



Sarala Women Welfare Society	Kolkata, INDIA
Section 25 Company	Report – June 2009

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CREDIT RATING	β+
RATING OUTLOOK*	<i>neutral</i>

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

Date of visit: 17-19 June 2009
 Date of previous rating: August 2008
 Previous rating: β

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

Main Performance Indicators		
	Mar-08	Mar-09
Gross Portfolio (Rs lakhs)	513.7	1,834.4
Number of members	19,838	53,932
Number of active borrowers	14,763	46,334
ROA	3.7%	4.5%
Portfolio Yield	26.3%	25.1%
Portfolio at Risk (>60days)	0.01%	0.01%
Operating Expense Ratio	11.2%	9.1%
Average Loan Disbursed (Rs)	4,798	6,084
Average Loan O/s (Rs)	3,480	3,959
Borrowers per field staff	352	459
CAR (including promoter's loan)	5.0%	6.4%

Synopsis

Sarala Women Welfare Society (Sarala) was incorporated as a section 25 company in July 2006 with its Head Office located in Kolkata. It has an improved performance on management and financial parameters, since the last rating in August 2008.

Since the last rating, Sarala is continuously making efforts to strengthen its HR verticals and has inducted some qualified personnel at key positions. It has been able to maintain excellent portfolio quality despite high growth in portfolio, which is commendable. It has stable yield of 25.1% and low OER of 9.1% leading to healthy OSS and RoA of 130.8% and 4.5% respectively. However, low capital adequacy position remains an area of concern. Also the promoter's contribution is still being treated as unsecured long term interest free loan, which is yet to be subordinated.

Though the Board of Sarala has independent Directors, having persons with microfinance experience would strengthen it. Moderate second line, internal control and monitoring systems despite of having good supervisory structures, also needs to be strengthened. Also, high competitive pressure compounded by the absence of diversified product portfolio may adversely affect its profitability in future. A rating update after one year is suggested to ascertain changes in the creditworthiness and absorptive potential of the institution. This rating is valid, subject to no significant changes in the organisational structure and external operating environment.

Highlights

Positive

- High portfolio growth
- Fund mobilization
- High operating efficiency and good staff productivity
- Excellent portfolio quality
- Profitable operations

Negative

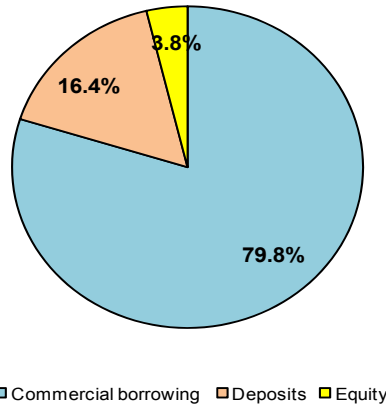
- Limited microfinance exposure of the Board and moderate second line
- High competition
- Moderate internal control and monitoring
- Low capital adequacy

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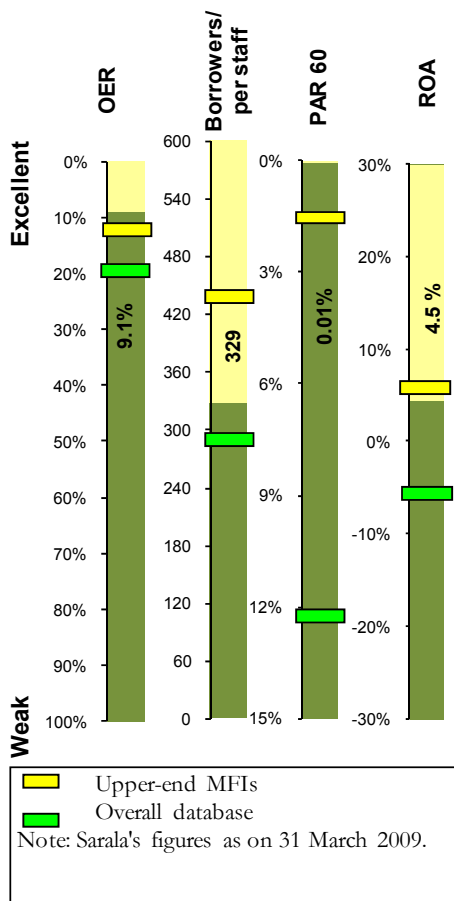
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Sources of Funding	Rating Rationale
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Sources of funding



Comparison of Sarala's performance with MFIs rated by M-CRIL

High growth in portfolio: Sarala's portfolio has grown at a CAGR of 264.6%, from Rs1.4 crores as on 31 March 2007 to Rs18.3 crores as on 31 March 2009.

Fund mobilization: Sarala has performed reasonably well on mobilizing debt as well as grant funds from diversified sources within a span of two and half years of its operations.

High operating efficiency and staff productivity: Sarala has high operating efficiency with an OER of 9.1% for the period ending 31 March 2009, owing to improved staff productivity of 459 borrowers per field staff during the period.

Excellent portfolio quality: Sarala has maintained an excellent portfolio quality despite high growth in portfolio, which is commendable. It has a current repayment rate of 99.9% with PAR (>60 days) at 0.01% as on 31 March 2009.

Profitable operations: Sarala has performed well on profitability and sustainability parameters, since inception. This is primarily on account of its "split and spread" strategy, which ensures that the new branch becomes financially viable from day one. The high yield along with the improved OER has resulted in an OSS of 130.8% as on 31 March 2009. RoA has also improved from 3.7% in March 2008 to 4.5% in March 2009.

Governing Board and second line of leadership: Sarala's Board lacks microfinance experience with the exception of the promoter cum Co-CEO, Dr Arabinda Sinha. Sarala's management has recently inducted one new member, who is a lawyer by profession, in the Board. However, he lacks microfinance experience. Sarala's second line of leadership needs grooming to take up leadership in future.

High Competition: Sarala is facing high competition from big MFIs like Bandhan, SKS etc operating in its area. The competitive pressure is bound to increase as it grows and expands, which may put pressure on its growth and profitability in future.

Moderate internal control systems: The internal control systems at Sarala are moderate despite of having good supervisory structure at each level. Some of the instances like disbursement of loans without prior approval of BM, more than 30 member's group, repayment collection of other group members etc were observed during the field visit by the rating team. The quality of monitoring needs significant improvement especially in view of the rapidly growing portfolio.

Low capital adequacy: The capital adequacy position of Sarala is low at 6.4% as on 31 March 2009.

Comparative Performance Highlights

Comparative Rating Grades

Category	Rating grade			Movement
	January 2005	June 2008	March 2009	
Governance & strategic positioning	β	β	β	↔
Organisation & Management	β+	β+	β+	↔
Financial performance	β+	β	β+	↑
Overall	β	β	β+	↑

Select indicators/ratios

Indicator/ratio	March 2007	March 2008	June 2008	March 2009	Change
1 Growth					
Loans outstanding (Rs lakhs)	138	514	564	1,834.4	↑
Outstanding borrowings (Rs lakhs)	155	403	418	1,449.9	↑
Active borrowers	4,825	14,763	18,678	46,334	↑
Average loan size (Rs)	3,856	4,799	4,828	6,084	↑
2 Credit performance					
Reported current repayment rate	100%	99.98%	99.98%	99.98%	↔
Portfolio at risk (>=60 days)	0%	0.02%	0.02%	0.01%	↑
3 Efficiency and profitability					
Borrowers per field staff	219	352	434	459	↑
Net loans to total assets	72.7%	93.7%	93.5%	94.9%	↑
Operating expense ratio	12.6%	11.4%	9.6%*	9.1%	↑
Annual return on assets	-2.0%	3.7%	5.3%*	4.5%	↓
Operating self-sufficiency	68.7%	126.2%	165.9%	130.8%	↓
Capital adequacy ratio (including promoter's interest free loans)	10.2%	5.0%	6.4%	6.4%	↔

Note: An upward arrow indicates improvement since the last rating.

Country overview

India has one of most extensive banking infrastructures in the world. However, millions of poor people in India do not have access to basic banking services like savings and credit. In the past, both public and private commercial banks in India perceived rural banking as a high-risk, high-cost business i.e. a business with high transaction costs and high levels of uncertainty. Rural borrowers, on their part, felt that banking procedures were cumbersome and that banks were unwilling to give them credit. However, it was not until the 1990s, that the Indian govt. realized the need for microfinance to provide the rural poor with savings and micro-credit services.

Quick Facts

Total population ¹	1.12 billion
GNI per capita (US\$) ²	720
% population under \$2/day (PPP) ³	79.9%
Total unemployment (% of labour force) ⁴	4.4%
% of population with access to banking services ⁵	<30%
Average inflation (Apr '06 to Mar '07) ⁶	5.3%

Sources

- 1 www.indiastat.com
- 2 World Bank 2006, www.worldbank.org
- 3 World Bank (2006) <http://devdata.worldbank.org> - Table 2.7/Poverty
- 4 Census 2001
- 5 www.treas.gov/press/releases/hp266.htm
- 6 Y. V. Reddy, May 2007, "Role of Monetary Policy in Attaining Growth with Stability: The Indian Experience"

In the early 1990s, the microfinance business was given a fillip by the innovative initiatives taken by non-government microfinance institutions (MFIs). They offered micro-credit i.e. credit provided to poor people for financial and business services and for self-employment in rural areas. Nevertheless, the existing banking policies, procedures and systems including deposit and loan products remained untailed to the requirements of the poor. The inadequacy of the banking sector to meet the needs of the poor despite vast infrastructure was explored by NABARD. The conclusions reached were; a) poor are bankable, b) poor need timely & better access to services and products rather than subsidized credit and c) need to build on synergy between existing groups of poor and financial resources of banks. To improve accessibility of the existing banking network to the poor, the Self Help Group (SHG)-Bank Linkage Model was launched by NABARD in 1992 to facilitate empowerment of the poor, while pursuing the macro-economic objective of overall economic growth.

Currently, a range of institutions in both the public sector and private sector offer microfinance services in India. Such institutions are broadly categorized into two categories, namely: formal institutions and informal institutions. The former category comprises of Apex Development Financial Institutions, Commercial Banks, Regional Rural Banks, and Cooperative Banks that provide microfinance services in addition to their general banking activities (microfinance service providers). The informal institutions that undertake microfinance services as their main activity being referred to as micro Finance Institutions (MFIs). Whilst both private and public

ownership can be found in the case of formal financial institutions offering microfinance services, the MFIs are mainly found in the private sector.

Types of MFIs	Estimated No.*	Legal status
1 Not-for-profit MFIs		
NGO-MFIs	400-500	Societies Registration Act, 1860, similar Provincial Acts/ Indian Trust Act, 1882
Non-profit companies	22	Section 25 of the Companies Act, 1956
2 Mutual Benefit MFIs		
Mutually-Aided Cooperative Societies (MACS) and similarly set up institutions	200-250	Mutually Aided Cooperative Societies Act enacted by State Government
3 For Profit MFIs		
Non-Banking Financial Companies (NBFCs)	25	Indian Companies Act, 1956 Reserve Bank of India Act, 1934
Total	700-800	

** This number includes only MFIs actually undertaking lending activity
Sources: 1) NABARD 2007, www.nabard.org 2) RBI, June 2006, 'Report on Trend and Progress of Banking in India'

Presently, there is no unified regulatory mechanism in place for MFIs. While NBFCs are regulated by the Reserve Bank of India NGO-MFIs, non-profit companies, and mutual benefit MFIs are regulated by the specific Act under which they are registered. As such, they are not subjected to minimum capital requirements and other prudential norms. The capital requirement for transformation into an NBFC is stringent—minimum entry capital of Rs2 crore (US\$0.5 million), maintenance of capital adequacy of 12% and liquid assets of 15% on public deposits.

In 2006, the MFI sector in India faced difficulties due to a hostile political situation in Andhra Pradesh (a hub of microfinance activities in India). MFIs were asked to reduce interest rates and to give an assurance that clients would not be pressurised unduly for the recovery of loans. Subsequently, Tamil Nadu and A.P. have passed ordinances against usurious rates of interest. State-led, subsidised SHG based programs continue to compete with MFIs. However, there has been a substantial improvement of the overall scenario and MFIs are attracting huge quantities of private investment from international and domestic sources (since Jan 2007, an estimated USD 43 million). Many MFIs are converting to NBFCs so as to mobilise public deposits, attract equity and loan funds. Banks have also lent substantially to MFIs (over Rs. 8000 crore or USD 1.9 billion) as part of their priority sector lending, in various forms such as partnership model loans, working capital term loans and overdraft facilities. Regional disparities are diminishing with more MFIs being established in the Northern part of the country, though of the largest 15 MFIs (in terms of client numbers) 11 are located in the Southern states. MFIs are now experimenting with new products (housing loans, micro-insurance tie-ups, investments, remittances) and loans to individuals. Some MFIs are also diversifying into livelihood support activities to offer more value to clients.

State overview of West Bengal

West Bengal has a population of 8.02 crore (interim figures of the 2001 census). It is the most densely populated state in India. The state has moderate to weak infrastructure and a literacy rate of 69.2% against a national average of 65.4%.



West Bengal has the third largest economy (2003–2004) in India, with a net state domestic product of US\$ 21.5 billion. West Bengal's gross state domestic product for 2006 is estimated at 236,044 crores. Agriculture is the leading occupation in West Bengal. Majority of the state population are cultivators and agricultural labors. However, the service sector is the largest contributor to the GDP of the state, contributing 51% of the state domestic product compared to 27% from agriculture and 22% from industry.

West Bengal is among one of the leading industrialized states of India. However, a significant part of the state is economically backward; around 25% of the population is BPL. Out of 15.7 million households around 9.9 million households (63%, for low income families it is around 80%) does not have access to banking services.

There are a number of MFIs/NGOs including SKS Micro Finance, Bandhan, Arohan, Village Welfare

Society, Sahara Utsarga Welfare Society, ASA International, KAS Foundation and Sarala Women Welfare Society, operational in the state and providing credit services to low-income families. Apart from these organisations, there are several SHGs linked to banks for savings and credit services under the SHG Bank Linkage Program (SBLP). As on 31 March 2008, only 15.4 lakh members are availing financial services through MFIs while 29.6 lakh members are availing financial services through SBLP. In all, 45.1 lakh members are covered by all the major MFIs and SBLP in the state, which is about 7.7% of the total population of the country.

Though the data shows a wide gap between demand and supply of the financial services in the state, a large proportion of un-served population is concentrated in and around Kolkata and adjoining districts (like Nadia, South and North 24 Parganas, Hawra and Hoogly). There is intense competition in these areas among the MFIs.

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Sarala's Microfinance operations

Main Indicators	31 Mar-07	31 Mar-08	31 Mar-09
Gross Loan Portfolio (Rs lakhs)	138.0	513.7	1,834.4
Number of Members	6,941	19,838	53,932
Number of Active Borrowers	4,825	14,763	46,334
Number of Branches	4	12	25
Asset Quality			
Portfolio at Risk (>60 days)/Gross Loan Portfolio	0.0%	0.01%	0.01%
Loan Loss Reserve/Avg. Gross Portfolio	0.0%	2.2%	2.0%
Efficiency and Productivity			
Operating Expenses/Average Gross Loan Portfolio	12.6%	11.2%	9.1%
Cost per Borrower (Rs)	72	68	62
Average Outstanding Loan Size (Rs)	2,860	3,480	3,959
Number of Borrowers/Field staff	219	352	459
Number of Borrowers/Total staff	193	255	329

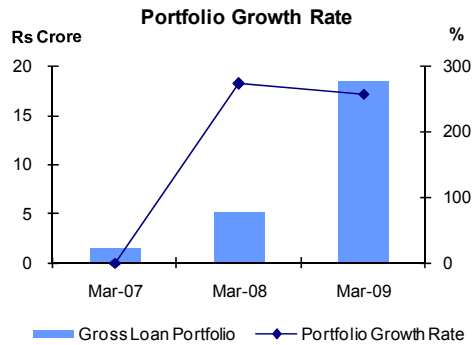
Sarala Women Welfare Society was incorporated as a section 25 company in July 2006 with its Head Office located in Kolkata. It was co-founded jointly by an U.S.A based non resident Indian, Dr Arabinda Sinha (having extensive experience in managing development projects) and Mr Pranab Rakshit (an accountant) with a mission to eradicate poverty through microfinance services to the poor. Before starting Sarala's microfinance operations, both (Dr Arabinda Sinha and Mr Pranab Rakshit) made exposure visits to ASA, BRAC and Grameen Bank in Bangladesh and later decided to follow the ASA model of microfinance. Accordingly, they approach ASA and ASA agreed to sustain Sarala's operations during the formative years by lending its own staff. Later in July 2006, the Regional Manager (RM) from ASA, Bangladesh came and started first branch in Uluberia in Howrah district.

The microfinance operations of Sarala started with initial contribution of USD25,000 (translates to Rs11.7 lakhs) from Dr Arabinda Sinha and his close associates. The amount has been given as interest free long term loan, which is yet to be subordinated to the external borrowings. The management of Sarala managed to mobilise Rs50 lakhs as term loan within two months of starting their operations and later many more funders came on board.

Sarala started its operations with first branch in Uluberia of Howrah district and later expanded to Hooghly, Kolkata and 24 Parganas- North. Presently, Sarala's microfinance programme is carried out through a network of 25 branches covering four districts and 453 villages as on 31 March 2009. It has an outreach of 53,932 members organised into 2,306 groups. The total active clients were 46,334 as on 31 March 2009.

The Co-CEO is assisted by the Senior Operations Officer, head of Finance and Accounts, IT & Systems, HR and Internal Audit. The Senior Operations Officer is further assisted by the Operations Officer as well as the field staff, which includes Divisional Manager (DM) and the Regional Manager (RM). However, the post of DM is vacant since April 09. As reported, one professional from ASA, Bangladesh is expected to join as DM in the next two months. The head of Finance and Accounts is assisted by the Finance and Accounts Officer. The IT and Systems is a one man department and is headed by the Chief Information Officer. The HR department is headed by the Assistant Manager who is assisted by one office assistant. The field operations are led by the Branch Manager (BM) who is assisted by 4 Credit Officers (COs). The DM and RM play supervisory role at the field level. The DM is responsible for supervising 4-5 regions and RM is responsible for supervising 4-5 branches within a region. The BM does the overall supervision of the day to day operations of the branch and cross-checks the reports submitted by COs, update the MIS and manage funds. The COs are responsible for disbursement, collections and also act as a cashier for 3 months on rotation basis.

In the last two and a half years of operations, Sarala's portfolio has grown at a CAGR of 264.57% from Rs138 lakhs as on 31 March 2007 to Rs1,834.4 lakhs on March 2009 (see figure below).



Microfinance policies

There have been no changes in the organization's operational policies since the last rating in August 2008. The organization largely follows the group based (ASA, Bangladesh model) individual lending methodology and its clientele includes women residing in the semi urban and rural areas.

Under the ASA model, lending is carried out only through women's groups of 8-30 members. The group becomes functional with 8 members and gradually increases to a maximum of 30 members. In the existing branches, the group is formed mostly through referrals from the existing clients where as in the new area, COs make several follow up visit to the area and meet the target client individually. Thereafter, those interested are organised in groups. In the first two group meetings, COs visits the houses and businesses of all the members, collects the membership fees@ Rs10 per member, distributes loan pass book and fills in loan application forms of all the members. As per the policy, the guardian of the respective member is also required to sign on the loan application form. KYC documents are collected during the third meeting. The BM also visits the member's house and cross checks the info given in the loan application form. Once satisfied, he approves the loan application and the loan is disbursed on the day of the fourth meeting at the branch office to all the members in the presence of BM, cashier and the concerned CO. In case of Small business loan, the loan is approved by the RM. The repayment is collected at the group meeting and the COs sign and updates the loan passbook. Prepayment is allowed after 40 weeks with penal charges. The organization also offers a grace period of up to a maximum of 6 weeks to its clients at the discretion of BM. The organization also has the policy of giving higher loan amount then the prescribed limit (in each loan cycle), subject to the approval from the respective RMs.

During the field visit it was observed that the client who foreclosed the loan got the subsequent loan on the same day at the branch office. This means that there is no proper loan evaluation system being followed for subsequent loans, which may have an adverse impact

on portfolio quality in future. Prepayments are collected by the CO in the group meeting.

For setting up a new branch in a new area, a team of two members is formed comprising of Operations officer and an experienced RM. The potential area is shortlisted on the basis of secondary data available, which is followed by a survey of the area. The major criteria for selecting a new area are the availability of banking service, physical infrastructure like road connectivity, economic activity, % of target population and number of MFIs operating in the area. Based on the recommendation of the team, CEO approves or rejects the area. If approved, a branch is set up with a BM and two COs in the area.

Loan products

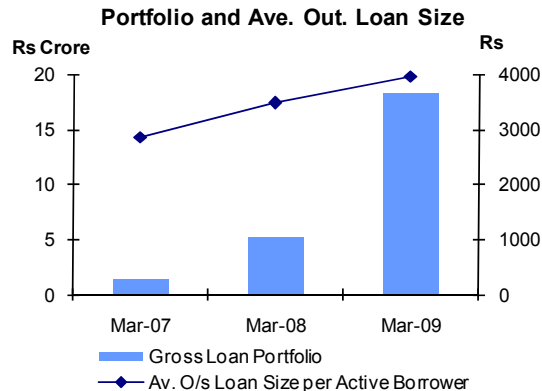
Sarala offers two loan products to its clients viz, small loan and small business loan. Small business loan has been introduced recently and is available to second cycle clients. Both the loans are available to the individual members in a group. In case of small loans, the interest rate has been reduced from 15% flat to 12.5% flat since March 2009. The following table displays the various loan products being offered and their contribution to portfolio as on 31 March 2009:

Features	Product	
	Small loan	Small business loan
Purpose	Both consumption as well as income generation	Micro enterprise
Interest rate	12.5% flat	15% flat
Security deposit (upfront)	10% of the loan amount	15% of the loan amount
Risk fund (upfront)	2% of the loan amount	2% of the loan amount
Loan tenure	45 weeks	46 weeks
Loan size	1 st cycle- Rs3,000-6000 and increases by Rs3,000 in every subsequent cycle	Rs15,000-25,000
Portfolio contribution	99%	1%

Deposits

Sarala collects 10% of the loan disbursed amount upfront as security deposit, which is refundable at the end of the loan term. The organization used to pay interest @6% p.a on the amount collected. However, this practice has been stopped since April 2008. As per the policy, if the client does not take subsequent loan then the entire security deposit amount is refunded and the client will be treated as a drop-out client and will not be considered for the subsequent loan. The total

outstanding balance of security deposit as on 31 March 2009 was Rs2.97 crores.



The average outstanding loan size has increased from Rs2,860 in March 2007 to Rs3,959 in March 2009 primarily on account of increase in the loan size from Rs3,855 to Rs6,084 during the period.

Insurance

As mentioned, the organization collects 2% of the loan amount as risk fund. The organization has a group insurance policy with LIC since August 2008, where only new client's (those who have been inducted in the programme since August 2008) life is covered to the extent of the amount borrowed. In the event of death of the client or her spouse, the organization writes-off the principle loan outstanding and returns the balance to the client/spouse. The premium is paid out of the risk fund. For old active clients (prior to August 2008), the claims are paid out of the risk fund collected. The total outstanding balance of the risk fund as on 31 March 2009 was Rs61.5 lakhs increased from Rs18.9 lakhs on March 2008. The total claim including premium paid was Rs9.3 lakhs for the period ending 31 March 2009 increased from Rs48,950 during the period ending 31 March 2008.

In addition to LIC, Sarala also has a tie up with Oriental Insurance Company, which provides accidental insurance to Sarala's clients under its flagship schemes "Rajrajeshwari Mahila Kalayan Bima Yojana". Under the scheme, Sarala has earned a total commission of Rs1,11,198 as on 31 March 2009.

Governance and strategic positioning

Sarala has performed moderately on the governance parameter with a grade of **β**, unchanged since the last two ratings in August 2008. This is primarily on account of limited microfinance experience of the Board and high competitive pressure, which is compounded by the absence of diversified product portfolio.

The Board of Sarala remains more or less the same since the last rating other than the induction of one

practicing lawyer as non-executive director, who does not have background in microfinance. Presently, Sarala has a non-executive four member Board. Dr Arabinda Sinha, who is also the Co-founder is also on the Board and is based out of United States. However, he is virtually involved (through skype, email, teleconferencing etc) in managing the affairs of the organization. Sarala's Board is quite diversified with none of them (barring Dr Arabinda Sinha) having microfinance experience. Dr Arabinda Sinha's experience in microfinance is also limited to his association with Sarala. The Board includes an academician, a retired DSP (West Bengal police), a retired Admin officer with a fertilizer company, researcher and a lawyer. Realising the limited microfinance experience of the Board, the management of Sarala has approached one retired microfinance professional from NABARD to join the Board. However, no final confirmation has been received from him till the time of the rating visit.

Sarala has recently (last month) formed a four member virtual advisory committee, out of which three members are based out of United States (with no prior microfinance experience) and one is with ASA, Bangladesh. The advisory committee meets virtually through skype/telephone and assist Board as and when required. The impact of the advisory committee on the functioning of the Board is yet to be seen.

The Board meets once every quarter with Dr Arabinda Sinha's virtual presence (over phone/skype) in the Board meeting. One of the Board member with whom the rating team interacted showed moderate awareness of the overall functioning of the organization. The Board meeting minutes do not reflect discussions on the policy related issues. In view of the rapidly increasing portfolio, M-CRIL strongly feels that Sarala's Board needs to be strengthened by inducting more qualified and experienced professionals from the sector.

Operational and growth strategy

The organization will continue to follow the ASA model in the near future and has no plans to deviate from the present position. However, in view of the increasing credit requirements, the organization has recently introduced small business loan for its second cycle clients for expanding their existing micro-enterprises.

To support its rapidly growing portfolio, it has strengthened its human resource base by inducting some qualified personnel at key positions (viz Operations, IT and Systems, Finance and Accounts. It is also planning to fully automate its MIS for smooth flow of information at various levels. A separate IT department has been created for the purpose, which has identified and analysed the requirements from the

software. Accordingly, it has decided to go with MIFOS software with some customization. The first pilot is expected in the next couple of months in two branches.

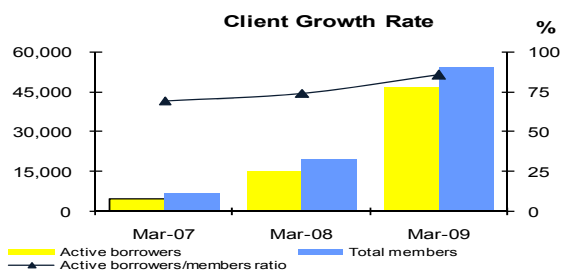
The organization is also planning to develop its in-house internal audit team, which is otherwise outsourced to a chartered accountant firm named K.C. Jain and Company at present. For the purpose it has already created an internal audit department.

In order to migrate to more appropriate legal form, the management of Sarala is in the process of acquiring a Kolkata based NBFC and change its legal status to NBFC in the near future.

For expansion, the organization mostly follows the 'split and spread' strategy. As per policy, a branch is supposed to handle a maximum of 2000 clients. The moment a branch reaches 2,000 clients, two more COs are inducted in the branch, taking total number of COs to 6. When the clientele base reaches to 3,000 the branch splits and a new branch is formed with 3 COs and 1,500 clients. The purpose is to make the new branch financially viable from the day one. The organization also has plans to expand to three new districts, viz Nadia, Murshidabad and Bardhaman in the current financial year. By the end of June 09, it has plans to open five new branches (one each in Nadia and Murshidabad districts and three by splitting the existing branches). It is planning to open 5-8 branches every quarter, which is subject to the availability of funds. By the end of the current financial year, it is expecting to increase its outreach to 100,000 clients with a portfolio size of Rs49.1 crores. The following table displays district wise distribution of the portfolio on 31 March 2009:

in Rs crores		
Districts	Loan Portfolio	% Portfolio
Howrah & Kolkata	14.1	77%
Hooghly	2.4	13%
North 24 Parganas	1.9	10%
Total	18.4	100%

The member base of Sarala has increased from 19,838 on 31 March 2008 to 53,932 as on 31 March 2009 and the active borrowers have increased from 14,763 to 46,334. The borrower's to member's ratio have also



increased from 74% to 86% during the same period (see figure below).

Competition

Sarala is facing fierce competition in its operational area from big as well as small MFIs. Some of the big and small MFIs operating in the area are Bandhan, SKS, Ujjivan, Sahara Utsarga, Sahara Uttarayan etc. During interaction with the COs in the branches visited by the rating team, it was observed that the COs also approach the areas where Bandhan is already operating and has formed groups in those areas. In one of the group visited, the rating team found that 4-5 members (including group leader) are also the members of Bandhan and the group meeting (both Sarala and Bandhan's group) takes place at the same venue. It was also observed that due to the high loan size as well as top up loans offered by SKS to its clients, the prospective clients shy away from joining Sarala's programme. To minimise the competitive pressure, it has recently reduced the interest rate on small loans from 15% flat to 12.5% flat and has introduced small business loan with a maximum loan size of Rs25,000 for its second cycle clients.

Second line of leadership

The second line (team) of management of Sarala is fairly new and consists of qualified personnel. The Co-CEO, who is an accountant by profession, is highly involved in managing the day to day affairs of the organization. He is well aware of the issues facing the organization. He works in close co-ordination with Dr Arabinda Sinha, who is also Co-CEO and is based out of USA. The Senior Officer- Operations, who is also the head of operations, is an MBA with four years of sales and marketing experience. He is being assisted by operations officer in managing day to day operations. The head of finance is a retired banker with 38 years of banking experience. He has been working with Sarala since October 2008. He is being assisted by a fresh MBA graduate, who has been working with the organization since April 2009. The head of the IT and Systems is a software professional with over 5 years of relevant experience. He has been working in his capacity since January 2009. He is well versed with the MIS customization requirements of the organization and related issues. The organization has recently created an internal audit department and has recruited a commerce graduate with 10 years of experience with central excise department of the steel industries. He has no prior experience of audit related work. The head of the HR is a commerce graduate with over one year of relevant experience. The decision making process is largely concentrated with Dr Arabinda Sinha in due consultation with Co-CEO.

Thus while the second line is competent, it needs grooming to take up leadership position in the future.

Fund mobilisation

Sarala has mobilised both grant as well as debt funds from diversified sources and the total outstanding long-term borrowings as on 31 March 2009 was Rs7.97 crores. The long-term borrowings also includes unsecured interest free loans worth Rs13.8 lakhs from the promoters (which is yet to be subordinated to the external borrowings and is withdrawable on demand by promoters) and Rs50 lakhs as transformation loan from SIDBI for possible transformation in to NBFC within four years. The short-term borrowings includes the cash credit limit of Rs7 crores with SBI, out of which Rs6.5 crores has been utilised and outstanding as on 31 March 2009. Most of these loans are hypothecated against the book value of the existing portfolio. The total grant received till date is Rs22.4 lakhs.

By the end of the current financial year, the organization intends to have a portfolio of Rs49.1 crores with 100,000 active borrowers. Accordingly, it has estimated a total funding gap of Rs35 crores and has approached various financial institutions, viz SIDBI, FWWB, Maanaveeya holdings, SBI, PNB, HDFC and ICICI bank for funds. As reported, SBI has agreed in principle to enhance the CC limit from present Rs7 crores to Rs10 crores along with a term loan of Rs10 crores. It has also sent a proposal to SIDBI and FWWB for Rs10 crores each and is expecting a sanction of Rs8 crores each in the current financial year. Besides, it is also expecting some funds from Maanaveeya holdings. The organization has also formed a five member finance committee (comprising of Dr Arabinda Sinha, Co-CEO, head of finance, accounts and systems) with a prime focus of mobilizing funds for their microfinance operations. The table below displays both short term as well as long term debt outstanding as on 31 March 2009

Rs in crores

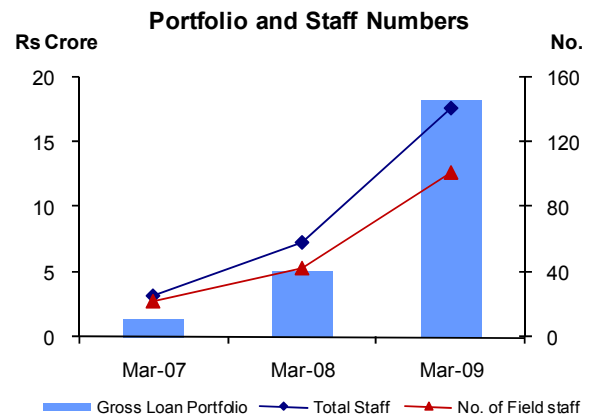
Lender	O/s on Mar-09	Interest Rate
SIDBI	3.0	12.5%
SIDBI (transformation loan to NBFC)	0.5	1%
FWWB	2.5	12.5%
Maanaveeya holdings	1.5	15%
HDFC	0.1	12.5%
SBI (CC limit)	6.5	11%
ICICI	0.20	11.5%
Unsecured loan from promoters	0.13	0%
Total	14.4	WACC-11.5%

Organisation and management

Sarala has preformed reasonably well on management parameters with a grade of $\beta+$. This is same as the last rating in August 2008. The organization is making efforts to strengthen its HR base by inducting qualified professional at key positions, which is a positive step. Its operating efficiency has also improved, owing to increased staff productivity. However, the performance is restricted on account of moderate internal control and monitoring systems, especially in view of the rapidly growing portfolio.

Human resource quality & management

The management of Sarala is continuously making efforts to strengthen its HR. The quality of HR has improved since the last rating in August 2008. It has recruited some qualified personnel at key positions viz Operations, Finance, Accounts, IT and Systems since then. Sarala has total staff strength of 141 as on 31 March 2009. The quality of management staff at HO is good. The roles and responsibilities of staff at each level are clearly defined.



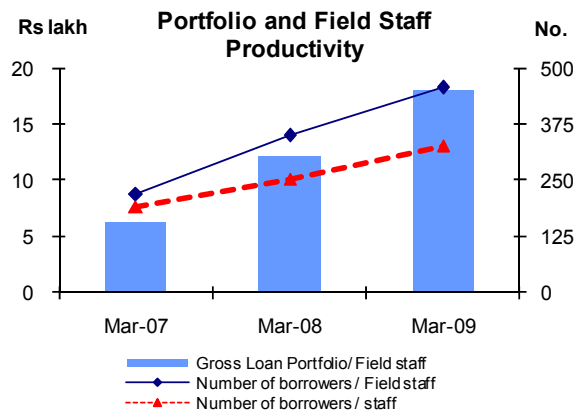
Sarala has a two member HR department. The recruitment of field staff is a three day process and is quite lengthy. It starts with the advertisement of vacancy in the local newspaper followed by screening of prospective candidates, pre-employment training for two days (both in-house and on-job) and personal interview. Thereafter, the organization prepares an empanelled list of trained candidates and if required, issues the appointment letters to some from the empanelled list on the same day or else as and when required. This practice is being followed since January 2009. The new recruits' first join on probation for three months and later becomes permanent based on their performance. For HO staff, the recruitment is mostly done through referrals from the existing staff or through advertisement of vacancy in the national newspaper followed by the personal interview. The interview is conducted by the Co-CEO and the HR.

There is no direct recruitment for any post (above CO level) at the field level.

There is no promotion policy as such. At the field level, all vacancies above CO level are filled through promotions. The promotions are performance based and is done as and when required. The organization does not have any transfer or staff rotation policy at the field level. The staffs are transferred from one branch to another as and when required.

Salaries are mostly fixed at the field level and are negotiable at the HO level. The organization does not have any incentive schemes for the field staff. This could be one of the reasons for high turnover of the field staff. However, a new staff incentive scheme has been formulated recently for the current financial year. The staff attrition rate is high at 15% as on 31 March 2009. The staff turnover is high at the field level as compared to the managerial staff.

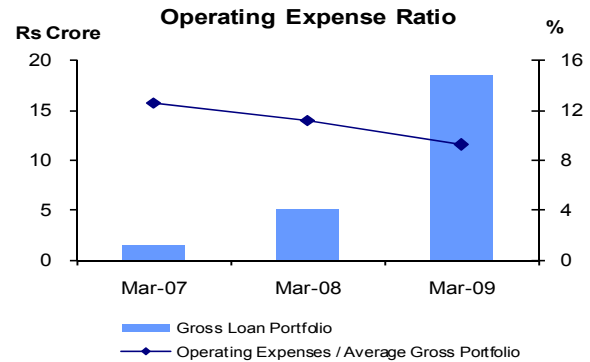
Staff productivity



The staff productivity of Sarala is good and has increased from 352 borrowers per field staff in March 2008 to 459 borrowers per field staff in March 2009. The total staff productivity has also increased from 255 borrowers per staff to 329 borrowers per staff during the same period. This is primarily because of the rapid expansion strategy adopted by the organization. This is clearly evident from the fact that the total number of branches has increased from 12 in March 2008 to 25 in March 2009 and so is the number of active borrowers, which have grown by 214%.

Operating efficiency

The operating efficiency of Sarala has improved with the OER declining from 11.2% on 31 March 2008 to 9.1% on 31 March 2009. The improvement in the operating efficiency is primarily because of the improved staff productivity and high growth in portfolio.



Accounting and MIS

For accounting and MIS, Sarala consolidates the data from the branches manually. At the branch level, all the transactions are first recorded from CO register (maintained separately by each CO for each day of the week) to the daily collection and disbursement register (with group wise break up), which serves as the primary document for MIS and accounts. Information from the daily collection and disbursement registers are transferred to the cash book on a day to day basis and the cash book is used to update the general ledger on a weekly basis. Each branch also prepares receipt and payment account (with supporting vouchers for petty expenses) on a monthly basis along with the monthly MIS report, which includes summary of product wise loan disbursement, demand and collection, past and current overdues, security deposit statement, monthly fund plan, salary statement and bank statement.

The receipt and payment account as well as the MIS report is being prepared by the respective BMs and forwarded to the HO without being verified by the respective RMs. The RMs crosschecks the reports with the branch records only when they are on monitoring visits to the branch. If they find any mistakes in the report, they resend the report to HO with necessary rectification. However, during the branch visit by the rating team, it was observed that the RM has not signed on some of the monthly MIS as well as the receipt and payment account. There is a high probability that these reports have not been verified by the RM and hence the accuracy of the data forwarded by the HO to the external agencies could be questioned. For instance, in one of those reports, the overdue amount figure did not tally with the figures calculated in the client wise overdue list and the same information is being shared with the external agencies. There is no system for multi level verification of the MIS report with the branch records.

Also, HO does not have any back-ups of the branch level records and in case of any untoward incident at the branches; all the relevant information will be lost.

The management of Sarala has realised this and has decided to go for complete automation of the MIS. As detailed earlier, the organization has created a separate IT department for the purpose, which is headed by qualified and experienced software professional. Based on the requirements, it has decided to go for MIFOS software (Grameen Koota), which requires some customization. Accordingly, it has identified a vendor based out of Ahmedabad for the necessary customization of the software. The organization is expecting to do the first pilot in two branches within the next couple of months.

For accounts, the organization uses Tally 9.0. The monthly receipt and payment account received from the branches forms the basis of accounting. Branch wise data are first punched in to the Ms-excel and later entered in to the tally software. The provisional financial statements are prepared on a monthly basis in the Ms-Excel and the audited financial statement is prepared annually. The time lag in preparation of audited financial statement is one and a half month.

Accounting practices of Sarala are moderate. It prepares accounts on accrual basis; however, due to limitations in its manual data, it is unable to compute interest accrued on loans but not due. The organisation currently recognises the interest income on flat rate basis. The current system does not allow the organisation to switch to more transparent interest recognition at a declining rate of interest.

The organization has started making provisions for loan loss reserve from the last financial year i.e. 2008-09. It has created a loan loss reserve of 1% of the gross portfolio. However, for the purpose of this rating, a loan loss reserve of 1% of the gross portfolio has been created for other years also.

Sarala being a section 25 company does not have the tax exemption certification under section 12(A) of the income tax act till the time of the rating visit and hence is liable to pay taxes. The organization has neither paid any taxes nor created any provisions for the same so far. However, for the purpose of this rating, M-CRIL has created a provision for taxation@30% of the net surplus. All grants and donations received by the organization have been treated as donated equity for the purpose of this rating. Depreciation has been calculated on written down value method. There is no write-off policy.

Tracking system for overdues

The tracking system for overdues at Sarala is reasonable. COs register serves as the primary document for tracking overdues, the moment the client defaults. Initial follow up with the default client is done by the respective CO and the BM. Later on, RMs also

visits the default clients when they are on a monitoring visit to the branch. Each branch prepares a client wise overdue report at the end of every month and forwards the summary of the report to the HO, without being verified by the respective RMs. The RM verifies the report only at the time of monitoring visit.

Internal audit and control systems

The internal control system at Sarala is moderate. There is a good supervisory structure at each level within the organization. As per policy, each RM supervises 4-6 branches and monitors each branch twice in a month. However, the quality of monitoring at the field needs significant improvement. There were instances where, the loan has been disbursed without the prior approval of the branch manager by the branch in-charge (for the day) in the absence of the BM and RM was not aware of such incidences. In such a scenario, there is a high probability of ghost loan being disbursed by the concerned CO. However, no such incidents have been reported so far. The major findings of the internal audit report reveals quite a few cases where COs have admitted more than 30 members in a group instead of forming a new group, which is a clear violation of the credit policy. There were cases where members of other groups are depositing their instalments not in their own group but in other groups, primarily because of their proximity to the other group. The organization may look into such cases to ensure that there were no dummy loans. Few cases have been registered where loans have been disbursed without collecting the KYC documents from the clients. There were cases where excess cash at the branch has been utilised by disbursing the loans to the clients a day ahead of the scheduled disbursement date. All such practices will make things more complex and open up the possibilities of committing frauds and misappropriation of funds by the field staff.

There is a system of monthly review meeting at the field level. At the branch level, BM conducts monthly meeting with the entire COs and review the progress made during the month. This meeting is conducted one day prior to the review meeting conducted by RMs with all the BMs of all the branches. In this meeting, the monthly MIS report of all the branches is reviewed and the target setting for the next month is done.

The internal audit function of the organization has been outsourced to a Chartered Accountant firm named 'K.N. Jain & Co'. At present each branch is being audited twice in a year. However, considering the size of the operations, the frequency of audit needs to be increased. The scope of audit includes financial audit, compliance on routine operational issues, credit and operational risk in accordance with the risk profile of the organization. The audit report is quite detailed

and is submitted to the Co-CEO with the follow-up being done in the next audit visit.

The management of Sarala is also making efforts to develop an in-house internal audit team. For the purpose, they have already recruited an internal audit officer, who at present is following up with the findings of the internal audit report submitted by K.N. Jain & Co with the respective branches. However, in the long run the idea is to strengthen its in-house internal audit team by inducting some of the experienced COs, who will take up the entire internal audit function from K.N. Jain & Co.

As per policy, each branch has to maintain a maximum closing cash balance of Rs10,000. In case, due to any reasons, if the closing cash balance is in excess of Rs10,000, a prior intimation is given to the concerned RM. Cash is kept in a two key safe, with one key with the BM and the other with the cashier. Each branch has a bank account and the funds are transferred internally. For funds transfer, RMs approval is required for transfer within the regions and between regions operations officer's approval is required. There is no cash in transit and cash at branch insurance.

Financial planning

The financial planning system at Sarala is good. It starts with the preparation of three year business plan on the basis of trends for the last three years. Besides, each branch prepares their own operational as well as six months fund plan and send it across to the HO, where

Financial Performance

Financial Ratios	31 March 2007	31 March 2008	31 March 2009
Capital Adequacy			
Risk Weighted Capital Adequacy ratio (including promoter's interest free loans)	10.2%	5.0%	6.4%
Asset Quality			
Portfolio at Risk (>60 days)/ Gross Loan Portfolio	0.0%	0.01%	0.01%
Loan Loss Provision Expense/Avg. gross Loan Portfolio	0.0%	2.2%	1.4%
Management			
Operating Expenses/Avg. Gross Loan Portfolio	12.6%	11.2%	9.1%
Number of Borrowers/Field staff	219	352	459
Number of Borrowers/Staff	193	255	329
Earnings			
ROE (Net operating income/Average Equity)	-286.4%	182.6%	138.7%
ROA (Net operating income/Average Assets)	-2.0%	3.7%	4.5%
Portfolio Yield	11.1%	26.3%	25.1%
Financial Cost Ratio (Int. & Fee expenses/Average Gross Loan Portfolio)	6.4%	8.5%	9.3%
Liquidity			
Cash & Liquid Assets/Total Assets	16.0%	0.3%	0.2%
Cash & Liquid Assets/Total Deposits	114.8%	1.6%	1.0%

it gets consolidated and the total fund requirements for the next six months is estimated.

For repayment to lenders, the organization maintains a repayment register, where the repayment schedule of all the lenders is recorded. This serves as the primary documents for identifying the amount of funds to be repaid each month. As detailed earlier, Sarala has a CC limit of Rs7 crores with SBI, which is also a centralised account of the HO. As almost all the branches have bank accounts with SBI, the surplus/idle cash at the branches is remitted to this centralised account as and when required. Hence, this account is used for making various repayments to lenders. Till the time of the rating visit no default was observed by the rating team.

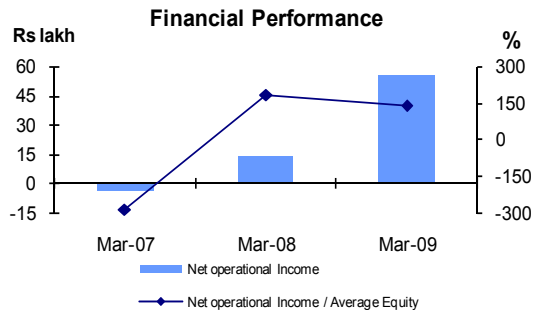
Quality of clients/member groups

Visited member groups showed reasonable performance on repayment of loans and overall credit discipline. Client awareness on products offered by Sarala is reasonable. Almost 50% of the clients were not aware of the risk fund. None of the clients were aware of the 6 weeks grace period being offered by the organization.

Infrastructure

The net fixed assets of Sarala form 0.9% of the total assets, which mainly comprises of Computers (hardwares and softwares), fixtures and furniture and vehicles.

Sarala has scored a grade of $\beta+$, which is one notch higher than the last rating. This is primarily on account of good portfolio quality maintained by the organization despite of high growth in portfolio, which is commendable. It has also performed well on profitability and sustainability parameters. Its profitability has increased, since the last rating in August 2008. However, its performance is restricted on account of low capital adequacy position, owing to increased borrowings and lack of adequate capital/grant infusion.



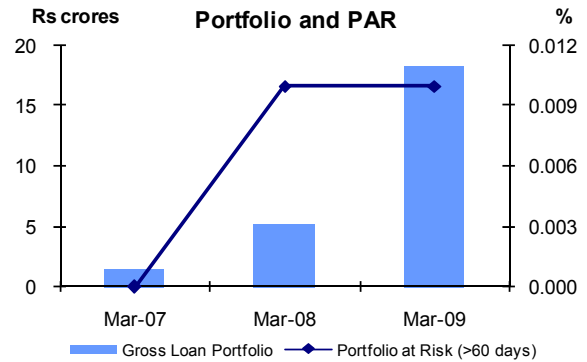
Credit performance and portfolio quality

Sarala has good portfolio quality with a repayment rate of 99.9% (as reported) and PAR (>60 days) of 0.01% as on 31 March 2009. It has maintained the same level of PAR (> 60 days) for the last two financial years despite the high growth in portfolio, which is commendable. The ageing of portfolio as on 31 March 2009 is given below:

Period (in days)	Portfolio at risk	PAR
0-30	0	0%
31-60	4,102	0.002%
61-90	7,413	0.004%
91-120	3,826	0.002%
>120	8,467	0.005%
Total	23,808	0.013%

In terms of diversification, the portfolio of Sarala is well diversified. However, the tailoring portfolio, which is as high as 35% of the portfolio, could be too much of a concentration risk. The following table displays the activity wise distribution of portfolio as on 31 Mar 09:

Activity	Portfolio O/s (Rs in crores)	% contribution
Agri & allied	3.1	17%
Petty business	6.8	37%
Tailoring	6.4	35%
Manufacturing	1.5	8%
Others	0.6	3%
Total	18.4	100%



Mobilisation of funds, equity and capital adequacy

As discussed earlier, Sarala has mobilised both short term as well as long term debt funds from diversified sources. It has a total debt outstanding (including short term) of Rs14.5 crores as on 31 March 2009 against Rs4.0 crores in March 2008, a significant growth of 263%. This also includes interest free unsecured long term loans worth Rs13.8 lakhs from the promoters, which is yet to be subordinated to the external borrowings and is withdrawable on demand by the respective promoters.

It has also mobilised security deposits from clients and the total outstanding as on 31 March 2009 was Rs2.97 crores against Rs1.01 crores in March 2008. It has also mobilised grant funds from various donor agencies worth Rs22.3 lakhs during the same period. The organization has not mobilised any equity capital so far.

The capital adequacy position of the organization as on 31 March 2009 was low at 6.4% (including promoter's interest free loan). For the purpose of calculating CAR, transformation loan of Rs50 lakhs from SIDBI is treated as subordinated loan and has been discounted @25% p.a. The tenure of the transformation loan is four years. Sarala urgently needs to mobilise more grant/capital funds to have a capital adequacy ratio at a comfortable level.

Asset, liability and equity composition

As on 31 March 2009, Sarala has deployed 95.9% of its total assets as loans, which is high. Its liquid assets (cash and bank) were quite low at 0.2% of the total assets. Short term deposits with other banks accounted for 3.2%, while net fixed assets accounted for 0.9% of total assets as on 31 March 2009, which is low considering the size of operations.

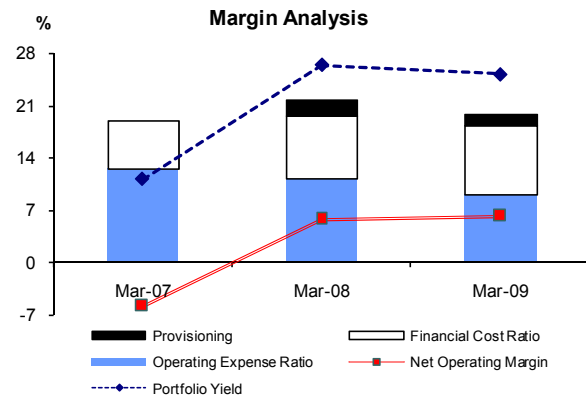
As on 31 March 2009, the total networth accounted for 3.6% of the total assets, out of which, capital fund, retained and current surplus and grants accounted for 1.9%, 65.4% and 32.7% respectively. Total funding liabilities, accounted for 92% of the total assets, out of

which long-term and short term borrowings accounted for 83% and security deposit from client accounted for 17% of the total funding liabilities on 31 March 2009. It is to be noted that security deposit is an interest free deposit from the client since April 2008.

Also, in the absence of certificate of exemption under section 12 (A) of the income tax act, a provision for taxation has been created for the purpose of this rating.

Profitability and sustainability

The yield on portfolio was well maintained at 25.1% for the period ending 31 March 2009. The yield to APR ratio was good at 94.3%. The operating expense ratio has also improved from 11.2% for the year ending 31 March 2008 to 9.1% for the period ending 31 March 2009. The financial cost has increased slightly from 8.4% to 9.3% during the same period, mainly on account of increased cost of borrowings. The impact of the increased cost of borrowings on the financial cost has been neutralised to some extent due to the non payment of interest on security deposit since April 2008. The organization has also mobilised transformation loan @1% p.a from SIDBI during the last financial year. The spread on portfolio is also high at 6.1%.



The high yield and the improved OER have resulted in the increase in the Operational Self Sufficiency (OSS) from 126.4% for the year ending 31 March 2008 to 130.8% for the period ending 31 March 2009. The Return on Assets (ROA) has also increased from 3.7% for the period ending 31 March 2008 to 4.5% for the period ending 31 March 2009. However, the profitability is expected to decrease in future, as the organization has reduced the interest rate on small business loan from 15% flat to 12.5% flat since March 2009, owing to high competition.

Future plans and prospects

Sarala is growing rapidly through its split and spread strategy. It has plans to open 5 five new branches by the end of the first quarter of the current financial year. It is also planning to have its presence in the three new districts viz Nadia, Murshidabad and Bardhman by the end of the current financial year. In order to achieve the economies of scale, it is planning to acquire a Kolkata based NBFC and transform its microfinance

activities to NBFC. For the purpose, it has already identified an NBFC based out of Kolkata. However, it is still in the negotiation stage. By the end of the current financial year, it is planning to have a portfolio of Rs45 crores with a total clientele base of 100,000. In order to achieve future growth strategy with operational soundness, Sarala needs to strengthen its control mechanism and complete MIS automation. .

Validity This rating is valid, subject to no other substantial inflows of loan funds into the organisation beyond the limits specified here and to no other significant changes in the organisational structure and external operating environment. A **rating update** (comprehensive repeat rating) is recommended whenever such changes take place or at the end of **one year** from the date of the initial assessment, whichever is earlier. Any substantial additional information that becomes available could also result in a rating update or a rating review (revision of rating grade based on a desk analysis).

Liability The rating assigned is a professional opinion of the assessors and M-CRIL does not guarantee the information and cannot accept any legal responsibility for actions arising out of the recommendations made.

Financial statements for Sarala operations

Balance Sheets as on ----

Rs

31-Mar-07	31-Mar-08		31-Mar-09
		Assets	
		<u>Current assets</u>	
76 128	51 780	Cash in hand	15 771
29 57 502	1 11 582	Cash in bank	2 88 482
16 25 000	21 75 000	Fixed deposits with banks	61 35 000
28 504	1 37 205	Interest accrued on FD	3 95 655
1 70 995	3 33 322	Loans and advances	9 89 113
63 800	47 850	Preliminary expenses (to the extent not w/o)	31 900
0	0	Accrued insurance commission	1 11 198
1 38 01 542	5 13 72 165	<i>Gross loan outstanding</i>	18 34 42 994
0	- 5 13 722	<i>Loan loss reserve</i>	- 18 34 430
1 38 01 542	5 08 58 443	Net loan outstanding	18 16 08 564
1 87 23 471	5 37 15 182	Total current assets	18 95 75 684
		<u>Long term assets</u>	
2 49 481	5 64 992	Net property and equipment	17 01 031
2 49 481	5 64 992	Total long term assets	17 01 031
1 89 72 952	5 42 80 174	Total assets	19 12 76 715
		Liabilities and Network	
		<u>Current liabilities</u>	
26 43 278	1 01 40 835	Security deposit from borrowers	2 97 97 195
35 500	1 20 510	Security deposit from staff	3 45 900
0	0	Interest payable to Maanaveeya	1 23 956
37 148	76 146	Payable against motor cycle revolving fund	3 44 796
0	4 05 758	Provision for taxation	20 80 329
1 51 628	1 81 246	Other liabilities and provisions	5 95 603
3 61 715	18 88 645	Insurance fund	61 53 502
		<u>Short term debt</u>	
9 39 394	6 06 061	Working capital loan from ICICI	2 12 122
0	1 99 98 387	Working capital loan from SBI	6 50 59 385
41 68 663	3 34 17 587	Total current liabilities	10 47 12 787
		<u>Long term liabilities</u>	
1 33 63 637	1 82 66 960	Long term borrowings	7 83 45 967
11 73 200	13 81 408	Unsecured interest free borrowings from promoters	13 81 408
1 45 36 837	1 96 48 368	Total long term liabilities	7 97 27 375
1 87 05 500	5 30 65 955	Total liabilities	18 44 40 162
		<u>Network</u>	
1 30 000	1 30 000	Capital Fund	1 30 000
5 20 000	5 20 000	Grants	22 35 000
0	- 3 82 548	Retained net surplus/(deficit)	5 64 219
- 3 82 548	9 46 768	Current net surplus/(deficit)	39 07 333
2 67 452	12 14 219	Total network	68 36 553
1 89 72 952	5 42 80 174	Total liabilities and network	19 12 76 715

Income statements (for the period ended)

			Rs
31-Mar-07	31-Mar-08		31-Mar-09
		Income	
7 23 817	61 83 287	Interest on loans to customers	2 29 06 954
74 820	1 54 020	Admission fees from borrowers	3 84 270
0	3 933	Bank interest	0
36 751	1 28 654	Investment income	3 78 709
5 137	6 879	Other Income	24 826
8 40 525	64 76 773	Total income	2 36 94 759
		Financial costs	
3 84 613	18 09 041	Interest on loans	78 37 835
19 853	1 76 303	Interest on deposits	0
4 36 059	44 91 430	Gross financial margin	1 52 39 844
0	5 13 722	Provision for loan losses	13 20 708
4 36 059	39 77 708	Net financial margin	1 39 19 136
		Operating expenses	
4 69 933	16 19 089	Salary	54 53 740
68 450	2 34 510	Rent	6 58 606
35 498	1 60 185	Travel and conveyance	4 63 774
10 686	87 403	Depreciation	3 30 298
64 503	1 18 113	Printing & stationary	4 21 689
15 950	15 950	Preliminary Expenses written-off	15 950
1 54 047	3 65 853	Administrative & other expenses	8 96 517
0	24 080	Group development and capacity building	96 657
8 19 067	26 25 183	Total operating expenses	83 37 231
- 3 83 007	13 52 525	Net surplus/(deficit)	55 81 905
		Non-operational income & expenditure	
459	0	Non-operational income	0
0	0	Non-operational expenses	0
- 3 82 548	13 52 525	Profit before tax	55 81 905
-	-	Tax expense/credit	0
- 3 82 548	13 52 525	Profit after tax	55 81 905
		Appropriations	
0	4 05 758	Provision for tax	16 74 571
- 3 82 548	9 46 768	Current surplus/(deficit) transferred to balance sheet	39 07 333

Notes to the financial statements

1. Sarala is a section 25 company and is still awaiting income tax exemption certification under section 12(A) of the income tax act. It has not paid any taxes so far. However, for the purpose of this rating provision for income tax has been created @30% of the net surplus.
2. Depreciation is calculated on a written down value basis
3. All income and expenses are recognized on accrual basis.
4. Grants received by Sarala have been treated as donated equity in the balance sheet (and not regarded as operational income). This includes operational as well as capital grants.
5. Loan loss reserve is 1% of the gross loan portfolio.
6. Yield on portfolio includes only the interest income.
7. For calculating CAR, transformation loan from SIDBI is considered as subordinated loan and has been discounted @25% p.a. The tenure of the loan is four years.

Glossary

1. Current repayment rate: Ratio of principal recovered (net of pre-payments) to the principal due for the last one year.
2. Portfolio at risk (PAR (>0days)): Ratio of the principal balance outstanding on all loans with overdues greater than or equal to 1 day to the total loans outstanding on a given date.
3. Yield on portfolio: The interest income on loans divided by the average loan portfolio for the year.
4. Other income to average portfolio: Total income other than from the interest on loans divided by average portfolio.
5. Financial cost ratio: Total interest expense for the year divided by the average portfolio.
6. Loan loss provisioning ratio: Total loan loss provisioning expense for the year divided by the average portfolio.
7. Operating expense ratio: Ratio of salaries, travel, administrative costs and depreciation expenses to the average loan portfolio.
8. Net operating margin: Difference of (yield on portfolio + yield on other income) and (financial cost ratio + loan loss provisioning + interest loss provisioning) – also known as spread on portfolio
9. Average loan portfolio: This represents the average loan outstanding for the year computed on a monthly basis.
10. Average total assets: This represents the average total assets for the year calculated on an annual basis.
11. Operational Self-Sufficiency: Ratio of total income to total costs for the year.
12. Financial Self-Sufficiency: Ratio of total income to total adjusted expenses for the year. Adjustments have been made for subsidised cost of funds (w.r.t. market interest rate), equity (w.r.t. inflation) and in-kind donations.
13. Risk weighted capital adequacy ratio: Ratio of networth to risk weighted assets
M-CRIL Risk weights: 100% for all assets except the following: fixed assets & interest bearing deposits: 50%; cash 0%.
14. Return on assets: Ratio of operational income/(loss) to average total assets
15. Return on equity: Ratio of operational income/(loss) to average net worth

Abbreviations

ASA	Activist for Social Alternatives
BM	Branch Manager
CO	Credit Officer
CS	Company Secretary
CSR	Corporate Social Responsibility
CAR	Capital Adequacy Ratio
CEO	Chief Executive Officer
CAGR	Compound Annual Growth Rate
DM	Divisional Manager
FCR	Financial Cost Ratio
FSS	Financial Self-Sufficiency
FWWB	Friends of Women's World Banking
GDP	Gross Domestic Product
HR	Human Resource
HDFC	Housing Development Finance Corporation
HO	Head Office
IOB	Indian Overseas Bank
IDBI	Industrial Development Bank of India
IT	Information Technology
LIC	Life Insurance Corporation of India
M-CRIL	Micro-Credit Ratings International Limited
MFI	Micro Finance Institution
MIS	Management Information Systems
NABARD	National Bank for Agriculture and Rural Development
NBFC	Non Banking Financial Company
NGO	Non Government Organisation
OER	Operating Expense Ratio
OSS	Operational Self-Sufficiency
PNB	Punjab National Bank
PAR	Portfolio At Risk
RBI	Reserve Bank of India
ROA	Return on Assets
ROE	Return on Equity
RM	Regional Manager
SARALA	Sarala Women's Welfare Society
SBI	State Bank of India
SIDBI	Small Industries Development Bank of India
SCB	Standard Chartered Bank
SHGs	Self Help Groups
SBLP	SHG Bank Linkage Programme
VWS	Village Welfare Society