Gramalaya Urban and Rural Development Initiatives and Network (Guardian) - Section 25 Company

{fourth update}

Trichy, Tamil Nadu, India

November 2014

Microfinance Institutional Rating

Investment Grade			
Investment Grade	Above	α	α+
			α
			α−
		β	β+
			β
	Below		β−
		γ	γ+
			γ

	Aug 2011	Aug 2012	Sept 2013	Nov 2014
RATING	β	β	β	β+
RATING OUTLOOK*	*positive*	*positive*	*positive*	*neutral*

Dimensions rated	Grade			
Governance & strategy	β	β+	β+	β+
Organization & Management systems	β+	β+	β+	β+
Financial performance	β	β	β	β+

*M-CRIL's viewpoint (positive, neutral or negative) of the future prospects of the organization

Visit: 03-06 November 2014

M-CRIL

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Structure

Synopsis

- Gramalaya Urban and Rural Development Initiatives and Network (Guardian) was established in November 2007 by its parent organization Gramalaya. It was registered under Section 25 of the Companies Act 1956 as a non-profit organization. Guardian provides water and sanitation (Watsan) loan products to poor households under the Joint Liability Groups (JLG) model.
- Guardian has gained significant expertise of lending Watsan loans. As Guardian solely lends for Watsan activities, it has a competitive edge over other MFIs who offer Watsan loans.
- As on 30th September 2014, Guardian is operational in 6 districts of Tamil Nadu through 9 branches (units). It has a borrower base of 22,156 as on 30th September 2014.
- Most of the borrowers drop-out after availing one loan as Guardian primarily offers loans for toilet construction and water connection purpose. This leads to higher operational cost related to identification of new clients.
- Guardian has a highly experienced 6 member board. One nominee director has been appointed by Acumen Fund Inc since September 2012. The board conducts regular meetings and plays an active role in the decision making process. Most of the key staff such as the manager of credit and regional manager of operations have been associated with Guardian since the beginning of its operations.
- Around 77% of Guardian's funding comes from IOB and Acumen Fund. Capital adequacy ratio is low at 5.6% on 30th September 2014 which restricts the ability of Guardian to mobilize funds.
- All loan features are communicated to clients in vernacular language and staff are polite while interacting with clients. However Guardian does not have written policies regarding fair treatment to clients, grievance redressal, multiple lending and protection of client data.
- Guardian has improved its Operating Expense Ratio (OER) from 9.7% during FY2013-14 to 8.2% (annualized) during the period April-September 2014. The portfolio quality improved as PAR_{60} decreased from 2.2% as on 31st March 2013 to 0.4% on 30th September 2014.

Synopsis ...continued

Main Performance Indicators				
	31-Mar-12	31-Mar-13	31-Mar-14	30-Sept-14
Gross Portfolio (Rs in lakh)	638.7	829.3	1132.3	1181.8
Number of active borrowers	11 944	15 962	21 890	22 156
Return on Assets (excluding grants)	(4.2%)	(4.3%)	(6.0%)	(2.9%)
Return on Assets (including grants)	1.2%	0.2%	0.6%	2.6%
Portfolio Yield	20.4%	21.0%	22.9%	21.6%
Portfolio at Risk (>60days)	1.3%	2.2%	0.3%	0.4%
OER (including grants)*	14.4%	10.4%	9.7%	8.2%
Financial Cost Ratio (FCR)	11.3%	13.0%	14.6%	12.7%
Avg. Loan Disbursement (Rs)	8 618	8 739	8 232	11 079
Avg. Loan Outstanding (Rs)	5 347	5 195	5 173	5 334
Borrowers per field staff	543	363	561	568
Capital Adequacy Ratio	6.2%	4.9%	4.2%	5.6%

*OER of Guardian is high at 14.9% during April–September 2014 if the grants (provided by Water.org through Gramalaya) are ignored for analysis.

A rating update after one year is suggested to ascertain changes in the creditworthiness of the institution. This rating is valid, subject to no other significant changes in the organizational structure and external operating environment.

Strengths

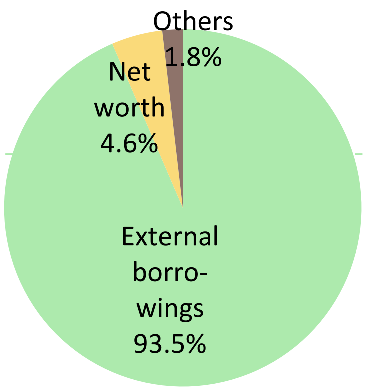
- Experienced and qualified board.
- Stable second line of management with requisite expertise.
- Improvement in portfolio quality - PAR_{60} has decreased from 2.2% as on 31st March 2013 to 0.4% on 30th September 2014.
- Comparatively low interest rate of 21% charged on a declining basis for all loans to clients (unchanged since last rating).

Issues

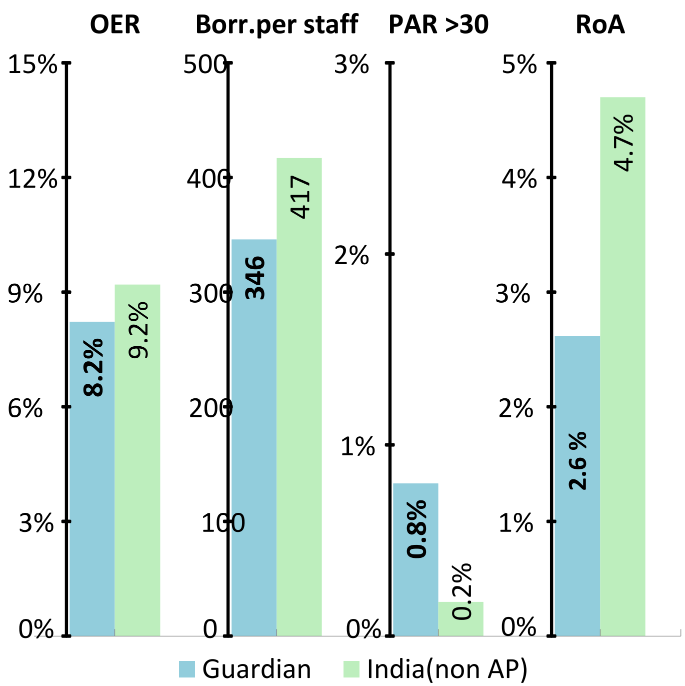
- High dependence upon IOB and Acumen Fund - constitute ~77% of total borrowings.
- Low CAR at 5.6% as on 30th September 2014.
- Fund mobilization is restricted as Watsan products at present do not come under the definition of microfinance loans.
- High OER at 14.9% during April-September 2014. OER is 8.2% with grant support from Water.org. Guardian operations are not self sustainable without this grant support.
- Despite having a well documented Performance Management System (PMS), staff performance appraisal is not being conducted.

Rating rationale

Sources of funding



Comparison of Guardian's performance With benchmarks as per M-CRIL database 2014



RoA is 2.6% during April-Sept 2014 after including grant support;. Without the support RoA is (2.9)%

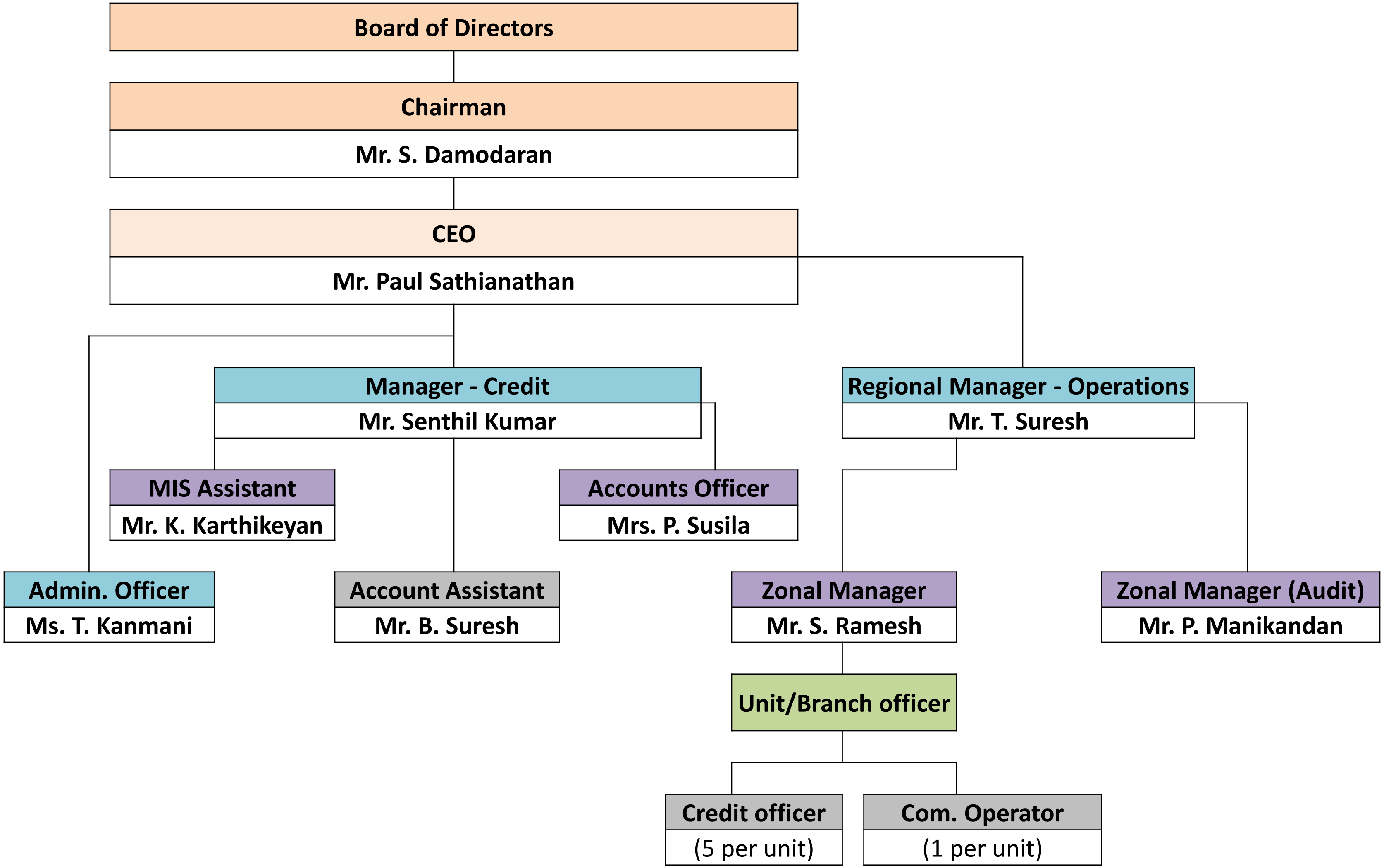
- ✓ Good Governance: Guardian has a strong governing body of 6 members who have diversified experience in development and finance. The board is actively involved in the decision making process.
- ✓ Strong second line of management: The second line of management is well experienced to efficiently manage the operations. Both Manager-Credit and Regional Manager-Operations have been associated with Guardian since its inception.
- ✓ Improvement in portfolio quality: In comparison to FY2012-13, PAR_{60} has decreased from 2.2% on 31st March 2013 to 0.4% on 30th September 2014.
- ✓ Improved Operating Efficiency: OER has decreased from 10.4% during FY2012-13 to 8.2% during April-September 2014. The OER inclusive of the grant support decreased to 14.9% during April-September 2014 from 16.3% during FY2012-13.
- ✓ Low Capital Adequacy: Capital Adequacy Ratio (CAR) is low at 5.6% as on 30th September 2014 though it marginally increased from 4.9% on 31st March 2013.
- ✓ Fund mobilization: Guardian is largely dependent on funds from IOB and Acumen which provides ~77% of its total borrowings as on 30th September 2014.
- ✓ Profitable only with support of Water.org: RoA is 2.6% during the period April-September 2014 (including support from Water.org through Gramalaya). However, without the grant support, RoA would be (2.9)%.
- ✓ Audit and Internal Control Mechanism: Regular monthly audits are conducted for all branches. The summary of the internal audit reports is presented and discussed every month at the PMC meetings.

Introduction

- On 6th November 2007, Guardian (Gramalaya Urban and Rural Development Initiatives and Network) was founded as a not for profit (section-25) company to provide microfinance services for the creation of water and sanitation facilities among poor households. Guardian was promoted by Gramalaya NGO, its parent organization, which is a forerunner in the field of rural development since 1987.
- As on 30th September 2014, Guardian operates through 9 units across 6 districts of Tamil Nadu – Tiruchirapalli, Puddukkotai, Perambulur, Namakkal, Karur and Salem, covering 22 blocks. Expansion to Karur and Salem districts was undertaken during April-September 2014. Guardian has 22,156 active borrowers with a portfolio of Rs11.81 crore as on 30th September 2014.
- Guardian has a 6 member Board which has remained the same since the previous rating. It is being chaired by the Founder Director of Gramalaya NGO, Mr S Damodoran.
- The Chief Executive Officer (CEO), Mr D Paul Sathianathan is assisted by manager-credit, regional manager-operations and an Administrative Officer. The managers are responsible for finance, operations, accounting and MIS functions while the Administrative Officer assists the CEO in handling human resources.

Particulars	Mar-12	Mar-13	Mar-14	Sept-14
Gross loan portfolio (Rs crore)	6.38	8.29	11.32	11.81
Outstanding borrowings (Rs crore)	6.37	9.74	13.22	13.74
Number of active clients	11 944	15 962	21 890	22 156

Organizational structure

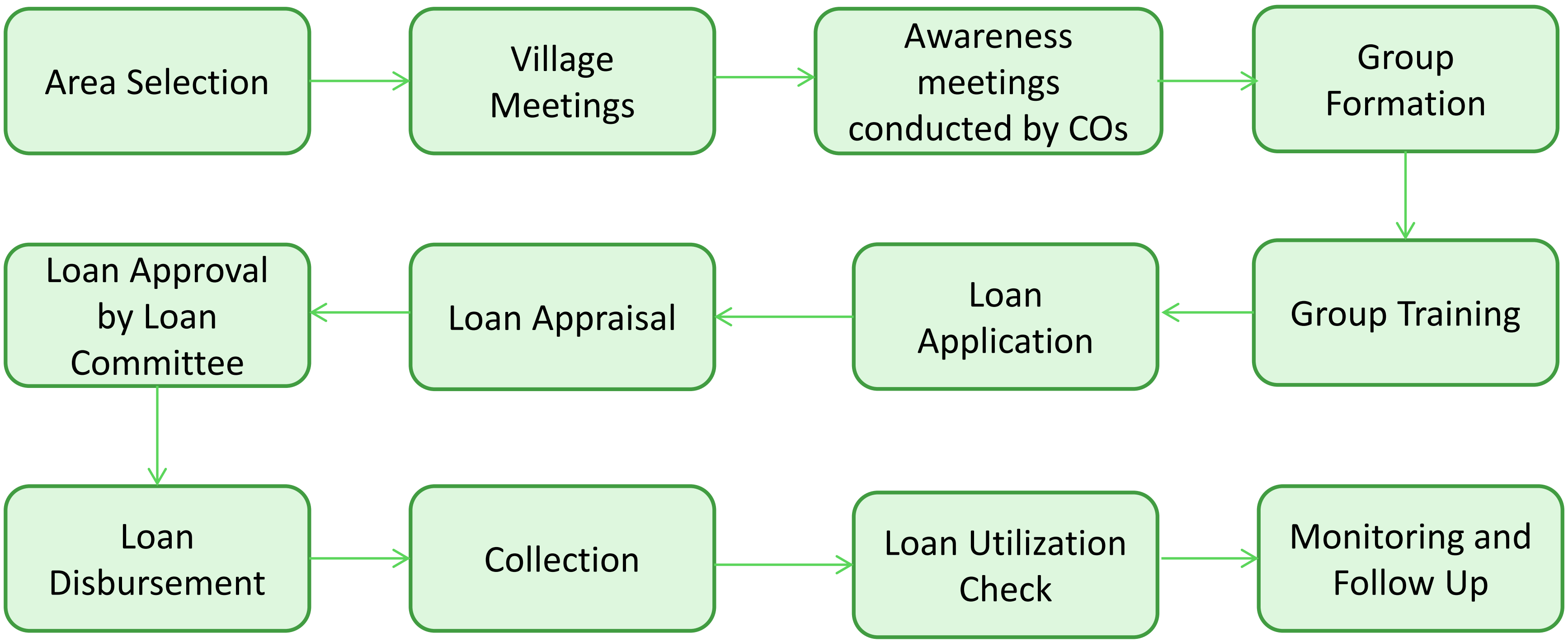


Microfinance policies

- Guardian lends for WatSan and related activities using the JLG model. Lending using SHG model has been discontinued since June 2012. Since the last rating in September 2013, there has not been any significant change in microfinance policies and processes.
- The Branch/Unit opening process commences with the area identification by the Unit Officer (UO). Credit Officers (COs) conduct a detailed survey of the villages based on a checklist to estimate the potential demand of loan products. Summary of 'Village Report' comprises data on population, number of households, availability of household toilets, public toilets, water connections, water tanks, hand pumps and average household income level.
- Once a potential area is identified, the field staff of Guardian coordinate with the Panchayat leaders to conduct awareness meetings where the COs explain the features and benefits of the various products to the prospective clients. Interested individuals are then mobilized to form 5 member groups.
- The CO prepares the loan application form (LAF) and recommends the loan amount depending on the household income and cash flow of the respective applicant. Post submission of the LAF by the CO, the UO conducts the appraisal after visiting the clients' households. Thereafter, the LAF is forwarded to the Loan Committee (LC), which consists of one director (Mr. Kumaraswamy), Regional Manager-Operations and Zonal Manager (ZM).
- Applications are rejected by the LC in case the age of the clients is more than 55 years, clients in a group are blood relatives, inconsistency in identity and address proofs, lack of space to construct toilets and issues of multiple lending. After the LAF is approved by the LC, it is sent to the CEO for authorization.
- Loan is disbursed at the Unit Office in presence of all the group members. Repayments are collected monthly by the COs from any one of the group members at a central designated point in the village.
- Loan Utilization Check (LUC) is conducted by the COs within a period of 60 days from the date of loan disbursement. The LUCs are continued till the construction of toilet/water connection is complete.

Microfinance policies...continued

The following diagram illustrates the lending procedure of Guardian.



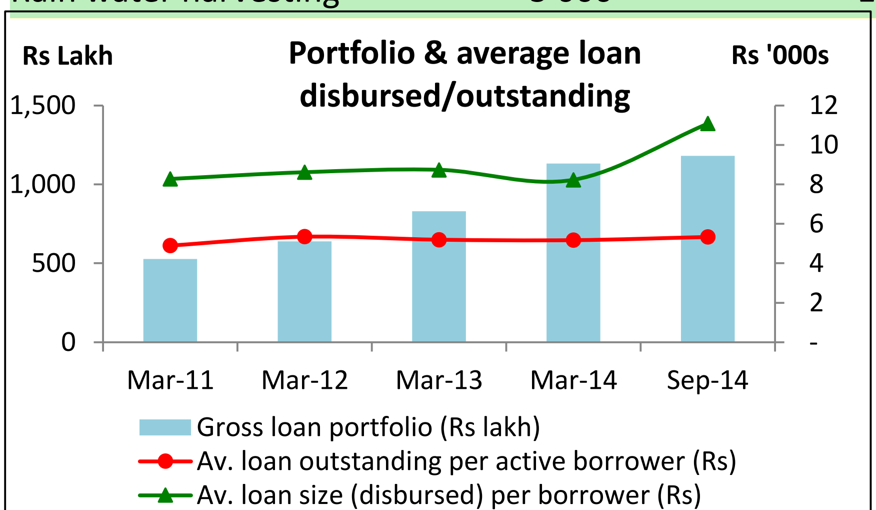
Technical Support is provided by Gramalaya

Loan products

- Guardian offers the following six loan products to its clients:

Loan Products	Urban/Rural (in Rs.)	Insurance & admin. Fees (in Rs.)	Loan Processing Fees (including 12.36% service tax) (in Rs.)	Monthly Payment (in Rs.)*
New Toilet Construction	14 000	100	157.3	910
New Water Connection	10 000/7 000	100	112.36/78.65	650/455
Renovation (Water / Toilet)	5 000	100	56.18	325
Water purifier	5 000	100	56.18	325
Biogas	10 000	100	112.36	650
Rain water harvesting	5 000	100	56.18	325

*The last installment is higher than the previous installments.



- The tenure of all the loan products is 18 months with an annually reducing interest rate of 21%.
- The loan processing fee (LPF) is 1%. The effective rate including the processing fee is 23.1%.
- Since FY2012-13, the loan size for 'New Toilet Construction' has increased by Rs4,000; 'New Water Connection' in urban areas by Rs3,000 and in rural areas by Rs2,000. Loan size of 'Water Purifier' loan product increased by Rs2,000.

Loan products

- No security deposit is collected from the clients.
- A penalty of Rs.100/month is charged from the group if a client delays the payment. The purpose of penalty is to induce repayment on time.
- No additional charges are levied by Guardian if clients seek to foreclose or prepay their loans.
- Part payment is allowed only for the collection of overdue loans.
- Currently, since Guardian lends for consumption purpose, its loans do not meet the definition of microfinance loans prescribed by the RBI. This restricts its ability to borrow from commercial banks under priority sector lending.

Insurance products

- Guardian's borrowers have to compulsorily take a life insurance cover equivalent to their loan amount from LIC.
- Insurance premium is Rs100 which covers the life of the borrower.
- The coverage is for a period of 2 years.

Governance and Strategy

Board of Directors
Operational growth & Strategy
Competition
Second line of leadership
Funding

Governance and strategy

Guardian has achieved a grade of β+ on governance. Board members have rich and diversified experience in varied sectors which includes microfinance, sanitation and rural development. It has a strong second line of management. Guardian has an edge due to limited competition in the sector. It has high dependence on a few lenders.

Board of Directors

- Guardian has a 6 member board which includes the Chairman and the CEO. Most of the board members have been associated with Guardian since its inception. Acumen Fund had appointed a nominee director since September 2012. However, the board does not have an audit committee.
- Quarterly meetings are held by the Board to review important aspects such as funds management, operations, outreach, key risks, strategic issues and future plan. There are 2 sub-committees of the Board which have been outlined below:
  - The Project Management Committee (PMC) comprises the Chairman, CEO, Regional Manager-Operations, Manager-Credit, 8 UOs, MIS (Management Information Systems) manager, Accounts officer, HR (Human Resource) and Zonal Manager-Audit. Previous month's performance and next month's targets are discussed by the PMC.
  - The Loan Committee (LC) comprises 1 Director, managers (credit and operations), zonal managers, administrative officer and accounts officer. Prior to disbursements, the LAFs are appraised by the LC.
- Monthly meetings are conducted by the above mentioned committees.
- The Board minutes are appropriately documented.

Board of Directors ...continued

- Quality of implementation of systems and processes in the field is ascertained by the initiative - Directors Annual Review Tour (DART) during which all directors visit the units. While reviewing the business plan and formulating the policies, clients' as well as staffs' feedback are taken into consideration. The Annual General Meeting (AGM) is preceded by the DART which assists the CEO on determining future course of action.

Alignment of practices with mission

- Guardian offers loans primarily for water and sanitation activities. It has disbursed only one 'Biogas' loan recently (October 2014). Loans for other purposes are not offered.
- Gramalaya assists Guardian by providing technical support, capacity building of field staff and organising meetings in villages to promote community awareness for adequate water and toilet facilities.
- The annually reducing interest rate on the loan products is 21% which is low if compared to that of NBFC-MFIs.
- Loan Utilization Checks (LUCs) are conducted for all loans within a period of 2 months. The COs conduct LUC to ensure that the loan is being utilized for the specified purpose. The UO verifies 100% of LUCs on field to confirm the data of the COs. Regional Manager-Operations and Zonal Manager verify 50% of the LUCs whereas the CEO verifies about 2%.

Operational growth

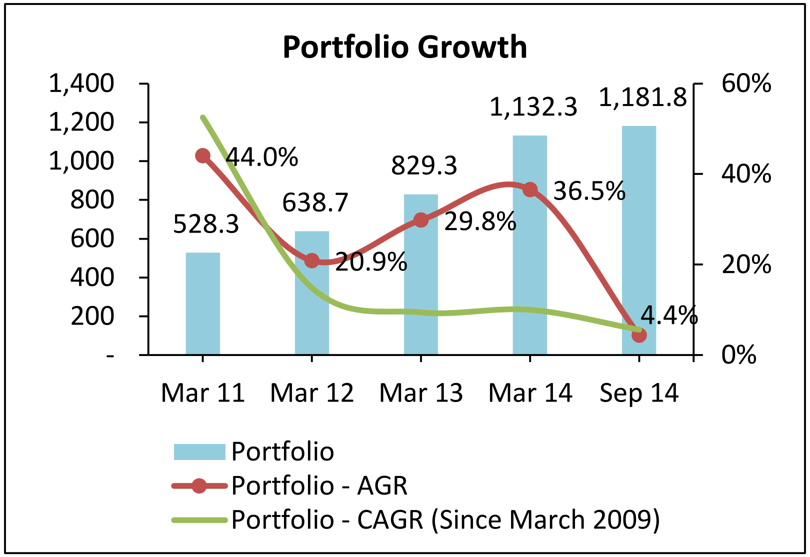
- Since March 2014, Guardian expanded its operations to 2 additional districts - Karur and Salem of Tamil Nadu.

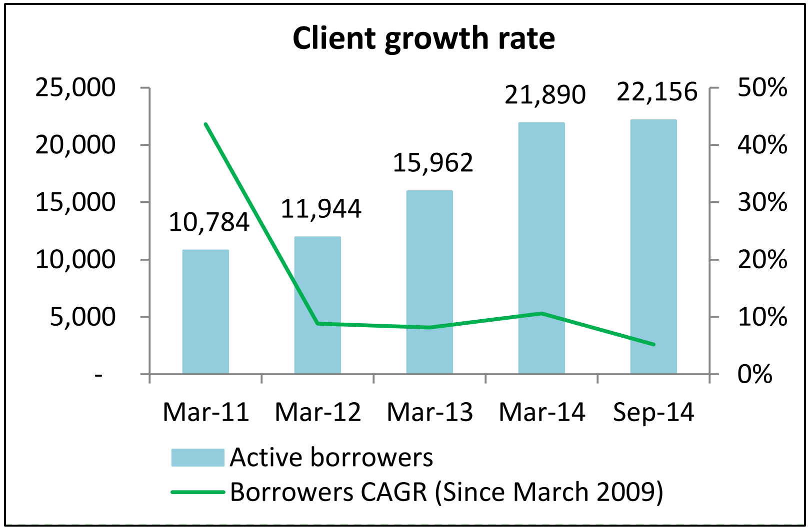
- The portfolio of Guardian has grown steadily at 5.6% CAGR (base year being March 2009) over the last 6.5 years to reach Rs11.81 crore on 30th September 2014. The growth rate has been declining over the years. The annual growth rate in FY2013-14 was 36.5% (an increase of 6.7% from FY2012-13) which dropped to 4.4% during April-September 2014.

- Guardian is still highly dependent on Acumen Fund and IOB which provides about ~77% of total funds.

- The client dropout rate has increased slightly from 20.5% during FY 2012-13 to 22% during April-September 2014.

- The client base of Guardian has grown at 7.4% CAGR during the last 6.5 years.





Competition – *limited*

- Despite the presence of MFIs such as Grama Vidiyal, Equitas, Grameen Sakthi, HIH, PAT and Business Correspondents, Guardian has the first mover advantage in Watsan loans. It exclusively provides loans for water and toilet constructions and their renovations, harvesting of rain water, water purification and biogas at a low interest rate.
- Guardian's core competence lies in its client friendly approach and support services (*technical and awareness related*).
- No cases of multiple lending were found among the groups visited by the M-CRIL team.

Second line of management – *consistent and experienced*

- Most of the key positions in Guardian's second line of leadership are occupied by staff who have been associated with the organisation since inception.
- The second line includes Mr. T. Suresh (Regional Manager-Operations) who has been promoted last year (September 2013), and Mr. M. Senthil Kumar (Credit Manager). Mr. Senthil is responsible for management of funds, MIS, accounting and credit. Monitoring of units and operations at field are led by Mr. T. Suresh. Both these managers are competent to handle their responsibilities efficiently and effectively.
- The Zonal Manager-Audit Mr. Manikandan was recruited in October 2013.
- Mrs. Kanmini T. is responsible for administrative work and in assisting the CEO for management of Human Resources since April 2009.

Fund mobilization

- Since March 2013, Guardian has been trying to obtain debt funds from multiple sources such as Milaap, Manaveeya and FWWB and moving beyond its dependence on Indian Overseas Bank (IOB) and Acumen Fund. Low CAR and low profitability are the main hindrances for Guardian to tap commercial borrowings.
- Since Guardian does not provide loans for income generation purpose and its loans do not fall under the definition of microfinance loans, it restricts its ability to borrow from commercial banks.
- Discussions are in the advanced stages for funding of Rs6 crore from IOB.
- Grant of ~1.2 crores would be disbursed by Water.org till February 2016.

Name of the lender	Loan Amount	Outstanding on 30 Sept 2014 (in Rs)	Interest rate (%)
IOB Term Loan – 3	2 75 00 000	18 57 780	11.75
IOB Term Loan – 4	1 50 00 000	28 43 151	11.50
IOB Term Loan – 5	2 50 00 000	181 09 326	13.75
IOB Term Loan – 6	6 00 00 000	5 30 65 844	13.75
Manaveeya Finance	3 00 00 000	2 25 00 000	15
Acumen Fund, USA	5 16 25 222	2 98 36 226	5.75
FWWB	25 00 000	4 40 361	9
Milaap	2 30 63 000	88 18 945	7.5
Total	**23 46 88 222**	**13 74 71 633**	
		Weighted Average Cost of Borrowings	**~11.7**

Organization and Management

Human resource quality & management
Staff Productivity
Operational efficiency
Accounting & MIS
Loan tracking system
Internal control system
Financial planning
Quality of clients and member groups
Client Protection

Organization and management

Guardian has maintained its performance under organisation and management with a grade of **β+.** Senior management is experienced and competent. Staff productivity has increased since the last rating. Pilot of hand held devices for repayment collection has been successful. However, written policies on fair and respectful treatment towards clients, grievance redressal and privacy of client data have not been drafted yet.

Human resource quality and management – *second line of leadership is stable and experienced; performance appraisal of staff is not conducted*

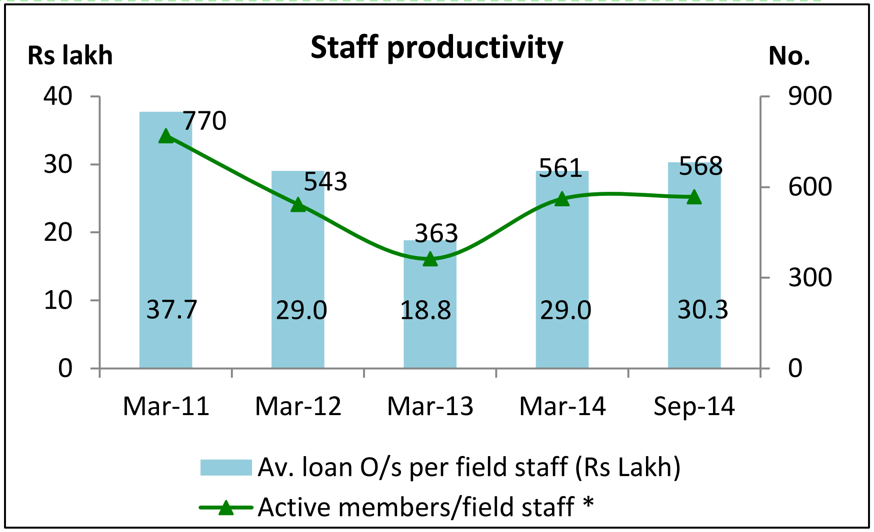
- Staff strength of Guardian increased marginally (10.3%) to 64 staff as on 31st March 2014 from 58 staff as on 31st March 2013. Number of staff remained unchanged on 30th September 2014 owing to equal number (6) of staff recruited and relieved during April- September, 2014. Field staff contributed to 61% of the total staff strength.
- Mr. T. Suresh, previously working as the ZM-Internal Audit was promoted to Regional Manager-Operations in September 2013 owing to the exit of the previous Manager-Operations. He is supported by Mr. Ramesh who has been promoted recently (October 2014) to fill in the position of the Zonal Manager (ZM), which was vacant during the last rating. Mr. P. Manikandan was recruited laterally in October 2013 to take care of the audit function.
- Apart from the aforementioned changes, the management team is intact since last year. The CEO, Manager-Credit, Regional Manager-Operations and ZM have suitable experience in microfinance as well as in managing WatSan loan products. Commitment and motivation of staff at all levels is high.
- There is a Purchase Committee which consists of Manager-Credit, Regional Manager-Operations and the accounts officer. This committee conducts its meetings once on a monthly basis.
- Human resource function is managed by the CEO, in assistance by the Administrative officer. HR manual documents all major HR policies and Code of Conduct guidelines. However the policies on grievance redressal, fair treatment to clients and privacy of client data are yet to be formulated. No changes/inclusions have been made in the HR manual since the last rating.
- Recruitments during April 2013–September 2014 have been done mostly through references. The process of one week induction training of new recruits at HO, as prescribed in the manual, is skipped and the recruits are directly deputed to their respective units.

Human resource quality and management …continued

- The new recruits shadow the activities of Senior Credit Officers and are regularly mentored by the Unit Officers (UO). Probation period is three months since their date of joining.
- Remuneration of Guardian staff is in line with the microfinance industry standards. Performance incentive is linked to on-time repayment. Travel Allowance (TA) of all staff is fixed at Rs2,000. However to boost growth, the management has recently decided to provide this allowance proportionately to the percentage of target achieved by the individual staff.
- There have been no changes in the perks (LTC, interest free personal loan up to Rs25,000 for hospital expenses and festival advance up to Rs5,000) since last year.
- Despite having a well documented Performance Appraisal System, formal appraisal of staff was not conducted last year. There have been promotions based on individual track records as discussed in the monthly review meetings of the management.
- Staff dropout rate increased marginally to 16.2% during FY2013-14 from 12.1% during FY2012-13. It increased to 18.8% (annualised) during April- September 2014.

Staff productivity – *increased*

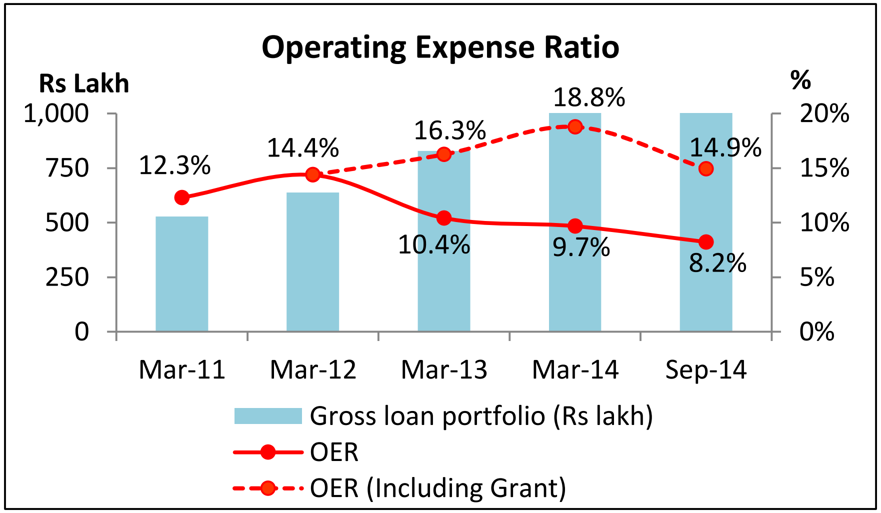
- The active borrowers per field staff increased from 363 as on 31st March 2013 to 568 on 30th September 2014 as the number of field staff has decreased to 39 from 44 on 31st Mar 2013. This is despite the fact that Guardian has increased its operations to 2 more districts. Staff attrition was 18.8% (annualised) during April-September 2014 which has increased from 12.1% during FY2013-14.
- Portfolio per field staff increased from Rs18.8 lakh on 31st March 2013 to Rs30.3 lakh on 30th September 2014.



*No. of active members is equal to the no. of loan accounts.

Operating efficiency –*increased*

- The operating expense ratio (OER) has been decreasing steadily across the years. It was 10.4% during FY2012-13 and fell to 9.7% during FY2013-14. OER further decreased to 8.2% during April-September 2014.
- However, if we include the grant provided by Gramalaya, OER gradually increased from 16.3% during FY2012-13 to 18.8% during FY2013-14. During the period April-September 2014, it came down to 14.9%.



Accounting and MIS – *hand held devices for collection, web based software* (*Delphix Nano*) *for real time tracking*

- Guardian has been using a web based software *Delphix Nano* (developed by BASIX) since August 2013. Acumen Fund Inc funded this software through Gramalaya, Guardian's parent organization. This software has given Guardian the edge of tracking real time data which was not existent in the previous software, FAMIS.
- Delphix Nano is suitable for Guardian's current scale of operations, with advanced security features and adequate storage capacity. Centralized control of the software helps in streamlining the information flow and prevents any tampering of data in the unit offices. All data corrections can only be done by the MIS assistant in the HO. Weak internet signals in branches at remote locations act as a limitation to the otherwise robust MIS.
- Entries in the Delphix software are done post LCM sanction and disbursement until which manual records are maintained. The MIS generates staff wise repayment schedules at the beginning of every month for collection as the repayment is collected from 5th to 10th every month. COs issue group wise receipts to the borrowers and preserve one copy. These receipts and collection sheets are used to enter data in the MIS by the computer operator.
- Guardian intends to shift to Hand Held Devices (HHD) for repayment collection by January 2015. Software of HHD was provided by BASIX while hardware was procured from Vision Tek, Hyderabad. Water.org has sanctioned Rs9 lakhs for the implementation of this device across all units. The pilot has been rolled out in Keeranur unit. According to the management, HHDs will increase efficiency, enhance monitoring, reduce risk of misappropriation and minimize data entry errors.
- Collection due data is uploaded in the HHDs one day prior to the due date by the computer operator. COs use the HHDs to enter the groups' repayment details and generate member wise receipts. Post collection, the computer operator downloads actual collection data from the devices to the computer and stores them as .csv files. These files are uploaded in the software, Delphix Nano. According to the management, branch staff are not permitted to edit these .csv files and any ratification will be processed only in the HO.
- Thermal receipts are generated by these HHDs which fade away soon making future reconciliation difficult. Also, the transaction time has increased as use of HHD is new to the staff. These issues are being addressed by trying out carbon paper for receipts and providing technical training to staff on using HHDs.

Accounting and MIS …continued

- Guardian has a well documented accounts manual.
- All income (incl. interest income) and expenses are accounted on accrual basis. Depreciation is accounted on the written down value method.
- Loans are written off in case of death of the borrower or if the overdue is for more than one year. Loans disbursed in 2010-11 which was PAR>360 days during FY2013-14 were written off by Guardian (including principal and interest on overdues) worth Rs2.44 lakh.
- '*Tally'* software is used for accounting. Data from Tally and Delphix Nano is reconciled every month at the HO.
- Staff collection register is maintained in each unit based on the receipts and collection sheets of every staff. The UO prepares the cash book and reconciles the entries with MIS software at the end of each working day. Consolidation of portfolio accounts from all units is done monthly in the HO.

Loan tracking system

- Loan repayments are collected during 5^{th} – 10^{th} every month based on daily collection sheets. The due date of groups are fixed at the time of disbursement which is followed throughout the tenure. Credit Officers make reminder phone calls to the respective group leaders 1-2 days prior to the due date.
- Joint liability is enforced if any member installment is delayed. Only group wise installments are collected, and in case of default, groups are revisited by the CO in the evening. Information of any overdue is communicated to the UO who reports to the ZM/Regional Manager-Operations. One of the management staff from HO discusses the reason of overdue with the client over telephone.
- UO makes the follow up visit next day of the default and the ZM/Regional Manager-Operations visits within a week if the problem persists. No legal action is initiated though regular visits are made by the unit staff.

Internal audit and control – *robust*

- Mr. P. Manikandan has been laterally recruited by Guardian in October 2013 as the ZM - Internal Audit, who is solely responsible for the Internal Audit function. He replaced Mr. T. Suresh, who got designated as Regional Manager-Operations in September 2013. Mr. Manikandan has a Masters in Commerce with more than 7 years of relevant experience in the financial audit domain. He was trained by Mr. Suresh for one month about policies and processes of Guardian.
- Guardian has a detailed internal audit manual and checklist drafted by MicroSave which enables standardized audit process. Scope of audit has not changed since the last rating.
- Each unit is audited monthly by the ZM – Internal Audit while the HO is audited quarterly. Visit schedule is prepared in the beginning of the month and the travel plan is shared with the CEO, Manager-Credit and Regional Manager-Operations. However the units are not informed about the tentative dates of audit.
- A 2 day audit is conducted at all the units which starts with verification of compliance and rectifications of previous audit findings. Cash, unit records and documents are verified in the office on the first day while group visits are conducted on the 2nd day. About 10-12 groups are verified on a random basis by the auditor in each unit. During client interaction, the auditor verifies all loan documents and repayment receipts and also conducts the loan utilization check.
- On the 2nd day of the visit, the auditor collates all findings and debriefs the unit staff. The audit reports are prepared by the weekend, as succeeding audits are conducted during the week.
- Internal audit reports are shared with the CEO, Manager-Credit, Regional Manager-Operations and ZM within a week of visit. It was observed all key areas are covered in the report with a few comments on high risk areas. The major observations in the IA reports of the last quarter were poor follow up on LUCs and overdue.

Internal audit and control … continued

- UOs submit the compliance report to the ZM-Internal Audit, Regional Manager-Operations and CEO within a week of the visit, mostly within 2-3 days. As mentioned earlier, this compliance report is verified in the next audit visit.
- Summary of audit findings of all units are presented in the monthly Project Management Committee (PMC) meetings.
- The ZM – Internal Audit does not present the findings to the board. Audit committee has not yet been constituted in Guardian's board.
- Senior management is involved actively in monitoring of units. Each unit is visited by some member of the management monthly. They do not draft visit reports, but record their observations on the unit visit register. All board members are involved in the DART (Directors Annual Review Tour) initiative which is an annual monitoring drive. During the visits, the directors refer to the IA reports for specific checks.
- Guardian has promoted one of its UO recently to take the position of Zonal Manager who assists the Regional Manager-Operations. The ZM is in-charge of four units while the UOs of 4 units report to the Regional Manager-Operations. Distribution of working area and concentrated efforts of the management has strengthened the monitoring and internal control system of Guardian.
- UOs are the head of the units and are responsible for supervising the COs and the computer operator. COs are the field staff in direct interaction with the members, and are responsible for the loan disbursement, repayment collection and loan utilisation checks.

Financial planning and cash management– *good*

- Manager-Credit of Guardian is efficient in cash planning and management. He has been taking care of this responsibility since Guardian's inception. Allocation across units is based on the monthly loan demand and fund availability.
- Fund transfer is done from HO to Unit bank accounts through cheque and from the units to HO through RTGS. The CEO validates and signs the cash and bank balances of HO everyday.
- Project Management Committee (PMC) meeting is held on 25th every month where the management reviews the achievements against the targets. Each unit sends their monthly expected recovery and tentative loan disbursement statements to the HO, which forms the basis of the next month's plans. The HO receives recovery, cash and bank status from each unit by the end of each day.
- Branch level cash balances are tracked by the finance department on a daily basis. The cash management is effective at the unit level. The average cash and bank balances as a percentage of average total assets for FY2012-13 was 3.1% which reduced to 2.5% for the FY 2013-14. Money transit insurance of Rs10 lakhs is done for all units.
- Repayments to all lenders are well planned and the schedule is rigorously followed.

Infrastructure – *adequate and employed effectively*

- All offices of Guardian are in rented premises.
- Book value of its net fixed assets is Rs7.2 lakhs on 30th September 2014 which is 0.49 % of the total assets. This has reduced from 1.05% on 31st March 2013.
- Fixed assets include computer, office equipment, furniture and fixtures. The current level of infrastructure seems adequate and employed effectively.

Client protection – adherence to the client protection principles

Assessment with reference to the seven client protection principles (Smart Campaign)

Guardian follows the unified Code of Conduct (CoC) which is jointly issued by two microfinance industry networks (Sa-Dhan and MFIN) though it is not a member of the networks. Guardian sends the data (financial and limited social) to the MIX Market which has given it five stars (highest score) for the level of disclosure of financial data.

1 Appropriate product design and delivery – *Loan sizes have been revised, WatSan products designed to suit the need of clients*

- Guardian is the only microfinance institution in India which focusses completely on water and sanitation activities. Guardian received an award in 2011 from European Microfinance Network for 'Best Product Innovation' and was first runner up in National Urban Water Award in 2009.
- Loan products of Guardian are exclusively for water (water connection loans, water purifier) and sanitation (new toilet, renovation of toilets). The loan sizes of these products have been revised (Refer Slide 11), in line with the increased cost of construction of toilets and acquiring water connections. Guardian has fixed loan repayment period of 18 months with monthly repayment frequency, which is appropriate for the clients.
- Loans for toilet construction contributes to about 76.4% of the loan outstanding of Guardian; loans for water connection and water purifier forms 23.3% and renovation loans only 2.3% of Guardian's portfolio.
- Loan utilization checks (LUC) are conducted for all loans within 60 days of disbursement. As toilet construction is a time intensive process, LUC visits are made by the COs till the whole structure is complete.
- Relevant training and technical assistance is provided by Guardian to its clients for WatSan activities. Gramalaya, Guardian's parent organization assists Guardian in these training initiatives but only in selected locations.

2 Prevention of over-indebtedness – *no formal policy; high dependence on informal checks by the staff in the absence of Credit Bureau checks*

- There is no formal mechanism drafted on avoiding multiple lending. Credit bureau checks are not done before lending which makes Guardian highly dependent on informal checks by the staff for verifying multiple loans.
- Though the management and staff claim that details of other loans are confirmed and compulsory, this data is not captured which leads to ambiguity in the process.
- Guardian captures the income and expenditure details in its loan application form to check the repayment capacity of its clients.
- All loans are sanctioned by the loan committee in the Head Office after in-depth scrutiny of the loan repayment capacity.
- Scope of audit does not cover checks on over-indebtedness and no such inclusions are made in the audit checklist yet.

3 Responsible Pricing – *interest rate unchanged at 21% on declining basis*

- As Guardian targets the low income segment, the interest rates on the loan products is priced at a relatively lower level with an APR of 23.1%.
- Guardian allows prepayments and foreclosure of loans without any charges. Part-payments are not allowed except for overdue clients.
- Penalty for late repayment of Rs100/group/month is taken from clients but is adjusted in the last instalment.

4 Transparency – *good*

- Guardian explains its products' features and processes during its village survey and initial interactions with the potential members and reiterates them during group formation and disbursement.
- Credit officers conduct multiple loan utilization checks till the construction work is complete.
- Loan documents are in the vernacular language which is easily understood by the clients. All features, terms ad conditions are mentioned in the loan document. Printed repayment schedule is provided to all the clients at the time of disbursement. Documentation was observed to be proper during the visit to the units.
- Guardian shares financial and operational data on its website and also with MIX.
- Repayment collection receipts are given group-wise and were found to be present in their registers during the time of visit. However, use of Hand held devices would allow the generation of receipts for individual members. Audit scope includes verification of the receipts with the unit records.

5 Fair and respectful treatment of clients – *need to have a written code of conduct*

- Fair and respectful treatment of clients in Guardian has been given importance since inception. Staff are regularly mentored about their demeanor during client interactions during the monthly all-staff meetings. The supervisors regularly monitor the conduct of staff and enquire the clients about any staff transgression, during their field visit.
- Operations manual of Guardian, unchanged since last rating, highlights credit discipline but does not list the appropriate collection practices and staff behaviour. Also, there is no categorization of management action sorted according to the extent of misconduct.

6 Mechanism for complaint resolution – *absence of formal mechanism*

- Clients contact the Credit Officers for most of their queries such as group formation and delay in disbursement. These issues related to the loan are addressed by the respective COs. Additionally, the contact numbers of the Unit and personal contact number of the UO are mentioned in the group register.
- Content of these calls are not recorded and no escalation mechanism has been formulated yet. In the absence of the call logs, tracking of the addressal of the issues by the management is limited.
- No other formal mechanism (e.g. complaint box, toll free number) is not existent in the units.
- The supervisors (CEO, Managers, Auditor) collect client feedback during their field visits .
- Directors Annual Review Tour (DART) initiative is an annual program where the board members meet a few clients of all the units and take their feedback on the services provided by Guardian.

7 Privacy of client data – *policy not yet drafted*

- Guardian has not yet drafted any policy on sharing of client data with third parties.
- Client data is only being shared with the insurer (LIC).
- No permission is being taken from the clients for data sharing.

Financial performance

Profitability and sustainability
Portfolio quality
Capital adequacy
Asset & Liability composition

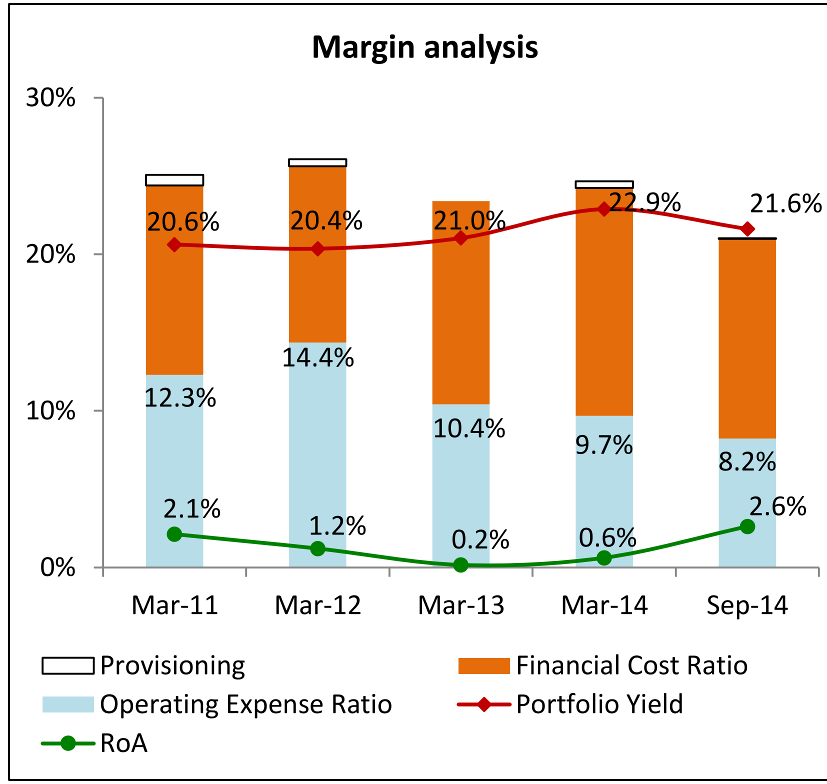
Financial performance

Guardian's financial performance is rated at β+ on account of improved portfolio quality, marginal increase in capital adequacy and assured grant support from Water.org till February 2016.

Financial Ratios	31-Mar-12	31-Mar-13	31-Mar-14	30-Sept-14
Capital Adequacy				
Risk Weighted Capital Adequacy Ratio	6.2%	4.9%	4.2%	5.6%
Asset Quality				
Portfolio at Risk (>60 days)/ Gross Loan Portfolio	1.3%	2.2%	0.3%	0.4%
Loan Loss Reserves/ Gross Portfolio	2.0%	1.3%	1.0%	1.0%
Management				
Operating Expenses / Avg. Gross Loan Portfolio	14.4%	10.4%	9.7%	8.2%
Number of Borrowers / Field Staff	543	363	561	568
Number of Borrowers / Total Staff	362	275	342	346
Cost per borrower (Rs)	602	442	397	218
Earnings				
Net operational income / Avg. Assets (RoA) *before donations*	(1.9)%	0.2%	0.8%	1.3%
RoA *after donations and tax*	1.2%	0.2%	0.6%	2.6%
Operating Self Sufficiency (OSS)	90.4%	101.4%	104.2%	115.2%
Portfolio Yield	20.4%	21.0%	22.9%	21.6%
Other income (*from donations, interest on staff loans etc.*)	3.2%	2.7%	2.8%	2.6%
Financial cost/Avg. Gross Loan Portfolio (FCR)	11.3%	13.0%	14.6%	12.7%
Liquidity				
Avg. Cash & Bank balances / Avg. Total Assets (excluding FDs)	3.5%	3.1%	2.5%	2.7%
Debt/Equity ratio	16	23	27	20

Profitability and sustainability

- OER decreased from 10.4% during FY2012-13 to 8.2% during the period April-September 2014. However, ignoring the grants received from Gramalaya, OER is 14.9% during April-September 2014 which decreased from 18.8% during FY2013-14.
- RoA has increased from 0.2% (FY2012-13) to 0.6% (FY2013-14). For the period April-September 2014, it is 2.6%. However the return on assets is negative at (2.9)% during April-September 2014 without grant support. This has improved from (4.3)% during FY2012-13.
- Yield increased from 21% in FY2012-13 to 22.9% in FY2013-14 but marginally decreased to 21.6% during the period April-September 2014.
- Guardian has to explore fresh avenues to mobilize funds for meeting the credit demands of its existing clients as well as to expand its outreach.



Portfolio quality – *improved*

- The portfolio of Guardian has grown from Rs8.29 crore on 31st March 2013 to Rs11.81 crore on 30th September 2014.
- PAR_{60} was high on 31st March 2013 at 2.2% due to staff attrition and poor follow-up. Better management, overdue tracking as well as consistent monitoring by the field staff has led to an improvement in PAR_{60} to 0.4% on 30th September 2014.
- The Loan Loss Reserve (LLR) has been maintained at 1% since FY2012-13 which is satisfactory.
- $PAR_{0\text{-}30\ days}$ has been high since April 2013 as the staff are not able to collect repayments within 5th -10th of every month and has to follow up with the clients during rest of the month.

Portfolio ageing on 30 Sept 2014

Overdue period (in days)	Loan principal outstanding	PAR %
Current	10 22 46 976	0.0%
1-30 days	1 45 11 078	12.28%
31-60 days	9 45 768	0.80%
>60 days	4 72 050	0.40%
Gross portfolio	**11 81 75 872**	**0.40%**

Capital Adequacy– *Low*

- Capital adequacy ratio (CAR) is low at 5.6% on 30th September 2014. It marginally increased from 4.9% on 31st March 2013. Guardian's net worth increased from Rs42.1 lakh in March 2013 to ~Rs68 lakh by end of September 2014.
- Portfolio increased by 43% during March 2013 to September 2014. The debt-equity of Guardian is still high at about 20 times despite a decrease from 23 during the FY2012-13.
- Low CAR of Guardian limits its ability to attract commercial borrowers.

Asset liability and equity composition

- Net loan portfolio to total assets ratio increased marginally from 78.5% as on 31st March 2013 to 79.6% as on 31st September 2014. Net fixed assets and other assets accounted for 0.49% and 2.07% respectively of total assets as on 30th September 2014.
- Cash and bank balance as a proportion of its average total assets on 30th September 2014 was 0.8%.
- The net worth constitutes 4.9% of the total source of funds as on 30 September 2014. IOB being the major funder contributed to 55% of Guardian's external borrowings followed by Acumen Fund at ~22% and Maanaveeyaa at ~16% as on 30th September 2014. Milaap (~6%) and FWWB (0.3%) had relatively low contributions.

Financial Statements of Guardian's microfinance programme

Balance Sheet on

31-Mar-12	31-Mar-13		31-Mar-14	30-Sept-14
		ASSETS		
		<u>Current assets</u>		
16 08 660	43 33 478	Cash in hand and bank	37 68 572	12 09 828
72 30 000	1 36 35 000	Fixed deposits	2 06 35 000	2 50 00 000
9 69 568	23 23 511	Advance(rent, festival, staff and project) receivable	29 42 209	22 05 027
3 68 440	0	Advance taxes (IT & TDS)	4 10 733	5 24 333
2 07 769	4 10 595	Staff loans	4 18 895	3 05 720
6 00 000	6 00 000	Investments - GMF	0	0
		<u>Loans outstanding</u>		
6 38 68 022	8 29 29 982	Gross loan outstanding	11 32 27 340	11 81 75 872
(12 77 360)	(10 55 996)	*Loan loss reserve*	(11 32 273)	(11 81 759)
6 25 90 662	8 18 73 986	Net loans outstanding	11 20 95 067	11 69 94 113
7 35 75 099	**10 31 76 570**	**Total current assets**	**14 02 70 476**	**14 62 39 021**
11 69 197	10 93 638	Net property and equipment	7 23 968	7 23 967
7 47 44 296	**10 42 70 208**	**Total Assets**	**14 09 94 444**	**14 69 62 988**

Balance Sheet on ...continued

31-Mar-12	31-Mar-13		31-Mar-14	30-Sept-14
		LIABILITIES AND NET WORTH		
		Current liabilities		
51 05 998	25 30 047	Cash security	62 450	59 950
13 63 968	0	Interest payable to Acumen Fund	31 56 128	12 86 478
3 76 920	0	Income tax	0	0
12 730	0	Others Payables	0	0
7 296	70 000	Others current liabilities	5 83 084	13 58 883
68 66 912	**26 00 047**	**Total current liabilities**	**38 01 662**	**27 05 311**
		Long term liabilities		
		Long term debt		
3 64 41 415	4 79 88 934	IOB	7 75 02 376	7 58 76 101
28 68 169	52 33 194	Milaap	64 46 210	88 18 145
2 44 83 026	4 42 37 565	Acumen Fund Inc, USA	3 45 28 952	2 98 36 226
0	0	Others (*Manaveeya, FWWB*)	1 37 92 014	2 29 40 361
6 37 92 610	**9 74 59 693**	**Total long term liabilities**	**13 22 69 552**	**13 74 71 633**
		Net worth		
5 47 165	5 32 685	Reserves(Risk Fund)	4 90 517	4 69 530
27 33 571	35 37 609	Retained net surplus/(deficit)	36 77 782	44 32 713
8 04 039	1 40 173	Current net surplus/(deficit)	7 54 931	18 83 801
40 84 774	**42 10 467**	**Total net worth**	**49 23 230**	**67 86 044**
7 47 44 296	**10 42 70 208**	**Total Liabilities and Net Worth**	**14 09 94 444**	**14 69 62 988**

Income Statements for the period

FY 2011-12	FY 2012-13		FY 2013-14	Mar to Sept-14
		Income		
86 96 252	1 33 13 885	Interest on loans	1 92 03 193	1 20 25 766
14 92 740	9 17 350	Processing fees received	13 39 820	6 97 300
5 61 185	6 49 222	Investment income	5 45 589	7 63 390
9 02 130	10 60 800	Insurance fee received	16 27 427	6 29 657
1 46 667	1 11 139	Other income	3 43 366	1 63 349
1 17 98 974	**1 60 52 396**	**Total operational income**	**2 30 59 395**	**1 42 79 462**
		Financial costs		
55 98 014	82 13 854	Interest expenses	1 20 87 874	75 00 447
0	0	Loan processing fees	9 37 280	0
38 949	5 67 684	Other charges	33 820	0
61 62 011	**72 70 858**	**Gross financial margin**	**1 00 00 421**	**67 79 015**
2 20 713	0	Provision for loan losses & write-off	3 91 471	49 486
59 41 298	**72 70 858**	**Net financial margin**	**96 08 950**	**67 29 529**
		Operating expenses		
38 85 357	35 80 889	Personnel Cost	38 47 099	27 50 273
6 87 148	4 31 736	Travel	4 61 185	1 86 867
3 39 490	2 82 461	Depreciation	3 79 232	0
22 72 950	27 32 131	Administrative expenses	33 12 658	15 34 414
2 961	4 951	Other expenses	6 85 972	3 68 916
0	19 095	Bad debts written off	0	0
71 87 906	**70 51 263**	**Total Operating expenses**	**86 86 146**	**48 40 170**
(12 46 608)	**2 19 595**	**Net Surplus/Deficit (Before tax & donations)**	**9 22 804**	**18 89 059**
34 55 756	23 453	Non-operational income /operational grants	6 09 126	12 50 772
10 28 189	1 02 875	Non-operational expenses	3 28 188	3 28 188
3 76 920	0	Taxes	4 48 811	9 27 842
8 04 039	**1 40 173**	**Net Surplus/Deficit (after tax & donations)**	**7 54 931**	**18 83 801**

Annexes

Profile of the Board

S.No.	Board Member	Position on Board	Experience	Since
1	Mr. S.Damodaran	Chairman	He is a double post graduate in commerce and business administration. He is the founder chairman of Gramalaya and has more than 25 years of experience in WatSan. He is a member of National Task Force under Ministry of Urban Development of Govt. of India and Executive Committee member in State-level Sanitation Society of Govt. of Tamil Nadu. He has participated in various SME and MF trainings and conferences.	October, 2011
2	Mrs. J.Geetha	Director	She is a graduate in Science and Sociology and has 12 years of experience in water and sanitation. She is also the CEO of Gramalaya Microfin Foundation, which is a section 25 company.	Inception
3	Mrs. S.Muthulakshmi	Director	A graduate in Economics and has 20 years of experience in water & sanitation. She is also the Administrative Officer of Gramalaya.	Inception
4	Mr. M.Elangovan	Director	He is a post graduate in commerce with more than a decade's experience in the development sector. He is also the Executive Director of Gramalaya.	Inception
5	Mr. S.Kumarasamy	Director	Over 35 years of experience in Health Dept. and 8 years in social service. Exposure to various microfinance models and has undergone various trainings on microfinance. He is also an excellent trainer and imparted various trainings on SHG model. He is the co-founder of Guardian	Inception
6	Mr. Nagaraja Prakasam	Nominee Director	He is has been appointed as the director by Acumen Fund Inc. Nagaraja is an MBA from Kennesaw State University and has rich experience in the financial sector. He is currently a venture advisor with Unitus Seed Fund.	Sept2012

M-CRIL rating grades

M-CRIL Grade	Description
α+	Strong governance, excellent systems and healthy financial position. Without a foreseeable risk ➢ Most highly recommended
α	Good governance, excellent/good systems, healthy financial position ➢ Highly recommended
α–	Good governance, good systems and good financial performance; Low risk, can handle large volumes ➢ Recommended
β+	Reasonable performance, reasonable systems. Reasonable safety but may not be able to bear an adverse external environment and much larger scale ➢ recommended, needs monitoring
β	Moderate systems. Low safety ➢ acceptable only after improvements are made on specified areas
β–	Weak governance, weak systems. Significant risk ➢ not acceptable but can be considered after significant improvements
γ+	Weak governance, poor quality systems. High risk ➢ needs considerable improvement
γ	Weak governance, poor systems, weak financial position. Highest risk ➢ not worth considering

In addition, a 'Positive' outlook given by M-CRIL suggests that the institution is expected to improve its rating in one year period to one higher notch, 'Neutral/Stable' suggests that the institution is likely to retain its rating till the end of one year from the rating, and 'Negative' outlook suggests that it is expected that the institution will lower its rating performance by one notch in one year period.

Abbreviations

CAR	Capital Adequacy Ratio
CEO	Chief Executive Officer
CO	Credit Officer
AO	Accounts Officer
Guardian	Gramalaya Urban and Rural Development Initiatives & Network
HO	Head Office
HR	Human Resource
IOB	Indian Overseas Bank
JLG	Joint Liability Group
LLR	Loan Loss Reserve
M-CRIL	Micro-Credit Ratings International Limited
MFI	Micro-Finance Institution
MIS	Management Information System
OER	Operating Expense Ratio
OSS	Operating Self-Sufficiency
PAR	Portfolio at Risk
PMC	Project Management Committee
RoA	Return on Assets
SHG	Self Help Group
UO	Unit Officer
WatSan	Water and Sanitation
WPI	Water Partners International

Glossary

Current repayment rate: Ratio of principal recovered (net of pre-payments) to the principal due for the last one year.

Portfolio at risk (PAR>0): Ratio of the principal balance outstanding on all loans with overdues greater than 0 days to the total loans outstanding on a given date.

Yield on portfolio: The interest income on loans divided by the average loan portfolio for the year.

Financial cost ratio: Total interest expense for the year divided by the average portfolio.

Loan loss provisioning ratio: Total loan loss provisioning expense for the year divided by the average portfolio.

Operating expense ratio: Ratio of salaries, travel, administrative costs and depreciation expenses to the average loan portfolio.

Average loan portfolio: This represents the average loan outstanding for the year computed on a monthly basis.

Average total assets: This represents the average total assets for the year calculated on an annual basis.

Operational Self-Sufficiency: Ratio of total income to total costs for the year.

Risk weighted capital adequacy ratio: Ratio of net worth to risk weighted assets

M-CRIL Risk weights: 100% for all assets except the following: Fixed assets: 50%; Cash and fixed deposits with banks: 0%. Portfolio outstanding is taken net of loan loss provisioning.

Return on assets: Ratio of net income/(loss) after tax to average total assets

Return on equity: Ratio of net income/(loss) after tax to average net worth