PERSPECTIVA

A Case Research Journal
Volume VII (2021)

Creation of a Vibrant Business Environment for Micro and Small Enterprises (Small Ticket Business) - A Case of Social Finance Ltd

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Abstract

This case study is an attempt to facilitate the students to understand the process flow of easy finance facilities offered to small businesses in developing countries like India. The existing financial system, which is still insufficient to cater to the mass population of India, has loose ends wherein the small businesses are forced to source finance from unorganized sector with hefty interest rates. This study is prepared after closely observing and interviewing the management, employees and customers of a well-established non-banking finance company registered in India, having pan India presence. However, to keep the anonymity of the organisation a hypothetical name Social Finance Limited is given and the names of the officials in the case study are also changed. However, the figures representing the financials are presented from the published sources.

Keywords: Non-Banking Finance Company, Micro Credit, Lending Process, Credit Appraisal, Asset Quality
JEL Codes: G21, G23, G50

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Introduction

Mr. Sohan was eagerly waiting for Mr. Aloysius to remit the daily interest on the loan which Sohan took from a local money lender. Mr. Aloysius is the collection agent and used to come around 1.30 PM every day. Sohan took a loan of Rs.50,000/ three weeks ago and the daily interest to be paid was Rs.1500/ until the principal is repaid. Sohan's revenue from his restaurant on that day was Rs.3,000/ and Sohan kept Rs.1,500/ exclusively marked for the repayment of the interest on loan. As a borrower, Sohan was very much thankful to Mr. Aloysius and his boss for providing the timely financial assistance. Without that, Sohan would have closed out his business.

The restaurant is on the wayside to one of the famous tourist spots in Central Kerala and the customer base was enriched with people from all social classes including celebrities. The restaurant is famous for its tasty, delicious and traditional Kerala menu. It was about 2 PM; Mr. Gilbert George, director of Social Finance Ltd., a registered non-banking finance company (NBFC), entered the restaurant to have his lunch. Mr. Gilbert was on his return journey after finishing his visits to certain branches and Regional office. While Mr. Gilbert was enjoying his lunch, Aloysius came to the restaurant and Sohan gave Rs.1,500/ and Aloysius made a small tick mark on a book which was kept in his trousers' pocket. Aloysius left the place without saying anything and Sohan also resumed his business. Mr. Gilbert was quietly observing these and was curious to know the details.

While paying for the check of his lunch, Mr. Gilbert asked Sohan about the transaction he just observed from a distance. Being a humble and innocent villager, Sohan was not hesitant to share the details and Mr. Gilbert understood the entire story. Mr. Gilbert left the place after appreciating Sohan for the tasty, delicious food and reminded him about the vested responsibility of maintaining the quality and taste. On his way back to Kochi, Mr. Gilbert was thinking about Sohan's transactions and there was no need for any calculator for the seasoned banker to understand the implied interest rate which was exorbitant. Mr. Gilbert was really worried about the masses like Sohan across the length and breadth of India. Despite having a strong financial system million of Sohans' are being exploited by these money lenders. Mr. Gilbert George, as the director of one of the fastest growing NBFCs in India, decided to find a solution using their wide branch network.

India is a large country with the second largest population is having a robust financial system. However, considering the population, the financial system with its intermediaries and/or service providers is facing difficulties to cater the masses. The Banking sector is predominantly servicing the nation with 18 Public Sector Banks, 22 private Banks and 46 foreign banks and their vast network of 116394 branches and 53 regional rural banks, 1,542 urban cooperative banks and 94,384 rural cooperative banks as of September 2019 (Source-IBEF website- Banking Sector analysis). Apart from the mainstream banking sector, the Government of India has identified Non-banking financial companies (NBFC) as the torch bearers of the system to reach out to the nation. With 11,522 registered NBFCs through their nationwide branch network, NBFCs help the system to achieve the objectives of financial independence and inclusion. Still, the existence of unorganized sector, including the indigenous money lenders, proves that the network of banks and NBFCs are not sufficient enough to cater the entire population of the country and there are still possible ways to enhance the efficiency of the system. Table 1 shows the branch network of Indian Banks.

Ignition of a spark:

The Indian corporates are legally bound to spend 2% of their net profit towards corporate social responsibility activities. However, the threshold limit is applicable such as only those entities which have either (1) a minimum net worth of Rs.50 billion or more, or (2) turnover of Rs.100 billion or more, or (3) having net profit of Rs.50 million or more are coming under this statute. As a corporate, Social Finance Ltd is coming under the threshold level and it is contributing towards the societal development through the Social Welfare Foundation.

However, Mr. Gilbert George, as a frequent traveller, felt that the places he visited across India were lacking something. The small businesses across the places were not prospering and the big ones were growing. When the growth opportunities for the *'aam-aadmi'* (common man) is still an unachievable dream, it's difficult for a country to progress and a proper plan to deliver to the small businesses run by the '*aam-aadmi'*. The basic idea was to cater the needs of such small businesses and partnering in their growth story. The Sohan incident that Mr. Gilbert had personally experienced resulted in fuelling the fire further more. The limitations that people like Sohan have can be multi-dimensional. Access to the organized banking system can be difficult, if at all happened to get an access; it will be difficult to get small business loans without collaterals. Adding more to the difficulties list, enormous time lag is consumed for getting the loan sanctioned from a commercial bank, whether in public sector or private sector. And people like Sohan have to visit the bank branches multiple times to get a loan sanctioned; if at all banks are providing such loans.

All these inefficiencies of the existing set up lead the small business owners to get credit facilities from unorganized sector. Unfortunately, these small businesses are not considering the NBFCs as a provider of business loans or working capital loans. The challenge here is to overcome these hurdles and to reach such business class to provide business credit without disturbing their business model or business days. Mr. Gilbert George shared the story of Sohan to his fellow directors in the board of the company and presented his idea of assisting the small ticket businesses in and around and thus partnering in their success. He convinced the board to venture into the micro and mini size business finance where the risks are higher than the normal business finance offered by Social Finance Ltd. However, the centre of attraction of the scheme is the uplifting of such businesses and owners.

The way forward to pursue this task was not a smooth highway; rather it was stacked up with obstacles everywhere. A change in the mindset of all the stakeholders was the first requirement. Starting from the management, all the stakeholders including the employees need to understand the importance of the task and act accordingly.

Process flow design:

The new initiative must have a pre-defined process flow and it has to be flawless one. Mr. Gilbert George assigned the task to his team and made Mr. Santhosh Mohandas (Associate Vice President-Operations) as the team leader. The entire idea was briefed in detail to the team as Mr. Gilbert believed that one can execute a task only if he or she understood the plan completely. The Associate VP was given the task of designing the process flow with the clear description of the time and cost involved in each stage of the process. The task for Mr. Santhosh was clear and he started envisaging the required process flow. He took the help of Mr. James Joseph, his team mate for this purpose. They have started their discussions and the conversation went like:
James: Good Morning sir. I am at your service.
Santhosh: James… Mr. Gilbert George wants me to design a process flow for his new business idea. I need your assistance for the same.
James: Of course. What's the new plan?
Santhosh explained the idea to James and both of them ensured that nothing left behind while explaining things.

James: Really!!! The idea is good. But I don't see any requirement for a new process flow. We can very well adopt the existing one here too. Can't we?
Santhosh: No James… We need to have something new here. Our existing customers can afford to have employees and they can engage them for visiting our branches for servicing the loans or they can even opt for online payments. Here I don't think that our target group can really afford this luxury.
James: Ohhh… that's right. We need to think about it. Sir, why can't we engage our field staff to get the repayment EMIs?
Santhosh: That can be done. But they are already having their schedules fixed. Let's see … How these customers are fitted to their area. Our Officers will have to spend more time on the field. Any way, we don't want the customers to disturb their business and visit our branches. We will send our team to them.
James: Shall I suggest something? Why can't we restrict the geographical limits initially? We will identify customers in the 500 metres locality around the branch.
Santhosh: Sounds good….
James: In that case, our officers need to spend only a little time for these customers. We can even schedule their visit timings so that the customers can arrange the money ready with them.
Santhosh asked James to wait there in his cabin and went to Mr. Gilbert George to share the idea. Mr. Gilbert liked the idea and asked to James to join them in his cabin.
Mr. Gilbert George: I am happy that you are moving in the right direction. What I am suggesting is to expand the geography from the 500 metres to 2 kilometres radius. Our Branch managers and Credit managers know their territories well and can really view such businesses. Each and every up and down of such businesses can be observed by our team and in case, they can even assume the role of a mentor and help these business owners to grow.
James: That's right sir. In that case, all our employees can visit them and instil confidence in them.
Mr. Gilbert: Okay. Then what about the other processes? Design one as early as possible.
Santhosh and James discussed further and came up with an initial process flow.
They have designed a process with four main stages viz., Pre- Sanction stage, Sanction & Fund Transfer stage, the Post Sanctioning stage or the Project functioning stage and finally the Closure and Add-on Stage. (Starts with the identification and profiling of the customers and the documentation and sanctioning of the loan). The process flow is shown in Exhibit II and Exhibit III.
Each of these stages is to be re classified into sub stages and the rules and guidelines are to be set for each of these stages. As an organization into the financing activities, one has to make the system fool proof and expose it to the frequent audits and cross checks. The sub stages involved are shown in Exhibit III.

Collection Mechanism:

The Social Finance Ltd has decided to make the repayment schedule in compatibility with the nature of the business of their customer. The nature of the business of the borrower was considered as the determinant for the repayment interval fixation. The hotels and food stall owners found it convenient to have a daily repayment scheme whereas the Garment stitching and small boutique kind of business preferred a weekly schedule. It was finalized that Equated Weekly Instalment (EWI) and Equated Daily Instalment (EDI) can be offered to the customers. The businesses that opted for the advances found it easier, as an organization like Social Finance is coming to their doorsteps to sanction loans, collection of repayments and even for getting add-on loans or second or tertiary stage of funding and ultimately help them grow. Since the Social Finance team's advice regarding the daily conducting of the business was also sought by the customers, the satisfaction level of the staff also increased beyond levels.
The model of this 2 kilometres radius business is having certain advantages for Social Finance as an organization. The customer base is expanding and more and more small vendors and business men are approaching them for financial assistance. Since the loans are

granted to the businesses within the vicinity of the existing branches of Social Finance, it's easy to observe the business and analyse the changes in their working pattern. Officers from Social Finance can visit these places without incurring any additional operational costs to the organization and all these visit timings are pre-arranged as per the convenience of the borrowers.

The onus is now with the entire team to build on the structure and to extend the reach of the Social Finance Ltd 2 kilometres lending to the community so that progress and development in the society become a reality.

The loan amounts in the first cycle of advances are limited from Rs.20,000/ to Rs.30,000/, and this can be expanded up to Rs.400,000/ in fourth or fifth cycle of the loan. The service aspect of this initiative becomes a success only when the borrower prefers to utilize his next cycle of advancing.

In 2018, Mr. Gilbert George revisited the restaurant of Sohan and found visible changes there. By this time, Sohan has utilized his fifth cycle of advance and realizing that the growth in his business is very much connected with the organized way of getting advances from Social Finance Ltd. The company is doing the 2 kilometres loans throughout India through its 3500 plus branches. Social Finance Ltd has decided to cater a large population through the 2km radius small business finance model and also decided to increase the exposure levels.

Conclusion

Servicing the under privileged businesses were not only a socially responsible business model but it proved to be profitable too. The product was designed in such a way that that it will not increase operational costs. The customers proximity towards branch ensured operational efficiency and asset quality. This kind of product design can ensure a win – win situation for both banker and customer.

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Exhibit I: Distribution of Branch Networks of Banks

Sr. no.	Type of bank	Number of Branches				
		Rural	Semi-Urban	Urban	Metropolitan	Total
1	Public Sector Banks	29,033	25,647	17,890	18,875	91,445
2	Private Sector Banks	4,822	7,803	5,158	6,878	24,661
3	Foreign Banks	9	9	39	231	288
Total		**33,864**	**33,459**	**23,087**	**25,984**	**116394**

Source: RBI database (March 2017)

Exhibit II: Different Stages of Financing

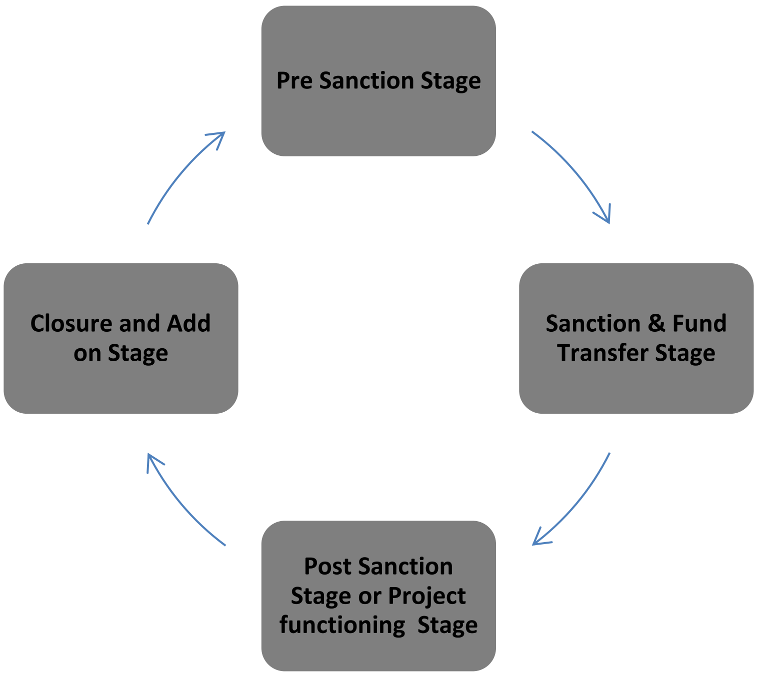

Exhibit III: Stages of Financing

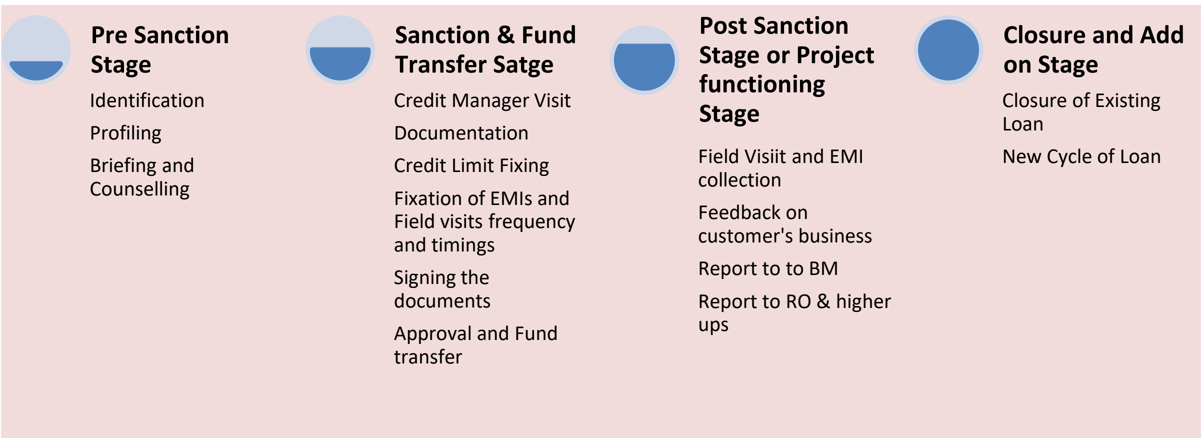

Exhibit IV: Branches and the business

Year	No of Branches	Average AUM per Branch (INR Crores)	Average Customers serviced per day across branches (Nos)
2014-15	3699	2.26	50,000
2015-16	3645	2.44	83,000
2016-17	3483	2.97	85,000
2017-18	3572	3.20	137,000
2018-19**	3530	3.21	137,000

*Source: Annual Reports & ** Directors Report 2018-19*

Exhibit V: Gross Income per Branch *(Amounts in INR Crores)*

	Gross Income (GI)	No of Employees	GI/Branch	GI/Employee
2014-15	2039	15289	2.76	0.13
2015-16	2085	14992	2.60	0.14
2016-17	2105	15436	2.52	0.14

Source: Collated from the financial statements

Exhibit VI: Operating Expenditure per Branch *(Amounts in INR Crores)*

	Opex	No of Employees	Opex/Branch	Opex/Employee
2014-15	739.80	15289	0.20	0.048
2015-16	801.90	14992	0.22	0.053
2016-17	835.92	15436	0.24	0.054

Source: Collated from the financial statements