

Utkarsh Micro Finance Private Limited



Loan Portfolio Audit

June, 2013

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MicroSave

Market-led solutions for financial services

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Abbreviations

Acronyms	Full forms
BM/AM/DM/RM/ZM	Branch/ Area/ Divisional/ Regional/ Zonal Manager
CGT	Compulsory Group Training
CO	Credit Officer
MEL	Microenterprise loan
GRT	Group Recognition Test
HO/BO/AO/DO/RO/ZO	Head/ Branch/ Area/ Divisional/ Regional/ Zonal Office
LPA	Loan Portfolio Audit
LUC	Loan Utilisation Check
MIS	Management of Information Systems
NBFC-MFI	Non Banking Finance Company- Microfinance Institutions
PAR	Portfolio at Risk
RM	Risk Management
TOR	Terms of Reference



Executive Summary

Executive Summary (1/2)

MicroSave conducted the loan portfolio audit of Utkarsh Micro Finance Pvt. Ltd in June 2013 to assess the quality of its loan portfolio and identify related key risk factors. The team visited 11 branches spread across UP, Bihar and MP, covering 36 centers and 615 clients. *MicroSave* used an analysis framework that covered 7 factors that have a direct bearing on an MFI's portfolio quality- portfolio diversity, field management, MIS, internal control, incentive systems, risk management, and quality of human resources. Key findings from the LPA exercise are summarised below.

Portfolio Diversity

- By spreading further up in to the North India (Uttarakhand and Delhi) and Central India (MP) beyond its traditional territories of East UP and West Bihar, Utkarsh will secure itself against systemic risks. However from here on, it should aim at saturating existing branches in these geographies before venturing into new ones
- Portfolio spread on other vectors like rural vs. urban and sectors spread is also well- keeled and offers no reason for concern. However, its about time that Utkarsh brings in product diversity in its portfolio by graduating the 3rd/4th cycle clients to MEL

Field Management

Overall the field management at Utkarsh is very robust and streamlined. There were no major issues that should cause of concern. Although, few points that require highlighting are presented in the report. Specifically:

- Ensuring center cohesion esp. in cases where either new members are added or dropped out ones replaced
- The persistent demand by a section of clients for higher loan amount underscores the need to roll-out the MEL to larger number of branches
- LUCs are done for all the clients, but field staff are finding it difficult to complete it within the mandated 2 weeks period. We have suggested some measures to improve the effectiveness of this process
- Centre attendance was found to be a bit lower than mandatory requirement as stated in credit policy
- Some of the others issues observed were need for faster settlement of insurance claims and greater diligence in investigating reasons for the drop out

Executive Summary (2/2)

MIS

- The loan tracking system in the MIS is robust and the MIS data is accurate. Utkarsh's management has already taken proactive measures to address the issue of 3 lag (3 days) in data entry of the MIS. A real time mobile based solution is being piloted in two of the branches with plans for a full scale rollout in near future

Internal Audit and Controls

The system is robust, comprehensive and well functioning.

- Utkarsh audit team should also incorporate customer service related aspects in the audit tools- through enhancing the existing audit tools/formats with section on *customer service*

Staff Incentive Policy

- Staff incentive policy of Utkarsh is able to strike a balance between the portfolio quality and business targets, besides drive compliance to policies and foster team spirit within the branch

Risk Management Practice

- Risk management practice is accorded high priority within Utkarsh – as evident from the well structured and an institutionalised mechanisms to deal with the risks
- Comprehensive risk assessments are being carried out at the branch, department and organisational level

Quality of Human Resource

- COs demonstrated high level of competence to carry out the tasks assigned to them
- There is a scope of improvement as regards centre management, LUCs and passbook maintenance ; whereas effectiveness of CGT process, CDS updation and TCO trainings can be improved with further investment in staff training

Summary Report – Portfolio Quality*

Key Considerations (N= 615)	Remark (Yes/No)
Loan Data <ul style="list-style-type: none"> Were there any instances of loan data (outstanding) mismatch between HO, branch and client records? 	No
Loan Appraisals <ul style="list-style-type: none"> Were there any instances of non-compliance to the policies and procedures in the pre-disbursement processes (group formation to CGT and GRT) 	High degree of compliance was found. However, the processes underwent some dilution in case of substitute or new clients joining an existing centre.
Loan Disbursements <ul style="list-style-type: none"> Were there any instances of difference in loan amount as stated in MFI records and the amount actually received by the clients? 	No
Loan Utilisation by clients <ul style="list-style-type: none"> Did the clients use the loan for the stated purpose? 	Mostly yes as LUC were performed for most clients. However, Utkarsh is finding some constraints in ensuring that 100% LUCs are done within 2 weeks of disbursement
Ghost Clients/Loans <ul style="list-style-type: none"> Were there any instances of ghost loans or clients observed? 	No
Unreported Arrears <ul style="list-style-type: none"> Were there any instances of unreported arrears? 	No
Pre-closure of Loans <ul style="list-style-type: none"> Were there any instances in which pre-closures were not done according to organisational policies? 	No
Incidental Charges (loan processing and insurance Fees) <ul style="list-style-type: none"> Were there any instances of clients being overcharged on loan processing fees and insurance premium? Were there any instances of clients paying commissions to external parties for accessing loans? 	No No

*As per the sample of 615 clients whose records were assessed during the course of the audit

About Utkarsh

- Mission & Vision
- Operational Model
- Organogram

Mission and Vision

Vision

- Serving one million households through a range of socially oriented products and services by 2016

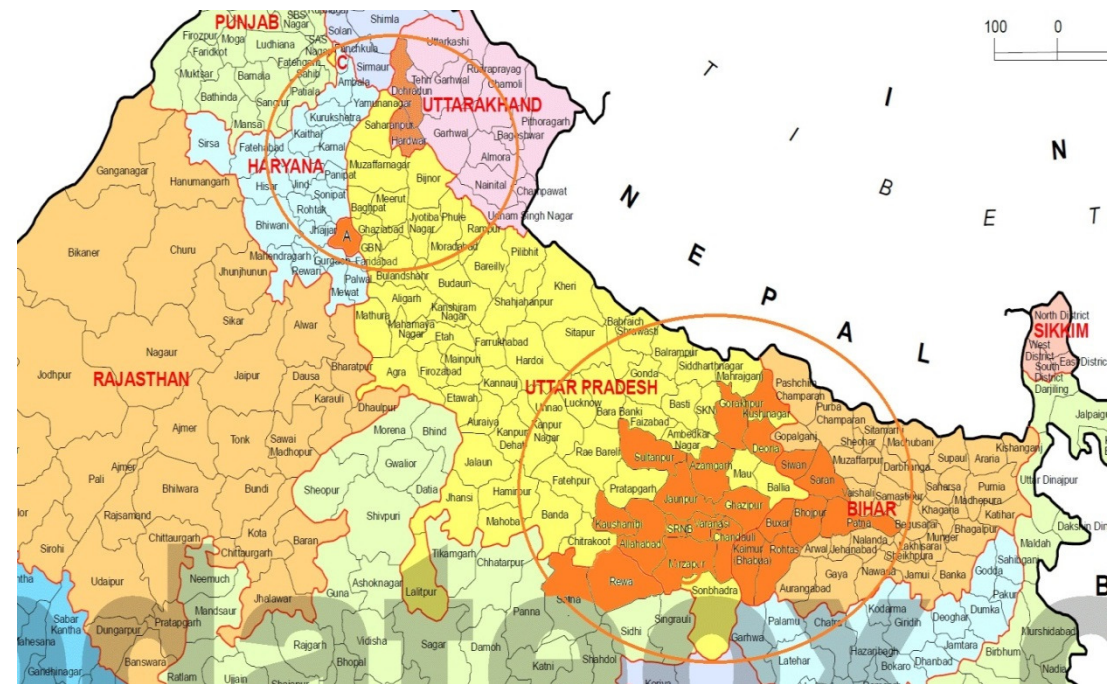
Mission

- Support underprivileged and underserved segments by providing financial and non-financial services through a socially responsible, sustainable and scalable institution



Operational Area

- Target area is Northern and Central belt of India
- As on 30th April, 2013 Utkarsh operates from 104 branches in 25 districts spread across 5 states
 - 13 districts in Eastern UP
 - 7 districts in Western Bihar
 - 2 districts in Uttarakhand
 - 2 in MP
 - 1 in Delhi
- Refer Annexure 5 for state and district-wise list of branches



Operational Model

Field Structure

- Branch reports to its nearest Area office (AO) , and AO reports to divisional office (DO) and DO reports to regional office (RO) and the RO reports to Zonal office (ZO)

Span of control

- Each ZO (headed by a ZM) has 3 ROs under its supervision and each RO (headed by a RM) has 3 DOs under its supervision
- Each DO (headed by a Divisional Manager) has 3 *Areas* under its supervision and 3 branches report to an Area Manager (AM)
- AM's and DM's have no separate office since they are always on move. One of the branches under them is made as their base branch to facilitate their movement in the field

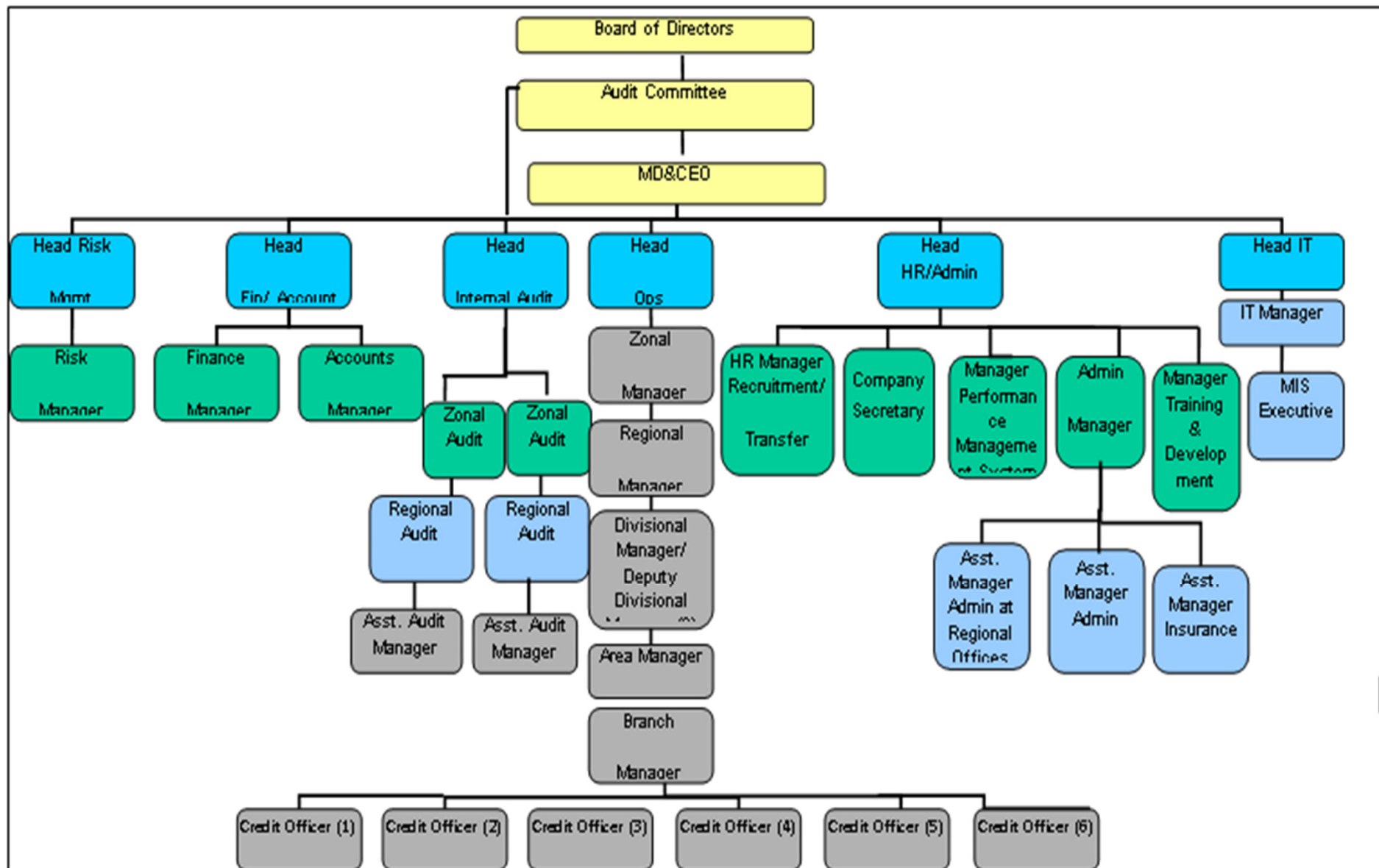
Branch Structure

- The BM is the head of the branch and supervises 3 to 6 CO (based on the branch size). They stay together at the branch premises. A branch operates in the radius of 15 Km
- COs are the front line employee and are allocated a cluster of about 20 villages each.
- CO is allocated 3 or 4 field routes to maintain maximum effective borrower contact hours by minimizing unnecessary travel and physical strain.

Lending Methodology

- The methodology of lending is under Grameen methodology (centers made up of groups of poor women).
- Women forming a new centre need at least 10 members (2 groups of 5 members each) chosen from among those they know, reside in close vicinity and trust in matters of money. They cross-guarantee each others' loans

Organogram



Loan Portfolio Audit

- Overview of Loan Portfolio Audit Process
- Methodology
- Analysis Framework

Overview of the Loan Portfolio Audit Process

Objective

To conduct the loan portfolio audit of Utkarsh Micro Finance Pvt Ltd to assess the quality of loan portfolio and identify related key risk factors

Methodology

Sample audit of portfolio

- Out of 105 branches of Utkarsh, *MicroSave's* team visited 11 branches spread across Uttar Pradesh, Bihar and Madhya Pradesh
- 36 centers and 615 clients were selected based on a mix of stratified and purposive sampling
- Transaction record of each of the 615 sampled clients were traced backwards from loan cards to branch books to the MIS collated from HO

Review of documentation and processes

- Loan documents of clients, registers / files and periodic audit reports maintained at branch were reviewed
- Loan collection and disbursement process and related MIS reports were thoroughly checked
- Deliberations were held with respective Credit Officers, Branch Managers, MIS operator, Area Managers and Divisional Managers to complement the findings of the study

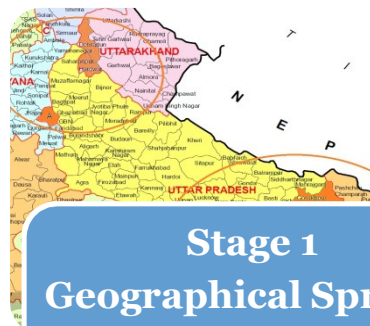
Sample Selection

- In the course of field assessment and verification of operational processes and procedures, a sample of 11 branches and 600 + clients were selected. Following criteria were used for selection of branches:
 - Geographical spread : spread across Uttar Pradesh, Bihar and Madhya Pradesh
 - Age of the branch : covering branches upto 1 year old, 1 to 3 years old ,and more than 3 years old
 - Portfolio size : Small (< Rs.1.00 cr), Medium (Rs.1.00 cr to Rs.2.50 cr) and Large (> Rs.2.50 cr)
 - Portfolio quality : covering branches with nil and existing overdues (PAR)

Methodology (1/3) - Sampling

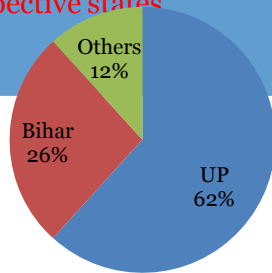
Sampling the branches

- As per the ToR, 600 client accounts across 10 branches were to be audited
- A 3-staged stratified random sampling was used to identify 11 branches
- Besides these, Kasimabad and Hanumanganj were selected purposively as they were the only 2 branches with PAR (albeit miniscule)



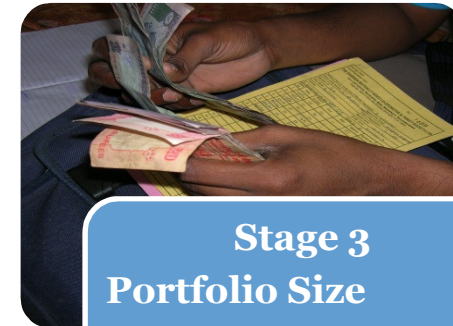
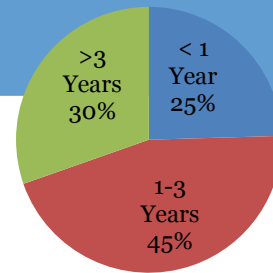
Stage 1
Geographical Spread

- 7 from UP, 3 from Bihar and one from MP
- In proportion to total **branches in respective states**



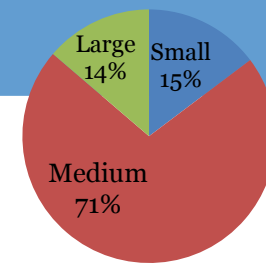
Stage 2
Branch Vintage

- 3 less than 1 year
- 5 between 1-3 years
- 3 greater than 3 years



Stage 3
Portfolio Size

- 2 large portfolio
- 7 with medium portfolio
- 2 with small portfolio



Sampling the Clients

- Within the sampled branches an average of 60 clients were selected
- Centres were chosen randomly from the list of centre meetings scheduled on the day of LPA

Methodology (2/3) - Branches Visited & Clients Covered

Branch	District	State	Age of the branch	Outstanding	PAR	No. of centers	No. of clients
Azamgarh	Azamgarh	UP	1 – 3 years	Rs.1 Cr – Rs.2.5 Cr	Nil	4	54
Handia	Allahabad	UP	1 – 3 years	Rs.1 Cr – Rs.2.5 Cr	Nil	3	42
Hanumanganj	Allahabad	UP	> 3 years	> Rs.2.5 Cr	Yes	3	36
Jalalpur	Jaunpur	UP	> 3 years	Rs.1 Cr – Rs.2.5 Cr	Nil	3	55
Kasimabad	Gazipur	UP	> 3 years	Rs.1 Cr – Rs.2.5 Cr	Yes	4	77
Naini	Allahabad	UP	< 1 year	Rs.1 Cr – Rs.2.5 Cr	Nil	3	50
Sahjanwa	Gorakhpur	UP	1 – 3 years	< Rs.1 Cr	Nil	2	39
Chapra	Saran	Bihar	1 – 3 years	Rs.1 Cr – Rs.2.5 Cr	Nil	5	76
Danapur	Patna	Bihar	1 – 3 years	> Rs.2.5 Cr	Nil	3	55
Majhi	Saran	Bihar	< 1 year	< Rs.1 Cr	Nil	3	62
Satna	Satna	MP	< 1 year	Rs.1 Cr – Rs.2.5 Cr	Nil	3	69
Total						36	615

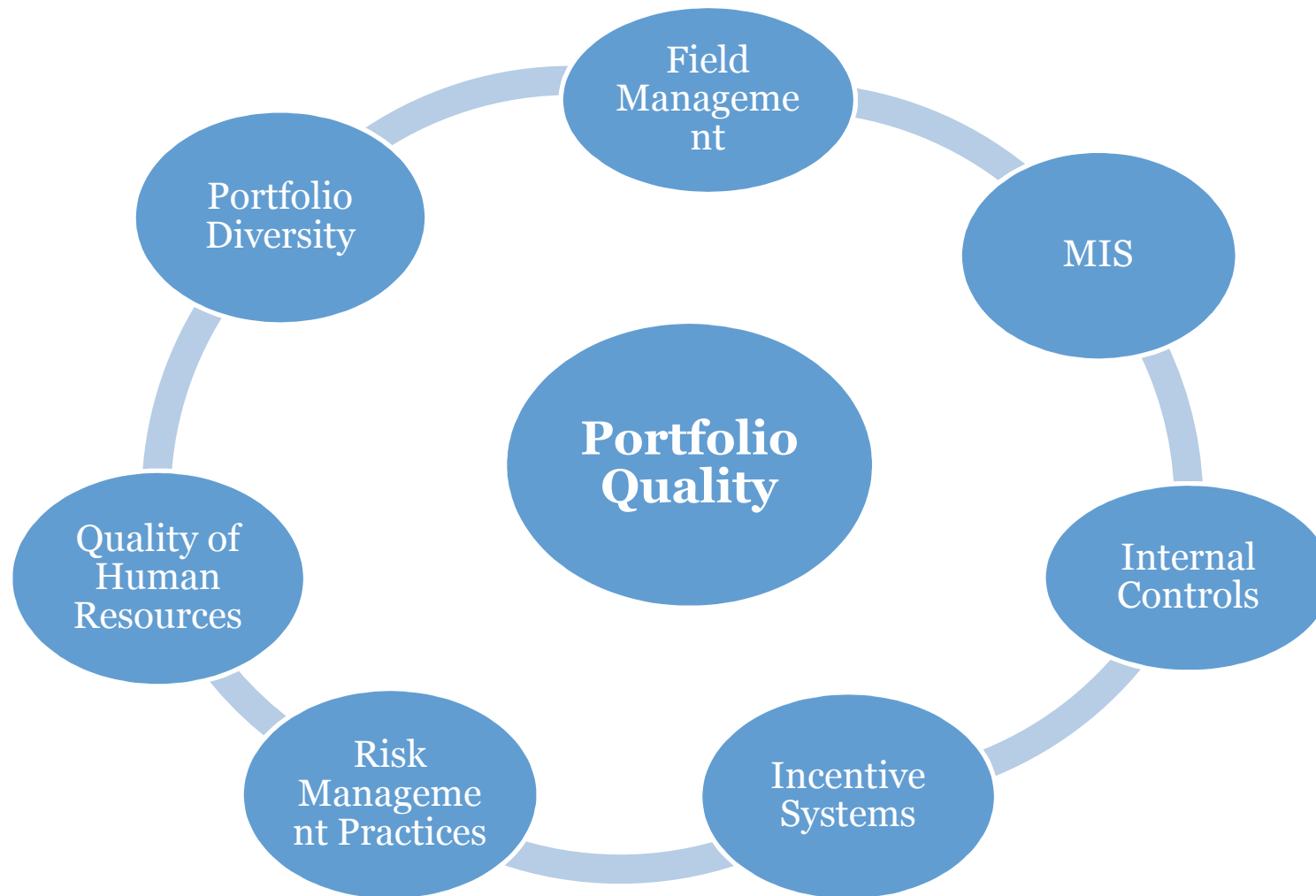
Methodology (3/3) - Documents Reviewed

Review of documentation and processes

- Loan documents of clients, registers / files and periodic audit reports maintained at branch were reviewed
- Loan collection and disbursement process and related MIS reports were thoroughly pursued
- Deliberations were held with respective Credit Officers, Branch Managers, MIS operator, Area Managers and Divisional Managers to complement the findings of the study
- Transaction record of each of the 615 sampled clients were traced backwards from loan cards to branch books to the MIS collated from HO

Analysis Framework

Portfolio is directly affected by 7 factors identified below. We analyse each of these to make a comprehensive assessment of the loan portfolio of Utkarsh.





Key Findings & Recommendations



Portfolio Diversity (1/2)

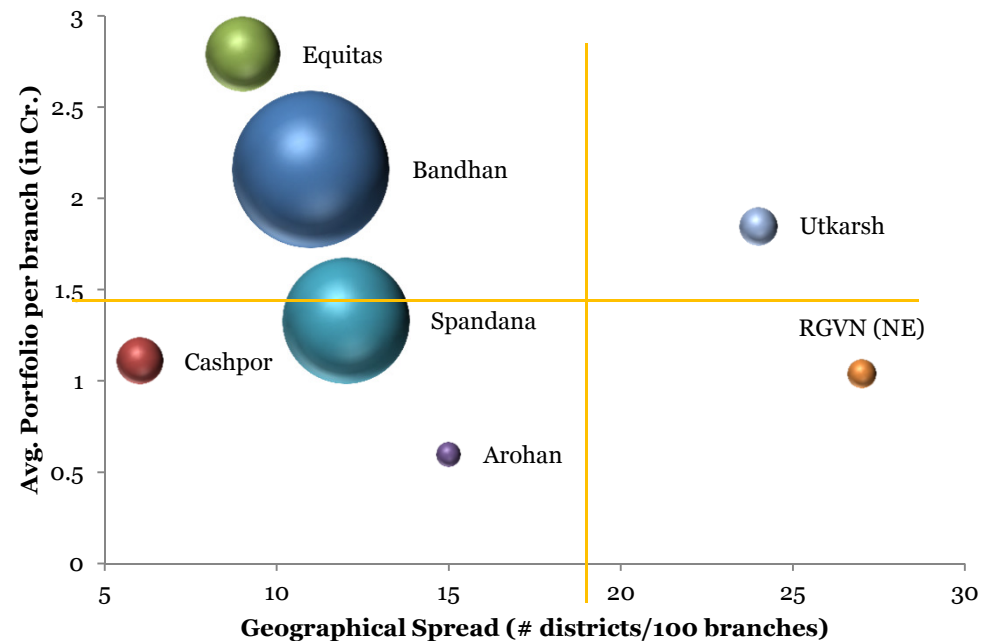
1. Geographical Spread

Bulk of the portfolio is concentrated in Eastern UP, which is justified given that Utkarsh started its operation from this region and subsequently spread outwards. However, in last four years, the management has made conscious effort to grow its portfolio organically into other geographies and as on date it has operations in 5 states

State-wise spread of Utkarsh Portfolio*

States (districts)	Number of Branches	Number of Active Clients	Outstanding Portfolio (In Cr Rs.)	Portfolio Percentage
U.P. (13)	63	135,979	121.7	68.9%
Bihar (6)	27	51,182	42.9	24.3%
UK (2)	5	5,839	6.5	3.7%
M.P (2)	5	4,635	5.2	2.9%
Delhi (1)	1	239	0.3	0.2%
Total	101	197,874	176.6	

- With Eastern UP portfolio maturing and saturating (as clients enter 3rd/4th cycle), the growth is likely to come from newer geographies
- However, geographic expansion comes with a cost. Wide coverage is likely to cause a resource stretch for Utkarsh.
- As seen from graph**, amongst its peers, Utkarsh has a high branch spread and a healthy portfolio outstanding per branch. With its current geographic spread, it should aim at saturating existing geographies than venturing into new ones.



*Includes only group loan portfolio which forms 99.99% of Utkarsh total Portfolio - Data as on 31st March, 2011

** Size of the bubble represents the outstanding portfolio of the MFI



Portfolio Diversity (2/2)

2. Rural Vs. Urban Split in Portfolio

- Utkarsh has a holistic approach towards urban and rural microfinance markets.
- The rural-urban portfolio split of its most mature portfolio's (Uttar Pradesh) matches the rate of urbanization in that geography.
- In other states as well, the portfolio splits are in sync with population profile of that state

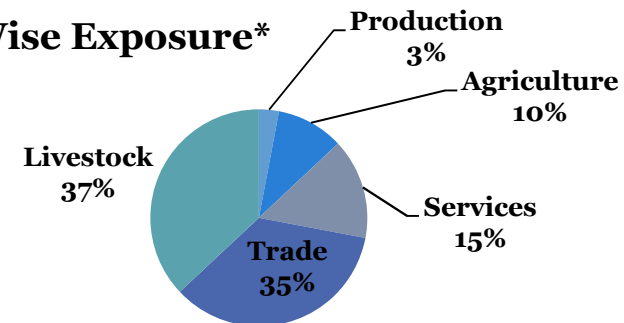
Urban vs. Rural Split of Utkarsh's Portfolio**

States	Urban Population	Urban Portfolio of Utkarsh	Rural Population	Rural Portfolio of Utkarsh
U.P.	22%	22%	78%	78%
Bihar	11%	21%	89%	79%
UK	31%	-	69%	100%
M.P	28%	33%	72%	67%
New Delhi	97%	100%	3%	-
Total		21.2%		78.8%

3. Sectoral Distribution

- Overall, Utkarsh's portfolio is fairly well distributed across different sectors.
- The sectoral distribution of portfolio reveals a focus on agri and allied activities. The loans are being used for asset creation and working capital investments in income generating activities

Sector-Wise Exposure*



4. Product diversity

- portfolio of Utkarsh is almost entirely composed (99.99%) of group lending products. It has recently ventured (March, 2012) into individual loans targeted at microenterprises. Utkarsh needs to build its microenterprise loan (MEL) portfolio especially with its existing clients in maturing geographies. Currently, it has 2 MEL branches (Varanasi & Allahabad) with portfolio of Rs. 1.47 Cr

*Includes only group loan portfolio which forms 99.99% of Utkarsh total Portfolio - Data as on 31st March, 2011

**Population Data – Census 2011

Field Management (1/6)



Strengths

- Utkarsh follows a systematic approach to client selection involving village surveys, group formation, CGT (3 days), house visits and GRT. In the observed sample, these processes were effectively undertaken and members had a fair understanding of processes and policies of Utkarsh
- Credit bureau data is used prior to all loan disbursements to filter out over-indebted clients
- As Utkarsh's Micro Enterprise Loan initiative matures, it will ensure smoother graduation for group loan clients with higher credit needs towards individual borrowing.

Areas of Improvement

- With an effort to have greater efficiency in operations through bigger centres, in few instances, the centre cohesion was apparently weak with few groups not well acquainted with other members/groups in the centre. Greater monitoring is required, especially while adding new members to a centre so as to ensure that centre cohesion is maintained. Special attention is needed in case of replacement members.
- While client were fairly sure of aggregate charges (loan processing and insurance fee) for a loan, majority of them were not able to recollect the breakup for the same. Utkarsh can look into printing the loan processing fee and insurance premium on client passbooks.

Field Management (2/6)



Strengths

- All the disbursement related documentation was found satisfactory in the observed sample
- Appraisals of individual loans are backed by proper cash flow analysis and the same was in line with the evaluation criteria as mentioned in the credit policy
- Disbursement process observed in the branches were found very effective. Clients and their guarantors are given all the key information regarding loan including loan amount, interest amount, tenure, centre meeting day and their stated loan purpose.
- All disbursements happen in cash at the branches (in presence of branch manager) to avoid the risk of carrying cash to the field

Areas of Improvement

- Few members in the sample expressed the need for higher loan amounts.
- *MicroSave* team believes that Utkarsh's current strategy of deciding the loan amount is effective and at the same time competitive. However, Utkarsh needs to quickly scale up its Micro Enterprise Loan initiative especially in matured geographies to address the needs of mature clients who need loans of higher ticket sizes.

Field Management (3/6)



Strengths

- Utkarsh's loan policy gives emphasis on loan utilisation checks and 100% of the disbursements needs to be backed by LUCs
- LUCs is made compulsory at all levels (BM – 50% of total disbursements, AM – 20% of total disbursements, DM – 10% of total disbursements)
- In the sample covered, LUCs for all the centres had been conducted and documents for the same had been filed in the centre files

Areas of Improvement

- LUC documentation was updated for all the **sampled** centres. However, LUC data for May revealed that LUCs were pending for many clients (*please refer to annexures for observed cases*). Also, BMs and AMs were unable to meet their LUC targets (as per the credit policy). Stricter monitoring is required to ensure LUCs are diligently conducted for all loan disbursements
- As of now the LUC form does not capture the pre-loan disbursement status of clients with regards to purpose for which the loan is being taken. In absence of this baseline data, it is very difficult to effectively conduct a LUC e.g. if a client wants loan for a sewing machine, data should be captured for number of sewing machines she already owns and with new loan she should be adding an extra machine to that tally. Utkarsh should rework its LUC form and capture such baseline data at the time of each loan disbursement in order to enhance the effectiveness of LUC process

Field Management (4/6)



Strengths

- Group discipline was found to be satisfactory in most centre meetings. Members were on time and the centre meetings were conducted as per the prescribed institutional processes for the same.
- Number of loan instalments paid/pending were re-stated by all the COs in the centre meeting
- Dual records of collections are maintained in all the centres i.e. client passbook and CDS files (MIS generated). The dual records minimises the chances of fraud or error in loan collections
- The overall effectiveness of the field management processes in general and collection practices in particular can be adjudged from the fact that in its 4 years of operations and with about 200,000 client, there has been negligible PAR (1 member each across 2 branches) in the institution.

Areas of Improvement

- In the sample, the centre attendance was observed to be a bit lower than as required by policy. Details of the same are given in annexures on the same.
- As per the policy, COs field are swapped every 6 months as a strategy to mitigate credit risks and frauds as a result of CO-centre collusion. However, 6 months is a relatively short period (12 visits) when it comes to maintaining effective control on groups. The management can look into extending this period up to 9-12 months. Majority members in the field were not able to recall the name of their loan officer and COs were not able to give much details on the members to whom they have not made disbursements

Field Management (5/6)



Strengths

- Utkarsh has tight monitoring structure as far their operational model is concerned . The span of control for each manager (AM upwards) is favourable (3 as compared to 4-6 for other MFIs. Every three branches form an Area which is supervised by a Manager. Additionally, every 3 such areas comprise a division which is supervised by a Divisional Manager.
- The team did not find any “high risk” findings in the monitoring visits for the sampled branches apart from few documentation errors

Areas of Improvement

- Visits to the sampled branches revealed that monitoring visits of Area Managers should be stepped up a bit given the fact that he/she handles only three branches. The monitoring visits for Area Manager was found to be lower for Naini and Hanumanganj branch.

Field Management- other observations (6/6)



- There were issues in cases of insurance claims for deceased members/guarantors. The settlements were taking more than 3 months in most observed cases (*please refer to the annexures for details*).
- In the current system, Utkarsh does not investigate cases of client dropouts i.e. the reasons are not captured. The dropout list prepared by MIS team has a standard reason “ *client business fail* ”. Also, it seems that number of such dropouts are not being properly monitored by AM/DM (no comments have been made on the same in monitoring reports). For instance, in Naini branch, for the month of May, the net addition of clients was negative as a result of high dropouts.

Utkarsh needs to develop systems to capture the reasons for dropouts through field teams. This will provide insights to the management, especially with regards to customer feedback on service levels. These insights shall be particularly useful given the fact that Utkarsh operates in a highly competitive market with more than 6-7 MFIs operating in most of its area of operations.

- For Naini branch, the bank account has not been opened. In order to cope up with the situation, the branch carries cash to and from nearest Utkarsh branch which is 6 kms away. While this may be risky and against the credit policy of Utkarsh, the *MicroSave* team during its visit to the branch also observed delays in disbursements. This is likely to have a negative impact on customer service at the branch. The management should take appropriate action to open bank account for the concerned branch

Management Information Systems



- Utkarsh has robust MIS to track its loan portfolio. In 2012, Utkarsh migrated from *Jayam Solutions* to *Crafts Silicon*- web based solution that is more versatile and with higher functionalities.
- The MIS at Utkarsh works on a hub and spoke model. An MIS executive is stationed in a cluster of 3-4 branches (at a branch with relatively better network connectivity) . S/he enters details of new clients, loan disbursement and collections received, based on physical documents received from branches at a frequency of twice every week (after every 3 days of field operations)

Strengths

- The loan tracking system in the MIS is robust and the MIS data is accurate (barring few non-financial fields) when matched with the field level data maintained at branches (loan applications, centre files and client passbooks).
- The MIS is secured with varying levels of access for different designations
- Effective controls are put in place to prevent chances of frauds/errors. Some such controls are: disallowing part payments and back-dated entries without due approvals
- MIS team also check the credit bureau data and informs concerned COs/BMs (SMS) on cases with loans from more than two MFIs

Areas of Improvement

- Currently, there is a lag of three days in the data fed into the MIS, hence daily reports of collection, disbursements and new clients are not available to the management through MIS on daily or 'live' basis. The same is collected manually over phone.
- Technological innovations are required to capture this data in MIS on real-time basis.
- Utkarsh's management has already taken proactive measures to address this issue. A real time mobile based solution is being piloted in two of the branches with plans for a full scale rollout in near future

Internal Audit & Controls (1/2)



Internal Audit Structure at Utkarsh

Internal Audit Head	<ul style="list-style-type: none"> • Chief of Audit Department – Reports to MD & CEO • Secretary in Audit Committee of the board
Zonal Audit Managers	<ul style="list-style-type: none"> • Monitors and supervises the activities of 3-4 Regional Audit Managers
Regional Audit Managers	<ul style="list-style-type: none"> • Monitors and supervises a team of 4-5 Assistant Audit Managers
Assistant Audit Managers	<ul style="list-style-type: none"> • Responsible for field Audit • Handles 4-5 branches

Types of Audit	Objective	Audit Cycle (As per policy)
Snap Audit	Single day surprise audits to check field and branch operations. As per the current policy, this has been discontinued	Min. of 1 audit per month per branch
Short Audit	3-4 day audit usually targeted at new branches. Older branches with caution centres are also targeted under such audit	Bimonthly (min.) (most branches)
Comprehensive Audit	Full fledged 5-6 day audit that all the branches have to go through every quarter. All field and branch related processes/documentation are checked. The ratings for such audits act as key determinant in staff incentives	Quarterly (min.) (all branches)

Internal Audit & Controls (2/2)



Strengths

- Overall the audit and internal controls at Utkarsh are robust and are being implemented as per the policy
- The internal audit tools/formats were well framed and cover all the key aspects related to service delivery, processes, documentation and branch administration
- For all the sampled branches, audits were being regularly conducted and the recommendations were being pro-actively addressed by the relevant operations staff
- The team did not find any “high risk” findings in the audit reports for the sampled branches apart from few documentation errors

Areas of Improvement

- The current audit tool only captures internal operations, process and documentation related aspects. Utkarsh audit team should also incorporate customer service related aspects in the audit tools
- This can be done through enhancing the existing audit tools/formats with section on *customer service* or it can design a more comprehensive *customer satisfaction survey* that are periodically administered
- A sample of clients may be quizzed on service related aspects and their suggestions should be reported to the management to take corrective actions. This may also help Utkarsh to analyse reasons for client dropouts which are currently not being captured in the system

Staff Incentives Policy (1/2)



Field Staff	Incentive Type	Incentive Basis	Institutional Objective
Credit Officers	Monthly	I. Number of loan disbursements (new clients + existing clients) II. Active loan clients/centre	<ul style="list-style-type: none"> ➤ Acquisition of new clients ➤ Promote efficiencies by ensuring bigger centres (15 or more) ➤ Promote organic growth ➤ Lowering credit risk per centre
	Quarterly	I. Achievement of business targets II. Audit rating of the branch III. Number of loans disbursed	<ul style="list-style-type: none"> ➤ Achievement business targets ➤ Compliance to institutional policies/procedures aimed at maintaining effective field/branch operations ➤ Fostering team spirit within branch
Branch Managers	Monthly	I. Fixed incentive (dependent on active loan clients/centre)	<ul style="list-style-type: none"> ➤ Promote efficiencies by ensuring bigger centres (15 or more) ➤ Promote organic growth ➤ Lowering credit risk per centre
	Quarterly	I. Fixed incentive (dependent on audit rating of branch)	<ul style="list-style-type: none"> ➤ Compliance to institutional policies/procedures aimed at maintaining effective field/branch operations

Staff Incentives Policy (2/2)



Strengths

- The staff incentive policy of Utkarsh is able to strike a balance between the portfolio quality and business targets, which often are at odds for most MFIs. It has also linked field staff incentives to overall branch audit rating which ensures policy/process compliance in all aspects
- The staff incentives are targeted more on loan disbursements than on loan size (outstanding). This ensures that staff do proper appraisals for loans, disburse appropriate amount to each clients, and service only the poor. This also reduces the risk of arrears. The policy caps incentives to a threshold business target thereby prevent reckless growth.
- The business target setting exercise follows a bottom-up approach to ensure realistic targets are set and the same are owned at all the staff levels of the operations team
- Utkarsh approach towards portfolio quality is one of prevention. The incentive policy does not promote curative measures like PAR recovery

Areas of Improvement

- The focus of staff incentive policy is on active loan clients/centre. While this promotes efficiencies, it can have adverse affects on customer service levels and overall group cohesion
- The staff, in an effort to form larger centres might combine group members from distant localities who might not be very comfortable with each other. For clients, there might be issues with accessibility as well. Such instances were observed during field visits – Centre 72 (Satna), Centre 57 , 105, 32 (Naini), Centre 49 (Chapra)

Risk Management Practices (1/2)



Risk Management at Utkarsh

- A systemic approach to risk management has seen it adopt a standardised processes towards risk management, that: 1. identifies risk; 2. assesses risk; 3. addresses risk; and 4. reviews & reports risk
- The above mentioned processes cover all the 4 major risk categories that get defied in a financial institution i.e.: 1. credit risk; 2. operational risk; 3. market Risk; and 4. liquidity risk
- The practice of risk management gets operationalized both at the branch level and at the overall organisational levels through policies and their effective implementation.

Risk management at an institutional level

- To minimise the credit risk, certain hygiene factors are followed across the processes from client identification to disbursement that ensures that only credit worthy clients are included and serviced by the system
- To minimise the operational risk, cash handling by staff is minimised, maker-checker concept is put in force for all the records and documents, regular audits are undertaken and systems are automated
- To minimise liquidity risks, liquidity position is constantly tracked, funding is secured as per a funding policy, capital efficient mechanisms like off balance sheet financing arrangements are explored and capital adequacy is maintained over the thresholds set by the regulator
- On market risk containment, Utkarsh doesn't have any levers to control it as such, besides complying with the interest rate margins specified by the RBI
- Each department is also subjected to risk assessments

Risk Management Practices (2/2)



Risk management at branch

- At the branch level the risk management gets practiced through '**Branch Risk Rating**' that covers the 14 parameters that cover credit (42.5%) and operational risks (57.5%) proxies.
- There are 4 credit risk indicators are portfolio concentration- across communities s, activity types and caution centres; and PAR
- There are 10 operational risk indicators are- Audit rating, Client acquisition and maintenance, staff turnover, client drop-out, competition, incidence of flooding in the area, cash handling, law and order situation, insurance and credit bureau
- It assigns a score to a branch based on the observation n of its portfolio concentration, audit score, field staff turnover, client acquisition and PAR. Accordingly, branches get tagged as critical, high, moderate and low risks

MicroSave's assessment

- Risk management is accorded high priority within Utkarsh- unlike many MFIs, Utkarsh had a separate risk management function from the first year of its inception
- Utkarsh has a well structured and an institutionalised mechanisms to deal with the risks
- As a results high degree of risk awareness has been built and a risk culture pervades the organisation
- Branch risk rating provides a comprehensive index of credit and operational risk at the branch.
- At the institutional level too, through various policy measures and monitoring checks the credit, operational and liquidity risks are managed.
- Similarly, the practice of risk assessments even at the departmental level has helped in percolation of risk culture across the organisation

Quality of Human Resources



Mostly, COs demonstrated high level of competence to carry out the tasks assigned to them. As shown in the table below, there is a scope of improvement as regards centre management, LUCs and passbook maintenance ; whereas effectiveness of CGT process, CDS updation and TCO trainings can be improved with further investment in staff training

Tasks	Compliance status	Comments
Identification of target groups	😊	We found no instances of targeting error.
Group formation	😊	Done in accordance to prescribed norms
CGT	😊	Majority clients remember the core CGT messages
Maintenance credit discipline	😊	COs demonstrate zero tolerance that has resulted is negligible default
Managing centre meetings	😐	Both attendance and punctuality were not up-to the mark
Loan disbursements	😊	No instances of deviations were found
Loan utilisation Checks	😞	These were conducted with significant delays
Enforcing repayments	😊	COs ensured that centre members felt collectively responsible
CDS updation	😐	Instances of rewriting/cutting and deviation*
Training of TCOs	😐	Some TCOs require deeper handholding
Smooth collections	😊	No instances of deviations were found
Maintenance of client passbook	😐	Few passbooks were torn and shabby, with illegible writing

Annexures

1. Field Observations – Audit Data, Insurance Claim Data, Centre Attendance Data, LUC Data
2. Product Details
3. Regulatory Compliances
4. Credit Policy
5. Operational Data
6. List of branches

Annexure 1 – Field Observations

Field Observations – Centre Attendance*

Branch	Centre No.	Attendance	Attendance %
Azamgarh	124	85/114	75%
	141	34/45	76%
	165	51/68	75%
Naini	105	66/80	83%
	32	80/105	76%
	57	85/100	85%
Handia	157	53/69	77%
	162	98/118	83%
Satna	83	91/100	91%
	52	95/120	79%
	72	74/95	78%
Hanumanganj	51	69/85	81%
	6	56/75	75%
	89	47/55	85%
Majhi	2	97/115	84%
	12	84/102	82%
Chapra	114	36/50	72%
	49	49/60	82%
Patna	121	83/125	66%
	99**	55/66	83%
	235**	27/30	90%
Jalalpur	18	81/125	65%
	13	73/106	69%
	87	37/48	77%
Kasimabad	18	42/70	60%
	60	56/65	86%
	136	95/125	76%
	159***	64/90	71%

*last five fortnight's attendance

** last 3 fortnight's attendance data

*** last 4 fortnights attendance data

Field Observations – LUC Data

Branch	Total Disbursements (in May)	No. of LUCs that should have been completed before the date of visit	Actual number of LUCs conducted	% completion of the total scheduled
Hanumanganj	175	165	84	51%
Naini	142	138	86	62%
Jalalpur	182	149	106	71%
Satna	162	160	133	83%

- As can be seen from the data above the LUC is falling short of the mandated 100%. In some branches, LUCs were done only for the 51% of the branches, where as in others it was as high as 83%. However, in none of the branches visited did the LUC reach the 100% mark

Field Observations – Insurance Claim Data

Client Name	Branch	Centre No.	Date of Death	Settlement
Shanti	Handia	39	24/01/2013	08/06/2013
Shyrnkali	Handia	111	05/02/2013	08/06/2013
Baskalli	Handia	114	09/02/2013	08/06/2013
Lalti	Handia	56	16/01/2013	27/05/2013
Poonami	Handia	113	02/03/2013	30/05/2013
Rajkumari	Hanumanganj	213	30/01/2013	Data not available
Kalui Devi	Hanumanganj	186	11/02/2013	30/04/2013
Reeta	Hanumanganj	73	20/12/2012	09/04/2013
Sona Devi	Hanumanganj	32	21/12/2012	09/04/2013
Nibula	Hanumanganj	221	05/11/2012	31/01/2013
Gulabpati	Hanumanganj	67	28/11/2012	21/03/2013
Kalavati	Naini	82	21/05/2013	Not yet settled
Seeta	Naini	93	18/05/2013	Not yet settled
Ushadevi	Naini	50	17/04/2013	Not yet settled
Beena	Naini	76	Data not available	02/05/2013

Field Observations – Internal Audit Data

Branch	Date of Short Audit*	Date of Comprehensive Audit*	Key Findings
Handia	5-9 April, 2013	29 May – 5 June, 2013	<ul style="list-style-type: none"> Weak monitoring by BM especially during second half of the day
Hanumanganj	10-12 April, 2013	11-15 March, 2013	<ul style="list-style-type: none"> Pending LUCs
Naini	N/A (relatively new branch)	18-22 March, 2013	<ul style="list-style-type: none"> No major findings
Satna	10-12 June, 2013	29 April – 6 May, 2013	<ul style="list-style-type: none"> No major findings
Chapra	4-6 March, 2013	14-21 May, 2013	<ul style="list-style-type: none"> Pending LUCs Risk of multiple borrowing by the members
Majhi	N/A (relatively new branch)	29 May – 6 June, 2013	<ul style="list-style-type: none"> Pending LUCs Poor group discipline Errors in disbursement register
Patna	11-12 April, 2013	17-24 May, 2013	<ul style="list-style-type: none"> Pending LUCs Centre leaders are not being rotated
Sahjanwa	8-9 April, 2013	14-17 May, 2013	<ul style="list-style-type: none"> LUC targets of AM and BM is not getting met
Jalalpur	3-9 April, 2013	4-8 Feb, 2013	<ul style="list-style-type: none"> Pending LUCs
Kasimabad	11-12 April, 2013	1-8 May, 2013	<ul style="list-style-type: none"> Pending LUCs
Azamgarh	1-4 April, 2013	3-8 June, 2013	<ul style="list-style-type: none"> Pending LUCs

*Last Audit Date

Annexure 2 – Product Details

Product Details

Product Name	Amount (In Rs.)	Tenure	Repayment Frequency	Interest Rate	Other Charges
Utkarsh Pragati	6,000-15,000	1 Year	Option of weekly, fortnightly or monthly repayments	25.94% (Reducing balance)	Processing Fees – 1% Insurance Fees – 1%
Utkarsh Kiran	18,000-30,000	2 Year	Option of weekly, fortnightly or monthly repayments		
Utkarsh Samridhi	25,000 – 300,000				

- More than 90% of Utkarsh’s portfolio comprises of loans with fortnightly repayments
- Fortnightly repayments is the key differentiator between Utkarsh and its competitors. This product feature is most liked by the clients and also adds to the overall efficiency of Utkarsh’s operations
- Besides the credit products, Utkarsh is also piloting/planning pension products (NPS) in partnership with IFMR & a retail life insurance product (endowment).
- The non financial welfare services are under the fold of a not for profit entity named *Samutkarsh Welfare Society*. Utkarsh has provided 3% of its PBT for credit plus activities.
- The overall product suite of Utkarsh including credit, non-credit and non-financial services augurs well for differentiating it from competition and building a stable business relationship with its clients.

Annexure 3 – Regulatory Compliances

Regulatory Compliances

NBFC MFI guide lines*	Satisfy	Remarks
Maintain minimum net owned funds of Rs. 3 crores	Yes	Rs.64.3 crore - as on 31 st March, 2013
85% of the net assets should be 'qualifying' assets	Yes	93.4% - as on 31 st March, 2013
Loans for income generation purpose are not less than 70% of total loans	Yes	Integral to the credit policy of Utkarsh. Almost all the loan cases observed in the sample met this criteria
NBFC MFI does not become the third lender to any client	Yes	Integral to the credit policy of Utkarsh. All loan applications have to go through credit bureaus
Compliance with annual income of Rs. 60,000 in rural areas and Rs.120,000 in urban areas	Yes	Integral to the credit policy of Utkarsh. Checked at the time of appraisal of loans
Membership of at least one credit bureau	Yes	Membership with Highmark and Equifax
Margin cap of 12% on the loans (till March 2014)	Yes	10.2% - as on 31 st March, 2013
Capital adequacy ratio should be 15% of the risk weighted assets	Yes	44% - as on 31 st March, 2013
Provisioning norms should be higher of these two <ul style="list-style-type: none"> • 1% of the total portfolio OR 50% provisioning for loans overdue between 90-180 days +100% provisioning for loans over 180 days 	Yes	From 1 st April, 2013 onwards

*Revised guidelines for NBFC MFI issued by RBI in August 2012

Regulatory Compliances

Product features are inline with the NBFC MFI guidelines:

- ✓ Loan disbursed to a borrower with a rural household annual income not exceeding Rs. 60,000 or urban and semi-urban household income not exceeding Rs. 1,20,000
- ✓ Loan amount does not exceed Rs. 35,000 in the first cycle and Rs. 50,000 in subsequent cycles
- ✓ Total indebtedness of the borrower does not exceed Rs. 50,000
- ✓ Tenure of the loan excess of Rs. 15,000 is not less than 24 months (with no prepayment charges)
- ✓ Loan is extended without collateral
- ✓ Aggregate amount of loans, given for income generation, is not less than 75 per cent of the total loans given by the MFIs
- ✓ Loan is repayable on weekly, fortnightly or monthly instalments at the choice of the borrower
- ✓ Interest does not exceed an annual reducing rate of 26%
- ✓ LPF does not exceed 1%
- ✓ No penalty on delayed payment is charged
- ✓ No penalty on prepayment is charged
- ✓ No collection of security deposit or collateral
- ✓ Moratorium of 1 week given for every loan
- ✓ Sanctioning and disbursement of loans is done at a central location
- ✓ Loan passbook/card is in vernacular language
- ✓ Loan passbook mentions the grievance redressal number

Annexure 4 – Credit Policy

Credit Policy

Salient Features of credit policy

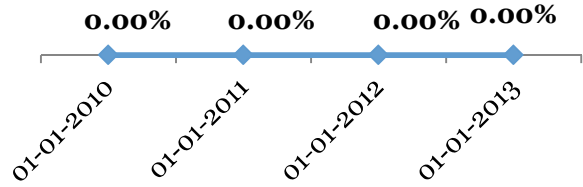
- Only women clients between the age group of 21 to 55 years are eligible to become Utkarsh members under its group loan facility
- Group size is 5 members; Centre size – 10-30 members (all the centre members are liable for loans taken by any other member in the centre)
- Client enrolment process has three core sub-processes – group formation (house visits), compulsory group training (CGT) and group recognition test (GRT)
- Key loan evaluation criteria - household should have maximum monthly income of Rs.5,000 (in rural area) and Rs.10,000 (in non rural area); household assets should not be more than Rs.20,000 (in rural area) and Rs.30,000 (in non rural area)
- Ineligibility criteria - Individuals who have outstanding loans from two or more formal financial institution on the date of application. All loans are disbursed after it has been checked with credit bureau and satisfies the above credit norms.
- No provision of top up/interim loans. At any given point in time, there can be only one active loan per client
- Field staff will not handle cash during entire loan cycle (disbursements/collections). Clients have to visit branch for all cash transactions
- Loans will be provided to eligible clients for income generation purposes only
- There is no pre-payment penalty under any of the Utkarsh loan products.
- Loan utilization checks mandatory for 100% of the disbursed loans

- In *MicroSave* team's opinion the credit policy has all the inbuilt checks and mechanisms that will ensure that credit risks are contained. Its policies on pre-payment, LUCs and strict adherence to the NBFC-MFI guidelines present a strong bulwark to counter potential credit risk events.
- However, as has been pointed out earlier as well, some measures like stricter monitoring and LUCs can further reduce the credit risk

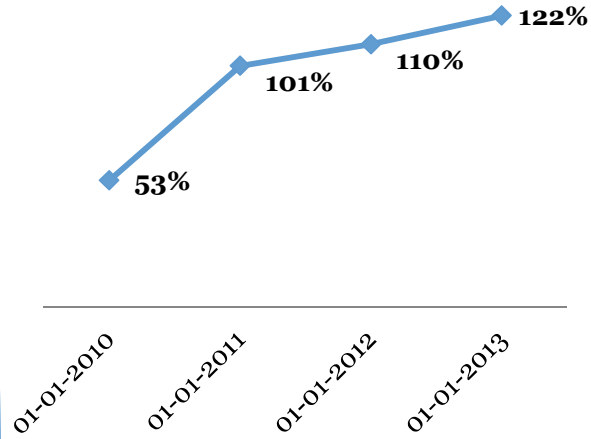
Annexure 5 – Operational Data

Operational Indicators	31/03/2010	31/03/2011	31/03/2012	31/03/2013
No. of Branches	13	52	75	102
<i>UP</i>	13	49	54	63
<i>Bihar</i>		3	21	27
<i>UK</i>				5
<i>MP</i>				6
<i>Delhi</i>				1
No. of Clients	8,208	55,506	106,371	198,181
<i>UP</i>	8,208	53,194	88,430	136,286
<i>Bihar</i>		2,312	17,941	51,182
<i>UK</i>				5,839
<i>MP</i>				4,635
<i>Delhi</i>				239
No. of Clients	8,208	55,506	106,371	198,181
<i>1st cycle</i>	8,208	34,414	71,859	125,038
<i>2nd cycle</i>		18,872	23,827	46,697
<i>3rd cycle</i>		2,220	10,462	21,051
<i>4th cycle</i>			223	5,277
<i>5th cycle</i>				118
No. of Drop-outs	78	5,024	20,202	49,590
Portfolio	63,436,480	318,557,242	753,084,511	1,782,516,075
<i>Utkarsh Navodaya</i>	63,436,480	291,831,826	14,731	-
<i>Utkarsh Unnati</i>		26,725,416	17,402,016	-
<i>Utkarsh Pragati</i>			727,246,635	1,394,289,924
<i>Utkarsh Kiran</i>			8,301,129	373,478,391
<i>Utkarsh Samridhi</i>			120,000	14,747,759

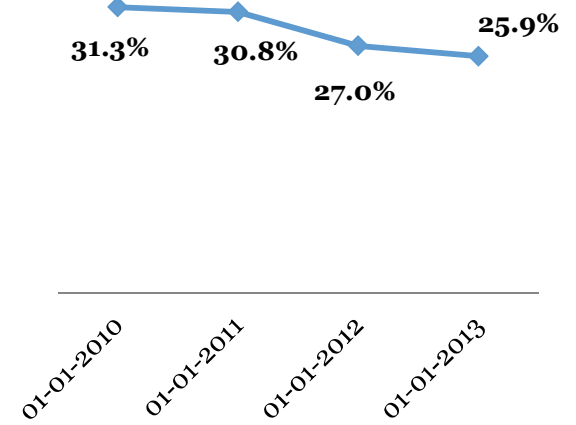
PAR > 30 days



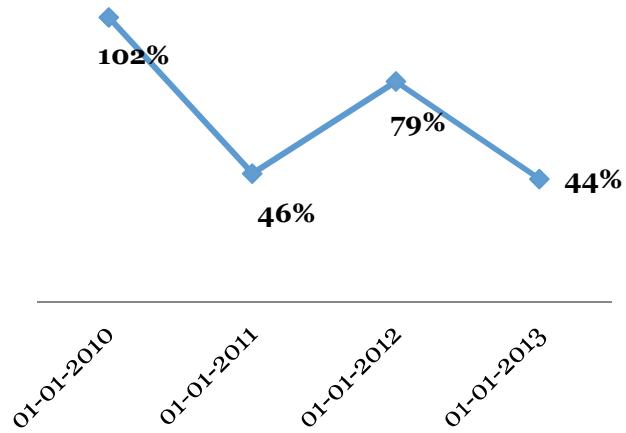
Operational Self Sufficiency



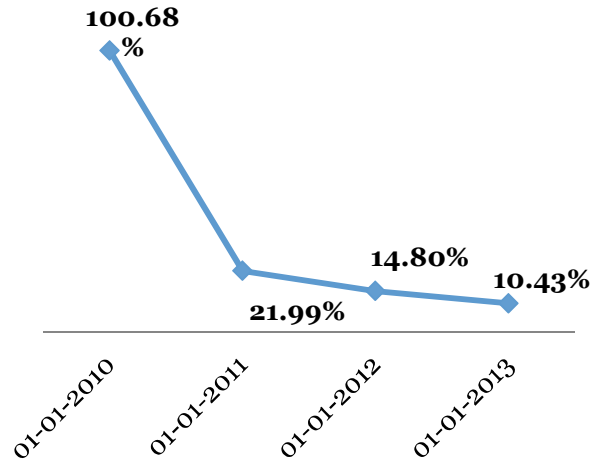
Yield on Gross Portfolio



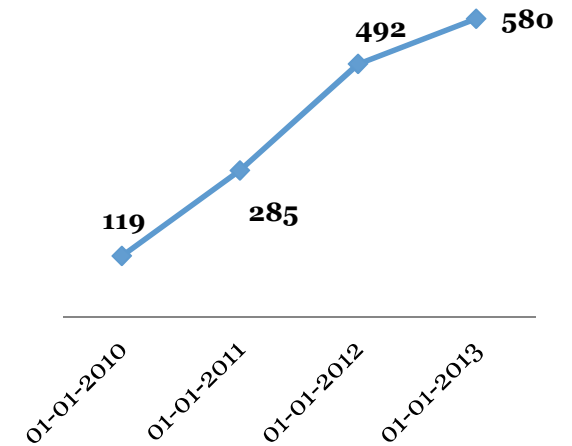
Capital Adequacy Ratio



Operating Expense Ratio



Active Clients Per CO



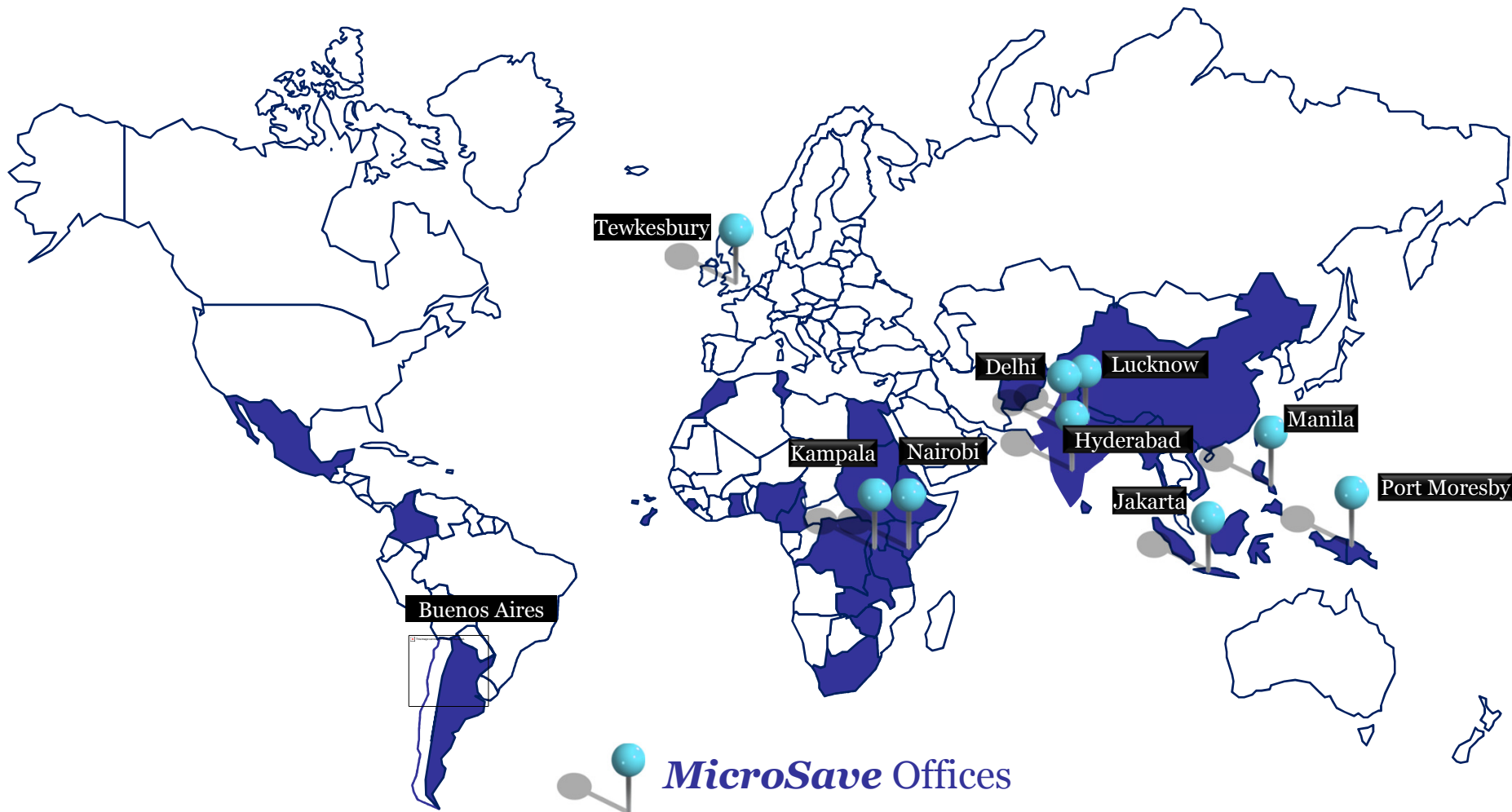
Annexure 6 – List of Branches

State-wise list of Branches

S.No	Branches	Districts	State
1	Allahabad	Allahabad	UP
2	Alopybag	Allahabad	UP
3	Gauhania	Allahabad	UP
4	Handia	Allahabad	UP
5	Hanumanganj	Allahabad	UP
6	Karchana	Allahabad	UP
7	Meja Road	Allahabad	UP
8	Naini	Allahabad	UP
9	Soraon	Allahabad	UP
10	Azamgarh	Azamgarh	UP
11	Lalganj	Azamgarh	UP
12	Mehnager	Azamgarh	UP
13	Aurai	Bhadohi	UP
14	Chauri	Bhadohi	UP
15	Gopiganj	Bhadohi	UP
16	Koirahana	Bhadohi	UP
17	Alinagar	Chandauli	UP
18	Chakia	Chandauli	UP
19	Chandauli	Chandauli	UP
20	Barhaj	Deoria	UP
21	Bhatani	Deoria	UP
22	Bhatpar Rani	Deoria	UP
23	Deoria	Deoria	UP
24	Pathardewa	Deoria	UP
25	Chandwak	Gazipur	UP
26	Dullahpur	Gazipur	UP
27	Ghazipur	Gazipur	UP
28	Kasimabad	Gazipur	UP
29	Nandganj	Gazipur	UP
30	Saidpur	Gazipur	UP
31	Chauri Chaura	Gorakhpur	UP
32	Geeta Vatika	Gorakhpur	UP
33	Gorakhpur	Gorakhpur	UP
34	Kauri Ram	Gorakhpur	UP
35	Pipraich	Gorakhpur	UP
36	Sahjanwa	Gorakhpur	UP

S.No	Branches	Districts	State
37	Jalalpur	Jaunpur	UP
38	Khutahan	Jaunpur	UP
39	Machhlishahar	Jaunpur	UP
40	Mariahu	Jaunpur	UP
41	Naupedwa	Jaunpur	UP
42	Permanatpur	Jaunpur	UP
43	Bharwari	Kaushambi	UP
44	Manauri	Kaushambi	UP
45	Hata	Kushinagar	UP
46	Bihasara	Mirzapur	UP
47	Jamalpur	Mirzapur	UP
48	Jamui	Mirzapur	UP
49	Mirzapur	Mirzapur	UP
50	Narayanpur	Mirzapur	UP
51	Putligarh	Mirzapur	UP
52	Kadipur	Sultanpur	UP
53	Kurebhar	Sultanpur	UP
54	Lambhua	Sultanpur	UP
55	Sultanpur	Sultanpur	UP
56	Ashok Vihar	Varanasi	UP
57	Chaubeypur	Varanasi	UP
58	Harhua	Varanasi	UP
59	Jansa	Varanasi	UP
60	Kakarmatta	Varanasi	UP
61	Panchkoshi	Varanasi	UP
62	Sigra	Varanasi	UP
63	Sindhora	Varanasi	UP
64	Umaraha	Varanasi	UP
65	Varanasi	Varanasi	UP
66	Herbertpur	Dehradun	UK
67	Prem Nagar	Dehradun	UK
68	Haridwar	Haridwar	UK
69	Jhabreda	Haridwar	UK
70	Roorkee	Haridwar	UK

S.No	Branches	Districts	State
71	Arrah	Bhojpur	Bihar
72	Behea	Bhojpur	Bihar
73	Jagdispur	Bhojpur	Bihar
74	Barhampur	Buxar	Bihar
75	Buxar	Buxar	Bihar
76	koran sarai	Buxar	Bihar
77	Purana Bhojpur	Buxar	Bihar
78	Bhabua	Kaimur	Bihar
79	Durgawati	Kaimur	Bihar
80	Kudra	Kaimur	Bihar
81	Ramgarh	Kaimur	Bihar
82	Bihta	Patana	Bihar
83	Danapur	Patana	Bihar
84	Dehri-on-sona	Rohtas	Bihar
85	Kochas	Rohtas	Bihar
86	Nokha	Rohtas	Bihar
87	Piro	Rohtas	Bihar
88	Sasaram	Rohtas	Bihar
89	Baniyapur	Saran	Bihar
90	Chhapara	Saran	Bihar
91	Dighwara	Saran	Bihar
92	Garkha	Saran	Bihar
93	Madhuara	Saran	Bihar
94	Majhi	Saran	Bihar
95	Mashrakh	Saran	Bihar
96	Parasa	Saran	Bihar
97	Sonepur	Saran	Bihar
98	New Delhi	New Delhi	Delhi
99	Mangawan	Rewa	MP
100	Mauganj	Rewa	MP
101	Rewa	Rewa	MP
102	Amarpatan	Satna	MP
103	Maihar	Satna	MP
104	Satna	Satna	MP



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