

Welfare Society of Eastern India*

A **TOFFE** Risk Assessment Report from

CREDIT WĀTĀĀHTM

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Executive Summary

WSEI is an NGO with solid record of developmental work for over a decade and microfinance activities over the last six years. WSEI has accomplished commendable *reach* in a relatively short time. It has a reasonable level of operational *efficiency* and a high level of financial and organizational *sustainability* with a high level of social capital. The only dimension in which WSEI has considerable room for improvement is in the operation of its formal Management *Information System* and Internal Control Systems.

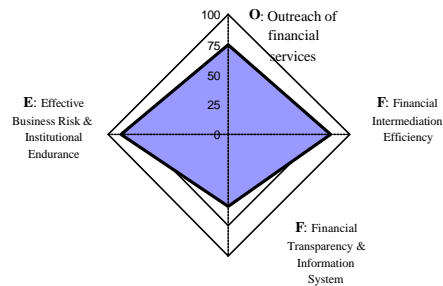
NGO Risk Analysis for BRWAS

Overall rating	AA (low risk)			
Dimensions	O	F	F	E
Score	75	85	60	90

O: Outreach of financial services
F: Financial Intermediation Efficiency
F: Financial Transparency & Information System
E: Effective Business Risk & Institutional Endurance

Max score: 100

The TOFFE Diamond



About TOFFE:

Over 500 NGO-MFIs are engaged in financial intermediation in different parts of India. These NGOs are mainly engaged in promoting Self-Help Groups (SHGs) and their federations at the cluster level and linking SHGs with Banks under the NABARD Bank Linkage Scheme. As bank managers come under increasing pressure to extend lending to NGO micro finance, their problem becomes *how to identify NGOs/SHGs, which are trustworthy and efficient for the limited financial intermediation under the bank linkage programme*. **TOFFE** (Test on Outreach of financial services, Financial Intermediation Efficiency, Financial Transparency & Information System and Effective Business Risk & Institutional Endurance) is *Creditwatch's* **NGO Risk Assessment Tool** designed for this purpose. As opposed to most standard rating systems, the TOFFE appraisal system pays attention to the developmental aspect of the MFIs as well as their financial viability and sustainability.

* Name Changed

I. Background

Introduction

Welfare Society of Eastern India (WSEI)* is an NGO operating in the South 24 Parganas district of West Bengal with a substantial microfinance program along with other developmental programs. Started in 1990 as a branch of the Kolkata-based Welfare Society, WSEI was incorporated as an independent society under the West Bengal Societies Act XXVI, 1961 on August 18, 1994. While WSEI is active in several areas of development including health, literacy, legal and family counseling, mental counseling for children; microfinance has emerged as its primary activity in recent years. The mission of WSEI includes bringing the poor and backward people into the mainstream of society by improving their socio-economic conditions; achieving socio-economic and political empowerment of women and removing gender inequality; helping every individual attain her fundamental rights; creating health, education and social consciousness among the poor and backward; protecting women and children rights; developing a fully literate, unpolluted and healthy society; and to develop agriculture by application of modern technology. Its focus groups consist of deprived women, children and the elderly people.

From beginnings in providing primarily health services, WSEI ventured into microfinance around 1995 and seriously began expanding its microcredit operations from 1997. Thus it has attained its commendable reach in a span of only about six years.

People

WSEI currently consists of 35 voting members who elect a Managing Committee comprising 11 members from amongst themselves every three years. The President, Executive Secretary, Assistant Secretary and Treasurer are members of this Managing Committee. The 17 member staff of WSEI reports to the Executive Secretary and their time is allocated between the different projects. In addition there are volunteers aiding in the functioning of WSEI. The present Managing Committee has five founder members while there are 20 founder members among the 35 voting members. WSEI requires that members of its managing committee cannot hold any political position. WSEI is also guided and assisted by a five-person Advisory Board including a well-known consumer activist and an advocate (but no microfinance expert) as well as a healthcare specialist.

The Executive Secretary Mr. Shyamal Mondal* is the effective executive head and leader of WSEI and is the initiator as well as driving force behind its microfinance activities. Mr. Mondal has a B.Com (Hons.) degree and has previously worked briefly for several NGOs including Palli Unnayan Samiti, Baruipur; Ramakrishna Mission Narendrapur's microfinance project, Jeevan Deep; and Bani Mandir's US-assisted microfinance project SAHAY. Mr. Mondal, 31, has been associated with WSEI since 1993 and has served as its honorary secretary from 1994 through 2001. In 2001 he took up the newly formed full-time position of the Executive Secretary.

* Name changed

Economic Environment

The area of operation of WSEI is largely characterized by agriculture, animal husbandry – dairy (cows) followed by poultry – and some sea-fishing activities. There are no major handicrafts in the area though the Rajarampur *gamchha* (towels) from the area are pretty well known. Petty business and trading provide livelihood to another considerable section of the population. The area is located within a couple of hours railway commute from Kolkata. Consequently, a number of poor women from the locality work as domestic help in Kolkata households. Organizing these commuting women into SHGs has proven to be a challenge. While there is no dearth of poor people in the area, the poverty situation in the area as a whole is marginally better than the more arid districts of West Bengal as well as the average Indian situation. Currently a major port at Kulpi is under construction. Completion of the port is expected to give a significant boost to economic activity in the region.

II. Scoring of WSEI on different dimensions of TOFFE

Outreach of financial services

As a microfinance institution, WSEI organizes people into SHGs, helps them develop a regular saving habit, provides “inter-loans” from the funds generated from these savings, and, most importantly, acts as an intermediary between banks and SHGs, borrowing funds from banks and lending them on to the SHGs. It also forms SHGs to connect them to the government’s Swarna Jayanti Gram Swarojgar Yojana (SGSY) whereby the groups get relatively large injection of government funds channeled through banks into their group accounts, with some incentive for the sponsoring NGO as well. At present WSEI runs 106 SHGs under the SGSY scheme and about 159 SHGs under its “*Swanirvar*” scheme under which it acts as a financial intermediary, borrowing funds from a bank and on-lending them to the SHGs.

The total number of people covered by the Swanirvar SHGs is 1381 while that for the SGSY scheme is 1291. 222 people are covered in the 15 “old age” SHGs run by WSEI. The current year has witnessed a sharp reduction in the number of borrowers from 687 in March 2002 to 332 in March 2003. Part of this reduction is caused by the more careful screening criteria being used by WSEI.

Financial Intermediation Efficiency

Under its Swanirvar project scheme, WSEI charges 24% rate of interest on loans and pays 5% on deposits. It receives funds from the bank (UBI) at about 12% rate of interest. Operating expenses for the Swanirvar project during the year ending March 2003 amounted to about Rs. 1.16 lakhs. For the previous year, the figure was Rs.1.05 lakhs. Given the mid-year loan size of about Rs.6.63 lakhs for the Swanirvar (i.e. non-SGSY) project and mid-year total savings of about Rs. 10.15 lakhs for the same project in the year ended 2003, this translates to a transaction cost of 6.90% of combined loans and deposits (17.46% of loans alone and 11.40% of deposits only).

Score on Efficiency factor:
85/100

For the previous year the mid-year loan figure was about Rs. 6.26 lakhs and the mid-year deposit figure was about Rs. 8.94 lakhs. Thus costs amounted to 6.93% of combined loans and savings (16.81% of loans alone and 11.78% of deposits only).

For the year 2002-2003, the recovery rate has been about 95%, which is quite commendable. Historically the figure has always been higher than 95%. Given the considerable size of the organization and the scale of its operations, this is a commendable performance.

***F*inancial Transparency and Information System**

WSEI produces annual financial statements and gets them audited. As far its own finances are concerned, WSEI maintains clarity and transparency. An equally important issue is of internal control system and management information system so that the NGO can detect lapses and monitor repayment performance of its SHGs on a continuous basis and in time for any action, if necessary. WSEI maintains an extensive MIS through its widespread network of volunteers as well as its close rapport with villagers. However this system is oral and informal. Its written, formal and periodic reporting does not capture problems with SHG payments till three monthly payments are missed, which may be too late in certain cases for avoiding a default. In terms of internal control too, the managing committee is not always on top of key financial ratios about its SHGs and its overall performance. Several of the standard sustainability indicator ratios are not routinely calculated and analyzed. Fortunately, the recovery rates have been high and these lacunae have so far not affected the performance of WSEI but they are likely to prove critical to the future performance of the organization.

Score on Transparency and Information System factor:
60/100

***E*ffective Business Risk and Institutional Endurance**

The sustainability aspect of an NGO is as important as its efficiency and reach. The issue of sustainability has at least two major aspects – financial and organizational.

Score on Sustainability factor:
90/100

Financial sustainability

With regard to *financial* sustainability, it is important to note that WSEI generated a surplus of Rs.26,644 in March 2003. The corresponding figure was

Rs.41,160 in the preceding year.

WSEI maintains a diversified portfolio of assets including significant fixed deposits with banks, farm and other small machinery that reduces its dependence on its loan performance for survival to some extent. According to its own estimates, WSEI has a portfolio at risk (non-payment for over 60 days) of about Rs. 25,000 (about 3.77% of its mid-year loan amount). It is important to note that this amount is less than the current surplus generated by WSEI and is, therefore, well within acceptable limits.

Of late, in a special effort to reduce portfolio risk as well as to control operational expenses, WSEI has substantially scaled back lending. During the financial year ending

March 2003, WSEI lending has dropped from over Rs. 8.57 lakhs to slightly over Rs. 4.68 lakhs, a reduction of over 45%! The organization is now focused on quality lending and cost effectiveness rather than indiscriminate expansion.

Organizational Sustainability

As for organizational sustainability, we focus on the employee retention and motivation at WSEI, the criticality of the key personnel and their likelihood of continuing with WSEI. In recent years WSEI has seen relatively low turnover among its staff and has succeeded in retaining 17 from the 25 hired so far. It takes special conscious measures like annual outing of all staff and managing committee members to improve employee motivation and morale. Operating with the help of several motivated volunteers and periodically training these volunteers internally, it keeps a reserve pool of manpower to draw from in case of loss of staff. The managing committee itself has remained dedicated to the cause with regular elections. The executive secretary, Mr. Shyamal Mondal, however, plays a pivotal role in the operation and success of WSEI. Being from the Singhapur* village itself and having practically built up the microfinance activities of WSEI on his own initiative, he has no plans of moving away from the organization in the near future. However, in case he leaves the organization, his is likely to be a difficult post to fill. The organization will then have to hire a new executive secretary *from outside* and the new hire would require substantial time, effort and ability to build the rapport and knowledge of Mr. Mondal.

Competition

As a financial service provider, WSEI faces limited competition from existing banks, a few other NGOs and moneylenders. In the formal sector, there are about 10-12 bank branches in the area of operation of WSEI. Three commercial banks – UBI, Allahabad Bank and Syndicate Bank – operate in the region through their *Grameen* branches. Two major co-operative banks, West Bengal State Co-operative Bank and West Bengal Co-operative Agriculture and Rural Development Bank also lend to people in the region. In addition there are several Primary Agricultural Credit Societies (PACS) that are active in the region. WSEI, however, has considerable advantage over these credit outlets in its closer relationship with the villagers and ease of credit access. On the informal sector side, moneylenders continue to function in the area, charging rates ranging from 10-24% per *month* and occasionally even 2% per *day*. These rates are exorbitant compared to 24% per *annum* charged by WSEI. Given its considerable size and history, WSEI combines a credibility level close to that of the formal sector and low interest rates with the accessibility and flexibility of the informal sector. It has developed extensive and deep level of trust among the common villagers through its provision of health services and other developmental activities. This has resulted in a committed and loyal customer base in its area. A few other NGOs had emerged in the area and had sought to compete with WSEI largely on interest rates. However, most of them have failed and effectively wound up operations.

* Name changed.

Intangible assets and ‘social capital’

The assessment of a microfinance institution remains incomplete in the absence of an understanding of the level of trust and ‘social capital’ it has developed among its clients. Social capital, while difficult to measure and quantify, plays a key role not only in its goodwill, reputation and growth but also in the success of its day-to-day functioning, dealings with SHGs and loan recovery.

WSEI is extremely strong in this respect. Being in operation for well over a decade and assisting villagers in almost every important aspect of their lives, it has developed a very high level of trust and understanding in the villages where it functions which stands in good stead in its microfinance practice. Its healthcare services particularly maternity treatment services have brought it close to the poor rural women – its microfinance clientele. Its literacy programs and child and family counseling services have also made inroads into poor households and have opened up the space where poor women can feel comfortable discussing their lives and livelihoods and domestic finances with their staff. This comfort level and trust takes years to build but serves as a pivotal asset for successful penetration and growth of microfinance. WSEI has been reaping the advantage of its synergistic developmental activities and much of its rapid growth so far can be attributed to this deep well of social capital.

III. Rating and Recommendations

Overall Rating and summary evaluation

On the basis of the scores obtained by WSEI on the different dimensions, we arrive at a rating of **AA** (“double-A”) for the organization (please refer to Annexure I for the rating system and detailed methodology applied). This rating signifies that WSEI is a *low risk* NGO. In fact it is just shy of the highest rating possible in the TOFFE system, **AAA** (triple-A) signifying *minimal risk* and is recommended for funding by banks and other funding agencies – international, domestic government as well as private and non-profit sources – for further expansion and growth.

WSEI is an NGO with solid record of developmental work for over a decade and microfinance activities over last six years. In terms of reach, WSEI has accomplished commendable levels over the short time-span of its activities. It has high level of financial and organizational sustainability and a reasonable level of operational efficiency. Its level of intangible assets in the form of “social capital” or trust is extremely high and this is a very positive feature of the operation of WSEI. The only dimension in which WSEI has significant room for improvement is in the operation of its formal Management Information System and Internal Control Systems. WSEI present system of internal accounting and MIS, with its reliance on informal and occasionally ad-hoc measures has served it adequately because of the superior performance of the SHGs developed by it. However, the same system may not be able to detect and signal problems at an early stage if and when such problems arise. However, of late, WSEI is working to bring about significant changes in this area of its operations moving from more informal MIS methods to standardized, written and formal systems. Overall then WSEI is a professionally run organization that has remained loyal to its mission and made commendable achievement that can move to even higher grounds by making a few changes in its MIS and internal control mechanisms.

Recommendations

On the basis of a detailed analysis of WSEI, we believe that the organization should pay greater attention and invest more resources to devising appropriate internal control mechanism and developing an effective and regular MIS. These are absolutely necessary features for an organization that has reached the size and reach of WSEI and will help it grow further from this stage.

Among other areas, WSEI may consciously work towards a succession and backup strategy, so that it reduces its dependence on one or more key individuals without instigating undue rivalry and competition in the managing committee. Also more members of the managing committee should take closer interest in the details of the functioning of the organization. This is admittedly a difficult proposition, and it is natural for the committee to develop a reliance on a whole time paid executive particularly if the executive happens to be a highly effective individual. However, developing greater participation from a larger number of members is key to organizational endurance and organic growth.

While the current focus on operational efficiency and maintaining loan quality is very important, WSEI must also seek to maintain a minimum loan disbursement target and reach so as to retain the developmental thrust of the microfinance endeavor.

Finally social capital and trust constitute the most important assets for WSEI. It must be conscious of this fact and careful in maintaining and nurturing this 'social capital'. Reputation and trust take years to build but can be lost overnight. A single case of abuse or embezzlement of funds or improper conduct on the part of an employee can have very serious implications for the future of its microfinance operations and the survival of SHGs. Consequently WSEI should remain forever vigilant on this aspect of its operations and take care to keep building and sustaining its intangible "Social Capital" as it has done in the past.

Annexure – I**The TOFFE NGO Risk Classification System – Interpretation and Methodology**

The different **risk categories** of the TOFFE System with explanatory remarks:

<u>Rating:</u>	<u>Interpretation:</u>	<u>Remarks:</u>
AAA	Minimal risk of loss/failure	Excellent opportunity for funding
AA	Low risk	Recommended for funding
A	Some risk	Fund with restrictions/provisions
A-	Considerable risk	A possible future funding opportunity
B	High risk	Not recommended for funding

Methodology in brief:

The TOFFE system scores an NGO on the following four dimensions:

- O: Outreach of financial services
- F: Financial Intermediation Efficiency
- F: Financial Transparency & Information System
- E: Effective Business Risk & Institutional Endurance

Each dimension is scored out of 100. An overall score is then computed taking into account the *average* as well as the *minimum* of the four scores. If the minimum is 50 or above, then the overall score is the average itself, else it is the minimum score.

The conversion from the overall score to the actual rating is as follows:

<u>Overall score:</u>	<u>Rating:</u>
80 and above	AAA
65 – 79	AA
50 – 64	A
35 – 49	A-
35 or below	B