indeed harmed the poor by starving them of access to credit and basic financial services.

42% of the Indian population exists on less than $1.25 (₹62) per day

1 in 3 people in India have no access to formal financial services

$5.3BN the size of the private microfinance sector in March 2011 was ₹26,255 Cr.

A BRIEF HISTORY OF THE INDIAN MICROFINANCE INDUSTRY

1974
The Self Employed Women's Association formed an urban cooperative bank, called the Shri Mahila SEWA Sahakari Bank, to provide banking services to poor women employed in Gujarat.
1974

1980s
The microfinance sector went on to evolve around the concept of Self Help Groups (SHGs), informal bodies that would provide their clients with much-needed savings and credit services.
1980s

2005
The Krishna District crisis followed unfounded allegations against some MFIs and the shutting down of branches; repayments dried up and the sector took two years to recover.
2005

2008 to 2010
Private sector MFIs grow to meet the needs of the poor:
Gross loan portfolios +80% p.a.
Client base +64% p.a.
2008

July 2010
SKS IPO raises ₹1,600 Cr. (USD 320MM)
October 2010
Andhra Pradesh MicroFinance Institutions (regulation of money lending) Ordinance, 2010 is issued
2010

December 2010
Microfinance legislation (the AP Act) passed by the Government of Andhra Pradesh

May 2011
Legatum issued a white paper – *A Crisis at the Bottom of the Pyramid* – which challenged the premise of the AP Act
2011

March 2012
The Microfinance Bill to be debated by Indian Parliament offers some new hope for the Indian microfinance industry
2012

FACTS&FIGURES

The top five private sector MFIs reach more than

20MM

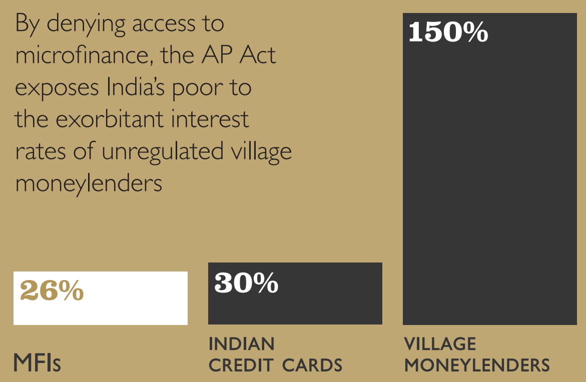
clients in nearly every state of India.

30%

of all MFI loans across India are in the state of Andhra Pradesh (AP)

ESTIMATED INTEREST RATES

By denying access to microfinance, the AP Act exposes India's poor to the exorbitant interest rates of unregulated village moneylenders



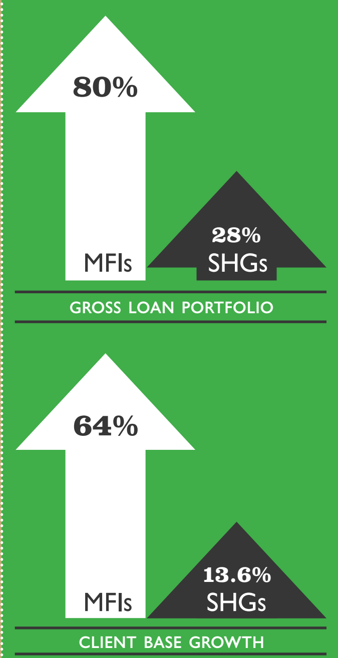
PRIVATE MFIS CRITICAL TO FINANCIAL INCLUSION

45%

The microfinance sector is a critical part of India's economy. When included in the mainstream financial system, the sector has a 45% share of all microcredit accounts nationally. Adding in SHGs, the total number of microcredit accounts is around

134MM

2008 to 2010
Comparative Growth p.a. Private MFIs vs. SHGs



By March 31 2011, the loan portfolio and clients grew at a reduced rate of 19% over the previous year (driven by good growth until October 2010 and then stagnant after the crisis) to ₹26,255 cr (USD 5.3Bn) in portfolio and 31.7 million clients

THE AP ACT CRISIS

2010
₹7,494CR
In the year before the AP Act was passed, MFIs disbursed USD 1.5BN to more than ten million households in Andhra Pradesh

2011
ZERO
Since the AP Act, the disbursements have dropped to almost zero.

9.2MM
women now form the largest bloc of blacklisted borrowers in the world thanks to the AP Act

90%
of loan portfolios in AP will likely be **written off** amounting to ₹4,919 Cr. (USD 984MM) to ₹6,395 Cr. (USD 1.3BN), or between 19 to 24% of the industry's entire portfolio in FY 2011.

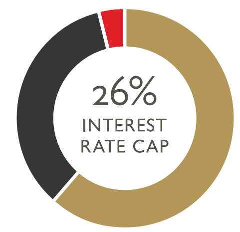
Repayment rates in AP plummeted from almost 100% to 5% following the AP Act.

A mere ₹472 Cr. (USD 94MM) in equity capital has been invested in the Indian microfinance sector since the AP Act was passed, down from ₹2,600 Cr. (USD 520MM) in Mar-Oct 2010 alone.

EQUITY CAPITAL INVESTMENT DOWN 82%

BUT...

The Bill's proposed **26% interest rate cap** takes no account of the fluctuation in bank lending rates which have recently risen from 12% to 14-16%



14-16% COST OF FUNDS
7-9% OPERATING EXPENSES
1-3% PROFIT

Is this a sustainable business model?

The requirement for capital adequacy of 15% will severely stress MFIs with large exposure in AP.

Limiting loans to households with less than ₹60k income encourages misrepresentation since loan recipients may find themselves suddenly excluded