

A new model of financial services completes a year

Conceptualised by IFMR Trust, a new model of offering a range of financial services in remote, rural locations of India has completed one year of operation. The model is being rolled out by IFMR Holdings, an IFMR Trust venture, through region-specific, not-for-profit entities called Kshetriya Gramin Financial Services (KGFS) companies, registered under Section 25 of the Indian Companies Act.

The first KGFS company, Pudhuaru KGFS (PKGFS), started operations in Thanjavur district of Tamil Nadu in June 2008. Two other KGFS entities have been launched more recently: Sahastradhara KGFS of Uttarakhand with proposed operations in the districts of Tehri Garhwal, Pauhri, Haridwar and Dehra Dun, and Dhanei KGFS in Orissa's Ganjam district.

These KGFS companies offer a range of financial services and products through branches located in villages. PKGFS branches serve villages within a radius of 3 km.

Beyond micro finance

KGFS's mandate, as enunciated in IFMR Holdings' mission, is to "maximise the financial wellbeing of every individual and every enterprise in remote rural India by providing complete financial services".

The KGFS model thus goes far beyond the scope of micro finance institutions (MFIs), which have made inroads in remote locations in many regions of India.

"The growth of micro finance in India has been unambiguously important for millions of poor households," says IFMR Trust President Bindu Ananth. "MFIs enable low-income households to take a loan when there is not enough money to meet some critical needs. This allows households to manage cash mismatches in ways that are superior to taking usurious loans from moneylenders, selling assets like gold or buffaloes, or pulling kids out of school."

However, she adds, much more can and should be done. "Just like their middle-income counterparts, low-income households need to have the



New customer registration at a PKGFS branch: technology plays a key role in operations

ability to move their resources across time and space, in such a manner that their needs for finance are met smoothly over a lifetime."

To be able to do this, low-income households require "the full suite of financial services, including savings, credit, risk mitigation and insurance and remittances".

KGFS's finance suite

KGFS companies are being developed to provide this full suite of services in remote, rural locations.

After much deliberation, 14 products and services have been identified, to be offered through KGFS branches to all households living within their area of operation.

These fall under four categories:

- **Loan products:** Joint liability group (JLG) loans, loans against mortgaged jewellery (called 'jewel loans' in the Indian banking industry), retailer loans, and loans for rural industries like brick kilns, coir units, and rice and *dal* mills.
- **Insurance products:** Personal accident insurance, cattle insurance, weather insurance, and life insurance.
- **Investment products:** Savings instruments that provide safety, liquidity and reasonable returns, fixed deposits of public sector finance companies, and a gold accumulation plan that helps customers accumulate their savings in the form of jewellery, and pension plan annuities.

- **Services:** Sale of certified gold coins, and remittance services to enable efficient delivery of money sent by migrant members of village households.

Most of these offerings are being made on behalf of mainstream financial institutions regulated by different bodies and laws. Of these 14 products and services, six are already being offered in rural Thanjavur through 15 PKGFS branches.

While JLG, jewel and retailer loans are being provided directly by PKGFS, the company is a re-seller for certified gold sold by a reputed public limited company. PKGFS is also an intermediary for a personal accident insurance product offered by a reputed private sector insurance company. Leveraging its approximately 10,000-member-strong customer base, PKGFS has negotiated very attractive premium rates for accident insurance cover of INR 25,000 and above.

Customer profile

Although Thanjavur is one of Tamil Nadu's 'prosperous' districts, with good rice, wheat, pulses and sugarcane production, the distribution of wealth in rural areas is unequal because of skewed land ownership.

Around 65% of PKGFS customers do not own agricultural land and work as farm and daily wage labourers. While male labourers get around INR 150 a day, women get half the amount. Cultivation is done during all three seasons of the year in Thanjavur, but

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labour work is available only for around 200 days.

Many low-income households earn supplemental income by rearing milch cattle, goats or poultry, growing vegetables and running small businesses like tea stalls. PKGFS's customer data profiling — which contains a few inconsistencies — indicates that around 47% of customer households have gross annual incomes of less than INR 60,000 from all sources.

Till PKGFS came into the picture, households had no place to park their savings safely and earn reasonable interest. There is a bank branch near only one PKGFS branch; around 97% of PKGFS customer households do not have bank accounts. As KGFS companies are not banks, they are not allowed to collect savings. The limitation was overcome by innovative product design.

Innovative product design

IFMR Holdings has developed a system for offering money market mutual fund (MMMF) products with benefits comparable to bank savings accounts, by acting as an intermediary for a reputed asset management company (AMC). Read a detailed story on the MMMF offering here: <http://ifmrtrust.co.in/fieldreports/mmmf.php>

Technology plays a key role in this process. Explains Anil Kumar SG, CEO, IFMR Holdings: "Distribution of mutual fund products is a highly data-intensive process requiring a lot of computation, with inputs from registrar and transfer agents (RTAs) of mutual funds."

IFMR Holdings has invested in a proprietary Customer Management System (CMS) for KGFS companies. Apart from capturing the demographic and socio-economic profile of customers, the CMS generates pre-populated application forms and transaction feeds for different products. It also acts as an interface, providing the RTA-relevant database for MMMF products.

Loan products

While the MMMF and personal accident insurance products have been launched recently, managing loan products currently constitute the bulk of PKGFS's operations.

Unlike banks, which offer loans to self-help groups that pool savings, PKGFS advances loans to JLGs formed under its initiative and direction. Members of

JLGs do not need to pool savings to be eligible for individual loans. Once a group of five is formed, members are immediately eligible for loans after a process of training and assessment. Every group is jointly liable for loans taken by each member.

As a Section 25 company, PKGFS can advance loans upto a maximum of INR 50,000 per person. In practice, in the first year of operations, loans of upto a maximum of INR 15,000 per member of an enrolled JLG have been offered. Loans are given without demanding any security. A 'guarantee' of repayment made by the group is the hallmark of the JLG model followed by most MFIs.

The repayment record has been astounding. In its first year of operations, PKGFS has not suffered a single JLG loan repayment default! Apart from the peer pressure factor, which is at the foundation of the JLG concept made famous by Bangladesh's Grameen Bank, zero default could also be attributed to the considerable amount of work done before a loan is advanced.

At the first stage, when a KGFS company enrolls customers — free of cost — it studies the relevant customer data thoroughly. Explains V Chandrachudan, Vice President, IFMR Holdings, who was in charge of the PKGFS roll-out: "We go beyond the Know Your Customer (KYC) requirements to be followed by banks. Our Wealth Managers (WMs) who manage the branches do not rely only on documents as proof. They actually visit each customer's house and make enquiries with neighbours and relatives to verify customer claims."

KGFS's CMS also captures a lot more data than do standard forms for opening bank accounts. Apart from demographic and family information, estimated income from various sources through the year is also recorded. So are details of property, livestock, household and other assets. Living standards are assessed by information on type of house, cooking medium used, and type of sanitation facility used by the household.

WMs also record information on loans taken previously by customers, and any jewellery they own or have pawned. The customer's education levels are recorded, as also caste category.

Once enrolled, customers decide to form groups. WMs train them on the norms and processes they have to follow. A group's level of knowledge is then assessed independently by an assistant regional manager who is above the rank of the WM. Only members of JLGs who pass this test are eligible for loans.



Joint liability groups are trained on norms and processes they have to follow

JLG loans are offered for a period of 50 weeks. Repayments have to be made on a specific day every week, according to a declining principal schedule. PKGFS insists that all members of JLGs visit a branch when repayments are to be made. After a loan is disbursed, WMs carry out a physical check to see whether the loan amount has been used for the purpose it was taken.

Unlike some MFIs, KGFS companies do not insist that loans be taken only for 'productive' purposes; PKGFS customers have even taken loans to meet consumption needs. Such applicants are usually farm labourers who need to make up for income shortfalls during the lean season. Other reasons for taking loans include closure of high-interest debts, meeting education-related expenses of children, house repairs, and purchase of milch animals.

KGFS customers can also take individual loans, with individual liability, by mortgaging their jewellery. The process of obtaining these 'jewel loans' is considerably simpler than it is in banks. A critical requirement in the processing of a jewel loan application is assessment of the value of the jewellery by a qualified appraiser. One appraiser often meets the needs of several bank branches, and, in any particular branch, an appraiser is available only at a specific time and date. As a result there may be considerable delays in obtaining a jewel loan.

At PKGFS branches, WMs themselves have been trained to determine the value of the jewellery by weighing it in a certified machine and testing for the purity of metal by using a simple acid test. Both activities are done at the branch itself, when the customer comes in with the jewellery. This makes the loan grant process quicker. An experienced jeweller employed full-time by PKGFS cross-checks the purity assessments made by WMs. Thus far, no major assessment errors have been recorded.

While almost all PKGFS JLG members are women, jewel loan applicants can be men or women. PKGFS has also recently introduced retailer loans for

small businesses. Applicants have to bring along sound guarantors not directly related to them.

Low cost of finance

PKGFS's JLG and jewel loans have had a very good response. Of the 10,729 customers enrolled by the company till May 2009, 7,924 have taken one or the other kind of loan.

A major attraction is rate of interest. While moneylenders in the area generally charge at least 48% interest per annum (pa), PKGFS's JLG and jewel loans are currently offered at 12% pa. Significantly, the interest rate is less than half that generally charged by MFIs in India.

The lower interest rate is due mainly to three factors. Firstly, unlike MFIs which generally have a single product, PKGFS offers multiple products. Hence, fixed and variable costs are spread across products and customers. This, coupled with use of high-end technology solutions, reduces the cost of serving clients.

Secondly, compared to typical finance ventures, IFMR Holdings has a long-term perspective of 7 to 10 years for recovering the cost of investment in KGFS companies. Thirdly, compared to MFIs, the KGFS model has lower operational costs as it is based on a fundamentally different approach to business expansion.

Anil Kumar SG, who headed the Microfinance Institutional Development Team at ICICI Bank, which created over 200 MFIs across the country in 25 states, explains that MFIs are typically driven by the need to expand rapidly. "The emphasis is not only on getting as many customers as possible, but also expanding geographically within a short span of time."

With this high-growth approach, early customers effectively pay for the organisation's growth, and, as it spreads, cost of delivery becomes high. In contrast, the KGFS model is based on restricted geographical growth. Each KGFS company is expected to cover a maximum population of 5 million, or two districts only (SKGFS in Uttarakhand will cover more districts as the size of districts is small). In its first year, PKGFS has covered only Thanjavur district, and all its branches are fairly close to each other. The maximum distance between two branches is 6 km; the maximum distance from a branch to the head office in Thanjavur city is 55 km.

Lean operations

Operating costs are also kept down by maintaining a lean front-end. Each KGFS branch is essentially a shop premise taken on long-term lease. The infrastructure in branches is minimal.

The walls are bare, there is no fancy décor, there is no air-conditioning, and customers sit on wooden benches. The most valuable fixed asset in a branch is a safe to store pledged jewellery. Other valuable assets are a desktop computer with an accessory to record fingerprints, a scanner-cum-printer, and a certified jewel-weighing machine.

KGFS branches, which currently serve around 1,000 customers each, are manned by two or three WMs. Working without support staff, they manage everything from outreach activities to recording and feeding in customer data, making loan disbursements, accepting repayments, and processing applications for various products.

WMs are young women and men recruited from the region. The



PKGFS customers take loans to meet consumption needs or invest in income-generating assets like livestock

minimum qualifications are that they should have studied at least till Std XII, they should be computer literate, and they should have a basic mathematical ability. After they are selected, they undertake a rigorous four-week training programme. Subjects covered include rural finance, insurance, business math, and branch-level processes and products.

Use of technology

Use of technology helps keep branch operations to a minimum. Computers in branches are linked, via towers installed over the branches, to the head office, and all data is subsequently transferred to servers maintained by FINO, IFMR Holdings' technology partner, which does the backend processing. Investment in this technology was the costliest part of setting up PKGFS, and also probably the most critical when one thinks of replicating this model in other remote rural areas.

Looking ahead

Even as it grapples with these issues, PKGFS is working on opening more branches and improving customer service. An important deviation in process being tried out in one village is collection of repayments at source —

as moneylenders do — to save people time and effort in visiting a branch.

Branch timings are also being reconsidered, to help customers visit branches outside of their work hours.

KGFS entities in Uttarakhand and Orissa are grappling with another set of challenges. While all PKGFS branches are situated in villages connected by all-weather tar roads, in Uttarakhand, branches of Sahastradhara KGFS (SKGFS) are in sparsely populated rural settlements, accessed by winding roads that are often difficult to negotiate due to inclement weather. Says SKGFS CEO Anupama Joshi: "On an average, people here walk 7-8 km every day to earn a living."

Likewise, in Ganjam, where Dhanei KGFS has started operations, many rural habitations are in difficult-to-access locations. On the flip side, unlike Thanjavur, Ganjam has a vibrant SHG movement with around 17,000 groups having aggregate savings of over INR 300 million.

Such conditions necessitate modifications in the processes that have proven successful in Thanjavur. Even the product mix for initial promotion could differ.

Gaining deeper understanding

These changes will help IFMR Holdings gain a better understanding of how the KGFS model can be rolled out across India, in different geographical, socio-economic and infrastructural environments. Lessons learnt on the ground will be supplemented by the outcomes of various research and funding efforts initiated through IFMR Trust Advocacy Unit (ITAU). Among ITAU's on-going projects of particular relevance to the KGFS model are:

- An effort by InnerWorlds, a group of researchers, to understand rural Indians and document their stories.
- Incubation support provided to the Centre for Innovative Financial Design (CIFD). A research centre at IFMR, CIFD has been established in partnership with 'ideas42' at Harvard University to design financial products to bridge the gap experienced by the poor between financial needs and access to financial services.
- Partnership with the Centre for Development Finance at IFMR and McKinsey to determine the effects of financial inclusion in PKGFS districts.

PKGFS itself is engaged in designing viable financial products. The immediate challenge is to devise a livestock insurance product that makes commercial sense to both low-income households as well as insurance companies.

IFMR Trust to support MIT research

IFMR Trust has set up a fund to support faculty and research scientists at the Massachusetts Institute of Technology (MIT) for projects in applied technology for development in India. Called the MIT-India/IFMR Trust Seed Fund, the fund is part of the MIT International Science and Technology Initiatives' (MISTI) Global Seed Funds.

Global Seed Funds supports MIT faculty and researchers in early-stage international projects and research collaborations. Applicants are encouraged to involve MIT students — both undergraduate and graduate — in their projects. The MIT-India/IFMR Trust Seed Fund will support initiatives such as:

- Design of personal finance and wealth management strategies for low-income rural households and migrant households, which could involve investigations into household psychology, anthropology, moral hazards, adverse selection.
- Human-centred design for channels through which rural remote households access financial services, solving problems that include customer identification, computing, printing, telecommunications, interface software, and physical architecture design.
- Breakthrough physical and materials design of equipment and utilities commonly used by the rural poor: drinking water plants, decentralised energy devices, housing materials, and irrigation implements.
- Innovative low-cost design ideas that facilitate businesses that aim to serve rural India. For example, designs that uniquely identify livestock in order to prevent insurance fraud and thereby improve supply; simple anti-tamper technology for drinking water plants and commodity warehouses; and cost-effective ways of detecting counterfeit notes.
- Computing and mobile innovations that could dramatically reduce the cost of financial services delivery in remote rural India.

The deadline for the 2009-2010 grant is September 14, 2009. Winners will be announced in early December 2009. The maximum award amount is USD 15,000.

For more information and application, please visit the MISTI Global Seed Funds website:
<http://mit.edu/misti/faculty/seed.html>

Vocational academy launched

To equip youth from rural and semi-urban areas with the skills required

in various emerging service sectors in India, the Hyderabad-based STRiVE has launched Vocational Academy India Pvt Ltd, in collaboration with Collabrant Incubators Pvt Ltd.



IFMR Trust's Vocational Training Network Enterprise (VTNE) has invested in STRiVE.

STRiVE provides assessment, counselling, apprenticeship, placement and certification services to students from rural and semi-urban areas.

STRiVE has counselled over 10,000 students so far from various parts of the country and has tied up with a host of training institutes to provide quality education and placements for students.

Read a story about STRiVE here:
<http://ifmrtrust.co.in/fieldreports/striving.php>

"Trained manpower remains the single largest impediment to growth in the service sector and we wish to fulfil that need through Vocational Academy," says Suresh Mutyala, CEO, STRiVE.



Under the brand name 'Vocad', Vocational Academy offers customised, job-oriented courses related to emerging businesses. Courses related to the banking, financial services and insurance (BFSI) sectors and technical courses will be launched soon.

The courses are devised by industry experts and taught in classes with a small number of students. Hands-on training is combined with faculty-led sessions and interactive sessions. At the end of each course, students have to undergo an internship.

At an average fee of INR 5000-7000, the courses are extremely affordable. "The fee structure is such that it is approximately equivalent to an expected month's salary on employment," Mutyala explains. Enrolment is done after a basic aptitude test administered to identify the student's strengths, aspirations and interests.

Vocad students will be offered jobs through 'JobsXchange' organised by the company, in association with leading corporates.

Vocad courses were launched in eight locations in April 2009. Vocational Academy has a business plan of establishing 600 learning centres within the next five to seven years, covering every district of India. Read more about Vocad here:

http://www.vocationalacademy.in/company_info.htm

VTNE has made an investment of INR 27.5 million in the



company. Says IFMR Trust's Senior Vice President Puneet Gupta: "We expect Vocational Academy to use the funds to increase market share by launching 50 centres by 2010, and having a presence in every district of the country by 2017."

IFMR Trust's VTNE acts as a supply chain enabler, linking first-time job-seekers from semi-urban and rural areas to the corporate sector. "VTNE invests in solutions that address the current gap in demand and supply of trained manpower," says Bindu Ananth, President, IFMR Trust. "In this context, Vocational Academy is a very strategic investment for us."

STRiVE's

collaborator, Collabrant Incubators,



provides business incubation services to small manufacturing enterprises and creates new brands and businesses. Over the last eight years it has created and established a number of businesses and brands in the fast-moving consumer goods, durables, apparel, footwear, lifestyle, retail and franchising sectors.



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