EMERGING TRENDS AND SHIFTS IN MICROFINANCE

Insights From A Multi-Stakeholder Study on the Impact of the Reserve Bank of India's Microfinance Regulatory Framework, 2022

A Joint Study by Dvara Research and Sa-Dhan

Fostering Inclusive Impact Finance

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Contents

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SUMMARY

The Reserve Bank of India (RBI) in March 2022 introduced The Regulatory Framework for Microfinance Loans, 2022, a decade after the earlier regulations of 2012[1] . The 2012 regulations were the first set of regulations by the RBI in the microfinance space, which came in the aftermath of the 2010 microfinance crisis. Thus, expectedly, it had a heavy prudential bent. The new regulations of 2022, however, are more open-ended and seek to enhance uniformity, responsibility and flexibility in the microfinance sector.

This study sought to understand the impact of the new regulations on the microfinance sector through the lens of different categories of stakeholders – customers, leadership at microfinance institutions (MFIs) and intermediating staff. Given the relatively mature market landscape[2] and the vastly varied customer cohorts that the microfinance sector is currently serving, the impact of the newly ushered regulations is bound to be uneven. By contrasting and comparing the perspectives and experiences of diverse stakeholders, we hope to glean a wholesome understanding of the different pathways through which regulatory changes are operating to repurpose, reposition and reorient the sector.

[1] The earlier regulations followed the Malegam Committee Report of 2011
[2] RBI Consultative Document on Regulation of Microfinance, 2021

1. INTRODUCTION

1.1 The New Regulations

The new regulations of 2022 depart from the 2012 regulations in certain specific areas and seek to provide adequate customer protection guardrails to microfinance borrowers. Tabled[3] below are some key regulatory changes that look to harmonise norms for various categories of lenders, provide enhanced customer protection, and allow competitive market forces to find an equilibrium.

	Pre – 2022 Regulations	Post - 2022 Regulations	Stated Objective[4]
Applicability	NBFC-MFIs	All entities working in the microfinance space, including SCBs, SFBs, NBFCs, NBFC-MFIs, and Non-Profit MFIs.	Addressing regulatory arbitrage
Microfinance Loan Qualification	• Collateral-free • Rural annual Household Income less than Rs. 60,000 (Later revised to Rs. 1,25,000) • Urban and semi-urban annual household income less than Rs. 1,20,000 (Later revised to Rs. 2,00,000)	• Collateral free. • Annual household income less than Rs. 3,00,000 for rural and urban customers.	Protection of borrowers from over-indebtedness
Household Income Assessment	No stated requirement to assess household income	• Board-approved policy for household income assessment • Indicative methodology for household income assessment • Mandatory submission of this information to Credit Information Companies (CICs). Discrepancies with existing numbers, if any, should be clarified, and CIC should be updated accordingly	
Repayment Obligation	Total indebtedness less than Rs. 50,000 (Later revised to Rs. 1,25,00)	Total monthly loan repayments should not exceed 50% of household's monthly income	
Pricing	• Caps on margins • Cap on maximum lending rate	• No cap on interest rates • Well-documented interest rate model that is board-approved • Interest rates shall be non-usurious and subject to supervisory scrutiny by RBI	Enabling competitive forces to bring down pricing
Limits on Loan Amount	Loan amount less than Rs. 35,000 in first cycle (later revised to Rs. 75,000) and not exceeding Rs.	No explicit limit on loan amount	Facilitating flexibility to design products/services

[3] The table seeks to highlight some of the prominent differences between the 2012 and 2022 regulations, and is not comprehensive in its coverage

[4] Keynote address delivered by Shri M. Rajeshwar Rao, Deputy Governor, Reserve Bank of India – November 04, 2022 - at the launch of MFIN's India Microfinance Review at Mumbai

	50,000 in subsequent cycles (later revised to Rs. 1,25,000)		
Limits on Loan Tenure	Not less than 24 months for loans exceeding Rs. 30,000 with prepayment without penalty	No explicit tenure norms or limits.	
Limits on Lenders	Not more than two NBFC-MFIs can lend to the same borrower	No explicit limit on the number of lenders.	
Loan End Use	Income generating loans is not less than 50% of the total loans given by the MFIs	No explicit requirement for end-usage	
Qualifying Assets Requirement	85% of net assets	75% of total assets	
Disclosures	Loan card with loan related information like interest rate, T&C, etc. in vernacular language	• Standardised Key Facts Statement with information about loans, grievance mechanisms, etc., in the local language apart from loan cards. Any fees charged are to be explicitly mentioned. • Acknowledgement of repayments • Sale of non-credit products should be made with the consent of the customer • Details of Grievance Redressal system to be provided to customers • Disclosures of interest rate ranges on websites	
Recovery	Fair Code of Conduct and some limits on customer follow-ups to ensure non-coerciveness	• Board-approved Fair Practice Code • Clear definition of harsh practice with time limits for house visitations • Dedicated grievance redressal for recovery • Mechanism for identification of distressed borrowers and provision of guidance about available recourse to such borrowers	Enhancement of customer protection measures
Responsibility for fair practice	NA	• Board-approved policy for employee conduct and system for recruitment, training and monitoring of employees • Accorded responsibility for all outsourced activities, including that of recovery agents	

This study looks to assess the impact of the new regulations on the microfinance industry and to understand how the industry is reshaping its policies and practices to comply with the new regulations.

In the following sections, we will delve into how three different stakeholders – MFI management, field staff, and customers – are experiencing the new regulatory regime and adapting to its changes.

1.2 Study Design

1.2.1 Sample MFIs

Dvara Research, in partnership with Sa-Dhan, engaged with a select set of 13 MFIs who consented to participate in the study. Of these MFIs, four can be categorised as small MFIs (with loan portfolio less than Rs. 100 crores), three as medium MFIs (between Rs. 100 crores and Rs. 500 crores), two as large MFIs (between Rs. 500 crores and Rs. 2000 crores), and four as very large MFIs (greater than Rs. 2000 crores). These participating MFIs have operations spread across different geographies and represent almost all regions[5] – Bihar and Uttar Pradesh in North, Odisha and West Bengal in East, Maharashtra and Rajasthan in West, and Karnataka and Tamil Nadu in South. Further, there is a representation of diverse forms of legal incorporation, including non-profit MFIs (registered as Section 8 companies), societies, and trusts.

1.2.2 Categories and Profiles of Stakeholders

We interviewed three categories of stakeholders in the microfinance sector:

(i) *30 interviews with Senior Management of MFIs*
Including Chief Executive Officers (CEOs), Chief Operating Officers (COOs), and Heads of Risk Management and Regulatory Compliance across all 13 participating MFIs.

(ii) *90 interviews with Field Staff of MFIs*
Including Field Officers, Branch Heads, Regional Managers, from 7 participating MFIs across all four regions.

Most interviewed field officers have been in the microfinance sector for less than five years, while branch managers and regional managers have between five and ten years of experience in the sector. Typically, field staff have been with the participating MFI for less than two years, while the more senior staff have been with the MFI for around five years.

Most have a bachelor's degree, and some have master's degrees. A few are secondary school or diploma graduates, especially in the Southern region. Almost all were either from the same or nearby districts as their service districts. A few who were not from nearby districts were however from the same state.

(iii) *Survey of 771 customers*
Including customers of 10 participating MFIs across all four regions.

[5] North-Eastern states were not covered in this study.

Three types of customers were surveyed – (a) customers whose loan applications were rejected, (b) customers with active loans and regular repayments, and (c) customers who were delinquent and went through the MFI recovery process.

As for these customers' occupation categories and vintage, most of the respondents were self-employed in agricultural and non-agricultural activities for their livelihood. 35% of these respondents have been microfinance customers for less than 2 years, 43% for 2 to 6 years, and 22% have more than 6 years of engagement with MFIs.

1.2.3 Study Administration

The interviews with MFI senior management were conducted virtually[6] between February and September 2024, while the interviews with field staff were in person[7] at the MFI's branch or regional offices conducted between August and September 2024. The customer survey was a combination of in-person[8] and telephonic[9] interviews conducted in September 2024 using customer data obtained from participating MFIs[10].

2. THE SUPPLY SIDE PERSPECTIVE

The senior management of all MFIs welcomed the new regulations and deemed them a step in the right direction. While there was some degree of dissonance with regard to the narrow leeway now available for non-qualifying assets, a fixed household income limit for all geographies, and the removal of the cap on the number of NBFC-MFI loans per borrower, the assessments were mostly positive about the changes with regard to household income assessment, information disclosures, limits on repayment, removal of pricing caps, etc. Moreover, all the MFIs expect the new regulations to create a level playing field. Even with varying costs of funds, diverse scales of operations, different levels of digitisation and overhead costs, diverse legal incorporations, and concentration in different geographies, they all look forward to competing on an equal footing. This signifies the ample flexibility afforded by the new regulations for different categories of MFIs to play to their strengths - be it operational efficiency, competitive costing or product innovation.

In this section, we will present insights from interviews with 30 senior executives from all MFIs that participated in the study with a specific focus on the new regulations.

[6] Long-form interviews lasting between 1 hour to 1.5 hours.
[7] Long-form interviews of 1 hour each.
[8] Semi-structured long-form interviews lasting 30 to 45 minutes.
[9] Structed short survey of 15 minutes.
[10] The 771 customers surveyed were split between in-person and telephonic surveys, and not all data points are available for all customers, due to differences in the nature of the two modes of the survey and the different categories of customers interviewed. Furthermore, some survey responses were compromised by the inability of respondents to either understand or answer the questions effectively. All insights from customer survey reports sample sizes for the specific question/data point under consideration.

2.1 Qualifying Income Limit

"Income levels vary from region to region. Household income limit could be linked to the state GDP or per capita income."

- CEO of a medium MFI

MFIs are welcoming of the increased threshold of Rs. 3,00,000, given that the old limit was outdated and not in sync with the present realities of the MFI customer segment. MFIs find that though a uniform limit is easy to implement, there are wide variations in incomes across different states, and a single limit makes a relatively large section of their mature clients ineligible in relatively better-developed states, particularly in South India.

Some MFIs offer prospective customers whose income exceeds the Rs. 3 lakhs threshold, loans under their non-qualifying assets book, while other MFIs reject such loans. The intended graduation of customers to regular financial services happens at different income levels in different parts of the country. It is contingent upon the levels of development and cost of living in that region, and many MFIs believe that any income limit for MFI loans should ideally incorporate such differences.

2.2 Household Income Assessment

"Household income is a big black hole."

- CEO of a large MFI

All MFIs, including small ones, have developed some tool or process to capture household income that they rely on to underwrite loans. Notwithstanding the RBI's indicative methodology, the data points that MFIs use for measuring household income vary widely. Some MFIs do corroborate self-reported income data with expenditures or household assets, but it still remains an unscientific exercise whose outcome is heavily influenced by the skill and incentive of the last-mile agent.

There is a lack of clear documentation to act as proof of income, and customers provide ballpark figures that are difficult to validate. This is further complicated by the informality, seasonality and unpredictability of income sources that typically characterise the MFI customer segment. Furthermore, operational considerations around prohibitively long questionnaires for underwriting small loans for groups of 4 to 6 women make the process time-consuming, costly and somewhat tiresome for field officers. This, along with the aligning of interest to give a loan for the field staff and to take a loan for the customer, results in some massaging of numbers to ensure eligibility for loans.

The current methodology is seen to be moving the needle on this difficult problem of household income assessment. Some MFIs were conducting some form of household income assessment even before the regulations, but the processes and methodologies varied greatly and the new regulations are seen to be streamlining this process across MFIs. However, the data so collected is far from reliable or accurate. Some MFIs are experimenting with methods to use data on assets, crops grown, occupations, etc., to extrapolate income numbers using internal benchmarks. However, these statistical prototype mapping techniques are still not accurate given the diversity of contexts encountered in different parts of a single state, let alone the country.

Credit bureau records are used to cross-verify incomes reported by customers. Still, in case of mismatch or discrepancies, there is currently no way to ascertain whether the self-reported income or the income recorded with the credit bureau is the actual reality of the customer at the time of querying. Furthermore, it is not easy to raise a red flag with the credit bureau on any disproportionate income figures in their records.

MFIs are hopeful that the uptick in their customer segment's usage of digital finance will start generating alternate sources of data about their cashflows that could be tapped to better understand household incomes and, hence, repayment capacities.

2.3 Repayment Capacity Assessment

> *"We follow the 50% FOIR rule diligently. But once we lend, the customer may borrow from elsewhere, and the FOIR is violated. This fluctuation is possible because income assessment is not scientific."*
>
> - CEO of a medium-sized MFI

MFIs are seen to be relying heavily on credit bureau records to validate household loan obligations, and most use the RBI limit of 50% FOIR (Fixed Obligation to Income Ratio[11]) to ascertain loan eligibility. However, vestiges of past regulations present themselves in how some MFIs choose not to lend to customers who already have outstanding loans from two other MFIs despite their total monthly loan repayments remaining below the 50% limit. In fact, one MFI was found to be an outlier in choosing to be more prudent by setting its internal Fixed Obligation to Income Ratio (FOIR) limit at around 30% well below the RBI-mandated limit of 50%.

Most MFIs report using comprehensive credit bureau records, but some MFIs resort to using MFI-only records, which limits information to just MFI loans. Even with comprehensive credit bureau records, MFIs have little visibility over certain types of loans, such as gold loans, SHG lending, cooperative society credit, Kisan Credit Card outstanding, FinTech loans, etc. This reduces their ability to calculate accurate repayment obligations, and they have to rely on self-reported loan data to arrive at the customer's FOIR. Furthermore, some customers (sometimes in collusion with MFI staff) are seen to be using multiple IDs to avail loans from different lenders. As a result, loan obligations get split between different IDs in credit bureau records, making FOIR calculations grossly inaccurate.

MFIs also have various internal rules about not lending to customers who are delinquent or have outstanding payments, that is, say, 30 days past the due date, etc. However, credit bureau records get updated with a significant lag for overdue or payment settlements, and this inevitably leads to errors in any new loan approval process. Certain kinds of loans, like SHG loans, which get split between all members, get recorded incorrectly (if at all), wherein the whole quantum of the loan shows up as loan amounts for each SHG member individually. This artificially inflates the FOIR, and the branch staff has to use their discretion to clarify this issue and then make a decision to lend.

[11] The Fixed Obligation to Income Ratio is a term used by the industry and not by the RBI. It is used to refer to the limit on monthly repayment obligations as mandated by the RBI.

Moreover, information about informal loans (not limited to just loans from money lenders, but also those from friends and family) is not sought out during repayment capacity assessment. The general belief or expectation is that in a Joint Liability Group (JLG) model, group members who have greater visibility over each other's financial lives would automatically weed out customers with unsustainable levels of informal borrowings. However, this blind spot is hardly acknowledged in repayment capacity assessment in any meaningful manner.

Most MFIs have seen substantial increases in rejection rates due to the 50% FOIR requirement, especially since loans of all household members need to be incorporated in the FOIR calculation. This is particularly true for mature customers who are in their fifth or sixth cycle of loans and are being rejected now for crossing the 50% FOIR limit. While most MFIs view this as a challenge for customer retention and group formation, some MFIs expect this to be a positive move for the microfinance sector to reach out to the genuinely underserved segments.

2.4 Pricing

"What is usurious? Come up with a formula that can be applied to all entities based on their cost, profile and geography. MFI borrowers are not price sensitive. What the borrowers are looking for is how fast we can give them the money."

- Managing Director of a medium-sized MFI

Interest rates have seen a marked upward trend since the lifting of the price cap by the new regulations. Most MFIs view this positively, given the rising cost of funds associated with rising *repo* rates. Public Sector Banks (PSBs) charge between 13% and 14%, while Non-Banking Finance Companies (NBFCs) charge anywhere between 15% and 19% to lend to MFIs. Past losses from the COVID-19 pandemic are also leading to increased write-offs and, hence, increased risk premiums. Further, operations costs are also on the rise owing to deteriorating group cohesion post the COVID-19 pandemic, which is changing the nature and frequency of customer engagement. All these have contributed to an average increase of about 300 to 350 bps in lending rates since the pandemic. Except for one very large MFI with diverse sources of funds (from domestic banks to international development organisations) that is able to lend at rates between 22% and 23.5%, the typical interest rate charged by most MFIs ranges between 24% and 27%. Almost all MFIs believe that rates have now become market driven.

Some observe that funds are flowing into the sector to capitalise on the increased interest rates and the apparent insensitivity of customers to interest rates in this sector. This is reportedly happening alongside the rising costs of operations post the COVID-19 pandemic. Another oft-repeated view among senior management is that customers are more focused on fast loan turnaround than on lower interest rates.

Furthermore, MFIs are not seen to be offering differential pricing for different categories of customers due to the potential impact on group dynamics and the operational complexity involved. A few MFIs are offering lowered interest rates for mature customers who have been consistent with their repayments over multiple loan cycles. Still, the price differential does not go past 50 bps. Notably, a couple of MFIs expressed a willingness to offer lower interest rates for digital payments.

2.5 Loan Usage

> *"If we start insisting that they invest money in the purpose for which they have taken the loan, the entire system will collapse. They are tending to their priorities from the loan funds."*
>
> \- COO of a very large MFI

MFIs view the repeal of productive end-use mandates positively. They believe that this reflects the reality of how loans are currently used and that restrictions on end-use are difficult to implement or monitor.

However, some are critical of its impact and consider this to be a dilution of microfinance's social impact purpose. They opine that if microfinance is to become some form of a personal loan, then the sector needs to contend with making significant changes to its design and approach.

2.6 Competition and Number of Lenders

> *"There is intense competition, but it is not reflected in the interest rates provided to borrowers."*
>
> \- CEO of a very large MFI

Nearly all MFIs complain that the market is overcrowded, with multiple MFIs operating in the same region. However, this intensity of competition is not leading to better interest rates or better services. Instead, turnaround times (TAT) for sanctioning loans are taking centre stage, and MFIs are competing with each other to service the same borrower. Instead of expanding access in newer geographies, MFIs are deepening their presence in the same geography due to difficulties in setting up shop in virgin markets and the opportunities opened up by the removal of the cap on the number of lenders. Though lenders are making efforts to follow the FOIR limit, customers borrowing from multiple lenders simultaneously, creating an intensely competitive market, making it challenging to follow FOIR limits after a certain point. Many MFIs are calling for reinstating the earlier cap of not more than two lenders per borrower, which had a moderating effect on the levels of competition.

2.7 Disclosures

> *"Customers are now well-trained. They can't calculate or compare interest rates, but they are able to compare EMIs of different lenders."*
>
> \- COO of a small MFI

MFIs have not witnessed any significant change in their approach towards information disclosure or customer sensitisation with the new regulations. Most MFIs report that their prior loan cards had most of the required information as prescribed by the RBI in the new regulations. Despite the largely positive view of the newly introduced Key Facts Statement, its potential impact on customer awareness is expected to be muted since this is dependent upon different pre-existing factors like the customers' levels of education, financial sophistication, language comprehension and literacy, etc.

MFI staff train customers on the terms and conditions of the loans during Compulsory Group Training (CGT) and Group Recognition Training (GRT), which is typically reported to be effective enough to sensitise customers about loan features. KFS, then, is expected to act as a tool for comparing the rates offered by different MFIs.

Some MFIs are also of the view that MFIs cannot be made responsible for customer education since it runs counter to the incentives of the business and that this responsibility would sit better with the likes of Self-Regulatory Organisations who are operating for the greater good of the sector as a whole.

2.8 Recovery

> *"MFIs need the concept of deferred performing assets that would be viewed differently from a non-performing asset. These would cover those indicating genuine distress."*
>
> - CEO of a medium-sized MFI

All MFIs use some form of persuasion to induce customers who are overdue to pay up. Typically, field staff apprise customers about the implication of overdue (OD) payments on their credit score and, therefore, their ability to borrow in the future. In most cases, this method seems to work, and customers ensure repayment through some means.

Targets for repayments on MFI staff ensure that there are regular follow-ups with OD customers by staff of various cadres, from field officers and branch managers to regional heads. All efforts are extended to prevent OD accounts from turning into non-performing assets (NPAs). Some MFIs state that rules around asset classification restrict their ability to help customers tide over genuinely difficult times like hospitalisation, job loss, etc. While some MFIs restructure loans for such customers, others don't.

Weak group cohesion that is seen post the stress of the COVID-19 pandemic makes it near-impossible to invoke group liability. Recovery, therefore, has become focused on the OD client with little recourse to the support of other group members. The nature of persuasion remains cordial and empathetic when the customer is seen to be in hard circumstances. Most instances of untoward behaviour during recovery happen in cases of wilful default or when ringleaders become involved.

Most recovery decisions—be it follow-ups, OD/NPA categorisation, restructuring, or write–off—are very contextual and made on a case-by-case basis in consultation with field staff who have visibility over the customer's circumstances.

2.9 Fair Practice Code and Training

"Frauds and attrition are increasing. We now have to become process-driven rather than human-driven."

\- CEO of a large MFI

All MFIs conduct initial training for their field and other staff at the time of recruitment, and the period of dedicated training typically varies between 7 to 15 days. These trainings focus on marketing, customer acquisition, household income assessment, credit underwriting, conduct, Fair Practices Code (FPC), etc., and cover the requirements of the new regulations. Many MFIs have designed Standard Operating Procedures (SOPs) for customer engagement that incorporate the FPC. In some cases, it goes to the extent of a standard script for customer interaction that is designed to be respectful and informative for the clients.

Although training is generally considered necessary and useful, the internalisation of these rules and knowledge is reportedly unclear. Most staff members build the necessary skill set and acumen on the job over some time. Therefore, most MFIs also offer refresher training at set intervals.

High attrition is a common problem cited by almost all MFIs. The demanding nature of the job is oftentimes difficult for new entrants to adjust to, and the phenomenon of moving between different MFIs for salary hikes also contributes to the high levels of attrition.

Technology is also used to standardise specific processes and reduce any arbitrariness in customer engagement. Furthermore, surprise branch audits are conducted to reduce the risk of personnel-related fraud, which is reportedly on the rise. Stringent oversight with a clear chain of command from the field to the district/region/state/head office helps maintain a good standard of service.

2.10 Grievances Redressal

"Grievance reports go all the way to the board."

\- CEO of a large MFI

Most MFIs have two kinds of grievance redress mechanisms – (i) a centralised toll-free number with call recordings that provide remote assistance and follow-ups with the relevant redressal authority within the organisation and (ii) a branch/region level contact person who would provide swift assistance that can be in-person or telephonic as needed. These contact details are published in customer loan books and at the branch office.

Most MFIs implicitly refer to the centralised toll-free number as the dedicated grievance redress mechanism for recovery-related grievances as stipulated by the new regulations. This could perhaps stem from the understanding that most recovery-related grievances would need to be registered away from the local branch, and the centralised mechanism automatically offers a pathway to do that. MFIs report expediting these complaints, bringing them to the attention of the highest authority within the organisation and ensuring consequences for staff engaging in untoward recovery practices.

3. CUSTOMER EXPERIENCE

Customers in the MFI ecosystem are passive recipients of the impact of any new regulations. While regulations are made with a keen focus on customer welfare, their implementation on the ground can take many forms, leading to unexpected and unintended outcomes. In our survey of 771[12] customers of the three categories —those whose loans were rejected, those who were regular with payments, and those who were delinquent—we find that while customer awareness about regulations is expectedly limited, MFIs follow the regulatory mandates for the most part.

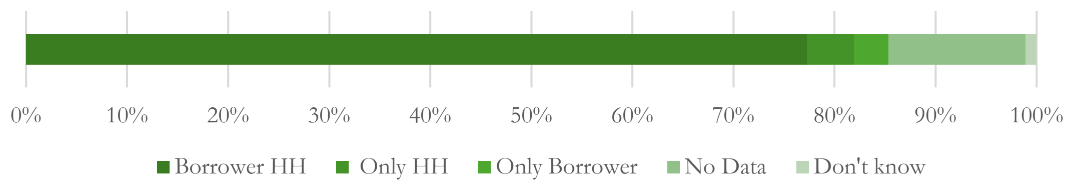
In this section, we will present some key insights from the survey of 771 customers with a view to understanding customers' experience of the new regulations.

3.1 Procedures for Loan Access

3.1.1 Household Income

Almost 82% of surveyed households reported that their household income data was collected at the time of loan application. However, while 3.4% of customers said that only their own income data was collected, another 13.6% reported that no information on household income was collected.[13]

Figure 1: Type of Income Data Collected



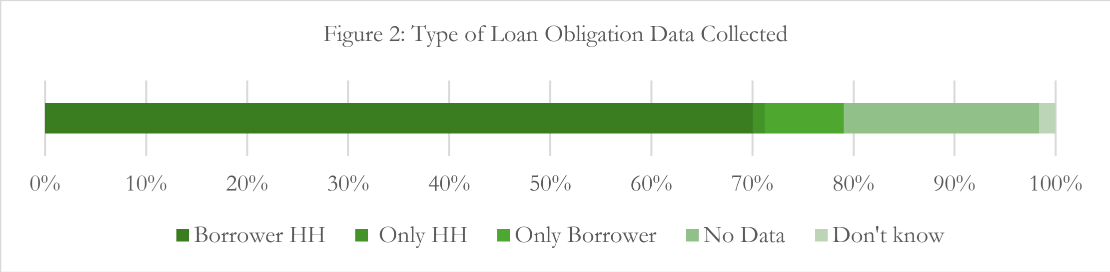
Sample Size: 758

3.1.2 Loan Obligations

While around 71% of responding customers said that the outstanding loan obligations of the entire household were collected, 7.8% said that only their own loan obligations were collected, and 19.4% said that information on their loan obligations was not collected at all.

[12] Although 771 customers were interviewed in total, not all customers answered all questions. Three sets of questionnaires were created for the three different categories of customers, with many overlapping questions and some dedicated questions based on whether they had experienced loan rejection or default. Furthermore, in certain cases, particularly in telephonic interviews, some customers did not understand a few questions and hence chose not to answer. Therefore, the sample for different data points will vary and the sample size for the reported statistic has been mentioned in the footnote to each graph.

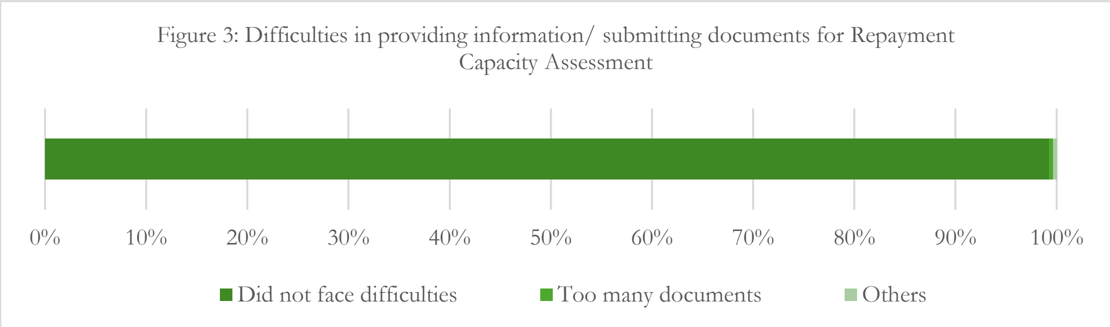
[13] Borrower HH implies that the relevant information for both the borrower and the household was collection. Only HH or Only Borrower denotes that only the household level information or only borrower level information was reportedly collected.



Sample Size: 758

3.1.3 Documentary Requirements

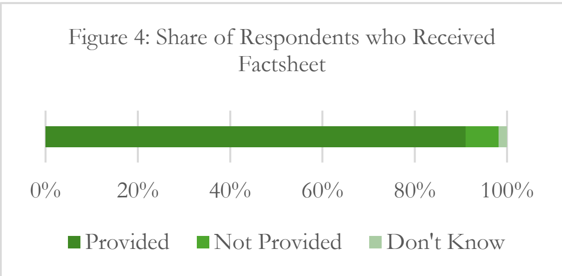
Almost all queried respondents maintained that they faced no difficulty in submitting any requested documents.



Sample Size: 283

3.2 Information Disclosures on Loans

The provision of fact sheets and payment schedules is relatively high, at around 91% and 93%, respectively. However, the provision of loan agreements is relatively lower, at around 82%. Of those who received any of these three documents, around 75% confirmed being able to comprehend the provided documents, while the rest could mostly not read or write.



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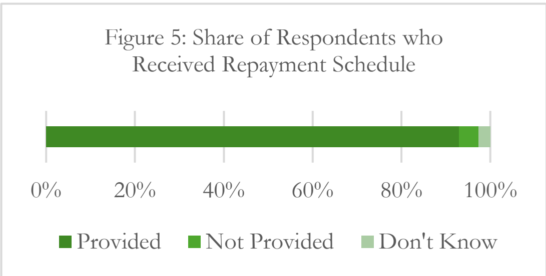
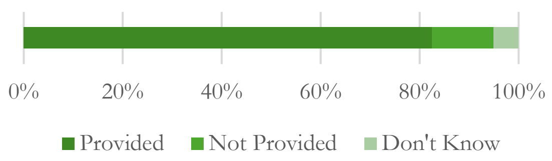


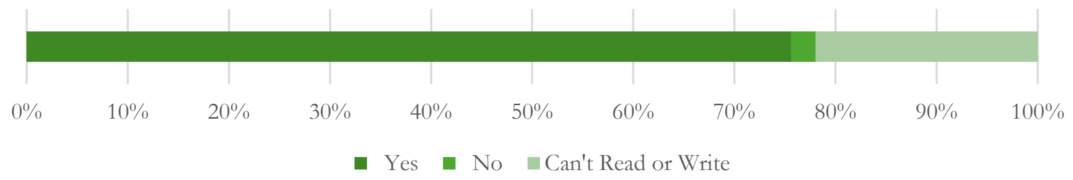
Sample Size: 758

Figure 6: Share of Respondents who Received Loan Agreement



Sample Size: 758

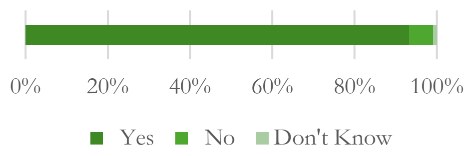
Figure 7: Comprehension of Loan Document Language



Sample Size: 758

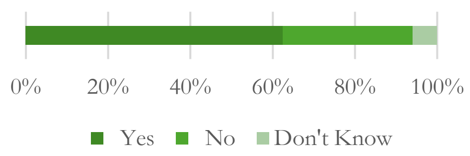
Around 93% of respondents confirmed that the MFI staff explained the terms and conditions of their loans. However, only around 62% of customers were explained the details of the MFI's grievance redressal system.

Figure 8: Share of Respondents who Reported Explanation of Loan T&C by MFI Staff



Sample Size: 757

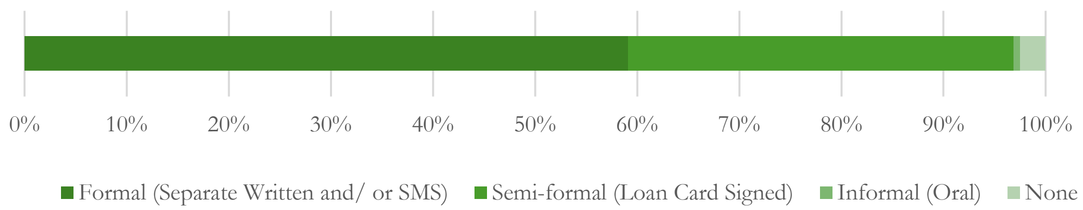
Figure 9: Share of Respondents who Reported Explanation of GR Contact by MFI Staff



Sample Size: 761

Around 60% of customers report receiving formal acknowledgements for their payments, while around 38% receive signed loan cards that could be construed as semi-formal acknowledgements.

Figure 10: Type of Repayment Acknowledgment Received

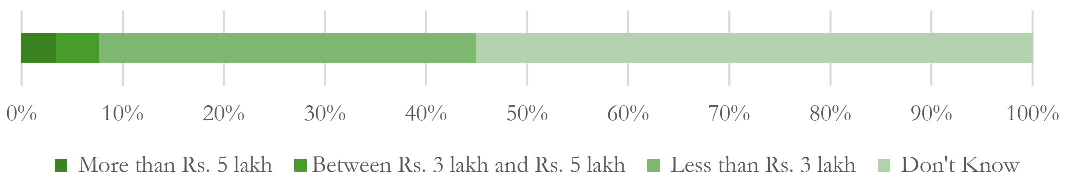


Sample Size: 758

3.3 Awareness about Regulations

Customers are seen to be aware of the new regulations to some extent. Around 37% of the respondents knew the income limit of Rs. 3 Lakhs, 55% reported not knowing about the limit at all, and the rest mentioned incorrect limits.

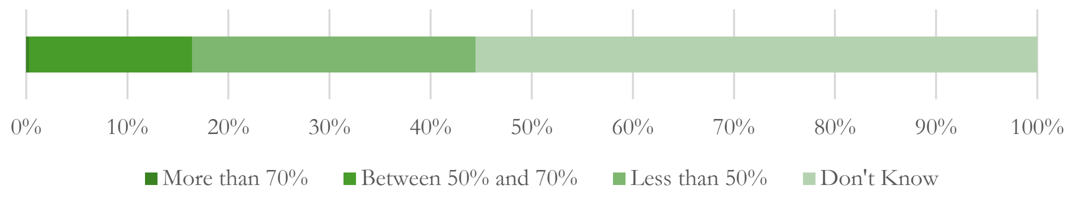
Figure 11: Understanding of House Income Limit as per New Framework



Sample Size: 378

As for loan obligation limits, 28% knew the correct limit of 50%, around 50% of respondents admitted to not knowing the limit, and the rest cited incorrect limits.

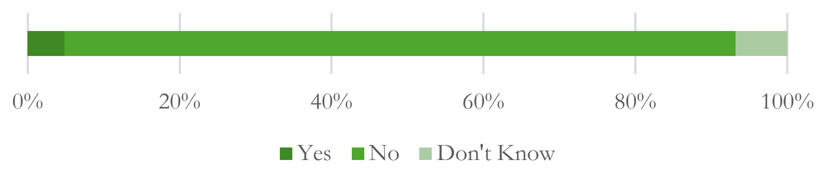
Figure 12: Understanding of Monthly Household Loan Obligation Limit as per New Framework as a % of Monthly Household Income



Sample Size: 378

Majority of respondents (around 88%) knew that there was no penalty associated with prepayment of loans; around 5%, however, thought that there was a penalty, while the rest admitted to not knowing about it.

Figure 13: Awareness about whether Pre-payment Penalty is applicable on Microfinance Loans

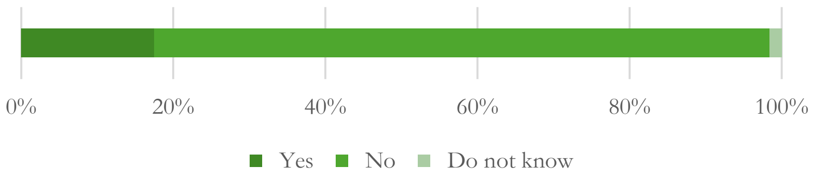


Sample Size: 758

3.4 Product Diversity and Consent

In trying to understand if MFI clients were being offered other financial products in addition to credit, we see that around 18% of respondents report availing non-credit products like life insurance, health insurance, accident insurance, or even consumer durables facilitated by the MFI.

Figure 14: Sale of Non-Credit Products along with Microfinance Loans



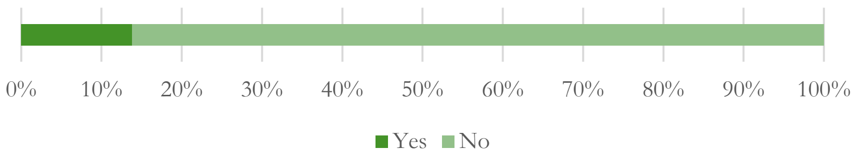
Sample Size: 378

Concerningly, in 16.1% of such sales, respondents reported that they did not give consent to purchase such products and in another 3.7% of such sales, they were not asked for consent.

3.5 Difficulties in Repayment

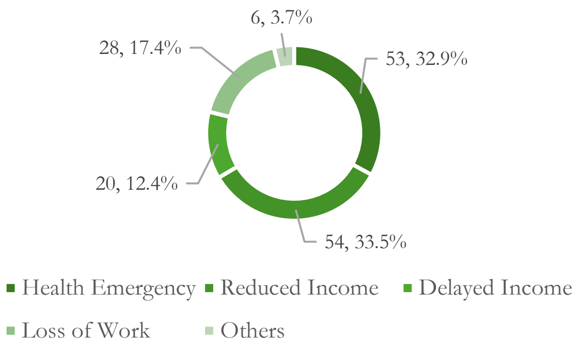
Even among those who were making regular repayments, around 14% reported facing difficulties. Reduced incomes and health emergencies were the most common causes of such difficulties.

Figure 15: Incidence of Repayment Difficulties even when Regular Repayments were made



Sample Size: 758

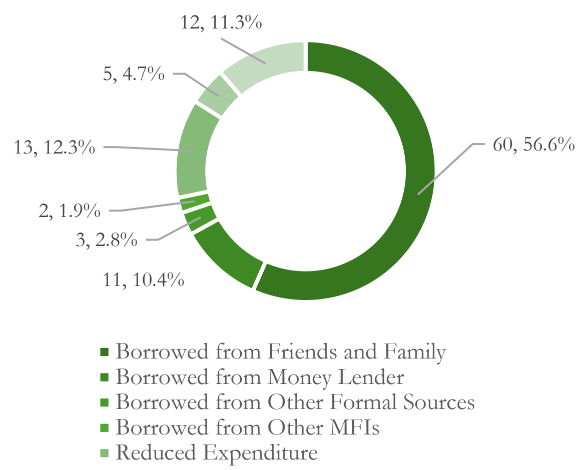
Figure 16: Reasons Cited for Repayment Difficulties



Sample Size: 105

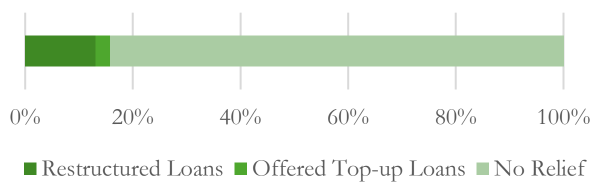
Most respondents, almost 57%, coped with such difficulties by borrowing from friends and family, while 11% borrowed from other formal sources to repay these loans. Another 10% of respondents borrowed from moneylenders to repay MFI loans.

Figure 17: Coping Strategies Used to Meet the Repayments



Sample Size: 105

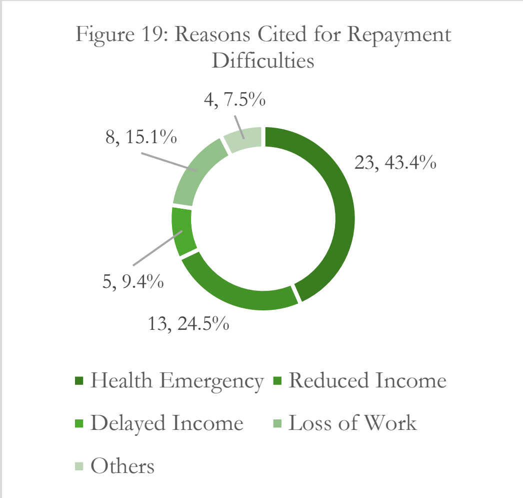
Figure 18: Type of Relief in Case of Delay or Default



Sample Size: 105

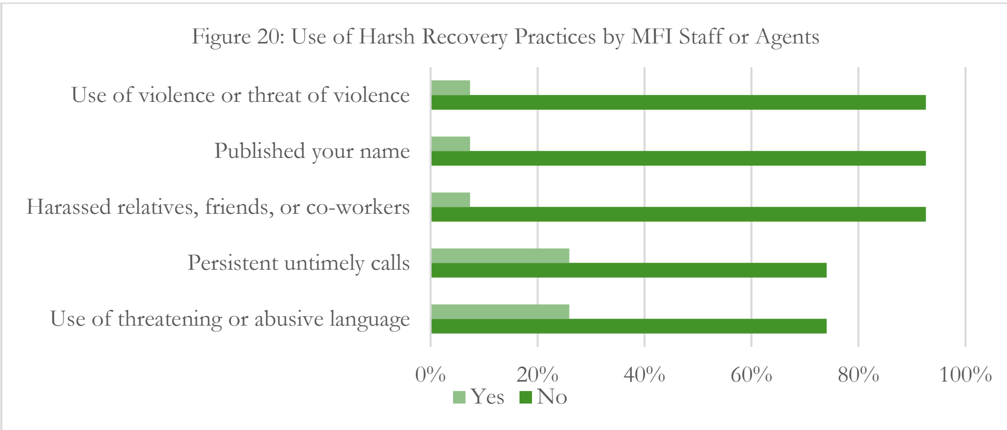
3.6 Defaulted

Among those who had defaulted on repayments, health emergencies and reduced income remained the most common reasons, just as the case with those reporting payment difficulties. Of those who faced default, the majority, around 84%, did not receive any relief from MFIs. Around 13% stated that their loans were restructured to accommodate their distress.



Sample Size: 38

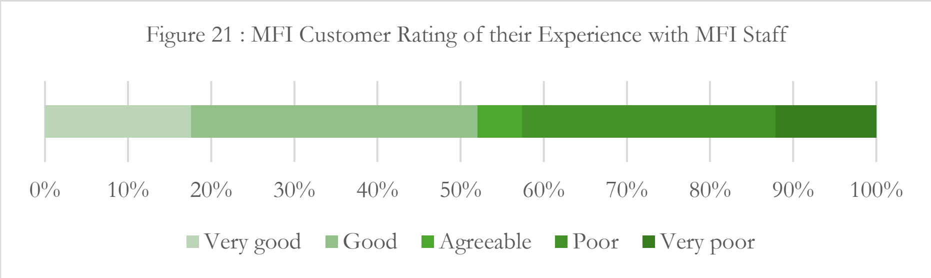
Of those customers who had gone through some recovery process, about 25% reported having been at the receiving end of harsh practices by MFI staff or agents, like untimely calls and threatening or abusive language. Violence or the threat of violence, naming and shaming, and harassment of friends and family were reported by around 7% of the respondents.



Sample Size: 27

3.7 Quality of Engagement

When asked to rate their experience interacting with MFI staff, around 17% and 34% of customers deemed it to be "Very good" or "Good," respectively. However, around 30% and 12% of customers also rated the interactions to be "Poor" or "Very Poor," respectively.



Sample Size: 761

4 TWO-SIDED VIEW FROM FIELD STAFF

Field staff from the participating MFIs were generally aware of the change in regulations and were able to articulate the rules well. Notwithstanding knowledge, the understanding of the rules appeared somewhat superficial, and there were a few discrepancies between the stated rules and the operational practices that they recounted. Notwithstanding instructions from the head office or SOPs handed out during training, the daily engagement of these last-mile personnel with customers shapes the implementation and impact of any regulation. In our study, therefore, these staff act not just as our ears on the ground but also as the canary in a coal mine, signalling stress or tensions in the sector.

In this section, we will outline the perspectives, observations, and opinions of the field staff that will augment and strengthen our understanding of the gaps and challenges in implementing the new regulations.

4.1 Credit Underwriting

"We go till the kitchen to understand the client's situation."

- Field Officer from Uttar Pradesh

Staff are, for the most part, aware of regulatory norms like the household income threshold of Rs. 3,00,000 or the 50% FOIR limit. Interestingly, however, these regulations get tweaked or watered down into simplistic and incorrect rules for loan processing. For instance, many Field Officers (FOs) reported varying limits for monthly income ranging between Rs. 15,000 to Rs. 25,000, with some even mentioning a minimum requirement of about Rs. 20,000 as monthly income. As for the 50% FOIR limit, almost all staff simplify it to a maximum EMI limit of Rs. 12,500 irrespective of household income. This would be 50% of the monthly income of a household earning Rs. 3,00,000 per annum. Notably, the spirit with which the RBI regulations tied repayment capacity to household income is lost in translation. MFI staffs are considering the absolute figure of Rs. 12,500 per month as maximum EMI, irrespective of the underlying household's income, thus construing the lending limit incorrectly. This reductionism stems partly from the need to have simple rules of thumb and partly from the incentive to lend to the maximum possible limit.

From our conversations with staff of various cadres across the country, we see that this deficiency of comprehension in implementing the regulation is a common phenomenon. This is, at least partly, explained by the pre-existing conditioning of past regulations, which had direct limits loan amounts. In fact, some MFI staff still follow the old rules of a maximum of three lenders per borrower.

Further, some finer aspects of the regulation, like the definition of a household, are operationally tweaked to be in sync with existing practices and the intuitive understanding of the staff about who constitutes a household. While the RBI mandate holds that the customer, the customer's spouse, and only unmarried children constitute a household, some branches include all members staying in the same house for annual household income assessment. This perhaps reflects the reality of who would step in to help with the repayment of a loan, which is what branch staff are optimising for with their income assessment.

The challenges with household income assessment or repayment capacity assessment are found to be uniform across all regions. Staff mention the informal nature of occupations, lack of proof of income, under or over reporting of income by customers, misinformation about existing loans, inability to recall incomes and expenditures, etc., as impediments to underwriting. They rely on their own local knowledge, awareness about the income and wage profiles of different categories of customers in the region, and intuition about the customers' circumstances, which they garner from initial engagements, to fine-tune data collection.

Data on incomes and loan obligations is cross validated with expenditure data in some cases and credit bureau records in most cases. Most staff also report conversations and enquiries with other group members and neighbours to be effective validation mechanisms.

4.2 Using Credit Bureau Records

"We can find out whether people are lying with the credit bureau data. They often lie. We will ask them why there is a mismatch, and we make a final decision based on their explanation."

- Field Officer in Uttar Pradesh

Most use Credit Bureau (CB) records to verify the income figures arrived at using their own board-approved methodology. However, there are often mismatches with the CB data. Since the customer segment's situation is prone to very quick changes, staff prefer doing household income assessments every time they lend (be it new or old customers) to verify repayment capacity. Our understanding is that staff make decisions to lend based on their own income assessment but do not update the CB data even if there is a mismatch. This is despite the requirement on MFIs to update household income after verification. Instead, they continue using the incorrect CB income figures for documentation purposes.

Staff are wary of self-reported loan figures and resort extensively to CB records to calculate monthly EMI obligations. In this regard, they report multiple challenges with CB data. For one, specific categories of loans like KCC outstanding, SHG loans, agricultural loans and gold loans are not reflected in CB records. Secondly, the problem of multiple KYCs being used by the same customer hinders visibility over all their loans. Therefore, MFI staff are forced to rely on customers to be forthcoming about their actual circumstances. Thirdly, the frequency of loan repayments could be different for different loans (from weekly to monthly), and it is sometimes not updated correctly in CB records. Therefore, it becomes hard to arrive at a monthly obligation without clarity regarding the frequency of payments. Fourthly, while most SHG loans are not updated, in cases where it is updated in CB records, there is inaccurate capturing where the entire loan amount is assigned to each member individually makes for incorrect outstanding amounts. Lastly, the delay in updating recent over dues or payments on CB records (reportedly for months in some cases) means that the overdue amount is not reflected in the records in time, or loans show up as outstanding for many weeks after the settlement of any dues[14].

Interestingly, while the incomes of all members of the household are considered to arrive at the annual household income, the monthly loan repayment obligations of only the customer and the spouse are considered to calculate FOIR. Furthermore, repayment obligations on secured loans like gold/agricultural loans, even when known, are reportedly not considered for calculating FOIR. This practice is counter to the intended purpose of doing household income assessment and having a FOIR to ensure repayment capacity.

When asked about their take on how much their typical customer ends up paying as EMI from their monthly income, more than one-third of the interviewed staff candidly responded that it would be much higher than 50%.

4.3 Customer Retention

"Whether we find customers or not, we keep running into one or two MFI staff since 10-15 MFI operate in the same region and keep doing house visits to check if there is any loan requirement."

- Field Officer from Karnataka

Customer retention is considered very important given the reportedly high levels of competition. Customers, despite facing more rejections due to the new regulations, are no longer bothered by such rejections since MFIs are willing to lend to regular customers in any way possible.

Almost all staff mention that they would reject applications that don't fall within the annual income threshold or go beyond the FOIR limit. However, many also mention that they would accommodate old customers and good applicants who are just above the threshold by modifying household incomes or outstanding EMI amounts. Some other workarounds that were mentioned to accommodate such customers were to pre-close some existing loans that are nearing completion, lower the loan amount, or lend as non-qualifying loans. The rationale is that if they do not do it, some other MFI will step in to provide that loan anyway. Such decisions are, however, made on a case-by-case basis after ascertaining intention and ability to repay.

[14] The interviews were conducted around the time when RBI had introduced new rules for updating credit bureau records. The timeline for updating records was brought down from around 30 days to 15 days. Our conversations with field staff were based on the previous reporting norms.

4.4 Repayments, Defaults and Challenges with Collections

> *"They wilfully default on repayments and use the rules of collection to their advantage. For example, they go to work early in the morning and return only after 7-8 in the evening, then insist that we should not visit them after 7 PM."*
>
> \- Field Officer from Tamil Nadu

Most make collections at centre meetings, but there is a general shift towards home collection, especially after the COVID-19 pandemic. Most report that repayments are regular. Default is reported to happen mostly in cases where customers have taken on more loans than they can handle or when there is a health emergency or income shock in the household.

In case of defaults, genuine customers reportedly engage with branch staff to figure out a solution. In such cases, branch staff, in consultation with senior management, provide grace time to ensure repayment. There are regular follow-ups, some efforts to enforce group guarantees, and warnings of 'black marks' in credit bureau records that could result in a ban on any further loans to persuade customers to make repayments. In some cases where customers are in dire situations, some MFIs offer restructuring of loans, while one mentioned offering emergency loans. Most reportedly do not offer top-up loans, and legal recourse is considered to be the very last resort.

In some cases, customers choose to wilfully default and use various tactics to avoid any engagements with field staff. In extreme cases, customers migrate away, making follow-ups impossible. Therefore, staff report not lending to people in rented accommodations to avoid the possibility of migration or absconding. In cases where ringleaders are involved, and the money has exchanged hands, it is very difficult to ensure repayment. Some report having to deal with inebriated spouses, verbally abusive customers or threats of police complaints while trying to make collections on overdue payments.

4.5 Debt Distress

> *"They either overestimate their returns from the money, or they do not calculate at all when presented with a large sum of money like a lakh. In some cases, there are threats that if you don't take it now, the MFI won't give the sum later. In those cases, they really don't have an option."*
>
> \- Branch Head from West Bengal

Most branches report that some customers are taking on way more debt than they can handle and that there are customer cohorts who are facing debt distress. Many questioned the end-use of MFI loans and commented upon consumptive and non-productive spending that keeps some customers relying on loans to just maintain their status quo. While some areas reported very high perceived levels of indebtedness (upward of 50% of their customer base), other areas saw this happening only to a small segment of their clients (around 5% to 10%).

Whatever the reported prevalence, most staff point to other MFIs' transgressions and aggressive loan disbursal strategies as of the main reasons for this over-indebtedness. Many were keen to bring back the old limit on the number of lenders per client to ensure optimal borrowing for customers.

4.6 Training and Job Satisfaction

"Often, we have to see pain and suffering, and can't do much to solve them."
- Collection Officer from West Bengal

Most reported that sufficient operational and conduct training was offered. Many, however, felt that while such training helped them understand changes in regulations or SOPs, most of the practical learning happens on the job with experience and input from seniors.

Many staff expressed that the regularity of incomes, the formality of the job, and opportunities for customer interactions are the high points of their jobs. Targets and incentives feature heavily on their minds, and many spoke about the pressure to meet disbursement, collection, and recovery targets and optimise for the highest possible monthly take-home salary.

Interestingly, there is some level of camaraderie between staff of different MFIs who run into each other on the field. Despite all the competition they face with customer leads, they sometimes help each other out by providing customer information or general intelligence about customer/region's circumstances.

4.7 Impact and Outcomes

"In the case of moneylenders, customers have to first think and then make a decision to go to them. In our case, with so much competition, MFIs are approaching customers and asking them to take loans. When someone comes to you with money, it is difficult to think and then decide. Who can say no?"
- Branch Manager from Tamil Nadu

About one-third of the interviewees felt that microfinance loans were helping their customers improve their lives. They felt that microfinance was way better than money-lender loans that push people into poverty. Most, however, were of the view that microfinance can help lives only when used right. Many said that only some of their clients (about 25% to 50%) were using microfinance loans effectively, and others were juggling between different loans to meet their ever-increasing needs. Easy loan availability that leads to unsuitable take-ups was cited as one of the reasons why microfinance creates suboptimal outcomes for some. A few opined that microfinance is no longer the welfare-oriented sector that it once used to be and that it has morphed into a purely profit-oriented sector with monthly targets and monetary incentives.

5 READING BETWEEN THE LINES – TRENDS AND PATTERNS

Our learnings from MFI senior management, staff and customers have been summarised and explained in some detail in previous sections, but within the contours of the new regulations. This study, however, also offered us a unique ring-side view of the microfinance ecosystem in these turbulent times, and we were able to decipher some trends and patterns that are shaping the sector. We lay out some of these observed phenomena with the intent to bring to focus some commonly known but little-discussed aspects of the workings of microfinance.

5.1 Competition

The increased influx of funds[15] since FY 2022 into the sector was enabled by the lifting of the price cap by the RBI and the expected indifference of customer to higher interest rates. This flow of funds also coincided with increased demand from customers who were recovering from the stress of the COVID-19 pandemic.

The availability of substantial funds also meant that there was a clamour to disburse loans and recover the pandemic-induced losses. MFIs primarily resorted to deepening their presence in existing markets, which was easier than going to newer markets[16]. This increased competition between MFIs to service the same set of clients. Aggressive lending was also enabled by the flexibility offered by the new regulations, which had removed the cap on the number of lenders, ended productive loan usage obligations, repealed absolute limits on loan amounts, etc.

MFIs competed on Turn Around Times (TATs) for loan approval and the ticket-sizes of loans offered to attract and secure clients. Speedy approvals of larger loans among existing customers who are now also borrowing from many other MFIs seem to have become a relatively common phenomenon. Targets, incentives, and appraisals for staff reflected this urgency and intense competition. While the extent to which rules around underwriting were violated remains unclear, the levels of reported and perceived over-indebtedness point to some degree of skirting, at least in certain parts of the market.

5.2 Group Culture

The deterioration in MFI group culture was a common lament among senior management and branch-level staff. The origin of this trend is often traced back to the COVID-19 pandemic when customers got accustomed to skipping centre meetings and waiting, instead, for doorstep collection. Further, the inability of MFIs to enforce group liability during the pandemic (given social distancing norms, the generalised levels of stress among all clients and the implementation of the moratorium) seems to have created a schism in the hitherto established group liability norms. It has since then become difficult for MFIs to engender the same level of group solidarity or cohesion when customers now know that it is, in fact, possible to evade the social pressure implicit in a group setting that was the mainstay of joint liability.

Further, the observed growth in the average ticket size of microfinance loans means that microloans are not-so-micro anymore, and hence enforcing joint liability becomes

[15] Outstanding equity, which stood at Rs. 4,637 crores in FY 2020-21, has increased to Rs. 13,188 crores in FY 2022-23. As for debt, outstanding borrowings has increased from Rs. 51,554 crores in FY 2020-21 to Rs. 1,13,332 crores in FY 2022-23.
[16] The year-on-year growth in Average Ticket Size (ATS) was 23% in 2020-21 and only now slowly coming down to 13% in 2023-24. In absolute terms, the ATS was around Rs. 39,627 for the year ending 2021 and has grown to Rs. 48,757 for the year ending 2024. Further, while the microfinance loan book grew at an annual rate of 22% between FY 2016-17 to FY 2023-24, the number of unique borrowers increased only by 6.9%.

challenging. Even if the absolute increase in ticket sizes is adjusted for inflation[17], the real increase in ticket sizes is still substantial enough. Moreover, the near stagnation in real wages for low-income households since the pandemic[18] also imposed restrictions on how much a household can take on as liability and squeezed the financial room for social obligations on which the idea of social collateral rests.

5.3 Fault lines

The reported weakening of joint liability in MFI loans has multiple implications. As a primary consequence, this can increase the risk of lending substantially since membership vetting by the community and default risk guarantee by the group both become ineffective. However, there are subtler implications that have the potential to change the sector's inherent purpose and promise.

Group liability is not a simple social collateral that assuages risk for lenders and ensures repayment. It also acts to place an obligation on the customer to weigh one's own personal risk alongside that of his/her group members. When a peer group is liable to be held accountable for a loan, one can imagine that any decision to borrow would be made after careful thought. Such borrowing would be constrained by the willingness of others to take on the risk of one's default, their perception of the possibility of default and the consequences that would follow such an event. When this group liability becomes ineffectual, it partly frees one from such considerations, and the risk from borrowing becomes personal. And this subtle distinction is not something to be brushed aside. For, it is possibly this socialisation of risk that tempers the proclivity of certain categories of customers - those who are in difficult circumstances, have a high-risk appetite, are prone to making poor choices or are overtly optimistic about future prospects – from overleveraging themselves. For others, it acts to instil a level of prudence such that group members, through the weight of their social pressure, parse any loan for its seeming validity. For instance, the social competition for prestige that gets expressed in the consumption of status goods has the potential to be fuelled further by credit when it is not being advanced in a group setting but rather to an individual.

If the risk becomes personal, vetting by other members gets diluted, and norms around end-use become open-ended, microfinance loans run the risk of becoming just another form of a personal loan with little transformative impact. This might not be particularly bad for customer segments who have some initial endowments of wealth or regular incomes to cushion any adverse consequences of their exuberance or difficult circumstances. However, for the relatively poorer MFI segment, who lack any such cushioning, community-enforced temperance plays a crucial role in avoiding the pitfalls associated with living on the edge. After all, it is the same community that is often called upon to help in times of distress, as can be seen from the overwhelming reliance on friends and family to pay back loans.

[17] There are some contentions that the growth in average outstanding loan per borrower has broadly kept pace with inflation. That is, it was Rs 39,353 in March 2020, and Rs 55,260 in March 2024. Considering average inflation of 5 per cent, it should have been Rs 47,833 in March 2024. After adjusting for inflation, the rise is around Rs 7,000.

[18] https://www.ideasforindia.in/topics/poverty-inequality/the-problem-of-india-s-stagnant-real-wages.html

Individualisation of debt obligation combined with aggressive oversupply seems to be creating pipelines where a substantial segment of borrowers juggles various loans and take from one provider to pay back another (often called "rotation" by industry stakeholders). This kind of juggling, which would be considered precarious even for well-established businesses that then face the risk of cashflow mismatch, is even more dangerous for low-income households that face significant contingent risks like job loss, crop loss, health event, etc., where one shock can set the family back on repayments.

5.4 Feedback Loops

Supply and demand are never truly independent. There is a feedback loop between the two that drives and shapes the trajectory of any sector. This feedback can be thought of as having four distinct strands:

(i) the contextual factors in the lives of customers that create the need for certain products that gets expressed in demand – MFI customers need affordable credit

(ii) the contextual factors in the supply chain of providers that make products available at certain places, times and prices – MFIs offering certain volumes of credit at certain rates

(iii) characteristics of demand changes in response to the supply of a product i.e., the initial need that was satisfied with the supply amps up or refines into something more or different, say in quality, quantity or variety – MFI customers demanding more loans and higher quantum of loans

(iv) supply adjusts itself to the new morphed preferences – MFIs providing micro-enterprise loans, looking to do cashflow-based lending, or taking interest rate insensitivity of the customer as a given.

In this feedback loop, the meeting of (i) and (ii) would enable the creation or formation of a market. The nature of the evolution of (iii) and (iv) would ensure the sustainability and stability of that very market.

The microfinance sector has matured enough that market formation is no longer an imperative in some parts of the country. There, it is now grappling with the matching of the messy signals from customers and lenders that are shaping supply and demand. In some other parts, it still seems to be contending with market making. It is therefore a diverse market, where pockets of maturity are interspersed with virgin markets.

In such a scenario, it is important for all stakeholders, particularly the regulator and MFIs who have the most agency in this market, to be aware of the stage of development of the market. Practices and processes from a mature market in one place, that probably also evolved with the evolving market, cannot possibly be exported into a new market indiscriminately. Here, lenders who can gain real-time insights into customers circumstances, capacities, etc. of the relatively newer market have the wherewithal to act on such cues and adjust their lending processes more dynamically than the regulator. For instance, the rate at which credit could be sustainably and productively absorbed in a state like Tamil Nadu would be vastly different than a state like Bihar or Assam. Similarly, oversupply, as seen in Karnataka, could have negative consequences for the loan culture of the region and, hence, its sustainability.

Scaling, however, demands such transpositions. For many markets, this might work, and even if it does not, the failure or destabilisation is costly only for the provider who took a business risk. However, for a sector like microfinance, that works with the underprivileged and has ostensibly committed to livelihood impact and poverty reduction, this is not just a business risk. The risk of destabilising the balance sheets of the financially precarious low-income customers places a responsibility on the lender and the regulator to become acutely aware of how demand is responding to supply (3rd strand of the feedback loop) and shape their own response to such changes in demand (4th strand of the feedback loop).

One can expect that business considerations around scaling, disbursements and infrastructure utilisations would reduce the bandwidth for, if not curtail, dynamic adjustments. Nevertheless, periodic and consistent market monitoring by the regulator (or industry self-regulatory body) that documents and signals cues from customers can provide a modicum of collective will to make necessary changes to the supply of loans.

The key to sustainability, therefore, lies in creating enabling conditions to bring about good adaptations. For example, standardised loan products that work well in nascent markets might be incompatible with more mature markets where customers might need just-in-time small loans. Concomitantly, maladaptive phenomena need to be stemmed at the earliest to avoid high market volatilities. For example, pipelining of loans, that has the potential to deteriorate the "credit culture" apart from hurting customers and providers when the music eventually stops (as it most often does).

5.5 Regulatory Dilemma

The regulator in such a market faces a difficult and unenviable task. It contends with an unevenly developed market and there would be variations in the effectiveness of the regulations in different parts of the market depending on its stage of maturity. Consequently, stakeholders would call for a short or long leash depending on which part of the market they are operating in. What is deemed to be friction by one segment of the market could very well be the traction that enables another segment of the market to thrive. Further, this market services customers, who, by the nature of their economic standing and the multiple contingencies that they are subject to, need relatively more protective measures.

Given the changing dynamics of the microfinance industry and the priorities around customer protection, the regulator has resorted to principle-based regulations but has also provided sufficient guardrails and ensured good flexibility for lenders. The largely positive take on the new regulations stands testament to their broad suitability.

Regulations apart, such a market direly depends on Self-Regulatory Organisations (SROs) to be able to do the important yet difficult task of building consensus around lenders' response to customer signals and cross-pollinating learnings across different segments of the market to ensure good outcomes for all stakeholders – MFIs, investors and customers.

6 CONCLUSION

The study finds widespread awareness about and acceptance of the new regulations. Given the vast diversity on both sides of the market – lenders and customers – the approaches to regulatory requirements vary widely, too. While most regulatory mandates are followed in letters, some are lost in administrative translations, and gaps arise in their practical implementation. For instance, the EMI limit is often watered down to an absolute value that defeats the purpose of mandating a FOIR. Overall, lenders seem rather preoccupied with disbursing as many loans as possible and ensuring repayment, and the ideal of providing appropriately sized, priced, and tenured loans is taking quite a backseat. Nevertheless, positive expectations around better data and better practices loom large, and lenders are proactive and keen about finding more suitable and appropriate underwriting processes and technology that would minimise credit and personnel risk for themselves while also helping customers access affordable and timely credit. However, MFIs are seeing increasing competition from other players in the ecosystem like non-MFI NBFCs, MFI-like unregulated lenders, gold loan companies, FinTechs, etc. The sector has seen little innovation in product offerings despite the high diversity among its customer segment and the evolving needs of customers who are graduating from microloans. Realising the original intent and promise of microfinance and its potentially transformative but yet-to-be-fully realised impact would depend crucially on the MFI sector aligning with the underlying spirit of the new regulations, i.e., customer protection and fair play. This, over the long term, would ensure sustainable and stable growth of the sector and the people it serves.

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