



# BUSINESS REVIEW

October 2014 | First Edition

Social Impact Bonds

*Pg 03*

Microfinance : The Bandhan Way

*Pg 05*

Benefits of Using Logical  
Framework Approach in Social  
Development Sector

*Pg 08*

Is Discounting the Only Way  
to Sustain an E-commerce  
Business?

*Pg 11*

The Economics of Technical Debt

*Pg 14*





*Bandhan Financial Services was set up in 2001 to address the dual objective of poverty alleviation and women empowerment.*

*IIM Calcutta PGPEX students had the opportunity of interviewing Mr. Chandra Shekhar Ghosh, Chairman and Managing Director, Bandhan.*

---

## MICROFINANCE: THE BANDHAN WAY

---

**Why don't commercial banks lend to near zero income groups? Is it because of the lack of collateral/security?**

For low-income individuals, either they don't have assets or their assets (e.g. the house where they stay) are not treated as collateral / security by commercial banks. But do they have potential? Yes, of course they do. It depends on the mentality of the bank to understand and evaluate the credit-worthiness of the individual. Most financial institutions in India are happy lending to the top 10%

Micro Finance Institutions (MFIs) treat those bottom layer individuals as potential customers and create a viable business model out of extending credit to them.

The viability, however, depends on evaluating the

borrower's need and unveiling its business potential rather than validating her current asset credibility. The evaluation is a 4-step process to understand:

- the borrower's purpose/motivation in seeking a loan
- the area in which he/she would like to work
- basic credibility of the individual in his village/ neighbourhood
- Know Your Customer (KYC) – as per statutory guidelines

**How does Bandhan mitigate the risk associated with lending?**

You will be surprised to know that, so far, Bandhan has managed to keep the bad debt at a meagre 0.07%

- Bandhan ensures that only one loan is given to a person at a time. Generally the repayment period is within a year.

- Bandhan staff assesses the potential borrower's credibility and evaluates the realistic amount of credit needed. "To me, this is a critical success factor. If you lend Rs. 3,000 to an individual needing Rs. 30,000 and vice versa, both will default," says Mr. Ghosh.

- The representative visits the borrower within 15 days from the day of disbursement to check whether the funds are being used properly and again within 15 days after the loan has been repaid to understand future requirements, if any.

- Staff are selected and appointed in such a way that their working area is at least a 2 hour commute from where they stay. This ensures unbiased loan disbursement and collection.

- Stronger bonds develop between individuals having similar background, income and language. Bandhan acknowledges this and encourages such person-person bonding.

### **How does Bandhan keep transaction costs down?**

The transaction cost at Bandhan is higher than commercial banks but lower than other MFIs. When an individual goes to the bank, his cost of transportation (howsoever minimal) is not borne by the bank, whereas MFI collectors go to the individuals and hence the cost of transportation is incurred by the MFI rather than the borrower. This works to the borrower's advantage however throwing tremendous challenge on Bandhan to reduce the cost of transaction.

Bandhan reduces the transaction cost by:

- Encouraging group collection / transactions

### **• Employing HTMs not ATMs**

For an Automated Teller Machine (ATM), the operational monthly expenses are around Rs. 30,000 including rent, electricity, security, transport of cash, servicing etc. The cost per transaction is calculated as Rs. 13.

The average Monthly Salary of a loan officer (or Human Teller Machine) is Rs. 10,000 only.

Consider a staff servicing 4 groups per day with 25 working days in a month, break-even will occur at Rs. 100 (i.e. Salary of Human Teller 10,000 / (4 times 25)). This means that even 10 borrowers at Rs. 10 per borrower's transaction cost can reach the break-even. In reality, the number of customers is much more which brings down the unit transaction cost even further.

**"The transaction cost at Bandhan is higher than commercial banks but lower than other MFIs."**

- Employing the right person for the job e.g. graduates employed through competitive exams at commercial banks want high salaries and / or facilities for rural postings. The field staffs at Bandhan are employed from among the strata of society they serve. Their salary / facility expectations are lower and they better understand the needs of the borrowers and also develop much closer relationships.

### **How is the staff motivated at Bandhan?**

All employees are permanent with salary, provident fund, and gratuity. A Loan Officer reports directly to his/her Branch Manager.

Total employee strength: 13,280 (July, 2014)

Loan officers: 10,000+

Bandhan understands the importance of change

management, especially after recently obtaining an approval for 'in-principal banking licence' from the Reserve Bank of India. It encourages team involvement and ensures transparency and effective communication across the organizational structure since inception.

Most of the staff members have a basic level of education. Due to lack of suitable employment opportunities, they use to sit idle and were not regarded well by society. In Bandhan, they are trained loan officers with permanent employment and salary. Not only they earn livelihood for themselves and family, they also gain respect from society. One of the staff members said, "When I go to remote areas as a staff member of Bandhan, everybody says Namaste. This keeps me motivated".

### **How did the recent economic recession affect Bandhan?**

There was no direct affect as the impact of the recession at the bottom level of the pyramid was much less than at higher levels. However, when the real-estate sector was hit by the recession, many labourers were laid off from their job and couldn't send money back home. This had an indirect effect.

### **What regulatory or policy support does Bandhan require from the Government?**

MFIs are often indistinguishable from chit-funds for the public. People are still quite reluctant to deal with them especially due to recent cases of chit-fund scams. Government policies and regulations should support MFIs in creating a general awareness about the sound credibility of MFIs. The recent recognition from the Reserve Bank of India in the form of an approval for 'in-principal banking licence' for Bandhan acts as a pat on the back and is a step in the right direction.

### **What are Bandhan's plans for business expansion?**

Bandhan plans to expand its business in clusters, but as an amoeba and not as a frog. The organization believes that until and unless it has covered at least 60% of an area, it will not be able to bring the impact and level of development required.

The organization wants to leverage on the strong network that it has developed across rural area in other sectors.

As interviewed by:

**Abhisek Bhattacharya** and **Raghvendra Upadhya**  
**PGPEX 2015**

## **BANDHAN EFFECT**

A woman in Bagnan, Howrah district of West Bengal, was stranded with two daughters after her husband passed away. She borrowed Rs. 3,000 rupees to set up her own tailoring shop. A year later, she has not only repaid the loan, but also made a net savings of Rs. 27,000. Her younger daughter is in XI standard while the elder one is now studying in a college in Kolkata.

